REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE
National Office Building
Quezon City

Sec. 40(C)(2) & 6(c), Tax Code
BIR Ruling No. S40M-350-2021
S40M - 010 - 2023
FEB 17 2023

MARTINEZ VERGARA GONZALEZ & SERRANO
33rd Floor, The Orient Square, F. Ortigas, Jr. Road
Ortigas Center, Pasig City

Attention: **Atty. Rosalia B. Alejo**
Atty. Mary Grace Aileen V. Estoy

Gentlemen:

This refers to your request on behalf of your client, **Lenovo International Cooperatief U.A.** ("Lenovo U.A."), for confirmation of your opinion that the transfer of shares of stock of Think Server Products (Philippines), Inc. ("Think Server"), a domestic corporation, from Lenovo (International) B.V. ("Lenovo B.V.") to Lenovo U.A., both nonresident corporations pursuant to a merger effected in accordance with the laws of Netherlands is not subject to tax in the Philippines.

It is represented that Lenovo U.A. is a cooperative organized and existing under the laws of the Netherlands, with address at De entrée 250, Unit a, 1101 EE Amsterdam, the Netherlands. Lenovo U.A. is organized under the laws of the Netherlands and registered with the trade register of the Dutch Chamber of Commerce under file number

On the other hand, Lenovo B.V. is an Amsterdam-based private limited liability company and with address at De entree 250, Unit A, 1101 EE Amsterdam. It was incorporated under the laws of the Netherlands on June 20, 1984 and wholly owned by Lenovo U.A.

Think Server is a corporation organized and existing under the laws of the Philippines, with principal office at 10F 11 Corporate Center, 11 Avenue corner Triangle Drive, Bonifacio Global City, Taguig City. It is engaged in the business of sale, distribution, leasing (except financial leasing), exporting, importing or otherwise dealing in, on a wholesale basis, any and all types of machines, office equipment, telecommunications equipment and goods, wares, merchandise and commodities of every description, and all other related or similar products, and all other activities incidental to or related to the foregoing.

On March 1, 2015, Lenovo U.A. and Lenovo B.V. concluded a legal merger within the meaning of Chapters 1, 2 and 3 of Title 7 of Book 2 Netherlands Civil Code, whereby Lenovo U.A., as the surviving company, acquired all assets and liabilities of Lenovo B.V. and the latter ceased to exist by operation of law. In particular, as a consequence of the merger, Lenovo B.V. transferred its shareholdings in Think Server to Lenovo U.A., as the surviving company. As of February 2015, Lenovo B.V. owns 88,759 common shares with a par value of P100.00 per share in Think Server.

Based on the foregoing representations, you now request for confirmation of your opinion that the transfer of Think Server shares from Lenovo B.V. to Lenovo U.A. pursuant to a merger effected in accordance with the laws of the Netherlands is not a taxable event in the Philippines.

In reply, please be informed as follows:

Capital Gains Tax / Income Tax

Section 40 (C)(2) and (6)(b) of the National Internal Revenue Code of 1997, as amended (Tax Code), does not make any qualification or distinction as to its application to a corporation. Thus, its application to a non-resident foreign corporation is well settled.[1] It provides that:

*"**SEC. 40.[2] Determination of Amount and Recognition of Gains or Loss. –***

x x x x x x x x x

(C) Exchange of Property. –

x x x x x x x x x

(2) Exception. – No gain or loss shall be recognized if in pursuance of a plan of merger or consolidation –

(a) A corporation, which is a party to a merger or consolidation, exchanges property solely for stock in a corporation, which is a party to the merger or consolidation; or

(b) A shareholder exchanges stock in a corporation, which is a party to the merger or consolidation, solely for the stock of another corporation also a party to the merger or consolidation;

(c) A security holder of a corporation, which is a party to the merger or consolidation, exchanges his securities in such corporation, solely for stock or securities in another corporation, a party to the merger or consolidation."

x x x x x x x x x

(6) Definitions. –

x x x x x x x x x

(b) The term 'merger' or 'consolidation,' when used in this Section, shall be understood to mean: (i) the ordinary merger or consolidation, or

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[1] BIR Ruling No. 377-2019 dated July 5, 2019

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> *(ii) the acquisition by one corporation of all or substantially all the properties of another corporation solely for stock: Provided, That for a transaction to be regarded as a merger or consolidation within the purview of this Section, it must be undertaken for a bona fide business purpose and not solely for the purpose of escaping the burden of taxation: Provided, further, That in determining whether a bona fide business purpose exists, each and every step of the transaction shall be considered and the whole transaction or series of transactions shall treated as a single unit: Provided, finally, That in determining whether the property transferred constitutes a substantial portion of the property of the transferor, the term 'property' shall be taken to include the cash assets of the transferor."*

Applying the above-quoted provisions in this case, the merger of Lenovo U.A. and Lenovo B.V. is a merger within the contemplation of Section 40 (C)(2), in relation to Section 40 (C)(6)(b) of the Tax Code because Lenovo U.A., as the surviving company acquired all assets and liabilities of Lenovo B.V. in accordance with the laws of the Netherlands. Such merger is being undertaken for a bona fide business purpose as a matter of strategic management to consolidate ownership in the companies' assets and liabilities and not for the purpose of escaping the burden of taxation. Thus it qualifies for non-recognition of gain or loss for income tax purposes in accordance with Section 40 (C)(2) of the Tax Code, and that no gain or loss shall be recognized by Lenovo B.V., as the transferor of all its assets and liabilities, to Lenovo U.A. pursuant to the Deed of Merger.

