

SHELL PHILIPPINES EXPLORATION B.V. AND CHEVRON MALAMPAYA LLC, PETITIONERS, VS. COMMISSION ON AUDIT, RESPONDENT.

G.R. No. 238846, February 25, 2025

Ponente: DIMAAMPAO, J.

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DIMAAMPAO, J.:

Impugned in these consolidated[1] Petitions for Certiorari[2] are Decision No. 2015-115[3] (assailed Decision) and Decision No. 2018-075[4] (challenged Resolution) of the Commission on Audit (COA), which affirmed Notice of Charge No. 2010-01-151(09).[5] The crux of the controversy is the purported undercollection of the government's share in the Malampaya Natural Gas Project from 2002 to December 2009 amounting to PHP 53,140,304,739.86.

Antecedents

On December 11, 1990, the Government of the Republic of the Philippines, represented by then President Corazon C. Aquino, executed a Service Contract[6] with Occidental Philippines, Inc. and Shell Exploration B.V., the predecessors-in-interest of Shell Exploration B.V. (SPEX), PNOC Exploration Corporation (PNOC-EC), and Chevron Malampaya LLC (Chevron), collectively referred to as the Contractors. Dubbed as the Malampaya Natural Gas Project, this Service Contract was entered into pursuant to Presidential Decree No. 87,[7] which was promulgated to hasten the discovery and production of indigenous petroleum through the utilization of government and/or private resources, local and foreign.[8]

Under the Service Contract, the Contractors were responsible to execute all operations for searching and obtaining petroleum in the contract area. They were obliged to furnish the necessary technology and financing, including the required services for petroleum operations, and assume all exploration risks without being entitled to reimbursement even if no petroleum in commercial quantity is discovered and produced. The agreement was subject to the control and supervision of the then Office of Energy Affairs (now the Department of Energy [DOE]).[9]

Section 7.3 of the Service Contract provides that 60% of the net proceeds of the petroleum operations shall be remitted to the government. Section 7.4 allots to the Contractors the 40% retention fee of the net proceeds.[10]

Under Section 12(a) of Presidential Decree No. 87, the Contractors are exempted from payment of all taxes except income tax. However, Section 19 provides that the Contractors shall be liable each taxable year for the Philippine income tax on income derived from petroleum operations under its Contract of Service, computed based on Sections 20 to 25 of the same law.[11]

The above Section 12(a) of Presidential Decree No. 87 is spelled out in Section 6.3 of the Service Contract:

The OFFICE OF ENERGY AFFAIRS shall assume and pay on behalf of CONTRACTOR and its parent company, on the first transaction in each instance where the tax is imposed, all income taxes payable to the

Republic of the Philippines based on income and profits and, with respect to CONTRACTOR, on the first transaction in each instance where the tax is imposed, all dividends, withholding taxes and other taxes imposed by the Government of the Philippines on the distribution of income and profits derived from Petroleum Operations to its parent company. The OFFICE OF ENERGY AFFAIRS shall promptly furnish to Contractor, without fee or other consideration, the official receipts issued in the name of CONTRACTOR by any duly empowered Government authority, acknowledging the payment of said taxes.[12] (Emphasis supplied)

Quite palpably, the 60% Philippine government share in the net proceeds includes the corporate income taxes of the Contractors from the start of commercial operations of the Service Contract in 2002 up to 2009.[13]

During the conduct of a post-audit in 2004, DOE Supervising Auditor Dolores T. Barraza (Auditor Barraza) noted that the corporate income taxes of the Contractors were deducted from the government's share. Consequently, Audit Observation Memorandum No. 2004-006 was issued where Auditor Barraza highlighted that the inclusion of the corporate income taxes in the government's share from January 2002 to November 2003 resulted in the understatement of the government revenue worth PHP 2.63 billion.[14]

Auditor Barraza computed that the total under collection of the 60% government share from service income up to December 2009 totaled PHP 53,140,304,739.86.[15] As a result, she issued Notice of Charge No. 2010-01-151(09)[16] identifying the persons liable for the transaction, namely: 1) Thelma M. Cerdeña (Cerdeña), Chief of the DOE Compliance Division; 2) Nora A. Tuazon (Tuazon), Officer-in-Charge of the DOE Financial Services; and 3) the Contractors.

DOE, SPEX, PNOC-EC, and Chevron sought recourse before the COA, which denied their appeal.[17]

Unflustered, the Contractors, DOE, Cerdeña, and Tuazon, filed their Petitions for Review before COA Proper.[18]

In the assailed Decision, COA denied the Petitions for Review and declared that the income taxes of the Contractors should not have been part of the 60% government share. COA disputed the argument of the Contractors that the government assumed their income taxes due and demanded that they settle their back taxes under the Service Contract.[19]

DOE and the Contractors' bid for a reconsideration of the assailed Decision was denied in the challenged Resolution. Taking issue with the disposition, the Contractors, as well as Cerdeña and Tuazon are now before this Court via their respective Petitions for Certiorari. Essentially, they impute grave abuse of discretion amounting to lack or excess of jurisdiction on the part of COA in issuing the repugned Decision and Resolution.

However, during the pendency of the instant Petitions, the Office of the Solicitor General (OSG) informed the Court of two existing international arbitration cases related to the case at bar: Shell Philippines Exploration B.V. v. The Republic of the Philippines, docketed as ICSID Case No. ARB/16/22 pending before the International Centre for Settlement of Investment Disputes (ICSID), and Shell Philippines Exploration B.V. (the Netherlands) and Chevron Malampaya LLC (USA) v. Government of the Republic of the Philippines, docketed as ICC Case No. 21096/CYK/PTA pending before the International Chamber of Commerce (ICC).[20]

Moreover, OSG furnished the Court with the ICSID Decision on Provisional Measures[21] in ICSID Case No. ARB/16/22, which states, among others, that:

(4)

The [Republic of the Philippines] shall refrain from taking any steps to enforce any of the three Notices of Charge against [Shell Philippines Exploration B.V.] or to collect any sums due thereunder from [Shell Philippines Exploration B.V.] until this Tribunal shall have decided the [Republic of the Philippines]'s jurisdictional objections identified in the Tribunals Procedural Order No.[.] 3 of August 28, 2017 or further

order[.][22]

On April 16, 2019, the ICC issued its Partial Final Award[23] in ICC Case No. 21096/CYK/PTA, which was followed by the release on December 16, 2019 of the Final Award[24] upholding the validity of the tax assumption mechanism in the Service Contract.

Commenting on all the Petitions, COA stood pat on its ruling, insisting that there was no provision in the law specifically providing that the income taxes of the Contractors would be part of the share of the Government.[25]

Issues

Stripped of unnecessary verbiage, the main queries brought to this Court for resolution are the following:

1.

Does the Government's 60% share under Presidential Decree Nos. 87 and 1459 include the Contractors' income taxes?

2.

Should the Contractors and petitioners Cerdeña and Tuazon be personally held liable for issuing the Notice of Charge?

On January 30, 2020, the OSG, acting on behalf of DOE, filed a Petition-in-Intervention[26] further fortifying its stance in the instant dispute between the Contractors and COA. The OSG stressed that Presidential Decree No. 87, Presidential Decree No. 1206[27] and Presidential Decree No. 1459[28] clearly provide that the Contractors' income taxes are included in the Government's 60% share in the net proceeds as stipulated in the Service Contract, and that tax assumption by the Government is permissible and not tantamount to a tax exemption.[29]

The Court's Ruling

The consolidated Petitions carry weight and conviction.

Courts consistently accord considerable deference to the factual findings of administrative bodies vested with expertise in their respective fields. Absent a showing of substantial evidence that such findings were premised on a misapprehension or misapplication of the evidence on record, they are deemed final, conclusive, and binding upon this Court.[30]

However, when there is a showing that COA has acted without, or in excess of jurisdiction, or with grave abuse of discretion amounting to lack or excess of jurisdiction, its findings may be set aside.[31] The Court has already discussed the scope of a certiorari proceeding when what is involved is a COA ruling—

A Rule 65 petition is a unique and special rule because it commands limited review of the question raised. As an extraordinary remedy, its purpose is simply to keep the public respondent within the bounds of its jurisdiction or to relieve the petitioner from the public respondent's arbitrary acts. In this review, the Court is confined solely to questions of jurisdiction whenever a tribunal, board or officer exercising judicial or quasi-judicial function acts without jurisdiction or in excess of jurisdiction, or with grave abuse of discretion amounting to lack or excess of jurisdiction.

The limitation of the Court's power of review over COA rulings merely complements its nature as an independent constitutional body that is tasked to safeguard the proper use of the government and, ultimately, the people's property by vesting it with power to (i) determine whether the government entities comply with the law and the rules in disbursing public funds; and (ii) disallow legal disbursements of these funds.[32] (Emphasis in the original)

The case at bench exemplifies the rare exception where the Court would overturn the factual and legal findings of COA.

The governing laws and Service Contract No. 38 expressly state that the Contractors' income taxes are included in the Governments share from the Malampaya Project's net proceeds

In the assailed Decision, COA found that there was no provision in the law which specifically provides that the income taxes of the Contractors should be part of the share of the Government.

This is a patent mistake committed by COA.

Section 18(b) of Presidential Decree No. 87 provides:

SEC. 18. Functions of the Petroleum Board. — In accordance with the provisions and objectives of this Act, the Petroleum Board shall:

....

(b) Enter into contracts herein authorized with such terms and conditions as may be appropriate under the circumstances including the grant of special allowance: Provided, however, That no depletion allowance shall be granted: Provided, further, That except as provided in Sections twenty-six and twenty-seven hereof, no contract in favor of one contractor and its affiliates shall cover less than fifty thousand nor more than seven hundred and fifty thousand hectares for on-sphere areas, or less than eighty thousand nor more than one million five hundred thousand hectares for off-shore areas: Provided, finally, That in no case shall the annual net revenue or share of the Government, including all taxes paid by or on behalf of the Contractor, be less than sixty per cent of the difference between the gross income and the sum of operating expenses and Filipino participation incentive. (Emphasis supplied)

So, too, Section 12(a)(i)(2) of Presidential Decree No. 1206 embodies the phrase "including all taxes paid by or on behalf of the contractor" in referring to the Government's annual net revenue or share:

SEC. 12. Transferred Powers and Functions. The following powers and functions are transferred as hereinafter indicated to the extent that they are not modified by any specific provision of this Decree:

....

(2) Enter into contracts herein authorized with such terms and conditions as may be appropriate under the circumstances: . . . And, Provided, finally, That in no case shall the annual net revenue or share of the government, including all taxes paid by or on behalf of the contractor, be less than sixty percent of the difference between the gross income and the sum of operating expenses and Filipino participation incentives[.] (Emphasis supplied)

Section 1(a) of Presidential Decree No. 1459 invariably echoes the above provision, viz.:

Section 1. Any provision of law to the contrary notwithstanding, the Secretary of Energy is hereby authorized to enter into petroleum service contracts, or re-negotiate and modify existing ones, upon the approval of the President of the Philippines, subject to the following conditions:

(a) The share of the Government, including all taxes, shall not be less than sixty per cent of the difference between the gross income and the sum of operating expenses and such allowances as the Secretary of Energy may deem proper to grant[.] (Emphasis supplied)

All the above quoted laws governing oil exploration and development industry in the Philippines clearly and unambiguously state that the Government's share includes all taxes. As the word include means "to take in or comprise as a part of a whole or group" or "to contain between or within"[33] and leaves no room for any other

interpretation, it becomes the duty of the Court to apply the law as it is worded.

"Under the [plainmeaning] rule or *verba legis*, wherever possible, the words used in the Constitution must be given their ordinary meaning except where technical terms are employed." [34] Here, the unequivocal language of Presidential Decree Nos. 87, 1206, and 1459 underscores two key principles: first, the income taxes paid by or on behalf of the Contractors are explicitly included in the government's guaranteed 60% share of the net proceeds from petroleum operations, and second, the government assumes and pays the Contractors' income taxes.

The intent of Presidential Decree No. 87 is a predominant factor in its interpretation

Even assuming that an interpretation should be had, the intent of the law is the most dominant influence in its interpretation. [35] Along this vein, former Prime Minister Cesar Virata, former DOE Secretary Raphael Perpetuo Lotilla, and former DOE Undersecretary Rufino Bomasang all confirmed through their respective Judicial Affidavits and Witness Statements that the petroleum fiscal system established under Presidential Decree No. 87 provides for tax assumption:

165.1. Prime Minister Virata initiated the policy study conducted by the petroleum industry expert Mr. Walter Levy and developed the draft legislation that was eventually promulgated as PD 87. Prime Minister Virata confirmed that the tax assumption system was intended to attract much needed foreign investments to the petroleum industry of the Philippines. It provides fiscal stability and enables foreign contractors to claim tax credits in their home jurisdictions. This benefit is legal and recognized in the investors' home countries. For the home countries of Petitioners in particular, this is evident from the tax treaties of (i) the Republic of the Philippines and the United States and (ii) the Republic of the Philippines and the Kingdom of Netherlands. In contrast, a mere tax exemption would not have given the same tax credit benefit.

165.2. Secretary Lotilla further confirmed that tax assumption is more favorable than tax exemption due to this tax credit benefit in the foreign investors home jurisdiction. From the standpoint of the Philippine Government, tax assumption has the same financial consequence as a tax exemption because under both, the Government gets its full 60% share. Hence, the tax assumption under PD 87 enables the Government to offer additional incentives to foreign contractors – in order to attract the necessary investments – without any cost or negative financial impact to the Philippines.

165.3. Undersecretary Bomasang said that throughout his 28 years of service as an energy official of the Government, the tax assumption system was a key incentive highlighted to entice foreign investors and was consistently acknowledged by the Government as legal, valid, and binding. [36] (Emphasis supplied)

Evidently, the intended scope and purpose of the law was to provide greater incentives to encourage private participation in the exploration and development of petroleum resources in the Philippines and attract foreign investors to take risks in the Philippine petroleum industry. Its key policy objective is to "hasten the discovery and production of indigenous petroleum through the utilization of government and/or private resources, local and foreign." [37] To achieve this, Presidential Decree No. 87 offered "more meaningful incentives to prospective service contractors," [38] one of which is the adoption of the tax assumption system. Correspondingly, from both the letter of the law and the intent of its framers, a rejection of the tax assumption system has no leg to stand on.

The correct interpretation, therefore, taking into consideration all the provisions of Presidential Decree No. 87, as well as its intent, is that: (a) the Contractor is liable to pay income tax, but b) the Contractors' income tax forms part of or is counted in the Government's 60% share.

Tax assumption is not tax exemption

COA postulates that Section 6.3 of the Service Contract infringes upon the sovereign prerogative of the Government to impose tax or exempt a class from taxation and therefore the said provision is not valid and

enforceable.[39]

The postulation is out on a limb.

Prefatorily, the word exemption is defined as "freedom from a duty, liability, or other requirement; an exception.[40] Exemption, being obnoxious to taxation, is not favored and never presumed; if at all, it must be categorically and unmistakably expressed in terms that admit of no doubt, yet such exempting provision must be interpreted in strictissimi juris against the taxpayer and liberally in favor of the taxing authority.[41] Even more crucially, the Constitution dictates that "[n]o law granting any tax exemption shall be passed without the concurrence of a majority of all the Members of the Congress."[42]

On the other hand, assumption is the "act of taking (esp. someone else's debt or other obligation) for or on oneself." [43] This means that the obligation or liability remains, although the same is merely passed on to a different person.[44]

From the foregoing perspective, it becomes quite clear that contrary to the standpoint of COA, the concept of an assumption is distinct and not synonymous to an exemption. Considering that Section 6.3 of the Service Contract is not in the nature of a tax exemption, it therefore does not infringe upon the sovereign prerogative of the Government, and the constitutional provisions on tax exemptions do not find application.

Upon this point, the case of *Republic v. City of Kidapawan*[45] is illuminating. The jugular issue of the controversy revolves around the purported exemption of Philippine National Oil Company-Energy Development Corporation (PNOC-EDC) from payment of real property taxes over the Mt. Apo Geothermal Reservation Area. Relatedly, the service contract entered into by the government and PNOC-EDC contained the similar provision in Section 6.3 of the subject Service Contract anent the payment of income taxes, viz.:

8.1

The GOVERNMENT shall assume and pay on behalf of CONTRACTOR all income taxes payable to the Republic of the Philippines based on income or profit derived from geothermal operations. It is understood, however, that such income tax payment shall come from the Government Share of sixty percent (60%) of the Net Value.[46]

The Court categorically held in *Kidapawan*:

Likewise, although it is the government which actually pays the income taxes, the contract nonetheless specifically provided that the payment is for and in behalf of PNOC-EDC and is chargeable against the 60% share of the government in the net profits derived by the PNOC-EDC arising from the geothermal operation. In reality, the PNOC-EDC is the actual payee while the government is only its agent in the payment of the income taxes. In fact, the official receipt is being issued in the name of PNOC-EDC.[47]

Evidently, it was decreed that "the exemption [from real property taxes] provided in the service contract cannot be given effect because the DOE, representing the government in the execution of the contract, has no authority to grant the same." [48] However, no such pronouncement was made with respect to the government's assumption of PNOC-EDC's income taxes.

It is likewise worthy to note that while the industry involved in the case at bench and in *Kidapawan* are distinct, it does not necessarily follow that the benefits which the respective contractors enjoy, such as tax assumption, must be construed differently. *Ubi lex non distinguit nec nos distinguere debemus*. When the law does not distinguish, we must not distinguish.

