

THIRTY-FIRST INFANTRY POST EXCHANGE AND FIRST LIEUTENANT DAVID L. HARDEE, THIRTY-FIRST INFANTRY, UNITED STATES ARMY, PLAINTIFFS, VS. JUAN POSADAS, JR., COLLECTOR OF INTERNAL REV...

G.R. No. 33403. September 04, 1930

Ponente: MALCOLM, J.

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MALCOLM, J.:

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The question involved in these original proceedings of prohibition is whether a tax may be levied by the Government of the Philippine Islands on sales made by merchants to Post Exchanges of the United States Army in the Philippines. The point of jurisdiction of this court has not been raised by the Attorney-General in representation of the defendant, and We do not propose to be supercritical in this respect.

The parties have submitted the case on the following agreed statement of facts:

"1. The plaintiff, Thirty-first Infantry Post Exchange, is now and for all the times material to this suit has been constituted as a post exchange in accordance with the Army Regulations (of which the court may take judicial notice) and the laws of the United States, with its place of business in the Cuartel de España in the City of Manila, P. I. It is an agency within the United States Army, under the control of the officers of the Army. It is recognized and authorized in general terms by the Congress of the United States in various enactments. First Lieutenant David L. Hardee, Thirty-first Infantry, whose residence is in the City of Manila, P. I., is the duly appointed and acting Exchange Officer of said exchange, and is charged with the immediate conduct and management of the business of said plaintiff Exchange. The defendant, Juan Posadas, Jr., is the duly qualified and acting Collector of Internal Revenue of the Philippine Islands, with office and residence in the City of Manila, P. I.

"2. The said plaintiff Exchange is designed for the accommodation, convenience, and assistance of the personnel of the Army. All of the goods sold to and purchased by the said plaintiff Exchange are intended for resale to and are in fact resold, as they have been in the past, to the officers, soldiers and the civilian employees of the Army, and their families. The goods sold to and purchased by the said plaintiff Exchange have consisted and do consist! largely of sundry articles for personal use, such as soaps, shaving materials, and other toilet articles, and other goods generally found in a well-stocked general store. Such purchases and resales, though fully authorized by law and the Army Regulations, are not specifically required by statutory enactment. The net proceeds derived from all such resales do not accrue to the general funds of the United States, that is, they are not deposited in the Treasury of the United States, but are used for the betterment of the condition of the enlisted personnel of the Army, to the end that thereby the morale and efficiency of the armed forces of the United States may be improved and increased.

"3. In the course of its duly authorized business transactions, the said plaintiff Exchange, under the direction of the said plaintiff David L. Hardee, as Exchange Officer, and his predecessors in that office, has, during the period of several years last past, made many purchases of various and divers commodities, goods, wares, and merchandise from various and divers merchants in the Philippine Islands, and is continuing to do so, and like purchases, by the said plaintiff Exchange from merchants in the Philippine Islands are intended and contemplated as necessary in the conduct of its duly authorized business.

"4. Following many and divers of the aforesaid purchases by the said plaintiff Exchange, the defendant, Juan Posadas, jr., Collector of Internal Revenue of the Philippine Islands, and his predecessors in that office, have collected from the merchants who made the sales of the commodities, goods, wares, and merchandise to the plaintiff Exchange, taxes at the rate of one and one-half per centum on the gross value in money of the commodities, goods, wares, and merchandise, sold by them to the plaintiff Exchange, and based on the actual prices at which the sales were made, and the average amount of money per annum for several years last past demanded and collected by the defendant and his predecessors in office as such taxes on the aforesaid sales to the plaintiff Exchange has been several thousand pesos, averaging more than two thousand pesos per annum since January 1, 1927.

"5. The defendant persists in demanding and collecting such taxes and at the said rates on the sales of commodities, goods, wares, and merchandise which are being effected by merchants in the Philippine Islands to the plaintiff Exchange. He intends and expects to continue to demand and collect such taxes and at said rates on sales of commodities, goods, wares, and merchandise sold by merchants in the Philippine Islands to plaintiff Exchange, and all other Army post exchanges in the Philippine Islands, unless certain statutes of the Philippine Islands and of the United States in respect thereof shall be modified or repealed, or he be restrained and prohibited therefrom by judgment of the proper tribunal. The statutes upon which the defendant relies as his authority for such demand and collection of taxes, particularly, are section 1459 of Act No. 2711, and Act No. 3243 of the public laws enacted by the Philippine Legislature; also the Act of June 4, 1918 (40 Stat., 597) and the Act of March 3, 1927 (44 Stat., 1390), enacted by the Congress of the United States, ratifying the said two enactments of the Philippine Legislature.

