

Republic of the Philippines
COURT OF TAX APPEALS
Quezon City

SPECIAL SECOND DIVISION

**ENERGY DEVELOPMENT
CORPORATION, (represented
by its Senior Vice President
Chief Finance Officer,
NESTOR H. VASAY),**
Petitioner,

CTA AC. NO. 90
For: Assessment

-versus-

Members:
CASTAÑEDA, JR., Chairperson
CASANOVA, and
MINDARO-GRULLA, JJ.

**SORSOGON CITY and HON.
ROBERTO D. DOOC, City
Treasurer (Officer-in-Charge),
SORSOGON CITY,**
Respondent.

Promulgated:

MAY 14 2013

x-----x
2:55 p.m.

D E C I S I O N

MINDARO-GRULLA, J.:

This is an appeal by way of Petition for Review pursuant to Sections 11 and 7(a)(3) of Republic Act (RA) No. 1125, as amended by RA No. 9282, in relation to Section 3(a)(3), Rule 4 of the Revised Rules of the Court of Tax Appeals (RRCTA).

The instant Petition seeks to reverse and set aside the Decision dated December 26, 2011 and the Resolution dated February 21, 2012 issued by the Regional Trial Court (RTC), Branch 53, Fifth Judicial Region, Sorsogon City, in Civil Case No. 2011-8255 entitled "ENERGY DEVELOPMENT CORPORATION (EDC), as represented herein by its Senior Vice-President and Chief Finance Officer, NESTOR H. VASAY vs. SORSOGON CITY and HON. ROBERTO D. DOOC, City

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Treasurer (Officer-in-Charge), Sorsogon City". The assailed Decision and Resolution dismissed the appeal of petitioner Energy Development Corporation, and thus, effectively affirmed the assessment made by respondent Sorsogon City, through the Office of the City Treasurer, for franchise tax against petitioner in connection with the latter's operation of the BacMan I Geothermal Plant ("Geothermal Plant" for brevity).

Petitioner Energy Development Corporation (EDC) is a private domestic corporation duly organized and existing under and by virtue of the laws of the Republic of the Philippines, with principal place of business located at the 38th Floor, One Corporate Center Building, Julia Vargas corner Meralco Avenue, Ortigas Center, Pasig City, Metro Manila. It is represented herein by its Senior Vice-President and Chief Finance Officer, Mr. Nestor H. Vasay.¹

Respondent Sorsogon City is a city situated in the Province of Sorsogon; while respondent Roberto D. Dooc represents Sorsogon City as its City Treasurer (Officer-in-Charge), with office address at the Office of the Sorsogon City Treasurer, City Government of Sorsogon, Cabid-an, Sorsogon City, Province of Sorsogon.²

Petitioner is engaged in the exploration, exploitation and development of geothermal resources through its BacMan Geothermal Production Fields ("Steamfields" for brevity) located within the Geothermal Plant, a portion of which is situated within the Municipality of Manito, Province of Albay, while another portion is located within the Municipality of Castilla and Sorsogon City; both within the Province of Sorsogon.³

Petitioner's right to conduct said exploration, exploitation and development activities is by virtue of

¹ Par. 11, The Parties, Petition for Review, Docket, pp. 4 to 5.

² Par. 12, id., p. 5.

³ Par. 13, Statement of Facts, id., p. 5.

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Service Contract (Geothermal Resources) No. 3⁴ dated October 16, 1981 ("Geothermal Service Contract" for brevity) and executed in accordance with and pursuant to Section 1 of Presidential Decree (PD) No. 1442⁵ by and between petitioner⁶ and the Department of Energy (DOE) [through its predecessor-in-interest, the Bureau of Energy Development], representing the Government of the Republic of the Philippines.⁷

On October 23, 2009, the "Geothermal Service Contract" was converted into the Geothermal Renewable Energy Service Contract No. 2009-10-003 Bacon-Manito, Albay-Sorsogon⁸ ("Geothermal RE Service Contract" for brevity) by and between petitioner and DOE, in accordance with RA No. 9513.⁹ Petitioner had been selling to National Power Corporation (NPC) the geothermal steam produced from its operation of the Steamfields by virtue of the Bacon-Manito Sales Contract for Geothermal Resources dated November 18, 1988 ("Sales Contract" for brevity) entered into between petitioner and NPC. Under the Sales Contract, NPC, within the same location, built the power plants that generated electricity from the geothermal steam produced by the Steamfields. NPC's power plants were later sold by the Power Sector Assets and Liabilities Management to BacMan Geothermal Inc., but said power plants have not been in operation since then.¹⁰

On August 11, 2010, petitioner received a Notice of Assessment¹¹ dated July 26, 2010 from respondents, demanding payment of franchise tax in the amount of Three Million Seven Hundred Eleven Thousand Seven Hundred Forty-Two Pesos and 66/100 (₱3,711,742.66) pursuant to Section 28, Chapter IV of Sorsogon City Revenue Code.¹² **C**

⁴ Exhibit "G" and Exhibit "5", RTC Records, pp. 82-133.

⁵ An Act to Promote the Exploration and Development of Geothermal Resources.

⁶ Then known as the Philippine National Oil Corporation-Energy Development Corporation

⁷ Par. 14, Statement of Facts, Petition for Review, Docket, pp. 5 to 6.

⁸ Exhibit "F" and Exhibit "6", RTC Records, p. 134.

⁹ Renewable Energy Act of 2008.

¹⁰ Decision, RTC Records, p. 227.

¹¹ Exhibit "D" and Exhibit "2", RTC Records, pp. 142.