To illustrate further, in the case of *Mitsubishi Corp.-Manila Branch v. Commissioner of Internal Revenue*,[49] the

Court ruled in favor of the private contractor's claim for tax refund by virtue of a "tax assumption" clause in an Exchange of Notes between Japan and the Philippines, which provides:

Paragraph [5(2)] of the Exchange of Notes provides for a tax assumption provision whereby:

(2)

The Government of the Republic of the Philippines will, itself or through its executing agencies or instrumentalities, assume all fiscal levies or taxes imposed in the Republic of the Philippines on Japanese firms and nationals operating as suppliers, contractors or consultants on and/or in connection with any income that may accrue from the supply of products of Japan and services of Japanese nationals to be provided under the Loan.[50] (Emphasis and underscoring in the original)

The Court then distinguished tax exemption and tax assumption, ruling that the restrictions on tax exemption do not apply to tax assumption:

To "assume" means "[t]o take on, become bound as another is bound, or put oneself in place of another as to an obligation or liability." This means that the obligation or liability remains, although the same is merely passed on to a different person. In this light, the concept of an assumption is therefore different from an exemption, the latter being the "[f]reedom from a duty, liability or other requirement" or "[a] privilege given to a judgment debtor by law, allowing the debtor to retain [a] certain property without liability." Thus, contrary to the CTA En Banc's opinion, the constitutional provisions on tax exemptions would not apply.[51] (Emphasis supplied)

Consequently, the Court ruled in *Mitsubishi* that, pursuant to the tax assumption provision in the Exchange of Notes, the Philippine Government, through its executing agency, is responsible for paying any form of taxes directly imposable under the Contract:

As explicitly worded, the Philippine Government, through its executing agencies (i.e., NPC in this case) particularly assumed "all fiscal levies or taxes imposed in the Republic of the Philippines on Japanese firms and nationals operating as suppliers, contractors or consultants on and/or in connection with any income that may accrue from the supply of products of Japan and services of Japanese nationals to be provided under the [OECF] Loan." The Philippine Government's assumption of "all fiscal levies and taxes," which includes the subject taxes, is clearly a form of concession given to Japanese suppliers, contractors or consultants in consideration of the OECF Loan, which proceeds were used for the implementation of the Project. As part of this, NPC entered into the June 21, 1991 Contract with Mitsubishi Corporation (i.e., petitioner's head office in Japan) for the engineering, supply, construction, installation, testing, and commissioning of a steam generator, auxiliaries, and associated civil works for the Project, which foreign currency portion was funded by the OECF loans. Thus, in line with the tax assumption provision under the Exchange of Notes, Article VIII (B) (1) of the Contract states that NPC shall pay any and all forms of taxes that are directly imposable under the Contract[.][52] (Emphasis supplied)

Ultimately, the Court concluded in *Mitsubishi* that the collection of taxes from entities otherwise enjoying the benefits of a tax assumption arrangement is erroneous and, thus, refundable.[53]

Similarly, under Service Contract No. 38, the Contractors remain liable for income taxes, but the Philippine government assumes and pays these taxes as part of its share of net proceeds. The language of Section 6.3 of Service Contract No. 38 closely mirrors the tax assumption provision upheld in the Exchange of Notes in *Mitsubishi*.

The Arbitral Awards upheld the validity of the tax assumption mechanism in the Service Contract

"Arbitration agreements are liberally construed in favor of proceeding to arbitration." [54] Along this grain, Section XII of the Service Contract is clear and categorical—

SECTION XII CONSULTATION AND ARBITRATION

12.1

Disputes, if any, arising between the OFFICE OF ENERGY AFFAIRS and CONTRACTOR relating to this Contract or the interpretation and performance of any of the clauses of this Contract, and which cannot be settled amicably, shall be settled by arbitration. The OFFICE OF ENERGY AFFAIRS on the one hand and CONTRACTOR on the other hand, shall each appoint one arbitrator within thirty (30) days after receipt of a written request of the other Party to do so, such arbitrator shall, at the request of the other Party, if the parties do not otherwise agree, be appointed by the President of the International Chamber of Commerce. If the first two arbitrators appointed as aforesaid fail to agree on a third within thirty (30) days following the appointment of the second arbitrator, the third arbitrator shall, if the Parties do not otherwise agree, be appointed, at the request of either Party, by the President of the International Chamber of Commerce. If an arbitrator fails or is unable to act, his successor will be appointed in the same manner as the arbitrator whom he succeeds. Unless the Parties agree otherwise, the Philippines shall be the venue of the arbitration proceedings. The English language shall be the language used.

12.2

The decision of a majority of the arbitrators shall be final and binding upon the parties. Judgment upon the award rendered may be entered in any court having jurisdiction or application may be made to such court for a judicial acceptance of the award and an order of enforcement, as the case may be.

12.3

Except as provided in this Section, arbitration shall be conducted in accordance with the Rules of Arbitration of the International Chamber of Commerce, then in effect.[55] (Emphasis supplied)

As it happened, the Contractors lodged two separate cases for arbitration. The case before the ICSID is still pending. Meanwhile, on April 16, 2019, the ICC, in ICC Case No. 21096/CYK/PTA, issued its Partial Final Award, ruling in this wise:

203.

Since Section 6.3 expressly requires the DOE to "assume and pay" the Contractor's income taxes, and Section 7.4 entitles the Contractor to 40% of Net Proceeds, the value of the Contractor's income taxes can only form part of the DOE's 60% share of Net Proceeds. There is no other way to read these provisions together and give them all meaning.

204.

The Tribunal wishes to emphasize that this interpretation has been accepted by the DOE and the OSG, which have consistently maintained that "the corporate income tax of the Contractor is a proper inclusion to and/or forms part of the sixty percent (60%) share of the Government citing Section 18(b) of [Presidential Decree No.] 87 and Section 6.3 of SC 38."

....

206.

This interpretation also comports with the implementing legislation which specifies that the Government's share of net proceeds "including all taxes paid by or on behalf of the contractor" cannot be less than 60%.

....

230.

The Respondent contends that Section 6.3 of SC 38 infringes upon the sovereign prerogative of the Philippines [sic] government to impose tax or exempt a class from taxation, and accordingly, that this tax assumption provision is not valid and enforceable. The Respondent challenges the validity of Section 6.3 of SC 38 and not SC 38 as a whole.

231.

The Tribunal disagrees with the Respondent.

232.

Firstly, the tax pertaining to the Claimants' income derived from their petroleum operations is paid to the government of the Philippines, albeit by the DOE. As noted earlier, such payment is made by the DOE on behalf of the Claimants pursuant to Section 8.4 of SC 38. Section 8.4 provides that:

The Office of Energy Affairs, upon payment by it of Contractor's income taxes shall procure official receipts in the name of Contractor evidencing such payment. Each of the second parties, if more than (1) shall be subject to tax separately on its share of income and the office of Energy Affairs shall supply each with an individual receipt in its own name.

233.

There is no evidence on the record that the Claimants' income tax has not been paid to the national government by the DOE. Thus, there is no diminution of the government's 60% share.

234.

Secondly, there is no evidence on the record that the applicable Presidential Decrees prohibit the practice of tax assumption when a particular agency of the government engages in business for profit.

235.

Tax assumption is a form of tax avoidance which is allowed in the Philippines. As well put by a tax scholar: "there is a distinction between tax avoidance and tax evasion. Tax avoidance is the use of legal means to

prevent accrual of the tax or to reduce the tax that may accrue, while tax evasion is the use of fraudulent means to defeat the taxes that have accrued. Tax avoidance is legal while tax evasion is illegal and punishable by law."

236.

In the case at hand, the tax assumption made by the DOE was done for a legitimate, not a fraudulent purpose, namely as an incentive for the Claimants to agree to explore oil and gas in the Philippines. The project enabled the government of the Philippines to earn billions of pesos.

237.

As testified by Claimants' fact witnesses, this tax assumption incentive is usual in the oil and gas industry business. There is no public policy offended when an agency of the government adopts it as a business strategy especially when its overall effect is beneficent to the government.

238.

Thirdly, in any event, the sovereign right of the government of the Philippines to tax is not at issue as, in fact, all the taxes due to the State have been paid.

239.

Fourthly, the case at bar does not involve any tax exemption claim on the part of the Claimants but rather tax sharing, a legitimate business practice in the oil industry.

240.

Finally, the Tribunal gives high persuasive effect to the positions of the different branches and agencies of the government of the Philippines that have recognized the legality of the tax assumption provision of Service Contract 38.

241.

The DOE, which represent[s] the government of the Philippines in Service Contract 38, has been unwavering in its position supporting the Claimants. The Bureau of Internal Revenue in charge of collecting income tax due to the Government has not assailed said tax assumption as unlawful. Neither have the Department of Finance nor the Department of Justice. The Commission on Audit has audited the 60-40 division of profits between the parties based on the tax assumption provision. It was only in 2010 that the COA asserted the illegality of the tax assumption provision in Service Contract 38. The Office of the Solicitor General, the official counsel of the government of the Philippines, has refused to defend COA's position in the Supreme Court that the tax assumption provision violates the 60% share of the Government in Service Contract 38. President Rodrigo R. Duterte maintains that the Government should honour its commitment in Service Contract 38. Congress has not amended PD 87 and other related presidential decrees to accommodate the COA's new interpretation.

242.

The consistency of these governmental opinions for the past thirty years support the Claimants' position that the tax assumption provision of Service Contract 38 is legally valid.

243.

On the basis of the foregoing, the Tribunal finds that Section 6.3 of SC 38 is valid and enforceable under Philippine law.

....

284.

Having carefully considered the Parties' arguments in their written pleadings and oral submissions, and having deliberated, for the reasons stated above and as summarized in Section VI, the Tribunal unanimously:

(a)

Dismisses the Respondent's arbitrability objection;

(b)

Declares that the Philippine Income Taxes paid by or on behalf of the Claimants form part of the Respondent's sixty per cent (60%) share of the Net Proceeds from Petroleum Operations under the Service Contract;

(c)

Declares that Section 6.3 of the Service Contract which provides, inter alia, that the Respondent "shall assume and pay" all the Consortium's Income Taxes, is a valid and enforceable clause;

(d)

Declares that the Respondent has already received in full its 60% share of the Net Proceeds from 2002 until the conclusion of the Hearing in September 2018;

(e)

Declares that the Respondent has no right to demand or collect from the Claimants any additional amount for the period of 2002 until the conclusion of the Hearing in September 2018;

(f)

Directs the Respondent to comply with its obligations under the Service Contract;

(g)

All other claims are reserved for decision in a Final Award.[56] (Emphasis in the original)

Invariably, in the December 16, 2019 Final Award, the ICC Arbitral Tribunal reaffirmed the Partial Final Award and upheld the validity of the tax assumption mechanism in the Service Contract. Given that the policy of the state favors arbitration, the exhaustive contribution of foreign arbitral tribunals, such as the ICC, is invaluable in resolving the case at bench. Considering that the ICC made a categorical finding in favor of the Contractors, the Court must perforce respect to such finding.

Be that as it may, even in the absence of the arbitral award, the Court's independent analysis of the COA's disposition inevitably leads to the same conclusion—the tax assumption mechanism under Service Contract No. 38 is lawful and consistent with the legislative framework established by Presidential Decree Nos. 87, 1206, and 1459.

Cerdeña and Tuazon are likewise absolved from liability

Considering that the Notice of Charge was issued by COA with grave abuse of discretion amounting to lack or excess of jurisdiction, a discussion on the liability of Cerdeña and Tuazon becomes superfluous. Similar to the Contractors, this Court absolves them from any liability under the Notice of Charge.

A final cadence. The Court is on all fours with COA to zealously ensure that the Government is never placed at a disadvantage and that it rightfully receives what is due it in all its transactions. Nevertheless, remaining bound by the Constitution and the laws of the land, the Government cannot be allowed to renege on its obligation, especially when such has been distinctly outlined in the contract it freely entered into and agreed to.

ACCORDINGLY, the consolidated Petitions for Certiorari are GRANTED. The April 6, 2015 Decision No. 2015-115 and the January 24, 2018 Decision No. 2018-075 of the Commission on Audit are REVERSED and SET ASIDE. The October 5, 2010 Notice of Charge No. 2010-01-151(09) is LIFTED.

SO ORDERED.

Gesmundo, C.J., Inting, Zalameda, M. Lopez, Gaerlan, Rosario, Marquez, Kho, Jr., and Singh, JJ., concur.

Leonen, S.A.J., see dissenting opinion.

Caguioa, J., see concurring opinion.

Hernando,[*] J., on official leave. See concurring opinion.

Lazaro-Javier,[*][*] J., no part.

J. Lopez, J., with separate concurring opinion.

[*] On official leave.

[*][*] No part.

[1] Rollo (G.R. No. 238846), pp. 4817-4818; rollo (G.R. No. 238852), pp. 458-459; rollo (G.R. No. 238862), pp. 281-282.

[2] Rollo (G.R. No. 238846), pp. 3-129; rollo (G.R. No. 238852), pp. 3-45; rollo (G.R. No. 238862), pp. 3-27.

- [3] Rollo (G.R. No. 238846), pp. 282-301; rollo (G.R. No. 238852), pp. 46-65; rollo (G.R. No. 238862), pp. 204-223. The April 6, 2015 Decision was signed by Commissioners Heidi L. Mendoza and Jose A. Fabia.
- [4] Rollo (G.R. No. 238846), pp. 306-337; rollo (G.R. No. 238852), pp. 66-97; rollo (G.R. No. 238862), pp. 28-59. The January 24, 2018 Resolution was signed by Commissioners Jose A. Fabia and Isabel D. Agito. Chairperson Michael G. Aguinaldo inhibited.
- [5] Rollo (G.R. No. 238846), pp. 418-419; rollo (G.R. No. 238852), pp. 129-130; rollo (G.R. No. 238862), pp. 129-130. The October 5, 2010 Notice of Charge (NC) No. 2010-01-151(09) was signed by Dolores T. Barraza, Supervising Auditor, Office of the Auditor, Department of Energy.
- [6] Rollo (G.R. No. 238846), pp. 216-254; rollo (G.R. No. 238852), pp. 1444-1482; rollo (G.R. No. 238862), pp. 60-98. Also referred to as Service Contract No. 38 or SC 38 in the proceedings below.
- [7] The Oil Exploration and Development Act of 1972.
- [8] Rollo (G.R. No. 238846), p. 283; rollo (G.R. No. 238852), p. 47; rollo (G.R. No. 238862), p. 205.
- [9] Id.
- [10] Rollo (G.R. No. 238846), pp. 237-238, 283; rollo (G.R. No. 238852), pp. 47, 1465-1466; rollo (G.R. No. 238862), pp. 81-82, 304.
- [11] Rollo (G.R. No. 238846), p. 283; rollo (G.R. No. 238852), p. 47; rollo (G.R. No. 238862), p. 205.
- [12] Rollo (G.R. No. 238846), p. 236; rollo (G.R. No. 238852), p. 1464; rollo (G.R. No. 238862), p. 80.
- [13] Rollo (G.R. No. 238846), p. 284; rollo (G.R. No. 238852), p. 48; rollo (G.R. No. 238862), p. 206.
- [14] Id.
- [15] Rollo (G.R. No. 238846), p. 285; rollo (G.R. No. 238852), p. 49; rollo (G.R. No. 238862), p. 207.
- [16] Rollo (G.R. No. 238846), pp. 418-419; rollo (G.R. No. 238852), pp. 129-130; rollo (G.R. No. 238862), pp. 129-130.
- [17] Rollo (G.R. No. 238846), pp. 603-615; rollo (G.R. No. 238852), pp. 255-267; rollo (G.R. No. 238862), pp. 192-203. The August 22, 2011 NGS-Cluster B Decision No. 2011-009 was penned by Rizalina Q. Mutia, Director IV, COA National Government Sector, Cluster B – General Public Services II and Defense.
- [18] Rollo (G.R. No. 238846), p. 286; rollo (G.R. No. 238852), p. 50; rollo (G.R. No. 238862), p. 208.
- [19] Rollo (G.R. No. 238846), pp. 291-293; rollo (G.R. No. 238852), pp. 55-57; rollo (G.R. No. 238862), pp. 213-215.
- [20] Rollo (G.R. No. 238862), pp. 283-297.
- [21] Rollo (G.R. No. 238846), pp. 4834-4887; rollo (G.R. No. 238862), pp. 298-351. This August 29, 2017 Decision was signed by the President of the Tribunal V. V. Veeder, Arbitrator Horacio A. Grigera Naón, and Arbitrator Brigitte Stern.
- [22] Rollo (G.R. No. 238862), p. 350.
- [23] Rollo (G.R. No. 238846), pp. 5051-5135; rollo (G.R. No. 238852), pp. 601-685; rollo (G.R. No. 238862), pp. 492-577. The April 16, 2019 Partial Final Award was signed by the Arbitral Tribunal composed of Hon. L. Yves Fortier, QC, President; Sir David A. R. Williams, QC; and Chief Justice Reynato S. Puno (Ret.).