"6. The effect of the demand and collection of taxes by the defendant on the sales of such commodities, goods, wares and merchandise thus sold to and bought by the plaintiff Exchange has been, is, and in the future will be unless the defendant be commanded to desist and refrain from such demand and collection, to increase the cost thereof to the plaintiff Exchange, by at least the amounts of such taxes demanded and collected as aforesaid in each instance."

What is known as the sales tax is in force in the Philippines. A percentage tax of 1 per centum is collected on merchants' sales. (Administrative Code, sec. 1459; Act No. 3243.) The taxes imposed by the Philippine Legislature in said section 1459 and in Act No. 3243 have by Acts of Congress been "legalized and ratified, and the collection of all such taxes * * * legalized, ratified, and confirmed to all intents and purposes as if the same had by prior Act of Congress been specifically authorized and directed." (Acts of Congress of June 4, 1918, and March 3, 1927, 40 Stat. L., 597, and 44 Stat. L., 1390.) Philippine law as thus enacted and expressly confirmed by the Congress, makes particular mention of the persons exempt from this tax, without, however, including in the enumeration commercial transactions with Army Post Exchanges. On the other hand, our general law provides express exemptions from other taxes for the United States and its agencies. (Administrative Code, secs. 344, 1418, 1439, 1449 [s], 1450, 1474, and 1478.)

Taxes have been collected from merchants who make sales to Army Post Exchanges since 1904. (Act No. 1189, sec. 139.) Similar taxes are paid by those who sell merchandise to the Philippine Government through the Bureau of Supply (Ruling, Bureau of Internal Revenue, March 5, 1925, and prior precedents), and we likewise assume, by those who do business with the United States Army and Navy in the Philippines. Only in the case at bar has

formal legal protest been made.

In 1916, the case of *Walter E. Olsen & Co. vs. Rafferty* ([1919], 39 Phil., 464), pertaining to the payment of specific taxes by Army Post Exchanges, arose. The revenue laws at that time, as they do now, provided that "no specific tax shall be collected on any articles sold and delivered directly to the United States Army or Navy for actual use or issue by the Army or Navy, and any taxes which have been paid on articles so sold and delivered for such use or issue shall be refunded upon such sale and delivery, * * *." Although in this case passing reference was made in the court below and in appellant's brief to some of the larger constitutional aspects, the Supreme Court confined its decision to determining whether or not merchandise, which is generally subject to the payment of internal revenue tax, is relieved from said tax when it is sold to the Army or Navy of the United States for resale to individuals by means or through the post exchanges or ship's stores. The court, in resolving against the contention of the plaintiff merchant, said:

"While 'post exchanges' and 'ship's stores' are institutions within the Army and Navy of the United States, and are recognized by Acts of Congress, and are under the control of the Army and Navy, and are organized for the convenience and assistance of the soldiers and sailors, we are not inclined to believe that goods sold to the soldiers and sailors of the Army and Navy, even though they be sold through said exchanges by the intervention of officers of the Army and Navy, are goods sold directly to the United States Army or Navy for actual use or issue by the Army or Navy. They are goods sold for the use and benefit of the post exchanges, etc., and not for the actual use or issue by the Army or Navy. We do not believe that the exemption provided for in the above-quoted section applies to goods sold to the United States Army and Navy to be resold to the individuals of said organization. The money used for the purchase of merchandise sold through the post exchanges, etc., is not supplied by, nor for, the United States Army and Navy. Neither does the money received in the resale of such merchandise through the post exchanges, etc., become a part of the general funds of the Army and Navy. In our opinion, the sale of merchandise through the post exchanges to the individuals of the United States Army and Navy are not goods sold and delivered directly to the United States Army or Navy for the actual use or issue by the Army or Navy and are therefore, not exempt from the payment of the internal revenue tax imposed by the law." (Italics those of court.)

