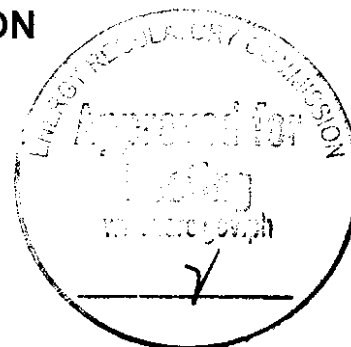


Republic of the Philippines
ENERGY REGULATORY COMMISSION
San Miguel Avenue, Pasig City



IN THE MATTER OF THE
APPLICATION FOR AUTHORITY TO
IMPLEMENT THE LOCAL
FRANCHISE TAX RATE IN THE CITY
OF CALAMBA, LAGUNA, WITH
PRAYER FOR PROVISIONAL
AUTHORITY

ERC CASE NO. 2008-049 RC

MANILA ELECTRIC COMPANY
(MERALCO),

Applicant.

x-----x

D O C K E T E D

Date: JAN 21 2009

By: *[Signature]*

D E C I S I O N

Before the Commission for resolution is the application filed by the Manila Electric Company (MERALCO) on August 20, 2008 for authority to implement the local franchise tax rate in the City of Calamba, Laguna, with prayer for provisional authority.

In its application, MERALCO alleged, among others, the following:

1. It was furnished with a copy of Resolution No. 204, Series of 2006 entitled "A Resolution Approving City Ordinance No. 371-2006, An Ordinance Enacting the Revised and Consolidated Revenue Code of the City of Calamba," enacted by the Sangguniang Panlungsod of Calamba on November 13, 2006. Said Ordinance imposes tax upon businesses enjoying a franchise at the rate of sixty-five percent (65%) of one percent (1%) of the gross annual receipts, to wit:

"k) **Franchise Tax** - There is hereby imposed a tax on business enjoying a franchise at a rate of sixty five percent (65%) of one percent (1%) of the gross annual receipts, which shall include both cash sales and sales on account realized during the preceding calendar year within this City....xxx"

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2. Resolution No. 204, Series of 2006 was published in the Southern Luzon Newstar, a weekly newspaper, on March 19, 26 and April 2, 2007. By virtue of said publication, Ordinance No. 371-2006 became effective on July 1, 2007, pursuant to Section 8.03 thereof which states that "this ordinance shall take effect on 1 July 2007."
3. In view of the nature of local franchise tax as a pass-through charge, it intends to implement Section 2B.03(k) of Ordinance No. 371-2006, in accordance with the declaration of the Commission in its Decision in ERC Case No. 2004-11 that:

"The Commission recognizes that national or local franchise tax rates are billed to the end-users by the distribution utilities as pass-through charges. Thus, distribution utilities should neither earn any additional revenue nor incur any additional cost from the imposition of these taxes.

xxx

On the other hand, in areas where MERALCO intends to implement said local franchise taxes, the **Commission finds it reasonable to allow it to collect the same from its customers because these are impositions of the LGUs exercising their authority.** [Emphasis Supplied]

Moreover, the collection/recovery of the Local Franchise Tax from its customers in the City of Calamba is consistent with the principle laid down in Section 43 (f) of Republic Act No. 9136, otherwise known as the Electric Power Industry Reform Act of 2001 (EPIRA). The relevant provision provides:

"Section 43 (f) – xxx The rates must be such to allow the recovery of just and reasonable costs and a reasonable return on rate base (RORB) to enable the entity to operate viably."

4. However, in ERC Case Nos. 2001-646 and 2001-900¹, the Commission ruled that any change in the franchise fee rate component on customer's bill shall be subject to ERC verification and approval, to wit:

"MERALCO is not authorized to unilaterally change the franchise fee rate component on customer's bills. If MERALCO

¹ Application for Approval of Revised Rate Schedules in Compliance with Section 36 of Republic Act No. 9136; ERC Order dated October 30, 2001, and Application for Approval of Appraisal of Properties with Prayer for Provisional Authority – MERALCO, Applicant



needs to change the franchise fee rate component due to any changes in franchise fee obligations, it shall petition the ERC for such authority and include in its filing all documentation necessary to verify the changes.”

5. Thus, in view of the foregoing, it hereby applies for an authority to implement the new local franchise tax rate within the City of Calamba, Laguna.