- [24] Rollo (G.R. No. 238846), pp. 5436-5478; rollo (G.R. No. 238852), pp. 979-1021; rollo (G.R. No. 238862), pp. 783-825.
- [25] Rollo (G.R. No. 238846), pp. 4945-5031; rollo (G.R. No. 238852), pp. 508-593; rollo (G.R. No. 238862), pp. 399-484.
- [26] Rollo (G.R. No. 238846), pp. 5817-5861; rollo (G.R. No. 238852), pp. 1346-1390; rollo (G.R. No. 238862), pp. 1150-1194.
- [27] Creating the Department of Energy (1977).
- [28] Authorizing the Secretary of Energy to Enter into and Conclude Service Contracts, or Re-Negotiate and Modify Existing Contracts Subject to Certain Limitations (1978).
- [29] See rollo (G.R. No. 238846), pp. 5827-5839; rollo (G.R. No. 238852), pp. 1356-1368; rollo (G.R. No. 238862), pp. 1160-1172.
- [30] See *Melloria v. Director Jimenez*, 944 Phil. 300, 307 (2023) [Per J. Dimaampao, En Banc].
- [31] See *National Power Corporation Board of Directors v. Commission on Audit*, 872 Phil. 671, 679 (2020) [Per J. Reyes, J., Jr., En Banc].
- [32] *Melloria v. Jimenez*, 944 Phil. 300, 308 (2023) [Per J. Dimaampao, En Banc]. (Citation omitted)
- [33] MERRIAM-WEBSTER DICTIONARY, "include," available at <https://www.merriam-webster.com/dictionary/include> (last accessed on October 9, 2024).
- [34] *Macalino v. Commission on Audit*, 949 Phil. 517, 521 (2023) [Per J. Marquez, En Banc].
- [35] See *Development Bank of the Phils. v. Commission on Audit*, 424 Phil. 411, 432 (2002) [Per J. Carpio, En Banc].
- [36] Rollo (G.R. No. 238846), pp. 62-63.
- [37] Presidential Decree No. 87 (1972), sec. 2.
- [38] 2[nd] Whereas clause of Presidential Decree No. 87 (1972).
- [39] Rollo (G.R. No. 238846), p. 296; rollo (G.R. No. 238852), p. 60; rollo (G.R. No. 238862), p. 218.
- [40] BLACK'S LAW DICTIONARY 717 (11[th] ed., 2019).
- [41] See *Commissioner of Internal Revenue v. Guerrero*, 128 Phil. 197, 201 (1967) [Per J. Fernando, En Banc].
- [42] CONST., art. VI, sec. 28(4).
- [43] BLACK'S LAW DICTIONARY 154 (11[th] ed., 2019).
- [44] *Mitsubishi Corporation-Manila Branch v. Commissioner of Internal Revenue*, 810 Phil. 16, 26 (2017) [Per J. Perlas-Bernabe, First Division].
- [45] 513 Phil. 440 (2005) [Per J. Ynares-Santiago, First Division].
- [46] *Id.* at 449.
- [47] *Id.* at 450.
- [48] *Id.*

[49] 810 Phil. 16 (2017) [Per J. Perlas-Bernabe, First Division].

[50] Id. at 25-26.

[51] Id. at 26.

[52] Id. at 26-27.

[53] Id. at 28.

[54] Bases Conversion Dev't. Authority v. DMCI Proj. Developers, Inc., 776 Phil. 192, 205 (2016) [Per J. Leonen, Second Division]. (Emphasis supplied)

[55] Rollo (G.R. No. 238846), pp. 243-244, rollo (G.R. No. 238852), pp. 1471-1472; rollo (G.R. No. 238862), pp. 87-88.

[56] Rollo (G.R. No. 238846), pp. 5115-5116, 5120-5122, and 5133-5134; rollo (G.R. No. 238852), pp. 665-666, 670-672, 683-684; rollo (G.R. No. 238862), pp. 557-558, 562-564, 575-576.

DISSENTING OPINION

LEONEN, SAJ.:

I dissent.

I

Presidential Decree No. 87,[1] the governing law on indigenous oil exploration, development and production, does not explicitly state that the government's share in petroleum revenues includes income taxes. Section 18 of Presidential Decree No. 87, the supposed statutory basis of Section 6.3 of the Service Contract, states:

SEC. 18. Functions of Petroleum Board.[2] — In accordance with the provisions and objectives of this Act, the Petroleum Board shall:

....

(b) Enter into contracts herein authorized with such terms and conditions as may be appropriate under the circumstances including the grant of special allowance: Provided, however, That no depletion allowance shall be granted: Provided, further, That except as provided in Sections twenty-six and twenty-seven hereof, no contract in favor of one contractor and its affiliates shall cover less than fifty thousand nor more than seven hundred and fifty thousand hectares for on-shore areas, or less than eighty thousand nor more than one million five hundred thousand hectares for off-shore areas: Provided, finally, That in no case shall the annual net revenue or share of the Government, including all taxes paid by or on behalf of the Contractor, be less than sixty per cent of the difference between the gross income and the sum of operating expenses and Filipino participation incentive;

(c) Provide for the manner and form of the income tax payment, the reimbursement of operating expenses, the payment of service fee, and payment of Filipino participation incentive allowance, if any, in the service contract[.] (Emphasis supplied)

The phrase "including all taxes paid by or on behalf of the Contractor" means "additionally" or "in addition to," such that both the annual net revenue or government's share in petroleum production and all taxes paid would be taken into account in meeting the minimum threshold of 60%. It comes from an understanding that the "taxes

paid" are part of the larger or broader group of revenues to the government, and not necessarily of the "annual net revenue or share of the government in petroleum production." Otherwise, had the latter been the intent, a clearer phrasing should have been used such as "which includes," "inclusive of," or any language clearly and unequivocally indicative of such intent.

This is the proper interpretation if we look at the immediate context of the provision stating the function of the Petroleum Board (now Department of Energy) to "enter into contracts. . . with such terms and conditions as may be appropriate" and "provide for the manner and form of the income tax payment. . ." and of Presidential Decree No. 87 as a whole. The purpose and objective sought to be attained and particularly those provisions outlining the privileges of contractors[3] and providing for their income tax liability.

In *Philippine International Trading Corp. v. Commission on Audit*: [4]

It is a rule in statutory construction that every part of the statute must be interpreted with reference to the context, i.e., that every part of the statute must be considered together with the other parts, and kept subservient to the general intent of the whole enactment. Because the law must not be read in truncated parts, its provisions must be read in relation to the whole law. The statute's clauses and phrases must not, consequently, be taken as detached and isolated expressions, but the whole and every part thereof must be considered in fixing the meaning of any of its parts in order to produce a harmonious whole. Consistent with the fundamentals of statutory construction, all the words in the statute must be taken into consideration in order to ascertain its meaning.[5] (Emphasis in the original, citations omitted)

The government's share in petroleum production is distinct from income tax, although ultimately, both are revenues of the government. To add, the government's share in the proceeds of the Malampaya Natural Gas Project springs from the State's ownership of the natural resource discovered, produced, and sold. On the other hand, the income tax payment flows from the Service Contractors' derivation of income from activities within the Philippines' territorial jurisdiction. It is a tax on the privilege of earning income.[6]

Again, Section 18(b) of Presidential Decree No. 87 should be construed to mean only that the government's share and all taxes paid by or on behalf of the contractor should not be less than 60%.

A contrary interpretation such as that being pressed upon this Court — that income taxes are included in the government's share—would run counter to Presidential Decree No. 87's policy of maximum revenues to the government and just return to the contractors from production of indigenous petroleum. More importantly, it amounts to an income tax exemption. To justify such result, it is imperative that the language employed be of the clearest and most satisfactory character. However, the clause relied upon in Section 18(b) of Presidential Decree No. 87 is indefinable.

II

Tax exemptions are strictly construed and are never presumed.[7] They must be clearly and categorically expressed and cannot be established by implications.[8] The reason for this is explained in Associate Justice Isagani Cruz's Dissenting Opinion in *Maceda v. Macaraig*[9]:

A tax exemption represents a loss of revenue to the State and must therefore not be lightly granted or inferred. When claimed, it must be strictly construed against the taxpayer, who must prove that he comes under the exemption rather than [the] rule that every one [sic] must contribute his just share in the maintenance of the government. If granted, tax exemption is strictly construed against the taxpayer.[10]

Section 6.3 of the Service Contract, which states that "The OFFICE OF ENERGY AFFAIRS shall assume and pay on behalf of CONTRACTOR and its parent company, on the first transaction in each instance where the tax is

imposed, all income taxes payable to the Republic of the Philippines based on income and profits . . ."[11] is not supported by law, particularly Section 18(b) of Presidential Decree No. 87.

It is tantamount to an income tax exemption and goes against the specific provisions under Presidential Decree No. 87, which allows exemption by the contractor from all taxes except income tax:

SEC. 12. Privileges of contractor. — The provisions of any law to the contrary notwithstanding, a contract executed under this Act may provide that the Contractor shall have the following privileges:

(a) Exemption from all taxes except income tax.

. . . .

SEC. 19. Imposition of tax.—The Contractor shall be liable each taxable year for Philippine income tax on income derived from its petroleum operations under its contract of service, computed as provided in Section 20, through 25.

Moreover, Section 6.3 of the Service Contract constitutes a usurpation of Congress' exclusive prerogative to grant a tax exemption. Article VI, Sec. 28 (4) of the 1987 Constitution particularly requires that "no law granting any tax exemption shall be passed without the concurrence of a majority vote of all the members of Congress."

Indeed, tax assumption may enable the foreign contractors to claim tax credit from their home jurisdiction.[12] In this sense, tax assumption is different from tax exemption. Nonetheless, from our standpoint, tax assumption ultimately has the effect of tax exemption:[13] it frees the taxpayer from the burden or charge of paying the tax.

In *Collector of Internal Revenue v. McGrath*,[14] it was declared that "[t]axes are not subject to agreements between the taxpayer and the tax officer, and if any such agreements are made, they cannot serve to defeat or discharge the liability that the law fixes as the full amount of the tax."

In the same vein, tax exemptions are granted by law and are not subject to contract between the Department of Energy, representing the government, and the foreign contractors. To repeat, Presidential Decree No. 87 explicitly provides the liability of the contractor for income tax, and there is nothing in the said law that clearly allows the shifting of this burden to the government.

III

The arbitral award in an investor-state arbitration done abroad cannot stay or overturn the prior finding of the Commission on Audit (COA)—an independent constitutional body tasked to safeguard public funds and properties.[15]

Under Section 2, Article IX-D of the 1987 Constitution, the COA is vested with the following:

[T]he power, authority, and duty to examine, audit, and settle all accounts pertaining to the revenue and receipts of, and expenditures or uses of funds and property, owned or held in trust by, or pertaining to, the Government, or any of its subdivisions, agencies, or instrumentalities, including government-owned or controlled corporations with original charters[.]

Consequently, Section 28 of Presidential Decree No. 1445[16] describes the examining authority of the COA:

SECTION 28. Examining Authority. — The Commission shall have authority to examine books, papers, and documents filed by individuals and corporations with, and which are in the custody of, government offices in connection with government revenue collection operations, for the sole purpose of ascertaining that all funds determined by the appropriate agencies as collectible and due the government have actually been collected, except as otherwise provided in the Internal Revenue Code of 1977.

The audit jurisdiction of the COA is extensive, covering all funds and properties of the government, its agencies and instrumentalities.[17] Further, Section 3, Article IX-D of the 1987 Constitution categorically provides that "[n]o law shall be passed exempting any entity of the Government or its subsidiary in any guise whatever, or any investment of public funds, from the jurisdiction of the COA." In *Feliciano v. Commission on Audit*,[18] the Court held that the said provision prohibits any scheme or device to escape the audit jurisdiction of the COA.

Nevertheless, while jurisprudence recognizes that the COA had primary jurisdiction over money claims against the government, such jurisdiction is not exclusive. In *Taisei Shimizu Joint Venture v. Commission on Audit*,[19] this Court held that "[o]ther tribunals/adjudicative bodies, too, may have concurrent jurisdiction with the COA over money claims against the government or in the audit of the funds of government agencies and instrumentalities." [20]

In *Development Bank of the Phils. v. Commission on Audit*,[21] the Court held that the COA does not have the sole and exclusive power to examine and audit government banks; this power is shared with the Central Bank. Nonetheless, the Court still recognized the primacy of the government audit conducted by the COA:

[D]espite the Central Bank's concurrent jurisdiction over government banks, the COA's audit still prevails over that of the Central Bank since the COA is the constitutionally mandated auditor of government banks. And in matters falling under the second paragraph of Section 2, Article IX-D of the Constitution, the COA's jurisdiction is exclusive. Thus, the Central Bank is devoid of authority to allow or disallow expenditures of government banks since this function belongs exclusively to the COA.[22]

In *Taisei Shimizu Joint Venture*, the Court held that the COA's primary jurisdiction over money claims against the government does not prevent the Construction Industry Arbitration Commission's exercise of jurisdiction:

Considering that TSJV and DOTr had voluntarily invoked CIAC's jurisdiction, the power to hear and decide the present case has thereby been solely vested in the CIAC to the exclusion of COA. Being a specific law, EO No. 1008 providing for CIAC's exclusive jurisdiction prevails over PD 1445, granting the COA the general jurisdiction over money claims due from or owing to the government. For this reason alone, the COA should have stayed its hands from modifying the CIAC's final arbitral award here, let alone from claiming exclusive jurisdiction over the case.[23]

The Court also clarified that the COA's review power over claims for judgment awards is limited. Due to the principle of immutability of judgments, the COA could no longer reverse or modify the final and executory arbitral award rendered by the Construction Industry Arbitration Commission and "should have restricted itself to determining the source of public funds from which the final and executory arbitral award may be satisfied pursuant to the general auditing laws the COA is tasked to implement." [24]

Notably, in *Taisei Shimizu Joint Venture*, the dispute was first brought to the Construction Industry Arbitration Commission, which had original and exclusive jurisdiction over construction disputes under the law.

Here, the COA first acquired jurisdiction over the subject matter through the conduct of post-audit proceedings. As a necessary part of its constitutional mandate to examine and audit government entities, the COA had the power and duty to rule on questions of law,[25] such as whether the corporate income taxes of the contractors were included in the government's share. Arbitration proceedings subsequently conducted abroad cannot interfere with the COA's exercise of its mandated powers and duties.

However, the COA's ruling on the question may be subject to judicial review. The Constitution prescribes the remedy of certiorari to this Court, from decisions and resolutions of the COA,[26] for the limited purpose of determining whether there has been a grave abuse of discretion amounting to lack or excess of jurisdiction.

To be sure, this Court's review power may be invoked only by filing a petition for certiorari within the 30-day reglementary period and in the manner provided by relevant laws and the Rules of Court.[27] If the proper remedy is not availed of and the ruling becomes final, execution will issue as a matter of right.[28]

This Court generally sustains the COA's rulings, cognizant of its audit power as a check and balance mechanism under the Constitution and its expertise on the subject matter. However, should there be any taint of grave abuse of discretion, this Court may intervene to correct them. *Delos Santos v. Commission on Audit*[29] instructs:

At the outset, it must be emphasized that the CoA is endowed with enough latitude to determine, prevent, and disallow irregular, unnecessary, excessive, extravagant or unconscionable expenditures of government funds. It is tasked to be vigilant and conscientious in safeguarding the proper use of the government's, and ultimately the people's property. The exercise of its general audit power is among the constitutional mechanisms that gives life to the check and balance system inherent in our form of government.

Corollary thereto, it is the general policy of the Court to sustain the decisions of administrative authorities, especially one which is constitutionally-created, such as the CoA, not only on the basis of the doctrine of separation of powers but also for their presumed expertise in the laws they are entrusted to enforce. Findings of administrative agencies are accorded not only respect but also finality when the decision and order are not tainted with unfairness or arbitrariness that would amount to grave abuse of discretion. It is only when the CoA has acted without or in excess of jurisdiction, or with grave abuse of discretion amounting to lack or excess of jurisdiction, that this Court entertains a petition questioning its rulings[.][30] (Citation omitted)

Therefore, government officials and agencies are bound by the findings and conclusions of the COA, unless such findings and conclusions are modified or reversed by the Court.

The foreign arbitral tribunal's ruling upholding Sec. 6.3 of the Service Contract on the assumption by the Department of Energy of the contractors' income tax violates the Constitution; hence, it is not binding upon us. Moreover, it undermines the COA's exercise of its mandated powers, duties, and functions and by-passes the prescribed mode of review of the COA's decisions.

ACCORDINGLY, I vote to DISMISS the Petition.

[1] Presidential Decree No. 87 (1972), The Oil Exploration and Development Act of 1972.

[2] On March 22, 1976, the Petroleum Board was abolished and its powers and functions under Presidential Decree No. 87 were transferred to the Energy Development Board created under Presidential Decree No. 910. A year later or on October 6, 1977, by virtue of Presidential Decree No. 1206, the Energy Development Board was abolished and said powers and functions were transferred to the Bureau of Energy Development of the Department of Energy. In June 8, 1978, Presidential Decree No. 1459 authorized the Secretary of Energy, upon the approval of the President, to enter into or renegotiate service contracts, subject to the following conditions:

- (a) The share of the Government, including all taxes, shall not be less than sixty per cent of the difference between the gross income and the sum of operating expenses and such allowances as the Secretary of Energy may deem proper to grant;
- (b) The service contractor must be technically competent and financially capable to undertake the petroleum operations required in the contract; and
- (c) The Secretary of Finance shall be consulted on all matters involving revenue.

[3] Presidential Decree No. 87 (1972), sec. 12 provides:

SEC. 12. Privileges of contractor. — The provisions of any law to the contrary notwithstanding, a contract

executed under this Act may provide that the Contractor shall have the following privileges:

- (a) Exemption from all taxes except income tax.
- (b) Exemption from payment of tariff duties and compensating tax on the importation of machinery and equipment, and spare parts and all materials required for petroleum operations subject to the conditions that said machinery, equipment, spare parts and materials of comparable price and quality are not manufactured domestically; and directly and actually needed and will be used exclusively by the Contractor in its operations or in operations for it by a subcontractor are covered by shipping documents in the name of the Contractor to whom the shipment will be delivered direct by the customs authorities; and prior approval of the Petroleum Board was obtained by the Contractor before the importation of such machinery, equipment, spare parts and materials which approval shall not be unreasonably withheld: Provided, however, That the Contractor or its subcontractor may not sell, transfer or dispose of these machinery, equipment, spare parts and materials without the prior approval of the Petroleum Board and payment of taxes due the Government: Provided, further, That should the Contractor or its subcontractor sell, transfer or dispose of these machinery equipment, spare parts or materials without the prior consent of the Petroleum Board, it shall pay twice the amount of the tax exemption granted: Provided, finally, That the Petroleum Board shall allow and approve the sale, transfer, or disposition of the said items without tax if made (1) to another contractor; (2) for reasons of technical obsolescence; or (3) for purposes of replacement to improve and/or expand the operations of the contract;
- (c) Exemption upon approval by the Petroleum Board from laws, regulations and/or ordinances restricting the (1) construction, installation, and operation of power plant for the exclusive use of the Contractor if no local enterprise can supply within a reasonable period and at reasonable cost the power needed by the Contractor in its petroleum operations, (2) exportation of machinery and equipment which were imported solely for its petroleum operation when no longer needed therefor;
- (d) Exemption from publication requirements under Republic Act Numbered Five thousand four hundred fifty-five; and the provisions of Republic Act Numbered Sixty-one hundred and seventy-three with respect to the exploration, production, exportation or sale or disposition of crude oil discovered and produced in the Philippines;
- (e) Exportation of petroleum subject to the prior filing pro-rata of domestic needs as elsewhere provided in this Act;
- (f) Entry, upon the sole approval of the Petroleum Board which shall not be unreasonably withheld, of alien technical and specialized personnel (including the immediate members of their families), who may exercise their professions solely for the operations of the contractor as prescribed in its contract with the Government under this Act: Provided, That if the employment or connection of any such alien with contractor ceases, the applicable laws and regulations on immigration shall apply to him and his immediate family: Provided, further, That Filipinos shall be given preference to positions for which they have adequate training: And provided, finally, That the Contractor shall adopt and implement a training program for Filipinos along technical or specialized lines, which program shall be reported to the Petroleum Board;
- (g) Rights and obligations in any contract concluded pursuant to this Act shall be deemed as essential considerations for the conclusion thereof and shall not be unilaterally changed or impaired; and
- (h) The privileges and benefits granted to a contractor under the provisions of this Act together with any applicable obligations shall likewise be made available to concessionaires under the Petroleum Act of 1949 and their authorized contractors and/or service operators, whether local or foreign, if they so elect.