The laws to be applied are, in effect, Acts of the Congress of the United States, and so form a part of Philippine Organic Law. (*Mitsui Bussan Kaisha vs. Manila E. R. R. & L. Co.* [1919], 39 Phil., 624.) We do not wish to be guilty of overstating the proper principle, but it would seem that since no law of the Congress forbids the taxation of merchants who deal with Army Post Exchanges, and since the Congress has legalized the applicable law, and in doing so has granted no immunity from taxation to merchants who deal with Army Post Exchanges, the Congress has permitted such transactions with Army Post Exchanges, on the assumption that Post Exchanges are agencies of the United States, to be taxed by the Philippine Government. It must be understood, however, that the waiver must be clear, and that every well grounded doubt should be resolved in favor of the exemption. (*Austin vs. Aldermen of Boston* [1869], 7 Wall, 694.)

As to the facts, the nature of Army Post Exchanges is explained in the stipulation of facts and in the case of *Walter E. Olsen & Co. vs. Rafferty*, supra. In addition, it might be advisable to state that the construction, equipment, and maintenance of post exchange buildings are provided for by appropriation Acts of the Congress. The Court of Claims in holding an officer in charge of a post exchange not a retail dealer in liquors, said that post exchanges "though conducted without financial liability to the Government, are, in their creation and management, governmental agencies * * *." (*Dugan 'vs. U. S.* [1899], 34 Court of Claims, 458.) The Judge Advocate General has said that "a post exchange is a voluntary unincorporated cooperative association of Army organizations, a kind of cooperative store, in which all share in the benefits and all assume a position analogous to that of partners." (Opinion, J. A. G., June 4, 1918v) Again, although we do not desire to overstate the matter, the rule is that whenever a state engages in a business which is of a private nature, that business is not withdrawn

from the taxing power of the Nation, or, conversely stated, whenever the National Government permits an organization under its control to engage in a business which is of a private nature, that business is not withdrawn from the taxing power of the state. (*South Carolina vs. U. S.* [1905], 199 U. S., 437.)

The plaintiffs in this case are the Thirty-first Infantry Post Exchange and the Exchange Officer of that Exchange. But the stipulation of facts concedes that it is the merchants who effect the sales to the Post Exchange who pay the tax. And it is the officers, soldiers, and civilian employees and their families who are benefited by the post exchange to whom the tax is ultimately shifted. Justice Holmes of the Supreme Court of the United States had quite similar facts in mind when in his dissenting opinion in the case of *Panhandle Oil Co. vs. Knox* ([1928], 277 U. S.f 218), he said: "If the plaintiff in error had paid the tax and had added it to the price, the Government would have had nothing to say." Here, it must again be stated that it is not the vendors of merchandise who are protesting, but it is the Army Post Exchange which is the complainant.

The foregoing might be sufficient to dispose of the case. However, we would not like to be charged with dodging the more vital issues, and so will take under view the larger constitutional aspects of the question.

Chief Justice Marshall was originally responsible for the rule that without Congressional consent, no Federal agency or instrumentality can be taxed by state authority. (*McCulloch vs. State of Maryland* [1819], 4 Wheat., 316; *Jaybird Mining Co. vs. Weir* [1926], 271 XL S., 609.) Naturally, in the course of time, attempts have been made to extend the exemption from state taxation, established by the case of *McCulloch vs. State of Maryland*, supra, beyond its terms. Only those agencies through which the Federal Government immediately and directly exercises its sovereign powers are immune from the taxing power of the states. The reason upon which the rule rests must be the guiding principle to control its operation. The limitations upon the taxing power of the state must receive a practical construction which does not seriously impair the taxing power of the Government imposing the tax. The effect of the tax upon the functions of the Government and the nature of the governmental agency determine finally the extent of the exemption. (*Metcalf vs. Mitchell* [1926], 269 U. S., 514; *Thomson vs. Union Pacific Railroad Co.* [1869], 9 Wall., 579.)