¹² Par. 15, Statement of Facts, Petition for Review, Docket, pp. 6 to 7.

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On October 8, 2010, petitioner filed a Protest Letter¹³ dated October 7, 2010 with respondents pursuant to Section 195 of RA No. 7160 or the Local Government Code (LGC), protesting the assessment of deficiency franchise tax on the ground, among others, that petitioner is not liable to pay franchise tax to Sorsogon City because petitioner does not have a franchise as contemplated under the LGC.

Respondents failed to resolve petitioner's protest within the sixty-day period provided under Section 195¹⁴ of the LGC; hence, petitioner filed a Petition with the RTC of Sorsogon on January 6, 2011,¹⁵ which was docketed as Civil Case No. 2011-8255. In said Petition, petitioner prayed that the Notice of Assessment issued by respondents be nullified and set aside for lack of legal and factual basis and for being contrary to law.¹⁶

On February 4, 2011, respondents filed their Answer¹⁷ stating, among others, that respondents are without knowledge or information to form a belief as to the truth of the averments made in paragraph 10 of petitioner's Petition insofar as the Service Contract executed by and between petitioner and the DOE, as there was no such evidence exhibited that the same is true and existing. Furthermore, respondents opposed petitioner's allegations that it has no franchise and that it is exempted from the payment of franchise tax. Thus, respondents prayed that the Petition be

¹³ Exhibit "E", RTC Records, pp. 30 to 42.

¹⁴ Sec. 195. *Protest of Assessment*. – When the local treasurer or his duly authorized representative finds that the correct taxes, fees, or charges have not been paid, he shall issue a notice of assessment stating the nature of the tax, fee, or charge, the amount of deficiency, the surcharges, interests and penalties. Within sixty (60) days from the receipt of the notice of assessment, the taxpayer may file a written protest with the local treasurer contesting the assessment; otherwise, the assessment shall become final and executory. The local treasurer shall decide the protest to be wholly or partly meritorious, he shall issue a notice cancelling wholly or partially the assessment. However, if the local treasurer finds the assessment to be wholly or partly correct, he shall deny the protest wholly or partly with notice to the taxpayer. The taxpayer shall have thirty (30) days from the receipt of the denial of the protest or from the lapse of the sixty-day (60) period prescribed herein within which to appeal with the court of competent jurisdiction, otherwise the assessment becomes conclusive and unappealable.

¹⁵ Petition, RTC Records, pp. 1 to 21.

¹⁶ Prayer, Petition, RTC Records, p. 20.

¹⁷ RTC Records, pp. 56 to 63.

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dismissed and that petitioner be ordered to pay the franchise tax based on the assessment of the City Treasurer, including penalties, interest and surcharges.

On February 28, 2011, petitioner filed its Reply,¹⁸ controverting and refuting respondents' allegations in their Answer and praying that the Notice of Assessment issued by respondents be nullified and set aside for lack of legal and factual basis and for being contrary to law.

On April 7, 2011, a Preliminary Conference was held for purposes of marking petitioner's exhibits or documentary evidence.¹⁹ On the other hand, a Preliminary Conference was held on May 26, 2011 for the marking of respondents' exhibits or documentary evidence.²⁰

On July 5, 2011, petitioner submitted a Request for Admission²¹ dated June 27, 2011 addressed to Hon. Leovic R. Dioneda, Office of the City Mayor, City Government of Sorsogon and Hon. Roberto D. Dooc, Office of the City Treasurer, City Government of Sorsogon in accordance with Sections 1 and 2, Rule 26 of the Rules of Court.

During the scheduled Pre-trial Conference held on July 14, 2011 at the RTC of Sorsogon, counsel for petitioner manifested to the Court that he had availed of the mode of discovery procedure and the Public Prosecutor is still in the process of making a reply thereto. The Court advised the parties to consider the filing of a Motion for Summary Judgment or a judgment on the pleadings considering that there are no genuine issues as to any material fact and that the issues to be passed upon are purely legal in nature. Since the counsels for both parties were receptive to the suggestion of the RTC of Sorsogon, petitioner was given ten (10) days from receipt of the Order within which to file the necessary pleading. Respondents were also given the same

¹⁸ RTC Records, pp. 68 to 81.

¹⁹ Minutes of the April 7, 2011 Preliminary Conference, RTC Records, pp. 180 to 181.

²⁰ Minutes of the May 26, 2011 Preliminary Conference, *id.*, pp. 182 to 183.

²¹ *Id.*, pp. 160 to 164.

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period from receipt of the necessary pleading from petitioner within which to file their comment or opposition. The RTC of Sorsogon reset the pre-trial of the case to September 1, 2011,²² which was again reset to October 6, 2011.²³

On August 23, 2011, petitioner filed a Motion for Judgment on the Pleadings and/or Summary Judgment dated August 15, 2011.²⁴ Respondents, on the other hand, opted not to file a comment or opposition on the motion. In a Resolution²⁵ dated October 3, 2011, the RTC of Sorsogon found that the primary and only matter which needed to be resolved is the determination of whether or not petitioner is enjoying a franchise which will make it liable for franchise tax and that since there is no genuine issue that had to be resolved in a contentious manner, the RTC of Sorsogon held that the case calls for a judgment on the pleadings under Rule 34 of the Rules of Court. Consequently, the RTC of Sorsogon gave due course to petitioner's motion and submitted the case for decision.

On December 26, 2011, the RTC of Sorsogon rendered the assailed Decision²⁶ dismissing petitioner's appeal. The dispositive portion of the said Decision is quoted hereunder:

"WHEREFORE, premises considered, judgment is hereby rendered DISMISSING the instant appeal.