[4] 635 Phil. 447 (2010) [Per J. Perez, En Banc].

[5] Id. at 454.

[6] *Maynilad Water Services, Inc. v. National Water and Resources Board*, G.R. Nos. 181764, 187380, 207444, etc., December 7, 2021 [Per J. Leonen, En Banc].

[7] *Luzon Stevedoring Corp. v. Court of Tax Appeals*, 246 Phil. 666 (1988) [Per J. Paras, Second Division];

Province of Abra v. Hernando, 194 Phil. 97 (1981) [Per C.J. Fernando, Second Division].

[8] PLDT v. City of Davao, 447 Phil. 571 (2003) [Per J. Mendoza, En Banc]; Wonder Mechanical Engineering Corp. v. Court of Tax Appeals, 159-A Phil. 808 (1975) [Per J. Esguerra, First Division]; E. Rodriguez, Inc. v. Collector of Internal Revenue, G.R. No. L-23041, 139 Phil. 354 (1969) [Per Barredo, En Banc].

[9] 274 Phil. 1060 (1991) [Per J. Gancayco, En Banc].

[10] J. Cruz's Dissenting Opinion in Maceda v. Macaraig, Jr., etc., et al., 274 Phil. 1060, 1117 (1991) [Per J. Gancayco, En Banc].

[11] Ponente, p. 4. (Citations omitted)

[12] Id. at 9-10.

[13] However, in Mitsubishi Corp.-Manila Branch v. Commissioner of Internal Revenue, 810 Phil. 16-30 (2017) [Per J. Perlas-Bernabe, First Division], the Court held that tax assumption is different from tax exemption and the constitutional provisions on tax exemptions would not apply.

[14] 111 Phil. 222 (1961) [Per J. Labrador, En Banc]. In this case, the taxpayer claimed exemption from liability for the remaining amount due under the law on the ground of the earlier acceptance by the tax officer of her payment, which allegedly constituted a "full settlement of the estate tax."

[15] Star Special Corporate Security Management, Inc. v. Commission on Audit, G.R. No. 225366, September 1, 2020 [Per J. Leonen, En Banc].

[16] Presidential Decree No. 1445 (1978), Government Auditing Code of the Philippines.

[17] Star Special Corporate Security Management, Inc. v. Commission on Audit, G.R. No. 225366, September 1, 2020 [Per J. Leonen, En Banc].

[18] 464 Phil. 439 (2004) [Per J. Carpio, En Banc].

[19] 873 Phil. 323 (2020) [Per J. Lazaro-Javier, En Banc].

[20] Id. at 342.

[21] 424 Phil. 411 (2002) [Per J. Carpio, En Banc].

[22] Id. at 433-434.

[23] Id. at 344.

[24] Id. at 355.

[25] See Oriondo v. Commission on Audit, G.R. No. 211293, June 4, 2019 [Per J. Leonen, En Banc].

[26] CONST. (1987), art. IX-A, sec. 7 states that "[u]nless otherwise provided by this Constitution or by law, any decision, order, or ruling of each Commission may be brought to the Supreme Court on certiorari by the aggrieved party[.]"

[27] Oriondo v. Commission on Audit, G.R. No. 211293, June 4, 2019 [Per J. Leonen, En Banc].

[28] J. Leonen's Separate Opinion in Bangko Sentral ng Pilipinas v. Commission on Audit, G.R. No. 210314, October 12, 2021 [Per J. Hernando, En Banc].

[29] 716 Phil. 322 (2013) [Per J. Perlas-Bernabe, En Banc].

[30] Id. at 332-333.

CONCURRING OPINION

CAGUIOA, J.:

The crux of the controversy stems from the alleged under collection of the government's 60% share in the Malampaya Natural Gas Project revenues amounting to PHP 53,140,304,739.86 from 2002 to 2009.

I concur with the ruling to grant the consolidated Petitions for Certiorari, reverse the Commission on Audit (COA) Decision No. 2015-115 dated April 6, 2015 (assailed Decision) and Decision No. 2018-075 dated January 24, 2018 (assailed Resolution), and lift the Notice of Charge No. 2010-01-151(09).

I write separately to emphasize that the tax assumption provision under Service Contract No. 38 is firmly rooted in the clear language of Presidential Decree No. 87,[1] otherwise known as the Oil Exploration and Development Act of 1972. The tax assumption mechanism is not only lawful but is also a cornerstone of the incentives designed to encourage private participation in the exploration and production of the nation's petroleum resources.

Brief review of the facts

To recall, the Government of the Republic of the Philippines, through the Department of Energy (DOE), entered into Service Contract No. 38 dated December 11, 1990 with Shell Philippines Exploration B.V. and Occidental Philippines, the predecessors-in-interest of Shell Exploration B.V. (SPEX), PNOC Exploration Corporation (PNOC-EC), and Chevron Malampaya LLC (collectively, the contractors). Service Contract No. 38 was entered into pursuant to the provisions of Presidential Decree No. 87.

Under Service Contract No. 38, the contractors shall perform all petroleum operations and provide all necessary technology and finance, as well as the required services in connection therewith.[2] Moreover, under the terms of Service Contract No. 38, 60% of the net proceeds of the operation shall be remitted to the government,[3] while the contractors shall retain 40% as a service fee.[4] Part of the incentives extended to the contractors under Presidential Decree No. 87 is exemption from all other taxes except income tax, which was to be paid by the DOE on behalf of the contractors.[5] This exemption is also granted to the contractors under Section 6.2 (a) of Service Contract No. 38.

A 2004 post-audit revealed that the contractors' corporate income taxes had been deducted from the government's 60% share of net proceeds, resulting in an understatement of government revenue by PHP 53,140,304,739.86 from 2002 to December 2009. This led to the issuance of Notice of Charge No. 2010-01-151(09), holding petitioners Thelma M. Cerdeña and Nora A. Tuazon, both from the Financial Services of the DOE, along with the contractors, liable.[6]

The DOE and the contractors appealed, but COA National Government Sector Cluster B denied their appeal. The parties then filed Petitions for Review before COA Proper, asserting that under Section 6.3 of Service Contract No. 38, the government had assumed responsibility for the contractors' income tax obligations.[7]

In its assailed Decision and Resolution, COA denied the petitions and declared that the inclusion of the contractors' income taxes in the government's 60% share was improper and unsupported by law, prompting the filing of Petitions for Certiorari before the Court.[8]

In the interim, related disputes were brought to international arbitration. The International Centre for Settlement of Investment Disputes (ICSID) tribunal, in Case No. ARB/16/22, issued provisional measures enjoining the

enforcement of the Notices of Charge during the proceedings, while the International Chamber of Commerce (ICC) Arbitral Tribunal upheld the validity of the tax assumption mechanism in Service Contract No. 38 in its Final Award issued in 2019.[9]

Before the Court, COA has steadfastly maintained its position, emphasizing that no specific provision of law explicitly authorizes the inclusion of the contractors' income taxes within the government's 60% share.

In ruling in favor of petitioners, the ponencia holds that both the text of Presidential Decree No. 87 and its legislative intent leave no doubt that the contractors remain liable for income tax, but such taxes are assumed by the government and included in its 60% share. The ponencia likewise applies the case of *Republic v. City of Kidapawan*,[10] where the Court upheld a tax assumption mechanism in a geothermal service contract between the government and PNOC-EDC, ruling that while the government assumed and paid PNOC-EDC's income taxes, these payments were charged against the government's 60% share of net proceeds. The Court emphasized that PNOC-EDC remained the actual taxpayer, with the government acting merely as its agent in the payment of income taxes, as evidenced by the issuance of official receipts in PNOC-EDC's name.[11]

As stated at the outset, I fully concur.

COA committed grave abuse of discretion in issuing the assailed Decision and Resolution, as the contractors' income taxes are included as part of the government's 60% share; tax assumption mechanism

COA as a constitutional office and guardian of public funds is endowed with the exclusive authority to determine and account government revenue and expenditures, and disallow irregular, unnecessary excessive use of government funds.[12] The case of *Metropolitan Waterworks and Sewerage System v. COA*[13] elucidated on this matter:

[COA as a constitutional office] is endowed with enough latitude to determine, prevent and disallow irregular, unnecessary, excessive, extravagant, or unconscionable expenditures of government funds. It has the power to ascertain whether public funds were utilized for the purpose for which they had been intended. The 1987 Constitution has expressly made COA the guardian of public funds, vesting it with broad powers over all accounts pertaining to government revenue and expenditures and the uses of public funds and property, including the exclusive authority to define the scope of its audit and examination, establish the techniques and methods for such review, and promulgate accounting and auditing rules and regulations.[14] (Emphasis supplied, citations omitted)

However, under Article IX-A, Section 7 of the 1987 Constitution, a decision, order, or ruling of COA may be brought to the Court on certiorari:

. . . Unless otherwise provided by this Constitution or by law, any decision, order, or ruling of each Commission may be brought to the Supreme Court on certiorari by the aggrieved party within thirty days from receipt of a copy thereof.[15]

The Constitution limits the permissible scope of inquiry over judgments or resolutions of COA only to errors of jurisdiction or those rendered with grave abuse of discretion.[16] The Court explained this in *Veloso v. COA*: [17]

It is the general policy of the Court to sustain the decisions of administrative authorities, especially one which is constitutionally-created not only on the basis of the doctrine of separation of powers but also for their presumed expertise in the laws they are entrusted to enforce. Findings of administrative agencies are accorded not only respect but also finality when the decision and order are not tainted with unfairness or arbitrariness that would amount to grave abuse of discretion. It is only when the COA has acted without or in excess of jurisdiction, or with grave abuse of discretion amounting to lack or excess of jurisdiction, that this Court entertains a petition questioning its rulings. There is grave abuse of discretion when there is an evasion of a

positive duty or a virtual refusal to perform a duty enjoined by law or to act in contemplation of law as when the judgment rendered is not based on law and evidence but on caprice, whim and despotism.[18] (Emphasis supplied, citations omitted)

The present consolidated cases challenge COA's ruling, which held that the income taxes of the contractors should not have been part of the 60% government share and demanded that the contractors settle back taxes under Service Contract No. 38. In deciding the present consolidated cases, the Court is thus tasked to determine whether COA's ruling was tainted with grave abuse of discretion. This review entails interpreting the provisions of Presidential Decree No. 87, Presidential Decree No. 1206, and Presidential Decree No. 1459 in relation to Service Contract No. 38 and determining whether COA's ruling disregarded their explicit terms. As explained below, I agree with the ponencia that COA committed grave abuse of discretion in issuing the assailed Decision and Resolution and in affirming the Notice of Charge No. 2010-01-151(09).

Presidential Decree No. 87 was enacted to encourage private participation in the exploration and development of petroleum resources in the Philippines. Its overarching policy objective is to "hasten the discovery and production of indigenous petroleum through the utilization of government and/or private resources, local and foreign".[19] To achieve this, Presidential Decree No. 87 provided "more meaningful incentives to prospective service contractors." [20]

Among these incentives is an exemption from all taxes except income tax:

Section 12. Privileges of contractor. — The provisions of any law to the contrary notwithstanding, a contract executed under this Act may provide that the contractor shall have the following privileges:

(a) Exemption from all taxes except income tax.[21] (Emphasis supplied)

Complementing the tax exemption privilege is the tax assumption mechanism and the government's guaranteed share of petroleum revenues under Section 18(6) of Presidential Decree No. 87:

Section 18. Functions of Petroleum Board. — In accordance with the provisions and objectives of this Act, the Petroleum Board shall:

....

(b)

Enter into contracts herein authorized with such terms and conditions as may be appropriate under the circumstances including the grant of special allowance: Provided, however, That no depletion allowance shall be granted: Provided, further, That except as provided in Sections twenty-six and twenty-seven hereof, no contract in favor of one contractor and its affiliates shall cover less than fifty thousand nor more than seven hundred and fifty thousand hectares for on-shore areas, or less than eighty thousand nor more than one million five hundred thousand hectares for off-shore areas: Provided, finally, That in no case shall the annual net revenue or share of the Government, including all taxes paid by or on behalf of the Contractor, be less than sixty percent of the difference between the gross income and the sum of operating expenses and Filipino participation incentive[.] [22] (Emphasis supplied)

The inclusion of taxes in the government's share is reinforced by subsequent legislation. Presidential Decree No. 1206,[23] which created the DOE, reiterates the government's guaranteed share in petroleum revenues in Section 12(a)(i)(2) as "including all taxes paid by or on behalf of the contractor," thus:

Section 12. Transferred Powers and Functions. — The following powers and functions are transferred as hereafter indicated to the extent that they are not modified by any specific provision of this Decree:

a.

With reference to Section 11(a) above, the powers and functions transferred to the Bureau of Energy Development are:

i.

The following powers and functions of the abolished Energy Development Board under Presidential Decree No. 87: Provided, That service contracts authorized under the said Decree, including the transfer or assignment of interest in said service contracts, shall require the approval of the Secretary:

....

2.

Enter into contracts herein authorized with such terms and conditions as may be appropriate under the circumstances: Provided, however, That no depletion allowance shall be granted: Provided, further, That except as provided in Section 26 and 27 in favor of Presidential Decree No. 87, no contract in favor of one contractor and its affiliates shall cover less than fifty thousand hectares nor more than seven hundred and fifty thousand hectares for on-shore areas, or less than eighty thousand nor more than one million five hundred thousand hectares for off-shore areas: And, Provided, finally, That in no case shall the annual net revenue or share of the government, including all taxes paid by or on behalf of the contractor, be less than sixty percent of the difference between the gross income and the sum of operating expenses and Filipino participation incentive[.][24] (Emphasis supplied)

Similarly, Presidential Decree No. 1459,[25] which authorized the DOE to enter and conclude service contracts, reaffirms the government's minimum share in Section 1(a):

Section 1. Any provision of law to the contrary notwithstanding, the Secretary of Energy is hereby authorized to enter into petroleum service contracts, or re-negotiate and modify existing ones, upon the approval of the President of the Philippines, subject to the following conditions:

(a)

The share of the Government, including all taxes, shall not be less than sixty per cent of the difference between the gross income and the sum of operating expenses and such allowances as the Secretary of Energy may deem proper to grant[.][26] (Emphasis supplied)

The above-mentioned provisions create a consistent legislative framework that guarantees the government its 60% share of the net proceeds from petroleum operations. The unequivocal language of these provisions underscores two key principles. First, the income taxes paid by or on behalf of the contractors are explicitly included in the government's guaranteed 60% share of the net proceeds from petroleum operations. Second, the government assumes and pays the contractors' income tax liabilities. This tax assumption mechanism, recognized in Presidential Decree No. 87, Presidential Decree No. 1206, and Presidential Decree No. 1459, is an integral part of the fiscal structure under Service Contract No. 38.

Service Contract No. 38 incorporates the fiscal terms set forth in Presidential Decree No. 87 and subsequent

decrees. Section 6.3 of Service Contract No. 38 reads:

6.3 The OFFICE OF ENERGY AFFAIRS shall assume and pay on behalf of CONTRACTOR and its parent company, on the first transaction in each instance where the tax is imposed, all income taxes payable to the Republic of the Philippines based on income and profits and, with respect to CONTRACTOR, on the first transaction in each instance where the tax is imposed, all dividends, withholding taxes and other taxes imposed by the Government of the Philippines on the distribution of income and profits derived from Petroleum Operations to its parent company. The OFFICE OF ENERGY AFFAIRS shall promptly furnish to CONTRACTOR, without fee or other consideration, the official receipts issued in the name of CONTRACTOR by any duly empowered Government authority, acknowledging the payment of said taxes.[27] (Emphasis supplied)

The contractors' incentives or privileges under Presidential Decree No. 87, as also stated in Service Contract No. 38, include, among others, service fee of up to 40% of net production, exemption from all taxes except income tax, and income tax obligation paid out of government's share. Service Contract No. 38 stipulates the following:

1.

A 60-40 production sharing scheme for the petroleum operations, where the government shall receive 60% of the net proceeds, while the contractors shall receive 40%;[28]

2.

the contractors are exempt from all taxes except income tax;[29] and

3.

the government, through the DOE, assumes and pays the contractors' income taxes.[30]

COA, however, contends that Presidential Decree No. 87 and Presidential Decree No. 1459 do not contain any clear and express provision stating that the contractors' income taxes are part of the government's share but, instead, explicitly provide that the contractors are subject to income tax.[31]

Indeed, it is not disputed that the contractors are subject to income taxes. The relevant tax provisions of Presidential Decree No. 87 state unequivocally that the contractors are liable for income taxes arising from their petroleum operations. Sections 12(a) and 19 of Presidential Decree No. 87 read:

Section 12. Privileges of contractor. The provisions of any law to the contrary notwithstanding, a contract executed under this Act may provide that the contractor shall have the following privileges:

(a) Exemption from all taxes except income tax.