Having found said application sufficient in form and in substance with the required fees having been paid, an Order and a Notice of Public Hearing, both dated August 27, 2008, were issued setting the same for initial hearing and preliminary conference on October 24, 2008.

MERALCO was directed to cause the publication of the Notice of Public Hearing, at its own expense, twice (2x) for two (2) successive weeks in two (2) newspapers of general circulation in the Philippines, with the date of the last publication to be made not later than ten (10) days before the scheduled date of initial hearing. It was also directed to inform the consumers in Calamba City, Laguna, by any other means available and appropriate, of the filing of the instant application, its reasons therefor, and of the scheduled hearing thereon.

The Office of the Solicitor General (OSG), the Commission on Audit (COA) and the Committees on Energy of both Houses of Congress were furnished with copies of the Order and the attached Notice of Public Hearing and were requested to have their respective duly authorized representatives present at the aforesaid initial hearing.

On October 17, 2008, MERALCO filed its *“Pre-Trial Brief.”*



During the October 24, 2008 initial hearing, only MERALCO appeared. No intervenor/oppositor appeared nor was there any intervention/opposition registered.

In the said hearing, MERALCO presented its proofs of compliance with the Commission's posting and publication of notice requirements which were duly marked as Exhibits "A" to "T-1", inclusive. Thereafter, it conducted an expository presentation of its application and moved that it be allowed to present its witness at the next scheduled hearing. Said motion was granted.

At the continuation of the hearing on October 28, 2008, only MERALCO appeared and presented its lone witness, Mr. Gener R. Montemayor, its Manager and Head of Tax Management-Tax Accounting, who testified on MERALCO's bases for implementing the new local franchise tax rates as a component of its customers' bills in Calamba City, Laguna. In the course thereof, additional documents were presented and marked as Exhibits "U" to "AA-7", inclusive. The direct examination having been terminated, the Commission propounded clarificatory questions and directed MERALCO to submit possible estimated additional charge of local franchise tax in Calamba City for the year ended December 31, 2007 in consonance with the modification to Mr. Montemayor's testimony as contained in his Judicial Affidavit, and as declared by him in open court.

On November 10, 2008, MERALCO filed its "Formal Offer of Evidence and Compliance" which are hereby admitted for being relevant and material to the final resolution of this application.



DISCUSSION

Section 5, Article X of the 1987 Constitution of the Republic of the Philippines provides that *"each local government unit shall have the power to create its own sources of revenues and to levy taxes, fees and charges subject to such guidelines and limitations as the Congress may provide, consistent with the basic policy of local autonomy. Such taxes, fees, and charges shall accrue exclusively to the local governments."*

In relation thereto, the Local Government Code modified the revenue raising powers of the local governments under the then Local Tax Code, pertinent portions of which are as follows:

- A. **"Section 129. Power to Create Sources of Revenue** – Each local government unit shall exercise its power to create its own sources of revenue and to levy taxes, fees, and charges subject to the provisions herein, consistent with the basic policy of local autonomy. Such taxes, fees, and charges shall accrue exclusively to the local government units."
- B. **"Section 132. Local Taxing Authority.** The power to impose tax, fee, or charge or to generate revenue under this Code shall be exercised by the Sanggunian of the local government unit concerned through an appropriate ordinance."
- C. **"Section 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 a 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."



D. **"Section 151. Scope of Taxing Powers** – 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.

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."

E. **"Section 186. Power to Levy Other Taxes, Fees or Charges.** – Local government units may exercise the power to levy taxes, fees or charges on any base or subject not otherwise specifically enumerated herein or taxed under the provisions of the National Internal Revenue Code, as amended, or other applicable laws: Provided, That the taxes, fees, or charges shall not be unjust, excessive, oppressive, confiscatory or contrary to declared national policy; Provided, further, That the ordinance levying such taxes, fees or charges shall not be enacted without any prior public hearing conducted for the purpose."

F. **"Section 191. Authority of Local Government Units to Adjust Rates of Tax Ordinance** – Local government units shall have the authority to adjust the tax rates as prescribed herein not oftener than once every five (5) years, but in no case shall such adjustment exceed 10% of the rates fixed under this Code."