It would be impracticable to point out all of the limitations to the general rule, but a few may be noted. Thus in the well considered decision in *Union Pacific Railroad Co. vs. Peniston* ([1873], 18 Wall., 5), it was said: "It cannot be that a state tax which remotely affects the efficient exercise of a federal, power is for that reason alone inhibited by the Constitution." Again, with more direct application, although contained in a dissenting opinion, Justice Thompson, in *Weston vs. City Council of Charleston* ([1829], 2 Pet., 449), said: "The unqualified proposition that a State cannot directly or indirectly tax any instrument or means employed by the general government in the execution of its power, cannot be literally sustained. Congress has power to raise armies, such armies are made up of officers and soldiers, and are instruments employed by the government in executing its powers; and although the army, as such, cannot be taxed, yet it will not be claimed that all such officers and soldiers are exempt- from State taxation." The United States Supreme Court has held that the use of machinery and boats in the harbor of San Juan, Porto Rico, in the performance of a dredging contract with the United States, does not exempt them from local taxation. (*Gromer vs. Standard Dredging Co.* [1911], 224 U. S., 362.)

It has been contended during the course of our deliberations that, all other questions to one side, the case is governed by the comparatively recent decision of the Supreme Court of the United States in the case of *Panhandle Oil Co. vs. Knox*, supra. There it was held by a closely divided court that (1) A state tax imposed on dealers in gasoline for the privilege of selling,, and measured at so many cents per gallon of gasoline sold, is void under the Federal Constitution as applied to sales to instrumentalities of the United States, such as the Coast Guard Fleet and a Veterans' Hospital; (2) that the substance and legal effect is to tax the sale, and thus burden and tax the United States, exacting tribute on its transactions for the support of the State; and (3) that such an exaction

infringes the right of the dealer to have the constitutional independence of the United States in respect of such purchases remain untrammelled. With all due deference to the pronouncements of the higher court which we are bound to abide by, we are yet convinced that the cited case is not controlling. We will point out some of the differences between the two cases. There the plaintiff in error was a private oil company which had been sued by the state to recover taxes; here the plaintiffs are not the private individuals who paid the taxes but are an Army Post Exchange and its Exchange Officer. There the law in question was an Act of the State Legislature; here the laws in question are Acts of the Philippine Legislature which have been ratified by the Congress of the United States and raised to the level of organic laws. There the right of the United States to make purchases was derived from the United States' Constitution'; here the right of the Army Post Exchange to make purchases is derived from Army regulations and Army practice. There the sale was made to instrumentalities authorized by the constitution, which consumed the merchandise; here the sales were made to Army Post Exchanges not so constitutionally authorized, which merely acted as intermediaries. There it must be taken for granted that the Coast Guard Fleet and the Veterans' Hospital were constructed and operated by Government funds; here, except that buildings are provided by the United States Government for the Army Post Exchanges, the latter are not so constructed and operated. .

The majority decision in the *Panhandle Oil* case carries the Marshallian theory of national supremacy just about to its extreme limits. We do not think that "the present case falls within those limits. When a merchant sells a case of hair pins to an Army post exchange, and the wife of an Army officer purchases a package of those hair pins, and when a merchant sells a quantity of tobacco to an Army post exchange, and a soldier provides himself with his tobacco; and when the merchants who perfect the sales make good the required taxes, "the exertion of national power" is not so burdened or interfered with, and "the exactions demanded" do not so infringe the constitutional independence of the United States as to exempt the sales from taxation, which every one else, including the merchant who sells to the Philippine Government, must pay. That is our understanding of the authorities and of the law.

There can exist no measure of doubt that the basic rule, together with its qualifications, applies not only to the States of the American Union, but also to unincorporated territories with, the status of the Government of the Philippine Islands.

Placing some emphasis on the point of long acquiescence in the imposition of the sales tax on vendors of merchandise to Army Post Exchanges; on the point that the Congress of the United States has virtually sanctioned such a sales tax by confirming Philippine revenue laws without reservation ; and on the point that a kind of cooperative store in the Army is akin to a private business enterprise which is not withdrawn from taxation, we desire with more emphasis to indicate the lack of standing of the plaintiffs to contest the tax. On still broader grounds, we would consider the effect's of the sales tax upon the United States Army, and the nature of an Army Post Exchange. The tax laid upon Philippine merchants who sell to Army Post Exchanges does; not interfere with the supremacy of the United States Government, or with the operations of its instrumentality, the United States Army, to such an extent or in^ such a manner as to render the tax illegal. The tax does not deprive the Army of the power to serve the Government as it was intended to serve it, or hinder the efficient exercise of its power. We rule that an Army Post Exchange, although an agency within the United States Army, cannot secure exemption from taxation for merchants who make sales to the Post Exchange. The question must, therefore, be answered in the affirmative. The plaintiffs have not made out a case.