....

Section 19. Imposition of tax. — The Contractor shall be liable each taxable year for Philippine income tax on income derived from its petroleum operations under its contract of service, computed as provided in Section 20, through 25.[32] (Emphasis supplied)

Additionally, Section 24 of Presidential Decree No. 87 emphasizes that every party to a service contract is separately taxed on its share of taxable income:

Section 24. Return and payment of tax. — Every party to a service contract shall render to the Petroleum Board

a return for each taxable year in duplicate in such form and manner as provided by law setting forth its gross income and the deductions herein allowed. The return shall be filed by the Petroleum Board with the Commissioner of Internal Revenue or his [or her] deputies or other persons authorized by him [or her] to receive such return within the period specified in the National Internal Revenue Code and the Rules and Regulations promulgated thereunder. Every party to a service contract shall be subject to tax separately on its share of taxable income arising from such contract.[33] (Emphasis supplied)

COA's primary mistake is interpreting Section 12(a) of Presidential Decree No. 87, which states that the contractors are exempt from all taxes except income tax, in isolation. COA incorrectly concludes that this means the contractors must personally bear their income tax liabilities. However, this narrow interpretation disregards Section 18(b) of Presidential Decree No. 87, which states that the government's share includes all taxes paid by or on behalf of the contractors. A holistic reading of these provisions reveals the correct interpretation: the contractors remain legally liable for income tax, but once the government assumes and pays these taxes on their behalf, they are counted as part of the government's 60% share. If the contractor were entirely exempt from income tax, there would be no tax left for the government to pay on its behalf or to include as part of its share. COA's interpretation renders the phrase "including all taxes paid by or on behalf of the contractor" in Section 18(b) of Presidential Decree No. 87 meaningless and superfluous. Its narrow reading of Presidential Decree No. 87 is fundamentally flawed as it disregards the law in its entirety and isolates certain provisions without regard to the broader fiscal structure. It is a fundamental rule in statutory construction that the clauses; phrases, sections and provisions of a law be read as a whole; never as disjointed or truncated parts, for a law is enacted as a single entity and not by installment of paragraphs here and subsections there.[34]

Tax assumption arrangements like that in the case at bar are not novel. In *Mitsubishi Corp.-Manila Branch v. CIR*[35] (*Mitsubishi*), the Court explained that these arrangements allow the tax liability generally imposed on the statutory taxpayer to be passed on to a different person, such as the Philippine government or its implementing agency. This was a concession to Japanese suppliers, contractors, or consultants in consideration of the loan extended to the Philippine government. The tax assumption provision under the Exchange of Notes in *Mitsubishi* provides:

Paragraph 5 (2) of the Exchange of Notes provides for a tax assumption provision whereby:

(2)

The Government of the Republic of the Philippines will, itself or through its executing agencies or instrumentalities, assume all fiscal levies or taxes imposed in the Republic of the Philippines on Japanese firms and nationals operating as suppliers, contractors or consultants on and/or in connection with any income that may accrue from the supply of products of Japan and services of Japanese nationals to be provided under the Loan.[36] (Emphasis in the original)

The Court then distinguished tax assumption from tax exemption in this wise:

To "assume" means "[t]o take on, become bound as another is bound, or put oneself in place of another as to an obligation or liability." This means that the obligation or liability remains, although the same is merely passed on to a different person. In this light, the concept of an assumption is therefore different from an exemption, the latter being the "[f]reedom from a duty, liability or other requirement" or "[a] privilege given to a judgment debtor by law, allowing the debtor to retain [a] certain property without liability." Thus, contrary to the CTA En Banc's opinion, the constitutional provisions on tax exemptions would not apply.[37] (Emphasis supplied, citations omitted)

In *Mitsubishi*, the Court decided that in line with the tax assumption provision under the Exchange of Notes, it is the Philippine Government, through its executing agency, which shall pay any form of taxes that are directly

imposable under the Contract:

As explicitly worded, the Philippine Government, through its executing agencies (i.e., NPC in this case) particularly assumed "all fiscal levies or taxes imposed in the Republic of the Philippines on Japanese firms and nationals operating as suppliers, contractors or consultants on and/or in connection with any income that may accrue from the supply of products of Japan and services of Japanese nationals to be provided under the [OECF] Loan." The Philippine Government's assumption of "all fiscal levies and taxes," which includes the subject taxes, is clearly a form of concession given to Japanese suppliers, contractors or consultants in consideration of the OECF Loan, which proceeds were used for the implementation of the Project. As part of this, NPC entered into the June 21, 1991 Contract with Mitsubishi Corporation (i.e., petitioner's head office in Japan) for the engineering, supply, construction, installation, testing, and commissioning of a steam generator, auxiliaries, and associated civil works for the Project, which foreign currency portion was funded by the OECF loans. Thus, in line with the tax assumption provision under the Exchange of Notes, Article VIII (B) (1) of the Contract states that NPC shall pay any and all forms of taxes that are directly imposable under the Contract:

Article VIII (B) (1)

B. FOR ONSHORE PORTION.

1.) [The] CORPORATION (NPC) shall, subject to the provisions under the Contract [Document] on Taxes, pay any and all forms of taxes which are directly imposable under the Contract including VAT, that may be imposed by the Philippine Government, or any of its agencies and political subdivisions...

This notwithstanding, petitioner included in its income tax due the amount of [PHP 44,288,712.00], representing income from the OECF-funded portion of the Project, and further remitted [PHP 8,324,100.00] as BPRT for branch profits remitted to its head office in Japan out of its income for the fiscal year that ended on March 31, 1998. These taxes clearly fall within the ambit of the tax assumption provision under the Exchange of Notes, which was further fleshed out in the Contract. Hence, it is the Philippine Government, through the NPC, which should shoulder the payment of the same.[38] (Emphasis supplied, citations omitted)

Thus, the Court in Mitsubishi recognized that the collection of taxes from entities otherwise enjoying the benefits of a tax assumption arrangement is erroneous and, thus, refundable:

Therefore, considering that petitioner paid the subject taxes in the aggregate amount of [PHP 52,612,812.00], which it was not required to pay, the BIR erroneously collected such amount. Accordingly, petitioner is entitled to its refund.[39]

Similarly, under Service Contract No. 38, the contractors remain liable for income taxes, but the Philippine government assumes and pays these taxes as part of its share of net proceeds. The language of Section 6.3 of Service Contract No. 38 closely mirrors the tax assumption provision upheld in the Exchange of Notes in Mitsubishi. To restate, Section 6.3 of Service Contract No. 38 reads:

6.3 The OFFICE OF ENERGY AFFAIRS shall assume and pay on behalf of CONTRACTOR and its parent company, on the first transaction in each instance where the tax is imposed, all income taxes payable to the Republic of the Philippines based on income and profits and, with respect to CONTRACTOR, on the first transaction in each instance where the tax is imposed, all dividends, withholding taxes and other taxes imposed by the Government of the Philippines on the distribution of income and profits derived from Petroleum Operations to its parent company. The OFFICE OF ENERGY AFFAIRS shall promptly furnish to CONTRACTOR, without fee or other consideration, the official receipts issued in the name of CONTRACTOR by any duly empowered Government authority, acknowledging the payment of said taxes.[40] (Emphasis supplied)

Both Section 6.3 of Service Contract No. 38 and paragraph 5(2) of the Exchange of Notes in Mitsubishi use the

term "assume". The tax assumption mechanism under Section 6.3 of Service Contract No. 38 is entirely consistent with the ruling in *Mitsubishi*, where the government assumed tax obligations without granting any tax exemption.

However, COA argues that the tax assumption mechanism violates the government's 60% share of the net proceeds and effectively increases the contractors' share beyond the 40% limit. For COA, when the government pays the contractors' income taxes, the money representing tax payment is effectively added to the share of the contractors, and the effect is that the contractors are receiving more than their maximum 40% share.^[41] Consequently, the tax assumption clause in Service Contract No. 38 resulted in the contractors being effectively exempt from income tax.^[42]

COA's contention that income taxes included in the government's share constitute a tax exemption misunderstands the distinction between tax exemption and tax assumption. The essence of a tax exemption is the immunity or freedom from a charge or burden to which others are subjected. It is a waiver of the government's right to collect the amounts that would have been collectible under our tax laws. Thus, when the law speaks of a tax exemption, it should be understood as freedom from the imposition and payment of a particular tax.^[43] Tax exemption requires congressional concurrence under Article VI, Section 28(4) of the 1987 Constitution. In contrast, tax assumption does not absolve the taxpayer of liability but merely shifts the responsibility for payment to another entity, in this case, the government.

Based on this premise, the mechanism under Service Contract No. 38 does not meet the criteria of a tax exemption, considering that the contractors are not immune from tax liability. The mechanism allows the government to assume and pay the contractors' income taxes on their behalf while ensuring that these payments form part of its 60% minimum share. As long as the sum of the government's net share and the contractors' income tax liabilities amounts to at least 60% of the net proceeds, the fiscal arrangement complies with the explicit provisions of Presidential Decree No. 87. In *Saguisag v. Ochoa*,^[44] the Court also held that tax assumption is not equivalent to tax exemption:

Finally, petitioners allege that EDCA creates a tax exemption, which under the law must originate from Congress. This allegation ignores jurisprudence on the government's assumption of tax liability. EDCA simply states that the taxes on the use of water, electricity, and public utilities are for the account of the Philippine Government. This provision creates a situation in which a contracting party assumes the tax liability of the other. In *National Power Corporation v. Province of Quezon*, we distinguished between enforceable and unenforceable stipulations on the assumption of tax liability. Afterwards, we concluded that an enforceable assumption of tax liability requires the party assuming the liability to have actual interest in the property taxed. This rule applies to EDCA, since the Philippine Government stands to benefit not only from the structures to be built thereon or improved, but also from the joint training with U.S. forces, disaster preparation, and the preferential use of Philippine suppliers. Hence, the provision on the assumption of tax liability does not constitute a tax exemption as petitioners have posited.^[45] (Emphasis supplied, citations omitted)

Essentially, COA seeks to remove income taxes from the computation of the government's share and reclassify these taxes as part of the contractors' share. This position is directly contrary to the explicit provisions of Presidential Decree No. 87, Presidential Decree No. 1206, and Presidential Decree No. 1459, all of which unequivocally state that the government's share includes "all taxes" paid by or on behalf of the contractor. Moreover, the inclusion of taxes as part of the government's 60% share reflects established practices in resource-sharing agreements and has been upheld by the Court in other contexts, such as mining agreements under the Philippine Mining Act of 1995. In *La Bugal-B'laan Tribal Association, Inc. v. Ramos*^[46] (*La Bugal-B'laan*), the Court upheld a similar fiscal arrangement under the Financial or Technical Assistance Agreements (FTAAs). The Court noted that:

The basic government share is comprised of all direct taxes, fees and royalties, as well as other payments made by the contractor during the term of the FTAA. These are amounts paid directly to (i) the national government (through the Bureau of Internal Revenue, Bureau of Customs, Mines & Geosciences Bureau and other national government agencies imposing taxes or fees), (ii) the local government units where the mining activity is conducted, and (iii) persons and communities directly affected by the mining project. The major taxes and other payments constituting the basic government share are enumerated below[.]

....

Apart from the basic share, an additional government share is also collected from the FTAA contractor in accordance with the second paragraph of Section 81 of [Republic Act No.] 7942, which provides that the government share shall be comprised of, among other things, certain taxes, duties and fees. The subject proviso reads:

"The Government share in a financial or technical assistance agreement shall consist of, among other things, the contractor's corporate income tax, excise tax, special allowance, withholding tax due from the contractor's foreign stockholders arising from dividend or interest payments to the said foreign stockholder in case of a foreign national, and all such other taxes, duties and fees as provided for under existing laws." [47] (Emphasis supplied, citation omitted)

Thus, La Bugal-B'laan affirmed that treating taxes as part of the government's share is a recognized and lawful practice in resource-sharing agreements. The arrangement in Presidential Decree No. 87 and Service Contract No. 38 mirrors the fiscal structure in La Bugal-B'laan, where taxes and other fiscal obligations are treated as integral components of the government's share.

By reducing the financial and administrative burdens on the contractors, the fiscal terms become more attractive to investors and encourage their participation in the high-risk and capital-intensive petroleum sector. This intent is further reinforced by the ponencia's ruling, which highlights that Presidential Decree No. 87 was designed to attract foreign investment by adopting a tax assumption system as a key fiscal incentive. The tax assumption mechanism provides stability for foreign contractors and enables them to claim tax credits in their home jurisdictions, unlike a tax exemption.[48]

COA's finding that the government's share was diminished by the contractors' income tax payments arises from its failure to account for the taxes remitted to the Bureau of Internal Revenue (BIR). Again, the government's share, as defined by Presidential Decree No. 87 and related laws, explicitly includes all taxes paid by or on behalf of the contractors. By disregarding the tax payments made to the BIR, COA artificially reduced the computed share of the government, leading to an incorrect conclusion that the contractors' taxes diminished the government's entitlement.

COA also appears to have narrowly interpreted "government" as used in Presidential Decree No. 87,[49] Presidential Decree No. 1206,[50] and Presidential Decree No. 1459[51] as referring solely to the amounts directly remitted to the DOE. This interpretation disregards the broader scope of the term, which necessarily includes payments made to other government entities, such as the BIR, in the form of taxes paid on behalf of the contractors. The fiscal framework established by Presidential Decree No. 87 and implemented under Service Contract No. 38 envisions a unified government share, which comprises both remittances to the DOE and taxes paid to the BIR on behalf of the contractors. In short, the combined proceeds received by both the DOE and the BIR must be recognized as fulfilling the government's 60% entitlement, as explicitly required by Presidential Decree No. 87, Presidential Decree No. 1206, and Presidential Decree No. 1459.

The ICC Arbitral Tribunal's recognition of the Court's jurisdiction

Section XII of Service Contract No. 38 provides for the consultation and arbitration:

....

12.1

Disputes, if any, arising between the OFFICE OF ENERGY AFFAIRS and CONTRACTOR relating to this Contract or the interpretation and performance of any of the clauses of this Contract, and which cannot be settled amicably, shall be settled by arbitration. The OFFICE OF ENERGY AFFAIRS on the one hand and CONTRACTOR on the other hand, shall each appoint one arbitrator within thirty (30) days after receipt of a written request of the other Party to do so, such arbitrator shall, at the request of the other Party, if the parties do not otherwise agree, be appointed by the President of the International Chamber of Commerce. If the first two arbitrators appointed as aforesaid fail to agree on a third within thirty (30) days following the appointment of the second arbitrator, the third arbitrator shall, if the Parties do not otherwise agree, be appointed, at the request of either Party, by the President of the International Chamber of Commerce. If an arbitrator fails or is unable to act, his [or her] successor will be appointed in the same manner as the arbitrator whom he [or she] succeeds. Unless the Parties agree otherwise, the Philippines shall be the venue of the arbitration proceedings. The English language shall be the language used.

12.2

The decision of a majority of the arbitrators shall be final and binding upon the parties. Judgment upon the award rendered may be entered in any court having jurisdiction or application may be made to such court for a judicial acceptance of the award and an order of enforcement, as the case may be.

12.3

Except as provided in this Section, arbitration shall be conducted in accordance with the Rules of Arbitration of the International Chamber of Commerce, then in effect.[52] (Emphasis supplied)

Pursuant to the foregoing arbitration provisions, the ICC Arbitral Tribunal issued a Partial Final Award on April 16, 2019, ruling that the Philippine income taxes paid by or on behalf of the contractors form part of the government's 60% share of the net proceeds from petroleum operations under Service Contract No. 38. The ICC Arbitral Tribunal also held that Section 6.3 of Service Contract No. 38, which provides, inter alia, that the government "shall assume and pay" all the contractors' income taxes, is a valid and enforceable clause. Subsequently, on December 16, 2019, the ICC Arbitral Tribunal issued a Final Award and upheld the validity of the tax assumption mechanism in Service Contract No. 38.

While the Arbitral Tribunal affirmed that the income taxes paid by or on behalf of the contractors form part of the government's 60% share, the ponencia's resolution of the issues in these consolidated cases does not rely on the arbitral award but instead rests on an independent judicial review of COA's assailed Decision and Resolution. Recognizing its own jurisdictional limitations, the Arbitral Tribunal expressly declined to rule on whether COA has correctly exercised its mandate:

... The Tribunal appreciates that the decisions of the COA are only subject to review by the Supreme Court. The Tribunal wishes to [emphasize] that it is not deciding whether the COA has correctly exercised its constitutional mandate and indeed the Claimants have not asked the Tribunal to do so. In this vein, the Claimants' request for relief is illustrative. The Claimants are seeking directions compelling the Respondent to comply with obligations under Service Contract 38. Such a direction is geared toward vindicating alleged

contractual rights, not reviewing the Notices of Charge. The Tribunal is concerned only with Section 6.3 and whether the Respondent has breached that provision. The Tribunal accordingly finds that the Claimants' case does not involve constitutionality issues in this respect.[53]

....

... The Tribunal stresses that in deciding the issue of the validity and enforceability of Section 6.3 of SC 38, it has taken extreme care not to encroach on the jurisdiction of the Philippine Supreme Court as the exclusive arbiter of constitutional issues over cases in its jurisdiction. The Tribunal also stresses that it does not seek to prevent the COA from discharging its audit duty under the 1987 Constitution of the Philippines.[54] (Emphasis supplied, citations omitted)

By these pronouncements, the Arbitral Tribunal itself confirmed that its Partial Final Award and Final Award do not and cannot override the Court's authority to review decisions of COA via Rule 64 petitions. While the ponencia's ruling aligns with the findings of the Arbitral Tribunal that the tax assumption mechanism under Service Contract No. 38 is valid, such ruling is not contingent on arbitration. Even absent the arbitral award, the Court's independent analysis of COA's ruling leads to the same conclusion—the tax assumption mechanism under Service Contract No. 38 is lawful and consistent with the legislative framework established by Presidential Decree Nos. 87, 1206, and 1459.

