REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE

Quezon City

Sections 27 (D) (4), 98, 106 of the Tax Code as amended; RR No. 6-2008, as amended by RR No. 6-2013
BIR Ruling No. OT-194-2021
OT- 092-2022
MAR 10 2022

PHILIPPINE NATIONAL BANK
Philippine National Bank Financial Center
Pres. Diosdado Macapagal Boulevard
Pasay City

Attention: AIDELL AMOR R. GREGORIO
Acting CFO

Gentlemen:

This refers to your request for confirmation that no taxable event will result in connection with the distribution by Philippine National Bank (PNB) of ommon shares in PNB Holdings Corporation (PHC) to all Shareholders of record of PNB as of May 18, 2021, by way of property dividends, either for the Corporate Shareholders and/or PNB itself.

Background:

Philippine National Bank is a corporation duly organized and existing under and by virtue of the laws of the Philippines, with offices at Philippine National Bank Financial Center, Pres. Diosdado Macapagal Boulevard, Pasay City Philippines 1300, with an authorized capital stock of Php , divided into common shares with a par value of Php per share, of which Php are subscribed and outstanding, consisting of ommon shares with a par value of Php per share. Among others, PNB is the owner of common shares in PHC with total par value of Php pursuant to the increase of capital stock of PHC that was approved by the Securities and Exchange Commission (SEC) on January 13, 2021, of which common shares in PHC (Subject Shares), is declared and will be distributed by PNB as property dividends.

During the executive session of the Board of Directors held on April 23, 2021, at which meeting a quorum was present and acting throughout, the board approved and confirmed the declaration and distribution of the Subject Shares by way of property dividend to all stockholders of record of PNB, as of May 18, 2021, to be distributed upon approval of the SEC.

As of December 31, 2020, the total retained earnings of PNB is Php thus, has sufficient retained earnings to declare the property dividends. Also, as of May 18, 2021, PNB has a total of 552 domestic Corporate Shareholders holding a total of common shares of PNB, and a total of 22 resident foreign Corporate Shareholders holding a total of common shares of PNB.

In view thereof, you now request for confirmation of the following:

1. The declaration and/or distribution by PNB of the Subject Shares by way of property dividends to the Corporate Shareholders are exempt from income tax on the part of the Corporate Shareholders pursuant to the provisions of

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Section 27(D)(4) and Section 28(A)(6)(d) of the National Internal Revenue Code (Tax Code) of 1997, as amended;

2. PNB does not realize any taxable income or gain on its declaration of dividends and the distribution of the Subject Shares by way of property dividends, and consequently, not subject to income tax and/or capital gains tax (CGT) upon its declaration of property dividends;

3. Considering that the declaration of dividends is not a donation and that PNB does not have any donative intent in declaring or distributing the Subject Shares by way of property dividends, the said declaration of property dividends is not subject to donor's tax;

4. Since the declaration of property dividends is not a sale, barter or exchange and that the Subject Shares are capital assets, not ordinary assets, of PNB, the said declaration of property dividends is likewise exempt from value-added tax (VAT) pursuant to the provisions of Section 105 of the Tax Code of 1997, as amended; and

5. The Subject Shares, when declared by PNB as property dividend and received by the Individual and Corporate Shareholders shall be recorded at its par value in their respective books.

In reply, please be informed as follows:

Exemption from Income Tax on the part of the Corporate Shareholders

Sections 27(D)(4) and 28(A)(6)(d) of the Tax Code of 1997, as amended, expressly state that:

"SEC. 27. Rates of Income Tax on Domestic Corporations. -

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(D) Rates of Tax on Certain Passive Incomes. -

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(4) Intercorporate Dividends. - Dividends received by a domestic corporation shall not be subject to tax under this Title: Provided, *That for foreign-sourced dividends to be exempt, the funds from such dividends actually received or remitted into the Philippines are reinvested in the business operations of the domestic corporation in the Philippines within the next taxable year from the time the foreign-sourced dividends were received and shall be limited to funding the working capital requirements, capital expenditures, dividend payments, investment in domestic subsidiaries, and infrastructure project:* Provided, further, *That the domestic corporation holds directly at least twenty percent (20%) of the outstanding shares of the foreign corporation and has held the shareholdings for a minimum of two (2) years at the time of the dividend distribution."*

"SEC. 28. Rates of Income Tax on Foreign Corporations. –

(A) Tax on Resident Foreign Corporations. -

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(6) Tax on Certain Incomes Received by a Resident Foreign Corporation. –

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(d) Intercorporate Dividends. - Dividends received by a resident foreign corporation from a domestic corporation liable to tax under this Code shall not be subject to tax under this Title."