Wherefore, the complaint will be dismissed, with costs.

Avanceña, C. J., Street, Villamor, Romualdez and Villa-Real, JJ., concur.

DISSENTING

Johns, J., with whom concurs Ostrand, J.:

This case was tried and submitted upon a stipulation of facts, from which it appears that the plaintiff is a post exchange operated under Army Regulations, of which the courts take judicial notice, and the laws of the United States, with its place of business in the City of Manila.

"It is an agency within the United States Army, under the control of the officers of the Army. It is recognized and authorized in general terms by the Congress of the United States in various enactments." First Lieutenant Hardee "is its duly appointed and acting Exchange Officer, and is charged with the immediate conduct and management of its business."

"2. The said plaintiff Exchange is designed for the accommodation, convenience, and assistance of the personnel of the Army. All of the goods sold to and purchased by the said plaintiff Exchange are intended for resale to and' are in fact resold, as they have been iii the past, to the officers, soldiers and the civilian employees of the Army, and their families. * * * Such purchases and resales, though fully authorized by law and the Army Regulations, are not specifically required by statutory enactment. The net proceeds derived from all such resales do not accrue to the general funds of the United States, that is, they are not deposited in the Treasury of the United States, but are used for the betterment of the condition of the enlisted personnel of the Army, to the end that thereby the morale and efficiency of the armed forces of the United States may be improved and increased.

"3. In the course of its duly authorized business transactions, the said plaintiff Exchange, under the direction of the said plaintiff David L. Hardee, as Exchange Officer, and his predecessors in that office, has, during the period of several years! last past, made many purchases of various and divers commodities, goods, wares, and merchandise from various and divers merchants in the Philippine Islands, and is continuing to do so, and like purchases by the said plaintiff Exchange from merchants in the Philippine Islands are intended and contemplated as necessary in the conduct of its duly authorized business.

* * * * *

"6. The effect of the demand and collection of taxes by the defendant on the sales of such commodities, goods, wares, and merchandise thus sold to and bought by the plaintiff Exchange has been, is, and in the future will be unless the defendant be commanded to desist and refrain from such demand and collection, to increase the cost thereof to the plaintiff Exchange, by at least the amounts of such taxes demanded and collected as aforesaid in each instance." . Army Regulations are prescribed by the Secretary of War, under section 161 of the Revised Statutes, and have the force of law when they do not contravene statute law. When Congress permits regulations to be promulgated and published and carried into effect year after year, legislative ratification must be implied. (Maddux vs. United States, 20 Court of Claims, 193, 198), and in Chattamal vs. Collector of Customs (42 Phil., 916-919), this court said that it would take judicial notice of Army Regulations. Congress in every annual appropriation since June 30, 1902, has made an appropriation "For the construction, equipment and maintenance of suitable buildings at military posts and stations for the conduct of post exchange, school, library, reading, lunch and amusement rooms."

In Dugan vs. United States, supra, at page 467 of the opinion, it is said that Army post exchanges, in their creation and management, are "governmental agencies."

In Post Exchange, 31st Infantry, vs. Kinney, G. R. No. 30920, [1]in speaking of them, this court said:

"While they are in a sense associations of military organizations for business purposes, they are simply governmental agencies or instrumentalities expressly recognized by Congress in the annual appropriation acts,

and are designed to carry out a governmental purpose. (Dugan vs. U. S., 34 Court of Claims, 458.)"

Hence, we have a post exchange established and operated under Army Rules and Regulations empowered and authorized to buy and sell its goods, wares, and merchandise to the personnel of the Army, and the question is squarely presented as to whether or not it is liable for the payment of the sales tax provided for by section 1459 of Act No. 2711 and Act No. 3248 of the Public Laws enacted by the Philippine Legislature, as such laws are ratified by the Congress of the United States. It will be noted that in neither section 1459 of Act No. 2711 nor Act No. 3243 or either act of Congress is there any reference to sales made to the United States or any of its instrumentalities, and it must be conceded that no State of the Union has the power to levy taxes upon property of the United States or its instrumentalities without the consent of Congress.