In sum, COA gravely abused its discretion in ruling that the tax assumption mechanism under Service Contract No. 38 was unlawful, as this system is explicitly authorized by Presidential Decree Nos. 87, 1206, and 1459 and forms an integral part of the government's 60% share in the net proceeds. Service Contract No. 38 grants no tax exemption. It merely provides for the assumption of tax liabilities by the government through its executing agency.

ACCORDINGLY, I vote to GRANT the consolidated Petitions for Certiorari.

[1] Amending Presidential Decree No. 8 Issued on October 2, 1972, and Promulgating an Amended Act to Promote the Discovery and Production of Indigenous Petroleum and Appropriate Funds therefor.

[2] Rollo (G.R. No. 238846), p. 520, Service Contract No. 38, sec. 6.1(a).

[3] Id. at 528, Service Contract No. 38, sec. 7.3(a).

[4] Id. at 529, Service Contract No. 38, sec. 7.4.

[5] Presidential Decree No. 87, secs. 12 & 18(b).

[6] Ponencia, p. 4.

[7] Id. at 4-5.

[8] Id.

[9] Id. at 6.

[10] 513 Phil. 440 (2005) [Per J. Ynares-Santiago, First Division].

[11] Ponencia, pp. 11-12.

[12] Philippine Health Insurance Corp. Regional Office-Caraga v. Commission on Audit, 838 Phil. 600 (2018) [Per J. Tijam, En Banc].

[13] 821 Phil. 117 (2017) [Per J. Bersamin, En Banc].

[14] Id. at 138.

[15] See also RULES OF COURT, rule 64, sec. 2. Presidential Decree No. 1445, sec. 50.

[16] See *Reblora v. Armed Forces of the Philippines*, 711 Phil. 401 (2013) [Per J. Perez, En Banc].

[17] 672 Phil. 419 (2011) [Per J. Peralta, En Banc].

[18] Id. at 432.

[19] Presidential Decree No. 87, sec. 2.

[20] Presidential Decree No. 87, Whereas Clause.

[21] Id. at sec. 12(a).

[22] Id. at sec. 18(b).

[23] *Creating the Department of Energy* (1977).

[24] Presidential Decree No. 1206, sec. 12(a)(i)(2).

[25] *Authorizing the Secretary of Energy to Enter Into and Conclude Service Contracts, or Re-Negotiate and Modify Existing Contracts Subject to Certain Limitations* (1978).

[26] Presidential Decree No. 1459, sec. 1(a).

[27] *Rollo* (G.R. No. 238846), p. 527, Service Contract No. 38, sec. 6.3.

[28] See id. at 528-529, Service Contract No. 38, secs. 7.3 & 7.4.

[29] Id. at 523, Service Contract No. 38, sec. 6.2(a).

[30] See id. at 527, Service Contract No. 38, sec. 6.3.

[31] *Rollo* (G.R. No. 238852), pp. 551-552, COA's Comment.

[32] Presidential Decree No. 87, sec. 12(a) and 19.

[33] Id. at sec. 24.

[34] *Samar II Electric Cooperative, Inc. v. Quijano*, 550 Phil. 523, 532 (2007) [Per J. Austria-Martinez, Third Division].

[35] 810 Phil. 16 (2017) [Per J. Perlas-Bernabe, First Division].

[36] Id. at 25-26.

[37] Id. at 26.

[38] Id. at 26-27.

[39] Id. at 28.

[40] *Rollo* (G.R. No. 238846), p. 527, Service Contract No. 38, sec. 6.3.

[41] See *rollo* (G.R. No. 238852), pp. 554-555, COA's Comment.

[42] Id. at 555-556, COA's Comment.

[43] *Purisima v. Lazatin*, 801 Phil. 395, 424 (2016) [Per J. Brion, En Banc].

[44] 777 Phil. 280 (2016) [Per C.J. Sereno, En Banc].

[45] Id. at 481-482.

[46] 486 Phil. 754 (2004) [Per J. Panganiban, En Banc] (Resolution).

[47] Id. at 847-849.

[48] Ponencia, pp. 10-11.

[49] The relevant provision reads: "in no case shall the annual net revenue or share of the Government, including all taxes paid by or on behalf of the Contractor, be less than sixty percent[.]" (Emphasis supplied)

[50] The relevant provision reads: "in no case shall the annual net revenue or share of the government, including all taxes paid by or on behalf of the contractor, be less than sixty percent[.]" (Emphasis supplied)

[51] The relevant provision reads: "(a) The share of the Government, including all taxes, shall not be less than sixty per cent[.]" (Emphasis supplied)

[52] *Rollo* (G.R. No. 238846), pp. 534-535, Service Contract, sec. 12.

[53] Partial Final Award, pp. 46-47.

[54] Id. at 69-70.

SEPARATE CONCURRING OPINION

HERNANDO, J.:

I fully concur in the ponencia's disquisitions. However, I am impelled to amplify the principle that an arbitration ruling should be accorded primacy and highest respect.

The issue in these cases is the alleged under collection of the government's share in the Malampaya Natural Gas Project from 2002 to December 2009 amounting to PHP 53,140,304,739.86.

The present controversy arose from the Service Contract dated December 11, 1990, entered into by the Government of the Republic of the Philippines, through the Department of Energy (DOE), with Occidental Philippines, Inc. and Shell Exploration B.V., the predecessors-in-interest of Shell Exploration B.V. (SPEX), PNOG Exploration Corporation (PNOG-EC), and Chevron Malampaya LLC (Chevron), collectively referred to as the Contractors.[1]

Under Service Contract No. 38, the contractors undertook to perform all petroleum operations and provide all necessary technology and financing, as well as the required services in connection therewith. Moreover, Section 7.3 of the Service Contract provides that 60% of the net proceeds of the petroleum operations shall be remitted to the government, while Section 7.4 allows the contractors to retain the remaining 40%. In addition, Presidential Decree No. 87[2] exempts the contractors from payment of all taxes except income tax, which is to be paid by the DOE on behalf of the contractors as provided in Section 6.3 of the Service Contract.[3]

On post-audit, DOE Supervising Auditor Dolores T. Barraza (Auditor Barraza) observed that the corporate income taxes of the contractors were deducted from the government's 60% share in the net proceeds, resulting in

an understatement of government revenue by PHP 53,140,304,739.86 from 2002 to December 2009. Consequently, Notice of Charge No. 2010-01-151(09) was issued attributing the under collection to petitioners Thelma M. Cerdeña (Cerdeña), Chief of the DOE Compliance Division, Nora A. Tuazon (Tuazon), Officer-in-Charge of the DOE Financial Services, as well as the contractors.[4]

DOE, SPEX, PNOC-EC, and Chevron sought recourse before the Commission on Audit (COA), which denied their appeal.[5] Aggrieved, the contractors, DOE, Cerdeña, and Tuazon filed petitions for review before the COA Proper, but the same were similarly denied. This prompted the contractors, Cerdeña, and Tuazon to file the instant petitions for certiorari, essentially imputing grave abuse of discretion amounting to lack or excess of jurisdiction on the part of COA in issuing the challenged Decision and Resolution.[6]

Meanwhile, the contractors submitted the controversy to international arbitration. The International Centre for Settlement of Investment Disputes (ICSID) tribunal, in Case No. ARB/16/22 titled: Shell Philippines Exploration B.V v. The Republic of the Philippines, issued provisional measures enjoining the enforcement of the Notice of Charge pending the proceedings.[7]

On the other hand, the International Chamber of Commerce (ICC) Arbitral Tribunal, in its April 16, 2019 Partial Final Award and December 16, 2019 Final Award in Shell Philippines Exploration B.V. (the Netherlands) and Chevron Malampaya LLC (USA) v. Government of the Republic of the Philippines, docketed as ICC Case No. 21096/CYK/PTA, upheld the validity of the DOE's tax assumption of the contractor's income tax and the inclusion thereof in the Government's 60% share in the net proceeds.[8]

In its Comment to the petitions, however, COA insists that it is not bound by the ICC Arbitral Award as it is not a party to the Service Contract and the arbitration clause therein. It further asserts that the controversy is not subject to arbitration.

As stated at the outset, this opinion shall be confined only to the discussion of the principle that an arbitration ruling should be accorded highest respect and finality.

Our jurisdiction adopts a policy in favor of arbitration. The Alternative Dispute Resolution (ADR) Act of 2004 and A.M. No. 07-11-08-SC or the Special ADR Rules both declare as a policy, that the State shall encourage and actively promote the use of alternative dispute resolution, such as arbitration, as an important means to achieve speedy and impartial justice and declog court dockets.[9] This pro-arbitration policy is further evidenced by the rule on presumption in favor of enforcement of a foreign arbitral award under Special ADR Rules, viz.:

Rule 13.11. Court action. - It is presumed that a foreign arbitral award was made and released in due course of arbitration and is subject to enforcement by the court.

The court shall recognize and enforce a foreign arbitral award unless a ground to refuse recognition or enforcement of the foreign arbitral award under this rule is fully established.

The decision of the court recognizing and enforcing a foreign arbitral award is immediately executory.

Arbitration is a voluntary dispute resolution process "outside the regular court system," where parties agree to submit their conflict to an arbitrator or panel of arbitrators of their own choice. Resort to arbitration requires consent from the parties, either through an arbitration clause in the contract or an agreement to submit an existing controversy between them to arbitration.[10]

In this case, it is undisputed that the Service Contract contains an arbitration clause which reads:

12.1

Disputes, if any, arising between the OFFICE OF ENERGY AFFAIRS and CONTRACTOR relating to this Contract or the interpretation and performance of any of the clauses of this Contract, and which cannot be settled amicably, shall be settled by arbitration. The OFFICE OF ENERGY AFFAIRS on the one hand and CONTRACTOR on the other hand, shall each appoint one arbitrator within thirty (30) days after receipt of a written request of the other Party to do so, such arbitrator shall, at the request of the other Party, if the parties do not otherwise agree, be appointed by the President of the International Chamber of Commerce. If an arbitrator fails or is unable to act, his[/her] successor will be appointed in the same manner as the arbitrator whom he[/she] succeeds. Unless the Parties agree otherwise, the Philippines shall be the venue of the arbitration proceedings. The English language shall be the language used.

12.2

The decision of a majority of the arbitrators shall be final and binding upon the parties. Judgement upon the award rendered may be entered into by any court having jurisdiction or application may be made to such court for a judicial acceptance of the award and an order of enforcement as the case may be.

12.3

Except as provided in this Section, arbitration shall be conducted in accordance with the Rules of Arbitration of the International Chamber of Commerce, then in effect. (Emphasis supplied)

Clearly, the parties to Service Contract No. 38, i.e., the Government of the Republic of the Philippines, through the DOE, and the contractors, agreed to settle any dispute relating to the Service Contract through arbitration. Thus, when the contractors commenced an arbitration pursuant to the said arbitration clause, they merely exercised their rights under the Service Contract.

COA posits that there is no real dispute between the DOE and the contractors relating to the interpretation of the contract, thereby rendering the arbitration clause inoperative.

This argument fails to persuade.

It is to be recalled that COA itself argued in its Comment to the petitions that the tax assumption clause in the Service Contract effectively increases the 40% share of the contractors and reduces the 60% share of the government in the net proceeds, which is tantamount to exempting the contractors from income tax and the amendatory income tax laws. Otherwise stated, COA argues that the DOE's tax assumption of the contractor's income tax and the inclusion thereof in the Government's 60% share in the net proceeds were invalid as it effectively resulted to the exemption of the contractors from payment of income tax. Contrary therefore to COA's supposition, there exists a dispute as to the interpretation of the Service Contract, which the ICC resolved in ICC Case No. 21096/CYK/PTA, when it upheld the validity of the DOE's tax assumption of the contractor's income tax and the inclusion thereof in the Government's 60% share in the net proceeds.

To stress, the ICC has interpreted Section 6.3 of the Service Contract and found without hesitation that the Philippine income taxes paid by or on behalf of the contractors under Service Contract No. 38 form part of the Government's 60% share of the net proceeds from petroleum operations carried out under the Contract. Accordingly, the Government has already received in full its 60% share of the net proceeds from 2002 until the conclusion of the Hearing in September 2018.[11]

Since the core issue as to the legality and enforceability of the tax assumption mechanism under Service Contract No. 38 has already been determined by the ICC which aptly exercised its jurisdiction over the controversy in

accordance with the arbitration clause in the Service Contract, the ICC ruling should be accorded highest respect and finality.

It bears stressing that the ICC's April 16, 2019 Partial Final Award and December 16, 2019 Final Award have long attained finality as no appeal is allowed from an international commercial arbitration award. This is clearly provided in Rule 19.7 of the Special ADR Rules thus:

RULE 19.7. No appeal or certiorari on the merits of an arbitral award. – An agreement to refer a dispute to arbitration shall mean that the arbitral award shall be final and binding. Consequently, a party to an arbitration is precluded from filing an appeal or a petition for certiorari questioning the merits of an arbitral award.

In fine, the Court finds no compelling reason to disturb the ICC's categorical findings and conclusions on the matter.

It must be emphasized that the State's declared policy is "to respect party autonomy or the freedom of the parties to make their own arrangements in the resolution of disputes with the greatest cooperation of and the least intervention from the courts." [12] Thus, judicial interference is actively restrained under the Special ADR Rules for arbitration to be a true alternative dispute resolution mechanism, and not merely an added preliminary step to judicial resolution. [13]

Moreover, COA must respect the arbitration agreement in the Service Contract because such arbitration agreement is the law between the parties, hence, they are expected to abide by it in good faith. [14] The arbitration clause should, thus, be given primacy in accordance with the State's policy of upholding the autonomy of arbitral awards.

ACCORDINGLY, I vote to GRANT the consolidated Petitions for Certiorari.

[1] Ponencia, p. 3.

[2] The Oil Exploration and Development Act of 1972.

[3] Ponencia, p. 3.

[4] Id. at 4.

[5] Id.

[6] Id. at 5.

[7] Id.

[8] Id. at 6.

[9] Mabuhay Holdings Corporation v. Sembcorp Logistics Limited, 844 Phil. 813, 833 (2018) [Per J. Tijam, First Division].

[10] Adapon v. Medical Doctors, Inc., 903 Phil. 647, 661 (2021) [Per J. Leonen, Third Division].

[11] ICC Partial Final Award, pars. 222 to 223.

[12] Adapon v. Medical Doctors, Inc., 903 Phil. 647, 680 (2021) [Per J. Leonen, Third Division].

[13] Id. at 664.

[14] S. COURT RULE ON ADR, Rule 2.2.

CONCURRING OPINION

LOPEZ, J., J.:

I agree with the ponencia.

The crux of the controversy is Section 6.3 of the Service Contract No. 38 (Service Contract) executed on December 11, 1990 between the Government of the Republic of the Philippines, represented by then President Corazon C. Aquino, and contractors Occidental Philippines, Inc. and Shell Exploration B.V., predecessors-in-interest of petitioners Shell Exploration B.V. (SPEX), Philippine National Oil Company Exploration Corporation (PNOC-EC), and Chevron Malampaya LLC (Chevron).

Section 6.3 of the Service Contract provides:

6.3

The OFFICE OF ENERGY AFFAIRS shall assume and pay on behalf of CONTRACTOR and its parent company, on the first transaction in each instance where the tax is imposed, all income taxes payable to the Republic of the Philippines based on income and profits and, with respect to CONTRACTOR, on the first transaction in each instance where the tax is imposed, all dividends, withholding taxes[,] and other taxes imposed by the Government of the Philippines on the distribution of income and profits derived from Petroleum Operations to its parent company. The OFFICE OF ENERGY AFFAIRS shall promptly furnish to Contractor, without fee or other consideration, the official receipts issued in the name of CONTRACTOR by any duly empowered Government authority, acknowledging the payment of said taxes. (Emphasis supplied)

This contractual stipulation is based on Section 18(b) of Presidential Decree No. 87 issued in 1972, which states that the Petroleum Board shall "enter into contracts herein authorized with such terms and conditions as may be appropriate under the circumstances including the grant of special allowance[. . .] Provided, finally, That in no case shall the annual net revenue or share of the GOVERNMENT, including all taxes paid by or on behalf of the contractor, be less than sixty percent of the difference between the gross income and the sum of operating expenses and Filipino participation incentive." [1]

Petitioners argue that the above provisions clearly state that the income taxes payable by the contractors under the Service Contract shall be assumed and paid for by the Government, particularly, the Department of Energy (DOE), on behalf of contractor, and counted as part of the Government's 60% share.

On the other hand, the Commission on Audit (COA) insists that Section 18(b) of Presidential Decree No. 87 does not clearly state that the income taxes of the contractors are to be assumed by the Government, arguing that the provision only says that the Government's share, including taxes paid by or on behalf of the contractor, cannot be less than 60%. According to COA, this means that the Government's share can be more than 60%, and, therefore, the assumption by the DOE of the contractor's income taxes as part of the Government's 60% share has no legal basis.

Based on this interpretation, COA proceeded to uphold Notice of Charge (NOC) No. 2010-01-151(09) in the amount of PHP 53,140,304,739.86 as under-collection of income taxes from 2002 to December 2009. The NOC instructed the DOE to direct the members of the Service Contract Consortium to settle immediately the said audit charge.

While reserving their right to pursue arbitration, SPEX and Chevron, together with their consortium partner, PNOC-EC, filed their Joint Appeal Memorandum on March 4, 2011. These appeals were denied via the August

22, 2011 NGS-Cluster B Decision No. 2011-009. On October 11, 2011, SPEX and Chevron (along with PNOC-EC) filed their joint Petition for Review before the Commission Proper of COA. On May 11, 2015, SPEX and Chevron received COA's assailed April 6, 2015 Decision No. 2015-115 (Decision No. 2015-115) denying the Petitions.