Clearly, the distribution of property dividends made by PNB in favor of its Corporate Shareholders, domestic corporations and resident foreign corporations, is not subject to income tax pursuant to Sections 27(D)(4) and Section 28(A)(6)(d) of the Tax Code of 1997, as amended. Hence, the Subject Shares to be distributed by way of property dividends shall not be subject to income tax and consequently to withholding tax on the part of the foregoing Corporate Shareholders

Income Tax and CGT

In distributing dividends, a corporation merely distributes its unrestricted retained earnings to its stockholders as return on capital, and thus there is no flow of wealth as to the distributing corporation. In the distribution of dividends, a corporation realized no taxable income since the distribution among stockholders is not a sale nor were assets used to discharge an indebtedness.

Since PNB will not realize any gains, it should not be liable for CGT. Revenue Regulations (RR) No. 6-2008, as amended, provides for the rules on the imposition of CGT on the stockholders, and is not applicable to the distribution of dividends.

The Court of Tax Appeals (CTA) in *Trans-Asia Oil and Energy Development Corp. vs. Commissioner of Internal Revenue*[1] had occasion to rule that distribution of dividends is not covered by RR No. 6-2008 as it is an equity transaction where there could be no recognition of gain or loss, as follows:

"Clearly from all the foregoing, Petitioner's declaration and distribution of property dividends to its shareholders in the form of TAPC shares of stock is not within the ambit of the term "other disposition of shares of stock" in RR No. 6-2008, as amended by RR No. 6-2013. Instead, it is a mere equity transaction since petitioner did not recognize any gain or loss therefrom."

Therefore, on the part of the distributing domestic corporation, it is not liable for income tax and/or CGT considering that PNB will not realize any income.

Donor's Tax

Well-settled is the rule that the essential elements of a valid donation are the following: (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).

Under Section 98 of the Tax Code of 1997, as amended, donor's tax is imposed upon transfer by any person of a property by gift or donation inter vivos, which shall be made with a clear element of donative intent present in the transfer of property.

In the same case of *Trans-Asia Oil and Energy Development Corp. vs. Commissioner of Internal Revenue*, the CTA ruled that a corporation declaring dividends is not "within the ambit of the term "other disposition of shares of stock" in RR No. 6-2008" and instead as already mentioned above, is an equity transaction and thus no gain or loss, therefore, there could be "no inadequacy of consideration to speak of," to wit:

"Preliminarily, the court finds that Petitioner's declaration and distribution of property dividend is not within the ambit of the term "other

[1] CTA Case No. 9078, September 28, 2018

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disposition of shares of stock" that would recognize gain or loss from such disposal, as contemplated in RR No. 6-2008, as amended by RR No. 6-2013.

Dividend has been defined in Section 73 of the NIRC of 1997, as amended, as follows:

SEC. 73. Distribution of Dividends or Assets by Corporations.

(A) Definition of Dividends. — The term 'dividends' when used in this Title means any distribution made by a corporation to its shareholders out of its earnings or profits and payable to its shareholders, whether in money or in other property."

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The term "dividend" both in the technical sense and its ordinary acceptation, is that part or portion of the profits of the enterprise which the corporation, by its governing agents, sets apart for ratable division among the holders of the capital stock. It means the fund actually set aside, and declared by the directors of the corporation as dividends and duly ordered by the director, or by the stockholders at a corporate meeting, to be divided or distributed among the stockholders according to their respective interests.

Dividends comprise any distribution whether in cash or other property in the ordinary course of business, even though extraordinary in amount, made by a domestic or resident corporation to the stockholders out of its earnings or profits. Property dividend consists of a portion of corporate property paid to shareholders instead of cash or corporate stock.

Petitioner declared and distributed property dividends to its stockholders out of its earnings or profits. The said property dividends distributed were comprised of petitioner's shares of stock/investment in its wholly-owned subsidiary, TAPC, and were recorded in Petitioner's books at its carrying/book value. In recording the property dividends at their carrying/book value, there was no profit or gain realized or recognized in the transaction."