SO ORDERED."²⁷

On January 18, 2012, respondents filed an Ex-Parte Motion for Clarificatory Judgment,²⁸ praying that the RTC of Sorsogon would clarify its decision and include an Order to petitioner to pay the franchise tax based on the assessment made by respondents, including penalties, interest and

²² Order dated July 14, 2011, RTC Records, p. 184.

²³ Notice of Pre-Trial, RTC Records, p. 199.

²⁴ RTC Records, pp. 206 to 221.

²⁵ RTC Records, pp. 224 to 225.

²⁶ *Id.*, pp. 227 to 234.

²⁷ *Id.*, p. 234.

²⁸ *Id.*, pp. 236 to 238.

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surcharges. In an Order²⁹ dated January 20, 2012, the RTC of Sorsogon denied respondents' Motion for non-compliance with the requirements set forth under Section 5, Rule 15 of the Rules of Court.

Petitioner received its copy of the Decision dated December 26, 2011 on January 10, 2012.³⁰ On January 25, 2012, petitioner filed by registered mail, an Urgent Motion for Reconsideration of the Decision dated December 26, 2011.³¹ In a hearing held on February 3, 2012, the RTC of Sorsogon gave respondents a period of fifteen (15) days from said date within which to file their Comment and/or Opposition to petitioner's Urgent Motion for Reconsideration; while petitioner was given a period of ten (10) days from receipt of said Comment within which to file its Reply thereto.³² In a Resolution dated February 21, 2012, the RTC of Sorsogon denied petitioner's Urgent Motion for Reconsideration.³³ Petitioner received said Resolution on February 28, 2012.³⁴

On March 28, 2012, petitioner filed the instant Petition for Review³⁵ (with Application for Suspension of Collection of Tax) and prayed that after due consideration, this Court would issue the following orders:³⁶

"1. Granting the issuance of a Suspension Order/Temporary Restraining Order and Writ of Preliminary Injunction ordering Respondent and/or the Regional Trial Court to maintain the status quo of Civil Case No. 2010-8255 [sic], and suspending/restraining the collection of the franchise tax relative to the RTC Decision, pending resolution by the Honorable Court of the instant Petition for Review;

²⁹ *Id.*, p. 239.

³⁰ Return Card, Mail No. 49 (attached at the back of the Notice of Judgement, RTC Records, p. 226).

³¹ *Id.*, pp. 277 to 307.

³² Order dated February 3, 2012, RTC Records, p. 308.

³³ RTC Records, p. 310.

³⁴ Return Card, Mail. No. 1196 (attached at the back of the Resolution dated February 21, 2012, RTC Records, p. 310).

³⁵ Petition for Review, Docket, pp. 2 to 39.

³⁶ *Id.*, p. 38.

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2. Granting the instant Petition for Review, thereby: (i) reversing and setting aside the RTC Decision dated 26 December 2011 and RTC Resolution dated 21 February 2012 in Civil Case No. 2010-8255 [sic] in their entirety; and (ii) setting aside and nullifying the Notice of Assessment of franchise tax addressed to Petitioner dated 26 July 2010 issued by the Office of the City Treasurer of Sorsogon, through the City Treasurer, for lack of legal and factual basis, and for being contrary to law.”

In a Resolution ³⁷ dated April 11, 2012, without necessarily giving due course to the Petition for Review, this Court ordered respondents to file their Comment within ten (10) days from notice and stated that petitioner may file its Reply thereto within five (5) days from receipt of respondents’ Comment.

Respondents filed their Comments/Opposition to Petitioner’s Petition for Review³⁸ on May 8, 2012 and prayed that the instant Petition for Review be denied for lack of merit.

Petitioner filed its Reply³⁹ to respondents’ Comments/Opposition to Petitioner’s Petition for Review on May 21, 2012.

In a Resolution⁴⁰ dated May 24, 2012, the Court gave both parties a period of thirty (30) days from notice within which to file their respective Memorandum.

In view of the filing of petitioner’s Memorandum⁴¹ on June 29, 2012 and the filing of respondents’ Memorandum by registered mail on June 27, 2012⁴² which this Court

³⁷ Docket, p. 121.

³⁸ Docket, pp. 125 to 130.

³⁹ Docket, pp. 141 to 148.

⁴⁰ Docket, p. 151.

⁴¹ Docket, pp. 152 to 192.

⁴² Docket, pp. 199 to 213.

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received on July 10, 2012, the instant Petition for Review was submitted for decision on July 12, 2012.⁴³

In the instant Petition for Review, petitioner alleged that the fundamental issue is whether or not petitioner is liable to pay the franchise tax being imposed by respondents under the Notice of Assessment.⁴⁴

Petitioner also raised the following assignment of errors⁴⁵ for this Court's resolution:

"A

THE REGIONAL TRIAL COURT GRAVELY ERRED IN DECLARING THAT PETITIONER 'ENJOYS' A SECONDARY FRANCHISE, THUS MAKING PETITIONER LIABLE TO PAY RESPONDENT THE FRANCHISE TAX ASSESSED

B

THE REGIONAL TRIAL COURT GRAVELY ERRED IN DECLARING THE PROSCRIPTION UNDER THE NON-IMPAIRMENT CLAUSE OF THE CONSTITUTION INAPPLICABLE IN THE INSTANT CASE"

In disputing the validity of respondents' Notice of Assessment assessing petitioner for franchise tax for the taxable year 2009, petitioner claims that it has never been granted nor issued any secondary franchise by the government. Thus, petitioner argues that it cannot be considered as a business enjoying a franchise for the purpose of the franchise tax imposed and collected under Section 137 of the LGC and the Sorsogon City Revenue Code.