On August 14, 2017, petitioners received from COA another NOC, alleging under collection of taxes from 2015 to 2016 amounting to PHP 16,372,484,686.47. The NOC similarly asked the DOE to direct the members of the Service Contract Consortium "to settle the said audit charge immediately." SPEX and Chevron, together with PNOC-EC, then filed with the COA National Government Sector Cluster 7 their Appeal Memorandum on the NOC. Through the January 24, 2018 Resolution (Decision No. 2018-075), COA denied the Motions for Reconsideration and affirmed the Decision No. 2015-115.

The above Decision Nos. 2015-115 and 2018-075 are the subject of these consolidated Petitions.

The above controversy is also the subject of an arbitration initiated by petitioners before the International Chamber of Commerce (ICC) in accordance with the arbitration clause of the Service Contract. The Arbitral Tribunal eventually ruled in favor of petitioners.

In an April 16, 2019 Partial Final Award (Partial Final Award) and December 16, 2019 Final Award (Final Award) (jointly referred to as the ICC Arbitral Award), the ICC Arbitral Tribunal unanimously upheld the DOE's assumption of the contractor's income tax and the inclusion thereof in the Government's 60% share.[2]

However, COA refuses to recognize the jurisdiction of the ICC Arbitral Tribunal, asserting that while it is part of the Government, which is the contracting party in the Service Contract, COA itself is not a party to the Service Contract and its arbitration clause. As such, COA argues that it is not bound by the ICC Arbitral Award. It further asserts that the controversy is not subject to arbitration.

Thus, the same controversy that has been ruled upon by the ICC Arbitral Tribunal is presented before this Court, with the same contract in question.

To be sure, this Court will never shirk away from its mandate or shy away from exercising its jurisdiction. However, considering that there is a claim of arbitrability of the dispute, this Court cannot pass upon the substantive merits of the case without first determining whether the dispute is indeed a matter that should be resolved through arbitration.

The initial query that must be addressed is thus: May a dispute arising out of an instruction of COA (i.e. to collect under-collected income taxes under the Service Contract) to another government entity or instrumentality bound by an arbitration clause (i.e. DOE), be the subject of arbitration?

The ICC Arbitral Tribunal's Jurisdiction; arbitrability of the controversy

The Service Contract contains the following arbitration clause:

12.1 Disputes, if any, arising between the OFFICE OF ENERGY AFFAIRS and CONTRACTOR relating to this Contract or the interpretation and performance of any of the clauses of this Contract, and which cannot be settled amicably, shall be settled by arbitration. The OFFICE OF ENERGY AFFAIRS on the one hand and CONTRACTOR on the other hand, shall each appoint one arbitrator within thirty (30) days after receipt of a written request of the other Party to do so, such arbitrator shall, at the request of the other Party, if the parties do not otherwise agree, be appointed by the President of the International Chamber of Commerce. If an arbitrator fails or is unable to act, his successor will be appointed in the same manner as the arbitrator whom he succeeds. Unless the Parties agree otherwise, the Philippines shall be the venue of the arbitration proceedings. The English language shall be the language used.

12.2 The decision of a majority of the arbitrators shall be final and binding upon the parties. Judgement upon the award rendered may be entered into by any court having jurisdiction or application may be made to such court for a judicial acceptance of the award and an order of enforcement as the case may be.

12.3 Except as provided in this Section, arbitration shall be conducted in accordance with the Rules of Arbitration of the International Chamber of Commerce, then in effect.

The Philippine jurisdiction has long adopted a policy in favor of arbitration. The policy in favor of arbitration has been affirmed in our Civil Code, which was approved as early as 1949. It was later institutionalized by the enactment of Republic Act No. 876, which expressly authorized, made valid, enforceable, and irrevocable parties' decision to submit their controversies, including incidental issues, to arbitration.[3] Indeed, it has long been settled that arbitration should receive every encouragement from the courts which may be extended without contravening sound public policy or settled law.[4] Hence, arbitration clauses are liberally construed to favor arbitration. Any doubt should be resolved in favor of arbitration.[5] Thus, if there were an interpretation that would render effective an arbitration clause for purposes of avoiding litigation and expediting resolution of the dispute, that interpretation shall be adopted.[6]

As pointed out by SPEX and Chevron, the 1987 Constitution does not proscribe arbitration even for matters subject to the jurisdiction of the COA. Article IX(A), Section 7 of the 1987 Constitution provides as follows:

Section 7. Each Commission shall decide by a majority vote of all its Members, any case or matter brought before it within sixty days from the date of its submission for decision or resolution. A case or matter is deemed submitted for decision or resolution upon the filing of the last pleading, brief, or memorandum required by the rules of the Commission or by the Commission itself. Unless otherwise provided by this Constitution or by law, any decision, order, or ruling of each Commission may be brought to the Supreme Court on certiorari by the aggrieved party within thirty days from receipt of a copy thereof. (Emphasis supplied)

The 1987 Constitution is thus clear. A petition for certiorari is not the sole and exclusive means by which a COA Decision may be assailed as the 1987 Constitution grants the legislature and the Supreme Court leeway to provide for other remedies. The Alternative Dispute Resolution (ADR) Act does not specifically exclude COA from its coverage of arbitration. There is no basis for any claimed blanket proscription against arbitration whenever the COA is involved. The ADR Act is a law that provides an alternative means of adjudicating the correctness even of COA actions or decisions. The same can be said of the New York Convention and the Model Law, which have been adopted as part of the law of the land and are recognized as a source of binding legal obligations.

Indeed, this Court already had the opportunity to pronounce that "other tribunals/adjudicative bodies, too, may have concurrent jurisdiction with the COA over money claims against the government or in the audit of the funds of government agencies and instrumentalities." [7]

More, COA's argument that COA Decisions are not covered by the arbitration clause in Section 12.1 of the Service Contract on the ground that COA is not a party to the contract is debunked by the fact that even COA is bound to respect the rulings of regular courts (or arbitral tribunals), even on matters that were the subject of COA rulings.

In *Taisei Shimizu Joint Venture v. Commission on Audit*, [8] this Court reiterated that although COA exercises broad powers pertaining to audit matters, it is devoid of authority to determine the validity of contracts, lest it encroaches upon such judicial function, and it further decreed that the COA's jurisdiction is limited to audit matters only. [9] Hence, it is not unusual for the government and its instrumentalities to be sued in the regular courts (or even arbitral tribunals) even when the action involves government funds or property since such an

action may entail resolution of issues falling within the jurisdiction of the courts or arbitral tribunals. As such, COA is bound to respect the rulings of regular courts (or arbitral tribunals) and stay its hands from modifying said rulings, let alone from claiming exclusive jurisdiction over the case:

Actions against the State are not excluded from the jurisdiction of courts. For although, as a rule, the State is immune from suit, it is settled that "a suit against the State is allowed when the State gives its consent, either expressly or impliedly. Express consent is given through a statute, while implied consent is given when the State enters into a contract or commences litigation."

We recently held that although the COA exercises broad powers pertaining to audit matters, it is devoid of authority to determine the validity of contracts, lest it encroaches upon such judicial function. We further decreed that the COA's jurisdiction is limited to audit matters only. Hence, we set aside a ruling of the COA disapproving a deed of exchange between the City Government of Cebu and a private corporation. The case clearly demonstrated why it was not unusual for the government and its instrumentalities to be sued in the regular courts even when the action involved government funds or property since such an action may entail resolution of issues falling within the jurisdiction of the courts.

Other tribunals/adjudicative bodies, too, may have concurrent jurisdiction with the COA over money claims against the government or in the audit of the funds of government agencies and instrumentalities.

In *Development Bank of the Philippines v. COA*, we held that under existing laws, the COA does not have the sole and exclusive power to examine and audit government banks. The Central Bank has concurrent jurisdiction to examine and audit, or cause the examination and audit, of government banks. Neither was there any statutory obstacle for a government bank to hire a private external auditor to examine its accounts without prejudice to its being concurrently subject to a COA audit. The Court took into account, among others, the Constitutional Commission's deliberations showing that the framers of the Constitution downvoted a proposal to add the word "exclusive" to describe the powers of the COA under Article IX-D, Section 2(1) of the 1987 Constitution. It also cannot be said, therefore, that the COA's "power, authority, and duty to[. . .] settle all accounts pertaining to the revenue and receipts of, and expenditures or uses of funds and property, owned or held in trust by, or pertaining to, the Government" is exclusive.

Further, *Civil Service Commission (CSC) v. Pobre* recognized a specific case over which the CSC and the COA each had a role in processing the leave benefits of public officers and employees, requiring the expenditure and use of funds, thus:

While the determination of leave benefits is within the functions of the CSC as the central personnel agency of the government, the duty to examine accounts and expenditures relating to such benefits properly pertains to the COA. Where government expenditures or use of funds is involved, the CSC cannot claim exclusive jurisdiction simply because leave matters are involved. Thus, even as we recognize CSC's jurisdiction in this case, its power is not exclusive as it is shared with the COA.

There, the Court reversed the ruling of the Court of Appeals that the COA had sole jurisdiction over the matter of computing a government employee's terminal leave benefits.

Later, *Pobre* would be cited in *De Jesus v. Civil Service Commission* where we held that although the COA had primary jurisdiction to determine the legality and regularity of the grant of allowances and benefits to members of the boards of water districts designated by the Local Water Utilities Administration (LWUA), the CSC similarly had jurisdiction to pass upon the issue in relation to an administrative case against LWUA officers for violation of the Code of Conduct and Ethical Standards for Public Officials and Employees.

In the recent case of *Tourism Infrastructure and Enterprise Zone Authority (TIEZA) v. Global-V Builders Co.*, the Court ruled that where TIEZA and the private contractor validly agreed to submit their construction dispute to

arbitration, the CIAC properly exercised its jurisdiction over the case.

....

Considering that TSJV and DOTr had voluntarily invoked CIAC's jurisdiction, the power to hear and decide the present case has thereby been solely vested in the CIAC to the exclusion of COA. Being a specific law, EO No. 1008 providing for CIAC's exclusive jurisdiction prevails over PD 1445, granting the COA the general jurisdiction over money claims due from or owing to the government. For this reason alone, the COA should have stayed its hands from modifying the CIAC's final arbitral award here, let alone from claiming exclusive jurisdiction over the case.[10] (Emphasis supplied, citations omitted)

The foregoing shows that while COA exercises broad powers pertaining to audit matters, its jurisdiction is limited to audit matters only. COA is still bound by, and cannot unilaterally ignore or refuse to recognize or declare as invalid, existing laws.

It is incorrect for COA to claim that while the Government is a party to the Service Contract, this should not include COA upon the mere claim that such would mean that COA would be estopped from questioning the validity, legality, and reasonableness of government contracts.

In *Cagayan de Oro City Water District v. Judge Pasal*,^[11] this Court held that a COA recommendation does not preclude the parties from submitting to arbitration. It even pronounced that the proper action for a government entity that is bound by an arbitration clause, when faced with a COA recommendation, is to submit to arbitration:

COA's recommendation does not preclude the parties from submitting to arbitration. On the contrary, COWD should, even more, submit to arbitration in order to pursue the nullification of the contract itself.

To repeat, the arbitral tribunal has the first opportunity to rule on whether it has jurisdiction to decide a dispute submitted for its resolution, including the validity of the contract itself. This is clear from Article 19 of the BWSA which clearly states that among the arbitrable issues is the nullity of the BWSA itself, thus:

19.02 Amicable Settlement

[...]

(c)

In the event that there is any disagreement, dispute, controversy, claim[,] or difference of any kind whatsoever arising out of or relating to this Agreement or any arrangement relating thereto or contemplated herein, or breach or termination or invalidity hereof, or dispute in the interpretation of any provision hereof (the Dispute), the Parties shall endeavor to resolve such Dispute in the first instance by mutual discussion between them[. . .]

[...]

19.03 Arbitration

[...]

(c)

Any Dispute that is not resolved as provided in Section 19.02 shall be finally settled by arbitration in accordance with the provisions of the Arbitration Law of the Republic of the Philippines.

[...]

Thus, if COWD is truly minded to follow COA's recommendation to initiate the nullification of the BWSA and

Supplemental Agreement, the proper forum, therefore, is the arbitral tribunal it ought to constitute together with Rio Verde.[12] (Emphasis supplied)

In the instant case, COA asked the DOE to direct the members of the Service Contract Consortium "to settle immediately the said audit charge." In other words, COA directed the DOE to act in a certain way. Hence and since the Government itself did not initiate arbitration, SPEX and Chevron were well within their rights to initiate arbitration to resolve the issues brought about by COA's directives.

Clearly, a dispute arising out of a COA action or decision is arbitrable. It may be the subject of arbitration proceedings and even COA is bound by the tribunal's ruling as the principle of conclusiveness of prior adjudications is not confined in its operation to the judgments of courts, but extends as well to those of all other tribunals exercising adjudicatory powers.[13]

The State has adopted a policy in favor of and for the active promotion of arbitration. Part of this State policy is not only preference for referral of disputes to arbitration but also respect for the autonomy of arbitration proceedings.[14] Such autonomy is reflected, among others, in the principles that provide for the greatest cooperation of and the least intervention from the courts:[15]

Rule 2.1. General policies. — It is the policy of the State to actively promote the use of various modes of ADR and to respect party autonomy or the freedom of the parties to make their own arrangements in the resolution of disputes with the greatest cooperation of and the least intervention from the courts. To this end, the objectives of the Special ADR Rules are to encourage and promote the use of ADR, particularly arbitration and mediation, as an important means to achieve speedy and efficient resolution of disputes, impartial justice, curb a litigious culture and to de-clog court dockets.

The policy to promote the use of arbitration and respect for the autonomy of arbitration proceedings recognizes the principle of "competence-competence," which means that the arbitral tribunal shall be accorded the first opportunity or competence to rule on the issue of whether or not it has the competence or jurisdiction to decide a dispute submitted to it for decision, including any objection with respect to the existence or validity of the arbitration agreement.[16]

Thus, when a court is asked to rule upon issues affecting the competence or jurisdiction of an arbitral tribunal in a dispute brought before it, the court must generally exercise judicial restraint and defer to the competence or jurisdiction of the arbitral tribunal by allowing the arbitral tribunal the first opportunity to rule upon such issues,[17] thus:

Rule 2.4. Policy implementing competence-competence principle. — The arbitral tribunal shall be accorded the first opportunity or competence to rule on the issue of whether or not it has the competence or jurisdiction to decide a dispute submitted to it for decision, including any objection with respect to the existence or validity of the arbitration agreement. When a court is asked to rule upon issue/s affecting the competence or jurisdiction of an arbitral tribunal in a dispute brought before it, either before or after the arbitral tribunal is constituted, the court must exercise judicial restraint and defer to the competence or jurisdiction of the arbitral tribunal by allowing the arbitral tribunal the first opportunity to rule upon such issues.

Where the court is asked to make a determination of whether the arbitration agreement is null and void, inoperative or incapable of being performed, under this policy of judicial restraint, the court must make no more than a prima facie determination of that issue.

Unless the court, pursuant to such prima facie determination, concludes that the arbitration agreement is null and void, inoperative[,] or incapable of being performed, the court must suspend the action before it and refer the parties to arbitration pursuant to the arbitration agreement.

In Cagayan de Oro City Water District, the principle of "competence-competence" was upheld as follows:

Under the principle of competence-competence, the arbitral tribunal has the first opportunity to rule on whether it has jurisdiction to decide a dispute submitted for its resolution. In other words, whether the trial court acted in grave abuse of discretion or otherwise grievously erred in directing COWD and Rio Verde to submit to arbitration is for the arbitral tribunal itself to determine, not the Court.

....

To repeat, only after the arbitral tribunal shall have already ruled on the issue of jurisdiction may the aggrieved party seek judicial recourse against submitting itself to the process of arbitration. Leapfrogging the judicial process in clear defiance of the Special Rules on ADR violates the principle of competence-competence and the State policy to actively promote the use of alternative modes of dispute resolution.[18]

Given that there is no basis to declare that the arbitration clause in the Service Contract is void and inoperative, or that the dispute regarding COA's actions is not arbitrable, respect for the principle of competence-competence behooves this Court to defer to the proper arbitral tribunals.

This Court thus finds that the dispute arising from the actions of COA is subject to arbitration under the Service Contract and the merits of the dispute are matters that are within the competence of the appropriate tribunals in the ICC and International Centre for Settlement of Investment Disputes (ICSID) arbitrations.

With this finding, this Court can defer to the findings and rulings of the ICC Arbitral Tribunal.

The applicable rules provide for the autonomy of arbitral awards and emphasize that the courts shall not disturb the arbitral tribunal's determination of facts and/or interpretation of law.[19] An arbitral award enjoys the presumption that it was made and released in due course of arbitration and is ultimately subject to confirmation by the court in the proper proceeding.

It must be noted that the ICC Arbitral Award has become final and executory because there is no appeal on an international commercial arbitration award. Rule 19.7 of the Special ADR Rules states that an arbitral award is "final and binding" and no appeal or certiorari on the merits of an arbitral award is available:

Rule 19.7. No appeal or certiorari on the merits of an arbitral award. — An agreement to refer a dispute to arbitration shall mean that the arbitral award shall be final and binding.

Consequently, a party to an arbitration is precluded from filing an appeal or a petition for certiorari questioning the merits of an arbitral award. (Emphasis supplied)

More, the ICC Rules of Arbitration provide that "[e]very award shall be binding on the parties" and "the parties undertake to carry out any award without delay." [20] Even the Final Award stated that the ICC Arbitral Award is "immediately enforceable:"

VIII. AWARD

124. The Tribunal has carefully considered the Parties' arguments in their written pleadings and oral submissions. For all of the foregoing reasons and rejecting all submissions to the contrary, the Tribunal hereby FINDS, DECLARES AND AWARDS as follows:

[...]