Accordingly, no gain or loss shall be recognized by Lenovo U.A., as the transferee, on its receipt of the Lenovo B.V. shares pursuant to and as a consequence of the merger.

Cost Basis

Section 40 (C)(5)(a) and (b) of the Tax Code states:

"(5) Basis. —

> *(a) The basis of the stock or securities received by the transferor upon the exchange specified in the above exception shall be the same as the basis of the property, stock or securities exchanged, decreased by (1) the money received, and (2) the fair market value of the other property received, and increased by (a) the amount treated as dividend of the shareholder and (b) the amount of any gain that was recognized on the exchange: Provided, That the property received as 'boot' shall have as basis its fair market value: Provided, further, That if as part of the consideration to the transferor, the transferee of property assumes a liability of the transferor or acquires from the latter property subject to a liability, such assumption or acquisition (in the amount of the liability) shall, for purposes of this paragraph, be treated as money received by the transferor on the exchange: Provided, finally, That if the transferor*

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> *receives several kinds of stock or securities, the Commissioner is hereby authorized to allocate the basis among the several classes of stocks or securities.*
>
> *(b) The basis of the property transferred in the hands of the transferee shall be the same as it would be in the hands of the transferor increased by the amount of the gain recognized to the transferor on the transfer."*

Indubitably, the basis of the Think Server shares transferred in the hands of the transferee Lenovo U.A. shall be the same as it would be in the hands of the transferor Lenovo B.V. increased by the amount of gain, if any, recognized to the transferor on the transfer.

Value-Added Tax (VAT)

Section 105 of the Tax Code states:

> *SEC. 105. Persons Liable. — Any person who, in the course of trade or business, sells, barters, exchanges, leases goods or properties, renders services, and any person who imports goods shall be subject to the value-added tax (VAT) imposed in Sections 106 to 108 of this Code.*
>
> *x x x x x x x x x*
>
> *The phrase 'in the course of trade or business' means the regular conduct or pursuit of a commercial or an economic activity, including transactions incidental thereto, by any person regardless of whether or not the person engaged therein is a non-stock nonprofit private organization (irrespective of the disposition of its net income and whether or not it sells exclusively to members or their guests), or government entity."*

In view of thereof, the transfer of the Think Server shares as a consequence of the merger is not subject to VAT pursuant to Section 105 of the Tax Code. The transfer of the Think Server shares as a result of the merger is not made in the course of business but by operation of law pursuant to the merger.

Donor's Tax

Well-settled in our jurisprudence is the fact that the essential elements of a valid donation are: (1) the reduction of the patrimony of the donor; (2) the increase in the patrimony of the donee; and (3) the intent to do an act of liberality (animus donandi).

Clearly there is no intention on the part of Lenovo B.V. to donate to Lenovo U.A. its Think Server shares since the transaction is being undertaken purely for business purpose. Thus, the merger will not be subject to donor's tax since there is no intention to donate and the transaction is a *bona fide* merger effected solely for business reasons.

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Documentary Stamp Tax (DST)

Section 199 (m) of the Tax Code, as amended by Republic Act No. 9243 and as implemented by Revenue Regulations (RR) No. 13-2004, states as follows:

> *"Sec. 199. Documents and Papers Not Subject to Stamp Tax. — The provision of Section 173 to the contrary notwithstanding, the following instruments, documents and papers shall be exempt from the documentary stamp tax:*
>
> *x x x x x x x x x*
>
> *(m) Transfer of property pursuant to Section 40 (c) (2) of the National Internal Revenue Code of 1997, as amended."*

Accordingly, no DST is due on the surrender by Lenovo B.V. shareholders of their Lenovo B.V. shares for cancellation pursuant to the merger.

Also, while Section 9 of RR No. 13-2004 states that the shares of stocks issued in exchange for property is subject to DST due under Section 174 of the Tax Code, if they are original issues, still, the shares of stock issued by Lenovo U.A. is not subject to DST on original issuance of shares under Section 174 of the Tax Code because Lenovo U.A. is a corporation organized and existing under the laws of the Netherlands, therefore, not within the Philippine taxing jurisdiction. Section 173 of the Tax Code only imposes DST on obligations or rights arising from Philippine sources or properties situated in the Philippines.

Strict compliance of requirements to avail of the non-recognition of gains provided for in Section 40 (C)(2) of the Tax Code

In order that the parties to the exchange can avail of the non-recognition of gains provided for in Section 40 (C)(2) of the Tax Code, they should comply with the requirements hereunder mentioned.

The parties shall cause the Corporate Secretary of Think Server to annotate at the back of the Certificates of Stock the date the merger was executed, the original or historical cost of acquisition of the shares of stock involved, and the fact that no gain or loss was recognized as a result of such merger; provided however, that any violation by the Corporate Secretary of this condition shall be penalized under Section 275 of the Tax Code.

It is further required that the Certificate of Stock that bears the annotation of substituted bases of the shares of stock transferred/received in connection with this transaction, as duly certified by the Corporate Secretary, should be submitted to the Law and Legislative Division, Bureau of Internal Revenue, 7/F National Office Building, Diliman, Quezon City within ninety

(90) days from the date of the receipt of this Ruling. Otherwise, this ruling shall be void and without effect, and the Chief, Law and Legislative Division shall refer the docket of the case to the Prosecution Division for appropriate action.

This ruling is being issued on the basis of the foregoing facts as represented. However, if upon investigation, it will be ascertained that the facts are different, then this ruling shall be considered null and void.

Very truly yours,

ROMEO D. LUMAGUI, JR.
Commissioner of Internal Revenue
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