Plaintiffs contend that if the Philippine Legislature intended that the tax in question should apply to the sales made to the United States or its instrumentalities, they are void as against the Constitution, citing 37 Cyc., p. 865, which says:

"The United States has no authority to tax the property of a state, nor a state to extract revenue from the property of the federal government, and from the nature of the case neither government will lay taxes upon its own property. Hence as a general rule all public property is exempt from taxation, either by express exemption or by necessary implication, including not only the property of the state itself, but also the public property of its political subdivisions, such as counties and municipal corporations. While in the absence of Constitutional-prohibition the state may include in its scheme of taxation such property of its own or of its municipal subdivisions, the presumption is always against an intention to do so, and such property is impliedly exempt unless an intention to include it is clearly manifested."

As we construe the stipulation of facts and the Army Rules and Regulations, the United States has created and operates the Army post exchange as an instrumentality for the carrying out of its functions in the exercise of its constitutional powers "To raise and support armies," and "To make all laws which shall be necessary for carrying into execution the foregoing powers."

It is stipulated that the plaintiff exchange "is designed for the accommodation, convenience, and assistance of the personnel of the Army," and that the net proceeds of all such resales "are used for the betterment of the condition of the enlisted personnel of the Army, to the end that thereby the morale and efficiency of the armed forces of the United States may be improved and increased." In other words, it is agreed that the post exchange is established and operated under Army Rules and Regulations designed for the accommodation, convenience, and assistance of the personnel of the Army "to the end that thereby the morale and efficiency of the armed forces of the United States may be improved and increased," and yet in the exercise, of that right post exchanges in the Philippine Islands are required to pay a sales tax to the local government, the effect of which under paragraph 6 of the stipulation of facts is "To increase the cost thereof to the plaintiff Exchange, by at least the amounts of such taxes demanded and collected as aforesaid." In other words, for the privilege of operating a post exchange must pay a sales tax to the Government of the Philippine Islands.

In the case of *Panhandle Oil Company vs. State of Mississippi* (72 Law. ed., 857), the syllabus says:

"1. States may not burden or interfere with the exertion of national power or make it a source of revenue or take the funds raised or tax the means used for the performance of Federal functions.

"2. A state may not impose a tax measured by the quantity sold upon the privilege of one of its citizens of selling gasoline to the Federal government for use of its Coast Guard Fleet or Veterans' Hospital which the United States is empowered by the Constitution to maintain and operate."

And in the opinion, it is said:

"The validity of the taxes claimed is to be determined by the practical effect of enforcement in respect of sales of the government. (Wagner vs. Covington, 251 U. S., 95, 102; 64 L. ed., 157, 167; 40 Sup. Ct. Rep., 93.) A charge at the prescribed rate is made on account of every gallon acquired by the United States. It is immaterial that the seller and not the purchaser is required to report and make payment to the state. Sale and purchase constitute a transaction by which the tax is measured, and on which the burden rests. The amount of money claimed by the state rises and falls precisely as does the quantity of gasoline so secured by the Government. It depends immediately upon the number of gallons. The necessary operation of these enactments when so construed is directly to retard, impede and burden the exertion by the United States, of its constitutional powers to operate the fleet and hospital."

It is true that decision was rendered by a divided court, but it is also true that the majority opinion is the law of that court, and upon the stipulation of facts it would seem to apply to this case, and hence should be followed by this court.

In the final Analysis, you have this situation. The United States at its own expense maintains an army in the Philippine Islands. Under long established rules and regulations, and as incidental to and as a part of it, the United States Army maintains and operates its post exchanges, one of which is the plaintiff, to improve and promote "the morale and efficiency of the armed forces of the United States,"

Why then should the plaintiff be required to pay a sales tax to promote "the morale and efficiency" of the personnel of the Army? Yet, in the final analysis, that is the legal effect of the majority opinion. It would seem on principle that where the United States at its own expense maintains an army in the Philippine Islands, and under Army Rules and Regulations has established and operates a post exchange, to improve the "morale and efficiency" of its members, that the personnel of the Army which affords that protection should be exempt from the payment of the sales tax to the Philippine Government which does not pay a centavo for such protection.

The writ should be granted, and we dissent.

[1] Promulgated August 28, 1929, not reported.

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