Hence, since there is no donative intent on the part of PNB to donate the Subject Shares and the transaction is being undertaken purely for business purposes, the declaration of dividends is not subject to donor's tax.

VAT

Sections 105 and 106 of the Tax Code of 1997, as amended, state that:

***"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.*

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*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.*

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SEC. 106. Value-Added Tax on Sale of Goods or Properties. -

(A) Rate and Base of Tax. - There shall be levied, assessed and collected on every sale, barter or exchange of goods or properties, value-added tax equivalent to twelve percent (12%) of the gross selling price or gross value in money of the goods or properties sold, bartered or exchanged, such tax to be paid by the seller or transferor.

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Considering that the Subject Shares are not held primarily for sale, barter or exchange in the ordinary course of its trade or business, and that the Subject Shares are capital assets, not ordinary assets, of PNB, the said declaration of property dividends is not subject to VAT pursuant to the provisions of Section 105 of the Tax Code of 1997, as amended.

Documentary stamp tax (DST)

Section 175 of the Tax Code of 1997, as amended, states that:

"SEC. 175. Stamp Tax on Sales, Agreements to Sell, Memoranda of Sales, Deliveries or Transfer of Shares or Certificates of Stock. *- On all sales, or agreements to sell, or memoranda of sale, or deliveries, or transfer of shares or certificates of stock in any association, company, or corporation, or transfer of such securities by assignment in blank, or by delivery, or by any paper or agreement, or memorandum or other evidences of transfer or sale whether entitling the holder in any manner to the benefit of such stock, or to secure the future payment of money, or for the future transfer of any stock, there shall be collected a documentary stamp tax of One peso and fifty centavos (P1.50) on each Two hundred pesos (P200) or fractional part thereof, of the par value of such due-bill, certificate of obligation or stock: Provided, That only one tax shall be collected on each sale or transfer of stock from one person to another, regardless of whether or not a certificate of stock is issued, indorsed, or delivered in pursuance of such sale or transfer: and Provided, further, That in the case of stock without par value the amount of documentary stamp tax herein prescribed shall be equivalent to fifty percent (50%)of the documentary stamp tax paid upon the original issue of said stock."*

Based on the above-quoted provisions, the transfer of the Subject Shares to the stockholders by way of declaration of property dividends is subject to DST.

Recording
(book/carrying value)

As regards the recording of the shares to be declared as property dividends, the Court of Tax Appeals in *Trans-Asia Oil and Energy Development Corp. vs. Commissioner of Internal Revenue*[2], has allowed the recording of the shares to be distributed as property dividends at book/carrying value in the books of the distributing and receiving corporation.

eCertificate Authorizing Registration (eCAR)/
Tax Clearance Certificate (TCL)

This Ruling is never intended, and shall not be construed, as giving authority to the Corporate Secretary of PHC to effect transfer of the Certificates of Stock in the name of the stockholders without the necessary eCAR/TCL issued by this Bureau. In this regard, this Ruling shall be presented to the Revenue District Office (RDO) concerned in order for the latter to issue the eCAR/TCL as prescribed in Revenue Memorandum Circular (RMC) No. 37-2012, in relation to RMC No. 39-2015.

[2] CTA Case No. 9078, September 28, 2018

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Based on all of the foregoing, it is our considered view that property dividends in the character of intercorporate dividends from one domestic corporation to another domestic corporation and from one domestic corporation to resident foreign corporation are exempt from income tax under Sections 27(D)(4) and 28(A)(6)(d) respectively, both of the Tax Code of 1997, as amended; exempt from income tax and/or CGT on the part of PNB; exempt from donor's tax under Section 99 of the Tax Code of 1997, as amended; and exempt from VAT under Section 105 of the Tax Code of 1997, as amended. This Office also confirms that the shares shall be recorded in the books of both distributor and receiving corporations at book/carrying value, provided that the book value of the shares distributed must be annotated at the back of the Certificate of Stocks which shall serve as the basis of the computation of the tax upon its subsequent disposition. However, the transfer of the Subject Shares to the stockholders by way of declaration of property dividends is subject to DST under Section 175 of the Tax Code of 1997, as amended.

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

Very truly yours,

CAESAR R. DULAY
Commissioner of Internal Revenue

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