Respondents maintain that petitioner is considered as a "business enjoying franchise", hence, liable to franchise tax; and that petitioner completely satisfies the requirements for the imposition of franchise tax as laid down in the case of **National Power Corporation vs. City of Cabanatuan**⁴⁶ 4

⁴³ Resolution dated July 12, 2012, Docket, p, 216.

⁴⁴ Par. 16, Part V, Issue, Petition for Review, Docket, p. 8.

⁴⁵ Part VI, Assignment of Errors, *id.*

⁴⁶ G.R. No. 149110, April 9, 2003.

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(*Cabanatuan case*), to wit: (1) that the taxpayer has a “franchise” in the sense of a secondary or special franchise; and (2) that it is exercising its rights or privileges under this franchise within the territory of the concerned local government unit (LGU). Respondents aver that petitioner fulfills the above requisites, on grounds that –

1. it has a “franchise” upon its incorporation when its articles of incorporation was approved and was duly incorporated under the general law, which is the Corporation Code of the Philippines; and
2. petitioner operates within Sorsogon City’s territorial jurisdiction.⁴⁷

In the assailed Decision, the RTC of Sorsogon sustained respondents’ position that petitioner enjoys a franchise and that petitioner is doing business within the territory of respondent Sorsogon City. The RTC of Sorsogon found that petitioner is enjoying an extraordinary privilege accorded by the government when it was appointed and constituted as the exclusive party to conduct geothermal operations within the territorial jurisdiction of respondent City of Sorsogon. The court *a quo* held that this privilege is in the nature of a secondary franchise, and thus, held that petitioner is a proper subject of franchise tax since petitioner is a business that enjoys a franchise and operates within the territorial jurisdiction of respondent City of Sorsogon.⁴⁸

The power of the city to impose a franchise tax is based on Section 151 of the LGC in relation to Section 137 of the LGC, which are both quoted hereunder:

“SEC. 151. *Scope of Taxing Power.* — Except as otherwise provided in this Code, the city may levy the taxes, fees, and charges which the province or municipality may impose: *Provided, however,* That the taxes, fees, and charges levied and collected by highly urbanized and independent component cities shall accrue to them and distributed in accordance with the provisions of this Code. **L**

⁴⁷ Pars. 4 and 5, Answer, RTC Records, pp. 57 to 58.

⁴⁸ Decision, RTC Records, pp. 232 to 233.

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The rates of taxes that the city may levy may exceed the maximum rates allowed for the province or municipality by not more than fifty percent (50%) except the rates of professional and amusement taxes.”

“SEC. 137. *Franchise Tax.* — Notwithstanding any exemption granted by any law or other special law, the province may impose a tax on businesses enjoying a franchise, at the rate not exceeding fifty percent (50%) of one percent (1%) of the gross annual receipts for the preceding calendar year based on the incoming receipt, or realized, within its territorial jurisdiction.”

Based on the above-quoted provisions of the LGC, a city may impose a franchise tax on “businesses enjoying a franchise”. Hence, this Court has to determine whether or not petitioner is enjoying a franchise thereby making it liable for franchise tax.

The records show that petitioner filed and served upon respondents a Request for Admission⁴⁹ during the pendency of the case before the RTC of Sorsogon pursuant to Rule 26 of the Rules of Court. In said Request for Admission, petitioner requested respondents to admit the due execution and genuineness of the documents listed, and the truth of the facts enumerated therein, to wit:

“1. The due execution and genuineness of the following documents, copies of which have been previously furnished to you through EDC’s Reply dated 21 February 2011, namely:

a. Service Contract (Geothermal Resources) No. 3 dated 16 October 1981; and

b. Department of Energy Certificate of Registration (Registration No. GRESC 2009 10-003) dated 23 October 2009;

2. The truth of the material facts, namely:☞

⁴⁹ RTC Records, pp. 160 to 164.

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a. That EDC is engaged in the production of geothermal steam and other geothermal resources in its steamfields (the '**Steamfields**') located within the BacMan I Geothermal Plant;

b. That from 16 October 1981 until 22 October 2009, EDC's operation of the Steamfields had been by virtue of Service Contract (Geothermal Resources) No. 3;

c. That from 23 October 2009 until the present, EDC's operation of the Steamfields has been by virtue of Geothermal Renewable Energy Service Contract No. 2009-10-003 (Bacon-Manito, Albay-Sorsogon), and Department of Energy Certificate of Registration (Registration No. GRESC 2009 10-003) dated 23 October 2009;

d. That EDC has not been operating the Steamfields by virtue of a franchise from the legislature or from an administrative agency through a delegation of a legislative delegation (sic);

e. That not all of the businesses operating within Sorsogon City hold a legislative or administrative franchise;

f. That not all of the businesses operating within Sorsogon City have been assessed franchise taxes by the Office of the City Treasurer of Sorsogon City;

g. That the geothermal steam and other geothermal resources produced by EDC through its operation of the Steamfields is sold only to National Power Corporation;

h. That in EDC's operation of the Steamfields, EDC has not been providing the geothermal steam and other geothermal resources produced to the public who has a right to demand for said service;

i. That under Service Contract (Geothermal Resources) No. 3, EDC was exempt from the payment of all taxes, except income taxes; and

j. That under Service Contract (Geothermal Resources) No. 3, the Government of the Republic of the 

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Philippines had been receiving sixty percent (60%) of the net value of the sale of the geothermal steam and other geothermal resources produced by the EDC in the Steamfields." (*Emphasis supplied*)

Sections 1 and 2, Rule 26 of the Rules of Court provide:

"SECTION 1. *Request for Admission.* — At any time after issues have been joined, a party may file and serve upon any other party a written request for the admission by the latter of the genuineness of any material and relevant document described in and exhibited with the request or of the truth of any material and relevant matter of fact set forth in the request. Copies of the documents shall be delivered with the request unless copies have already been furnished."