(c) The Tribunal's Partial Final Award and Final Award are immediately enforceable notwithstanding the availability or pendency of any other proceeding or application, including an action to set the award aside[.][21]

The ICC Tribunal Award

In the April 16, 2019 Partial Final Award and the December 16, 2019 Final Award, the ICC Tribunal unanimously upheld the "tax assumption" and the inclusion of the contractor's income tax in the Government's 60% share. Interpreting Section 6.3 of the Service Contract, the ICC Tribunal ruled that COA NOC breached the Service Contract:

203. Since Section 6.3 [of Service Contract No. 38] expressly requires the DOE to 'assume and pay' the Contractor's income taxes, and Section 7.4 [of Service Contract No. 38] entitles the Contractor to 40% of Net Proceeds, the value of the Contractor's income taxes can only form part of the DOE's 60% share of Net Proceeds. There is no other way to read these provisions together and give them all meaning.

[. . .]

206. This interpretation also comports with the implementing legislation which specifies that the Government's share of net proceeds "including all taxes paid by or on behalf of the contractor" cannot be less than 60%.

[. . .]

245. Having determined that Section 6.3 is valid and enforceable under Philippine law, the Tribunal finds that the Respondent, through the COA's four Notices of Charge attempting to recover up to approximately USD 3.4 billion from the Consortium representing alleged under collection of the Government's share, has clearly breached Section 6.3 of [Service Contract No. 38], a contractual obligation having 'the force of the law' and which must be 'complied with in good faith'. "[22] (Emphasis supplied)

The ICC Arbitral Tribunal also ruled that the Government already received in full its 60% share:

222. For the foregoing reasons, the Tribunal, without any hesitation, finds that the Philippine income taxes paid by or on behalf of the Claimants under [Service Contract No. 38] forms part of the Respondent's 60% share of the net proceeds from petroleum operations carried out under the Contract and the so-called limiting words in no way limit the Philippines' assume and pay obligation.

223. In the circumstances, the Tribunal also finds that the Respondent has already received in full its 60 percent share of the net proceeds from 2002 until the conclusion of the Hearing in September 2018. The Tribunal notes that this was, at no time, disputed by the Respondent. Accordingly, the Respondent cannot demand or collect any additional amount from the Claimants for income taxes during this period.[23]

Notably, the Malampaya Project was commissioned in 2001 and began commercial operations in 2002. Since then, it has been producing natural gas that has been used by power plants to generate electricity for Luzon. For the period 2002 to 2015, the Malampaya Project fueled as much as 40% of Luzon's power needs. Today, its fuels about 20% of Luzon's power needs. Indeed, this is the desired outcome of the incentives designed in Presidential Decree No. 87.

Indubitably, the Malampaya Project is the fruit of the policy framework, incentives and efforts made by the Philippines across many decades and different administrations. From the groundwork laid down by Presidential Decree No. 87 and similar laws in the 1970s, the promotional campaigns in the late 1980s and early 1990s, and the contract implementation in the 2000s – all these contributed to a successful outcome that continues to enhance the country's energy security and economic development.

It is further important to emphasize that a fiscal incentive where the Government assumes the contractor's income tax is not invalid. The assumption of income taxes and its inclusion in the Government's share is not an unusual fiscal incentive.

This was also adopted and implemented in the geothermal industry. In the case of *Republic v. Kidapawan*,^[24] which involved a Service Contract under Presidential Decree No. 1442, this Court recognized the assumption of taxes by the Government and its inclusion in the 60% share of the Government:

Likewise, although it is the government which actually pays the income taxes, the contract nonetheless specifically provided that the payment is for and in behalf of PNOC-EDC and is chargeable against the 60% share of the government in the net profits derived by the PNOC-EDC arising from the geothermal operation. In reality, the PNOC-EDC is the actual payee while the government is only its agent in the payment of the income taxes. In fact, the official receipt is being issued in the name of PNOC-EDC.^[25] (Emphasis supplied)

This is also present in the mining industry. In *La Bugal-B'Laan Tribal Assoc., Inc. v. Ramos*,^[26] a case involving mining contracts under Republic Act No. 7942 (the Philippine Mining Act of 1995), this Court recognized that the share of the Government includes income tax:

The basic government share is comprised of all direct taxes, fees[,] and royalties, as well as other payments made by the contractor during the term of the FTAA. These are amounts paid directly to (i) the national government (through the Bureau of Internal Revenue, Bureau of Customs, Mines & Geosciences Bureau and other national government agencies imposing taxes or fees), (ii) the local government units where the mining activity is conducted, and (iii) persons and communities directly affected by the mining project. The major taxes and other payments constituting the basic government share are enumerated below:

....

- Contractor income tax – maximum of 32 percent of taxable income for corporations[.][²⁷] (Emphasis supplied)

At least three pieces of legislation directed that taxes are part of the Government's share in petroleum projects:

1. Section 18(6) of Presidential Decree No. 87, otherwise known as the Oil Exploration and Development Act of 1972, categorically refers to the Government's share as "including all taxes paid by or on behalf of the contractor."

"(b) Enter into contracts herein authorized with such terms and conditions as may be appropriate under the circumstances including the grant of special allowance . . . Provided, finally, That in no case shall the annual net revenue or share of the Government, including all taxes paid by or on behalf of the contractor, be less than sixty per cent of the difference between the gross income and the sum of operating expenses and Filipino participation incentive."

2. Section 12(a)(i)(2) of Presidential Decree No. 1206, Creating the Department of Energy, states the Government's share is "including all taxes paid by or on behalf of the contractor:"

"(2) Enter into contracts herein authorized with such terms and conditions as may be appropriate under the circumstances: . . . And, Provided, finally, That in no case shall the annual net revenue or share of the government, including all taxes paid by or on behalf of the contractor, be less than sixty percent of the difference between the gross income and the sum of operating expenses and Filipino participation incentive."

3. Section 1(a) of Presidential Decree No. 1459, Act Authorizing the Secretary of Energy to Enter Into and Conclude or Re-negotiate and Modify Existing Contracts Subject to Certain Limitations, provides that the Government's share is "including all taxes."

(a) The share of the Government, including all taxes, shall not be less than sixty per cent of the difference between the gross income and the sum of operating expenses and such allowances as the Secretary of Energy may deem proper to grant.

Such "tax assumption" incentive has been held by this Court to be valid and different from "tax exemption."

In *Mitsubishi Corporation-Manila Branch v. Commissioner of Internal Revenue*,^[28] this Court ruled in favor of the private contractor's claim for tax refund by virtue of a "tax assumption" clause in an Exchange of Notes between Japan and the Philippines. In overturning the Court of Tax Appeals En Banc (CTA En Banc), this Court explained the difference between "tax exemption" and "tax assumption" and that the restrictions on "tax exemption" do not apply in "tax assumption:"

To 'assume' means '[t]o take on, become bound as another is bound, or put oneself in place of another as to an obligation or liability.' This means that the obligation or liability remains, although the same is merely passed on to a different person. In this light, the concept of an assumption is therefore different from an exemption, the latter being the '[f]reedom from a duty, liability[,] or other requirement' or '[a] privilege given to a judgment debtor by law, allowing the debtor to retain [a] certain property without liability.' Thus, contrary to the CTA En Banc's opinion, the constitutional provisions on tax exemptions would not apply.^[29] (Emphasis supplied, citations omitted)

This Court then went on to say that since the Government agreed to assume the tax obligation of the contractor, it was erroneous to collect the said tax from the contractor. Therefore, the tax refund was proper.

In this case, it is fairly apparent that the subject taxes in the amount of [PHP] 52,612,812.00 was erroneously collected from petitioner, considering that the obligation to pay the same had already been assumed by the Philippine Government by virtue of its Exchange of Notes with the Japanese Government. Case law explains that an exchange of notes is considered as an executive agreement, which is binding on the State even without Senate concurrence. In *Abaya v. Ebdane*:

[...]

Paragraph 5 (2) of the Exchange of Notes provides for a tax assumption provision whereby:

(2)

The Government of the Republic of the Philippines will, itself or through its executing agencies or instrumentalities, assume all fiscal levies or taxes imposed in the Republic of the Philippines on Japanese firms and nationals operating as suppliers, contractors or consultants on and/or in connection with any income that may accrue from the supply of products of Japan and services of Japanese nationals to be provided under the Loan.

....

All told, petitioner correctly filed its claim for tax refund under Sections 204 and 229 of the NIRC to recover the erroneously paid taxes amounting to [PHP] 44,288,712.00 as income tax and [PHP] 8,324,100.00 as BPRT from the BIR. To reiterate, petitioner's entitlement to the refund is based on the tax assumption provision in the Exchange of Notes. Given that this is a case of tax assumption and not an exemption, the BIR is, therefore, not without recourse; it can properly collect the subject taxes from the NPC as the proper party that assumed petitioner's tax liability.^[30] (Emphasis supplied, citations omitted)

It is well to note that various agencies of the Government have likewise affirmed that the "tax assumption" and the inclusion of income tax in the Government share are valid.

More, the BIR, which is the agency tasked to implement tax laws, has stated that tax assumption is "not novel as it can be found in many financing transactions." It even recognized that the Republic of the Philippines has assumed taxes in certain bonds it issued. According to November 5, 2012 BIR Ruling No. 604-12:

As represented, a key feature of the Bonds is the assumption by the Republic of the final withholding tax on interest due on the Bonds. This 'tax assumption' feature is not novel inasmuch as it can be found in many

financing transactions involving Philippine parties, some of which were the subject of past BIR rulings. For this transaction, the tax assumption feature was introduced to place the Bonds at par with the bonds issued by the Republic offshore (commonly referred to as 'ROP Global Bonds'), with which the Republic undertook to make whole its bond holders from Philippine taxes due on amounts they will receive by making such additional payments necessary to cover Philippine taxes.

Different offices of the Government have maintained that "corporate income tax of the Contractor is a proper inclusion to and/or forms part of the 60% share of the Government." [31]

The foregoing shows that the ICC Tribunal Award is consistent with State policy as it is with this Court's own pronouncements in jurisprudence, legislation, other similar contracts in the geothermal industry and mining industry, as well as the position of various agencies of the Government. Even COA accepted the implementation of the tax assumption incentive for decades, until it recently decided to change its view.

More, Article III, Section 10 of the 1987 Philippine Constitution directs "[n]o law impairing the obligation of contracts shall be passed." This provision "ensures that the integrity of contracts is protected from any unwarranted State inference." [32] It is supposed "to encourage trade and credit by promoting confidence in the stability of contractual relations." [33] Indeed, "[a]s a rule, contracts should not be tampered with by subsequent laws that would change or modify the rights and obligations of the parties. As noted by Justice Isagani A. Cruz, '[T]he will of the obligor and obligee must be observed; the obligation of their contract must not be impaired.'" [34]

This constitutional proscription is violated if the State changes the terms of the contract or imposes new conditions:

There is an impairment when, either by statute or any administrative rule issued in the exercise of the agency's quasi-legislative power, the terms of the contracts are changed either in the time or mode of the performance of the obligation. There is likewise impairment when new conditions are imposed or existing conditions are dispensed with. [35] (Citations omitted)

Verily, "Impairment is anything that diminishes the efficacy of the contract." [36] As explained in *Clemons v. Nolting*: [37]

Under the Civil Code the contract constitutes the law of the parties unless it violates some provision of law or public policy. The parties themselves make the law by which they shall be governed, and it is the business of the courts to see that the parties to a legal contract comply with its terms. A law which changes the terms of a legal contract between parties, either in the time or mode of performance, or imposes new conditions, or dispenses with those expressed, or authorizes for its satisfaction something different from that provided in its terms, is law which impairs the obligation of a contract and is therefore null and void. An interference with the terms of a legal contract by legislation is unwarranted and illegal. A contract is not fulfilled by the delivery of one thing which is different from the thing the contract provides for. Words in contracts are to be given the meaning which they were understood to have by the parties at the time of the making of the contract. There cannot exist in this jurisdiction one law for debtors and another law for creditors. The genius, the nature, and the spirit of our Government amount to a prohibition of such acts of legislation, and the general principles of law and reason forbid them. [38] (Emphasis supplied)

The 2019 case of *Manila International Airport Authority v. Commission on Audit* [39] is instructive. In that case, this Court reversed COA for contradicting the intention of the parties when they entered into certain agreements, thus:

The Court finds the action of the COA not only erroneous but also in contravention of the doctrine of *pacta sunt servanda* and, most importantly, contrary to the intention of the parties in entering into the supplemental

agreements.

To reiterate, the applicable law in interpreting and construing the agreements should be the canons of international law, particularly the doctrine of *pacta sunt servanda*. Yet, in affirming the NDs, the COA proposed that the Government negate its accession to the executive agreements without any valid justification. Obviously, this approach should not be adopted. In *Agustin v. Edu*, we stressed that "[i]t is not for this country to repudiate a commitment to which it had pledged its word. The concept of *pacta sunt servanda* stands in the way of such an attitude, which is, moreover, at war with the principle of international morality."

[. . .]

By going against the intention of the parties as to how the cost of man-months should be charged against, as well as the manner of charging items against contingency, and thus affirming the NDs, the COA contravened the Constitution and international law, and thereby gravely abused its discretion amounting to lack or excess of jurisdiction[.][40] (Emphasis supplied, citation omitted)

Following these principles, Government, including COA, must abide by the agreed terms and conditions of the Service Contract, including Section 6.3.

Further, the protection under the nonimpairment clause of the Constitution is strengthened by Presidential Decree No. 87. Section 12(g) of Presidential Decree No. 87 provides that the "[r]ights and obligations in any contract concluded pursuant to this Act shall be deemed as essential considerations for the conclusion thereof and shall not be unilaterally changed or impaired." This is also found in Section 6.2(g) of the Service Contract, which states that the "[r]ights and obligations in this Contract shall be deemed as essential consideration for the conclusion thereof and shall not be unilaterally changed or impaired."

All told, this Court has no reason to disturb the ICC Tribunal's determination of facts and/or interpretation of law. I thus join the ponencia in granting the consolidated Petitions.

[1] Presidential Decree No. 87 (1972), sec. 18(b).

[2] See ponencia, pp. 14-17.

[3] *Lanuza, Jr. v. BF Corporation*, 744 Phil. 612, 631 (2014) [Per J. Leonen, Second Division].

[4] *Eastboard Navigation, Ltd. v. Ysmael and Company, Inc.*, 102 Phil. 1, 16 (1957) [Per J. Bautista Angelo, En Banc].

[5] *LM Power Engineering Corporation v. Capitol Industrial Construction Groups, Inc.*, 447 Phil. 705, 714 (2003) [Per J. Panganiban, Third Division].

[6] *Lanuza, Jr. v. BF Corporation*, 744 Phil. 612, 633 (2014) [Per J. Leonen, Second Division].

[7] *Taisei Shimizu Joint Venture v. Commission on Audit*, 873 Phil. 323, 342 (2020) [Per J. Lazaro-Javier, En Banc]. (Emphasis supplied)

[8] *Id.*

[9] *Id.* at 341.

[10] *Id.* at 341-344.

[11] 914 Phil. 403 (2021) [Per J. Lazaro-Javier, First Division].

- [12] *Id.* at 424-425.
- [13] *Taisei Shimizu Joint Venture v. Commission on Audit*, 873 Phil. 323, 348 (2020) [Per J. Lazaro-Javier, En Banc].
- [14] *Fruehauf Electronics Philippines Corporation v. Technology Electronics Assembly and Management Pacific Corporation*, 800 Phil. 721, 742 (2016) [Per J. Brion, Second Division].
- [15] Special Rules of Court on Alternative Dispute Resolution, A.M. No. 07-11-08-SC (2009), Rule 2.1.
- [16] Special Rules of Court on Alternative Dispute Resolution, A.M. No. 07-11-08-SC (2009), Rule 2.4.
- [17] *Id.*
- [18] 914 Phil. 403, 419-420 (2021) [Per J. Lazaro-Javier, First Division].
- [19] Special Rules of Court on Alternative Dispute Resolution, A.M. No. 07-11-08-SC (2009), Rule 11.9.
- [20] ICC Rules, Rule 34(6).
- [21] See Final Award, par. 124(c).
- [22] See ICC Partial Final Award, pars. 203, 206, and 245.
- [23] See ICC Partial Final Award, pars. 222 and 223.
- [24] 513 Phil. 440 (2005) [Per J. Ynares-Santiago, First Division].
- [25] *Id.* at 450.
- [26] 486 Phil. 754 (2004) [Per J. Panganiban, En Banc].
- [27] *Id.* at 847.
- [28] 810 Phil. 16 (2017) [Per J. Perlas-Bernabe, First Division].
- [29] *Id.* at 26.
- [30] *Id.* at 25-30.
- [31] See Partial Final Award.
- [32] *Banco De Oro Unibank, Inc. v. International Copra Export Corporation*, 901 Phil. 88, 120 (2021) [Per J. Leonen, Third Division].
- [33] *The Provincial Bus Operators Assn. of the Phils. v. DOLE*, 836 Phil. 205, 270 (2018) [Per J. Leonen, En Banc]. (Citation omitted)
- [34] *Siska Development Corp. v. Office of the President of the Phils.*, 301 Phil. 678, 684 (1994) [Per J. Quason, En Banc].
- [35] *The Provincial Bus Operators Assn. of the Phils. v. DOLE*, 836 Phil. 205, 272 (2018) [Per J. Leonen, En Banc].
- [36] *Siska Development Corp. v. Office of the President of the Phils.*, 301 Phil. 678, 684 (1994) [Per J. Quason, En Banc].
- [37] 42 Phil. 702 (1922) [Per J. Johnson, En Banc].

[38] Id. at 717.

[39] 865 Phil. 526 (2019) [Per C.J. Bersamin, En Banc].

[40] Id. at 552-554.

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