The Commission, in its Decision dated March 20, 2003 in ERC Case No. 2001-900 entitled, *"In the Matter of the Application for Approval of Revised Rate Schedules in Compliance with Section 36 of Republic Act No. 9136 and ERC Order dated October 30, 2001, and for Approval of Appraisal of Properties with Prayer for Provisional Authority – MERALCO, Applicant"*, substantially ruled that a local franchise tax is a valid pass-through charge which may be recovered from consumers within the franchise area of the imposing city or municipality provided that the charge is reflected as a separate line item in the bill.

National or local franchise tax rates are billed by the DUs to electricity end-users as pass-through charges. The DUs should neither earn any additional revenue nor incur any additional cost from the imposition of these charges.



However, the foregoing provisions of law and Decisions of this Commission must be read and implemented in conjunction with Rule 7, Section 4 (q) of the Implementing Rules and Regulations (IRR) of the EPIRA, *to wit*:

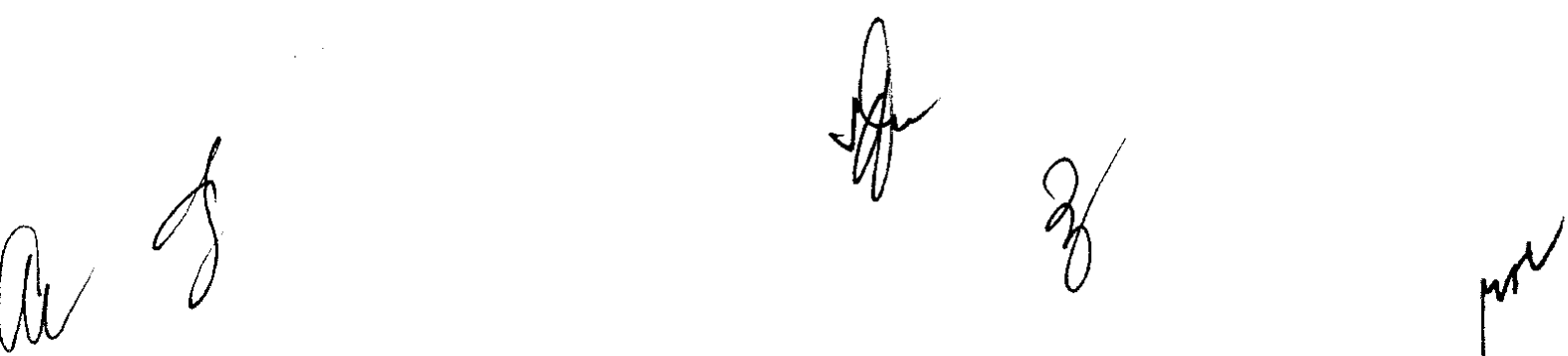
“Section 4. Obligations of a Distribution Utility. x x x

- q) A Distribution Utility shall pay a franchise tax only on its distribution wheeling and Captive Market supply revenues. To this end, the DOF shall issue the necessary guidelines.”

Evidence shows that MERALCO has not paid the increment in the subject local franchise tax to the City of Calamba, Laguna since the effectivity of the local franchise tax rate on July 1, 2007. Thus, the billing, collection and recovery by MERALCO from affected customers must be confined to that stated under the aforementioned provision of the EPIRA-IRR.

After a thorough review and evaluation of the local tax ordinance and other supporting documents submitted by MERALCO, the Commission finds said submission to be in accordance with the pertinent provisions of Republic Act No. 7160.

WHEREFORE, the foregoing premises considered, the application for authority to implement the new local franchise tax rates in the City of Calamba, Laguna, with prayer for provisional authority, filed by Manila Electric Company (MERALCO) is hereby **APPROVED**.



Accordingly, MERALCO is hereby authorized to implement the new local franchise tax rate of 65% of 1% on its customers' bills based on its distribution revenues in the City of Calamba, Laguna pursuant to the Sangguniang Panlungsod of Calamba City Ordinance No. 371-2006 as adopted through Resolution No. 204, Series of 2006 starting the next billing cycle from receipt hereof.

Further, MERALCO is directed to submit for the Commission's approval, a scheme for the recovery of paid taxes from the effectivity of the Ordinance imposing new local franchise tax until the implementation of the Decision for confirmation and verification.

SO ORDERED.


Pasig City, January 12, 2009.


ZENAIDA G. CRUZ-DUCUT
Chairperson


RAUF A. TAN
Commissioner


MARIA TERESA A.R. CASTAÑEDA
Commissioner


ALEJANDRO Z. BARIN
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