"SECTION 2. *Implied Admission.* — Each of the matters of which an admission is requested shall be **deemed admitted unless**, within a period designated in the request, which shall not be less than fifteen (15) days after service thereof, or within such further time as the court may allow on motion, **the party to whom the request is directed files and serves upon the party requesting the admission a sworn statement either denying** specifically the matters of which an admission is requested **or setting forth in detail the reasons why he cannot truthfully either admit or deny those matters.**

Objections to any request for admission shall be submitted to the court by the party requested within the period for and prior to the filing of his sworn statement as contemplated in the preceding paragraph and his compliance therewith shall be deferred until such objections are resolved, which resolution shall be made as early as practicable." (*Emphasis supplied*)

In **Vicente Uy Chao vs. De la Rama Steamship Co., Inc.**,⁵⁰ the Supreme Court explained the purpose of the rule governing requests for admission of facts and genuineness of documents, in the following manner:

"The purpose of the rule governing requests for admission of facts and genuineness of

⁵⁰ G.R. No. L-14495, September 29, 1962.

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documents is to expedite trial and to relieve parties of the costs of proving facts which will not be disputed on trial and the truth of which can be ascertained by reasonable inquiry (Federal Rules of Civil Procedure, U.S.C.A. Title 28, Section 723c, p. 624). **The reason for the requirement that such request must be made after the pleadings are closed is that the questions of fact involved in a case are inquired into only when it reaches the stage of proof.** But where this stage, as to any particular relevant fact, is accelerated by a motion to dismiss which cannot be fairly resolved without evidence thereon being received, the purpose of the rule comes into play. In so far as that fact is concerned the issue is already joined and the pleadings may be deemed to be closed within the meaning of Rule 23. To hold otherwise would be to substitute technicality for substance and hamper expeditious inquiry into the facts, contrary to the principle of liberal construction of the rules 'in order to promote their object and to assist the parties in obtaining just, speedy and inexpensive determination of every action and proceeding. (Section 2, Rule 1)." *(Emphasis supplied)*

Moreover, in the case of **Republic of the Philippines (Presidential Commission on Good Government) vs. Sandiganbayan, et al.**,⁵¹ the Supreme Court categorically ruled that failure to specifically deny the matters of which an admission is requested shall be deemed an admission of the matters stated in the request. Relevant portions of said decision are quoted hereunder:

"(T)he sanctions for refusing to make discovery have already been mentioned. So, too, discovery under Rule 26 is begun by nothing more complex than the service on a party of a letter or other written communication containing a request that specific facts therein set forth and/or particular documents copies of which are thereto appended, be admitted in writing. That is all. Again, the **receipt of such a communication by the party has the effect of imposing on him the obligation of serving the party requesting admission with 'a sworn statement either denying specifically the matters of which an**

⁵¹ G.R. No. 90478, November 21, 1991.

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admission is requested or setting forth in detail the reasons why he cannot truthfully either admit or deny those matters,' failing in which '(e)ach of the matters of which admission is requested shall be deemed admitted.' (*Emphasis supplied*)

The records show that respondents did not admit or deny the matters contained in petitioner's Request for Admission. Thus, as aptly pointed out by petitioner, respondents are deemed to have admitted the matters stated in the request which necessarily include the fact that "from 16 October 1981 until 22 October 2009, EDC's operation of the Steamfields had been by virtue of Service Contract (Geothermal Resources) No. 3"; "that from 23 October 2009 until the present, EDC's operation of the Steamfields has been by virtue of Geothermal Renewable Energy Service Contract No. 2009-10-003 (Bacon-Manito, Albay-Sorsogon), and Department of Energy Certificate of Registration (Registration No. GRESC 2009 10-003) dated 23 October 2009"; and "that EDC has not been operating the Steamfields by virtue of a franchise from the legislature or from an administrative agency through a delegation of a legislative franchise."⁵²

In the *Cabanatuan* case, the Supreme Court enumerated the requisites for the imposition of franchise tax under Section 137 of RA No. 7160, to wit:

(1) that petitioner has a "franchise" in the sense of a secondary or special franchise; and

(2) that it is exercising its rights or privileges under this franchise within the territory of the local government concerned.

Since respondents impliedly admitted that petitioner operates the Steamfields pursuant to the Geothermal Service Contracts (which was later on amended by the Geothermal RE Service Contract) executed by and between

⁵² "delegation" in the Request for Admission.

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petitioner and the DOE and that petitioner has not been operating the Steamfields by virtue of a franchise from the legislature or from an administrative agency through a delegation of a legislative franchise, the first requisite for the imposition of a franchise tax as laid down by the Supreme Court in the *Cabanatuan case* is absent herein. In the absence of a secondary or special franchise granted to petitioner by the Government or its agency, respondents have no legal and factual basis to impose a franchise tax on petitioner.

Even assuming *arguendo* that there was no such admission on the part of respondents, the records clearly show that petitioner's right to operate the Steamfields was by virtue of the Geothermal Service Contract it entered into with the DOE pursuant to the specific mandate of PD No. 1442⁵³ dated June 11, 1978, which was later on amended by the Geothermal RE Service Contract it entered into with the DOE pursuant to RA No. 9513.

It is significant to note that PD No. 1442 and RA No. 9513 do not demand that a secondary franchise must first be granted or issued by the Government or its agency to private persons or corporations prior to the exploration, exploitation, and development of geothermal resources. PD No. 1442 and RA No. 9513 simply require that the Government should enter into service contracts in connection with the exploration, exploitation, and development of geothermal resources.

Section 1 of PD No. 1442 authorized the Government to enter into service contracts for the exploration, exploitation, and development of geothermal resources with a domestic or foreign contractor who must be technically and financially capable of undertaking the operations required in the service contract. Section 1 of PD No. 1442 states: ❹

⁵³ An Act to Promote the Exploration and Development of Geothermal Resources.

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"SECTION 1. *Exploration of and Development of Geothermal Resources by the Government.* - Subject to existing private rights, **the Government may directly explore for, exploit and develop geothermal resources. It may also indirectly undertake the same under service contracts awarded through public bidding or concluded through negotiation, with a domestic or foreign contractor who must be technically and financially capable of undertaking the operations required in the service contract; Provided, that if the service contractor shall furnish the necessary services, technology and financing, the service contractor may be paid a fee not exceeding forty *per centum* (40%) of the balance of the gross value of the geothermal operations after deducting the necessary expenses incurred in the operations; *Provided, further,* that **the execution of the activities and operations subject of the service contract, including the implementation of the work program and accounting procedures agreed upon, shall at all times be subject to direct supervision of the Government, through the Bureau of Energy Development.****

Service contracts as above authorized shall be subject to approval of the Secretary of Energy.

Geothermal resources mean (a) all products of geothermal processes, embracing indigenous steam, hot water and hot brines; (b) steam and other gases, hot water and hot brines resulting from water, gas, or other fluids artificially introduced into geothermal formations; (c) heat or other associated energy found in geothermal formations; and (d) any by-product derived from them."
(*Emphasis supplied*)

On the other hand, RA No. 9513 establishes the framework for the accelerated development and advancement of renewable energy resources. Under RA No. 9513, the Government, through the DOE, may enter into a service agreement or contract with a renewable energy (RE) developer for the exploration and development of a particular RE area. Section 4(tt) of RA No. 9513 defines an RE contract, as follows: 4

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"SECTION 4. *Definition of Terms.* - As used in this Act, the following terms are herein defined:

xxx xxx xxx

(tt) 'Renewable Energy Service (Operating Contract (RE Contract))' refers to the service agreement between the Government, through the DOE, and RE Developer over a period in which the RE Developer has the exclusive right to a particular RE area for exploration and development. The RE Contract shall be divided into two (2) stages: the pre-development stage and the development/commercial stage. The preliminary assessment and feasibility study up to financial closing shall refer to the pre-development stage. The construction and installation of facilities up to operation phase shall refer to the development stage."

In the case of **La Bugal-B'Laan Tribal Association, Inc., et al. vs. Victor O. Ramos, et al.**,⁵⁴ (*La Bugal-B'Laan case*) the Supreme Court extensively discussed the meaning of "Service Contract System" in relation to the development of natural resources, to wit:

"PRESIDENTIAL DECREE NO. 87, THE 1973 CONSTITUTION AND THE SERVICE CONTRACT SYSTEM

The promulgation on December 31, 1972 of Presidential Decree No. 87, otherwise known as THE OIL EXPLORATION AND DEVELOPMENT ACT OF 1972 signaled such a transformation. P.D. No. 87 permitted the government to explore for and produce indigenous petroleum through '**service contracts.**'

'Service contracts' is a term that assumes varying meanings to different people, and it has carried many names in different countries, like 'work contracts' in Indonesia, 'concession agreements' in Africa, 'production-sharing agreements' in the Middle East, and 'participation agreements' in Latin America. **A functional definition of 'service contracts' in the Philippines is provided as follows:**

A service contract is a contractual arrangement for engaging in the exploitation and development of petroleum, mineral,

⁵⁴ G.R. No. 127882, January 27, 2004.

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energy, land and other natural resources by which a government or its agency, or a private person granted a right or privilege by the government authorizes the other party (service contractor) to engage or participate in the exercise of such right or the enjoyment of the privilege, in that the latter provides financial or technical resources, undertakes the exploitation or production of a given resource, or directly manages the productive enterprise, operations of the exploration and exploitation of the resources or the disposition of marketing or resources.

In a service contract under P.D. No. 87, service and technology are furnished by the service contractor for which it shall be entitled to the stipulated service fee. The contractor must be technically competent and financially capable to undertake the operations required in the contract.

Financing is supposed to be provided by the Government to which all petroleum produced belongs. In case the Government is unable to finance petroleum exploration operations, the contractor may furnish services, technology and financing, and the proceeds of sale of the petroleum produced under the contract shall be the source of funds for payment of the service fee and the operating expenses due the contractor. The contractor shall undertake, manage and execute petroleum operations, subject to the government overseeing the management of the operations. The contractor provides all necessary services and technology and the requisite financing, performs the exploration work obligations, and assumes all exploration risks such that if no petroleum is produced, it will not be entitled to reimbursement. Once petroleum in commercial quantity is discovered, the contractor shall operate the field on behalf of the government.

P.D. No. 87 prescribed minimum terms and conditions for every service contract. It also granted the contractor certain privileges, including exemption from taxes and payment of tariff duties, and permitted the repatriation of capital and retention of profits abroad.

Ostensibly, **the service contract system had certain advantages over the concession regime.** It

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has been opined, though, that, in the Philippines, our concept of a service contract, at least in the petroleum industry, was basically a concession regime with a production-sharing element.

On January 17, 1973, then President Ferdinand E. Marcos proclaimed the ratification of a new Constitution. Article XIV on the National Economy and Patrimony contained provisions similar to the 1935 Constitution with regard to Filipino participation in the nation's natural resources. Section 8, Article XIV thereof provides:

'SEC. 8. All lands of the public domain, waters, minerals, coal, petroleum and other mineral oils, all forces of potential energy, fisheries, wildlife, and other natural resources of the Philippines belong to the State. With the exception of agricultural, industrial or commercial, residential and resettlement lands of the public domain, natural resources shall not be alienated, and no license, concession, or lease for the exploration, development, exploitation, or utilization of any of the natural resources shall be granted for a period exceeding twenty-five years, renewable for not more than twenty-five years, except as to water rights for irrigation, water supply, fisheries, or industrial uses other than the development of water power, in which cases beneficial use may be the measure and the limit of the grant.'

While Section 9 of the same Article maintained the Filipino-only policy in the enjoyment of natural resources, **it also allowed Filipinos, upon authority of the Batasang Pambansa, to enter into service contracts with any person or entity for the exploration or utilization of natural resources.**

'SEC. 9. The disposition, exploration, development, exploitation, or utilization of any of the natural resources of the Philippines shall be limited to citizens, or to corporations or associations at least sixty per centum of which is owned by such citizens. **The Batasang Pambansa, in the national interest, may allow such citizens, corporations or associations to enter into service contracts for financial, technical, management, or**

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other forms of assistance with any person or entity for the exploration, or utilization of any of the natural resources. Existing valid and binding service contracts for financial, technical, management, or other forms of assistance are hereby recognized as such.’ [Emphasis supplied.]

The concept of service contracts, according to one delegate, was borrowed from the methods followed by India, Pakistan and especially Indonesia in the exploration of petroleum and mineral oils. The provision allowing such contracts, according to another, was intended to ‘enhance the proper development of our natural resources since Filipino citizens lack the needed capital and technical know-how which are essential in the proper exploration, development and exploitation of the natural resources of the country.’

The original idea was to authorize the government, not private entities, to enter into service contracts with foreign entities. As finally approved, however, a citizen or private entity could be allowed by the National Assembly to enter into such service contract. The prior approval of the National Assembly was deemed sufficient to protect the national interest. Notably, none of the laws allowing service contracts were passed by the Batasang Pambansa. Indeed, all of them were enacted by presidential decree.

On March 13, 1973, shortly after the ratification of the new Constitution, the President promulgated Presidential Decree No. 151. The law allowed Filipino citizens or entities which have acquired lands of the public domain or which own, hold or control such lands to enter into service contracts for financial, technical, management or other forms of assistance with any foreign persons or entity for the exploration, development, exploitation or utilization of said lands.

Presidential Decree No. 463, also known as THE MINERAL RESOURCES DEVELOPMENT DECREE OF 1974, was enacted on May 17, 1974. Section 44 of the decree, as amended, provided that a lessee of a mining claim may enter into a service contract with a qualified domestic or foreign contractor for the exploration, development and exploitation of his claims and the processing and marketing of the product thereof.☞

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Presidential Decree No. 704 (THE FISHERIES DECREE OF 1975), approved on May 16, 1975, allowed Filipinos engaged in commercial fishing to enter into contracts for financial, technical or other forms of assistance with any foreign person, corporation or entity for the production, storage, marketing and processing of fish and fishery/aquatic products.

Presidential Decree No. 705 (THE REVISED FORESTRY CODE OF THE PHILIPPINES), approved on May 19, 1975, allowed 'forest products licensees, lessees, or permittees to enter into service contracts for financial, technical, management, or other forms of assistance . . . with any foreign person or entity for the exploration, development, exploitation or utilization of the forest resources.'

Yet another law allowing service contracts, this time for geothermal resources, was Presidential Decree No. 1442, which was signed into law on June 11, 1978. Section 1 thereof authorized the Government to enter into service contracts for the exploration, exploitation and development of geothermal resources with a foreign contractor who must be technically and financially capable of undertaking the operations required in the service contract.

Thus, virtually the entire range of the country's natural resources – from petroleum and minerals to geothermal energy, from public lands and forest resources to fishery products – was well covered by apparent legal authority to engage in the direct participation or involvement of foreign persons or corporations (otherwise disqualified) in the exploration and utilization of natural resources through service contracts." (*Emphasis supplied; citations omitted*)

In relation to the development of natural resources, a "service contract" actually refers to a contractual arrangement whereby the service contractor undertakes to render services, for a fee, in favor of the Government or in favor of a private person who was a recipient of a right or privilege from the Government. In the latter case, said private person is the one who actually authorizes the service

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contractor to provide services to the private person for a stipulated fee.

On the other hand, the term "franchise" for purposes of the imposition of the franchise tax under Section 137 of RA No. 7160 is clearly defined under Section 131(m) of RA No. 7160, in this wise:

"SECTION 131. *Definition of Terms.* – When used in this title, the term:

xxx

xxx

xxx

(m) 'Franchise' is a right or privilege, affected with public interest which is conferred upon private persons or corporation, under such terms and conditions as the government and its political subdivisions may impose in the interest of public welfare, security, and safety."

As pointed out by petitioner, Sorsogon City Revenue Code likewise defines the term "franchise" in exactly the same manner as it was defined in RA No. 7160.⁵⁵

In the *Cabanatuan case*, the Supreme Court clearly explained the definition of the term "franchise", to wit:

"In the case at bar, section 151 in relation to section 137 of the LGC clearly authorizes the respondent city government to impose on the petitioner the franchise tax in question.

In its general signification, **a franchise is a privilege conferred by government authority, which does not belong to citizens of the country generally as a matter of common right.** In its specific sense, **a franchise may refer to a general or primary franchise, or to a special or secondary franchise.** The former relates to the right to exist as a corporation, by virtue of duly approved articles of incorporation, or a charter pursuant to a special law creating the corporation. The right under a primary or general franchise is vested in the individuals who

⁵⁵ Section 4(m), Chapter I, Title Two, Sorsogon City Revenue Code

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compose the corporation and not in the corporation itself. On the other hand, **the latter refers to the right or privileges conferred upon an existing corporation such as the right to use the streets of a municipality to lay pipes of tracks, erect poles or string wires.** The rights under a secondary or special franchise are vested in the corporation and may ordinarily be conveyed or mortgaged under a general power granted to a corporation to dispose of its property, except such special or secondary franchises as are charged with a public use.

In Section 131 (m) of the LGC, Congress unmistakably defined a franchise in the sense of a secondary or special franchise. This is to avoid any confusion when the word franchise is used in the context of taxation. As commonly used, a *franchise tax* is 'a tax on the privilege of transacting business in the state and exercising corporate franchises granted by the state.' It is not levied on the corporation simply for existing as a corporation, upon its property or its income, but on its exercise of the rights or privileges granted to it by the government. Hence, a corporation need not pay franchise tax from the time it ceased to do business and exercise its franchise. It is within this context that the phrase '**tax on businesses enjoying a franchise**' in section 137 of the LGC should be interpreted and understood. Verily, to determine whether the petitioner is covered by the franchise tax in question, the following requisites should concur: (1) that petitioner has a 'franchise' in the sense of a secondary or special franchise; and (2) that it is exercising its rights or privileges under this franchise within the territory of the respondent city government." (*Emphasis supplied; citations omitted*)

Based on the foregoing, a "franchise" is a right or privilege to undertake certain acts imbued with public interest **granted** upon private persons or corporations by the Government or its agencies or political subdivisions, which right or privilege is not generally available to all private persons or corporations. 

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All told, it is clear that no secondary franchise was granted by the Government or its agency in favor of petitioner. First, the grant of such franchise is not required under PD No. 1442 and RA No. 9513 for the exploration, development, and operation of geothermal resources. Second, considering the meaning of the terms "service contract" and "franchise", petitioner's operation of the Steamfields located within the Geothermal Plant is by virtue of a service contract or agreement whereby petitioner undertakes to perform all the obligations stated under Section VI of the Geothermal Service Contract.

In this regard, the RTC of Sorsogon therefore erred in declaring that petitioner enjoys a secondary franchise for purposes of the imposition of the franchise tax. This error of the RTC of Sorsogon merits the reversal of the assailed Decision dated December 26, 2011 and Resolution dated February 21, 2012.

Since petitioner does not have a secondary franchise as it is not required by law to be granted one, there is no basis to hold petitioner liable for franchise tax under Section 137 of the LGC and the Sorsogon City Revenue Code. Accordingly, this Court rules that the Notice of Assessment dated July 26, 2010 issued by the Office of the City Treasurer of Sorsogon, assessing petitioner for deficiency franchise tax in the amount of ₱3,711,742.66, is void for lack of legal and factual basis.

Being a void assessment, said Notice of Assessment does not give rise to an obligation on the part of petitioner to pay deficiency franchise tax to respondent Sorsogon City who had no authority to collect the same.

Having disposed of the fundamental issue as well as the first assigned error, discussion of the other assigned error is no longer necessary. **└**

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WHEREFORE, premises considered, the instant Petition for Review is hereby **GRANTED**. Accordingly, the assailed Decision dated December 26, 2011 of the Regional Trial Court, Branch 53, Fifth Judicial Region, Sorsogon City and its Resolution dated February 21, 2012 in Civil Case No. 2011-8255 entitled "ENERGY DEVELOPMENT CORPORATION (EDC), as represented herein by its Senior Vice-President and Chief Finance Officer, NESTOR H. VASAY vs. SORSOGON CITY and HON. ROBERTO D. DOOC, City Treasurer (Officer-in-Charge), Sorsogon City" are hereby **REVERSED** and **SET ASIDE**. The Notice of Assessment dated July 26, 2010 issued by the Office of the City Treasurer of Sorsogon, through the City Treasurer, assessing petitioner for deficiency franchise tax in the amount of ₱3,711,742.66, is hereby **SET ASIDE** and **NULLIFIED** for lack of legal and factual basis and for being contrary to law.

SO ORDERED.


CIELITO N. MINDARO-GRULLA
Associate Justice

WE CONCUR:


JUANITO C. CASTAÑEDA, JR.
Associate Justice


CAESAR A. CASANOVA
Associate Justice

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ATTESTATION

I attest that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court’s Division.

Juanito C. Castaneda, Jr.
JUANITO C. CASTANEDA, JR.
Associate Justice
Chairperson

CERTIFICATION

Pursuant to Article VIII, Section 13 of the Constitution, and the Division Chairperson’s Attestation, it is hereby certified that the conclusions in the above Decision were reached in consultation before the case was assigned to the writer of the opinion of the Court’s Division.


ROMAN G. DEL ROSARIO
Presiding Justice