REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE
Quezon City

Section 40(C)(2) and (6)(b) of the Tax Code of 1997, as amended
BIR Ruling No. S40M-474-21
S40M- 190 - 2022
APR 27 2022

SM RETAIL, INC.
SM Corporate Offices Bldg. D,
J.W. Diokno Blvd., Mall of Asia Complex,
Brgy. 076 Zone 10, CBP-IA
Pasay City

Attention: **CECILIA R. PATRICIO**
Authorized Representative

Gentlemen:

This refers to your request for confirmation of your opinion that the statutory merger of **SM Retail, Inc. ("SMRI")**, as the surviving corporation, with **Forsyth Equity Holdings, Inc. ("FEHI")**, **HFS Corporation ("HFSC")**, **Morrison Corporation ("MC")**, **San Mateo Bros., Inc. ("SMBI")**, and **Tangiers Resources Corp. ("TRC")**, as the absorbed corporations, is a tax-free transfer/exchange pursuant to Section 40 (C) (2) in relation to Section 40 (C) (6) (b) of the National Internal Revenue Code (Tax Code) of 1997, as amended.

Background:

SMRI is a corporation duly organized and existing under the laws of the Philippines primarily to receive, purchase, or otherwise acquire, obtain an interest in, own, hold, pledge, mortgage, assign, with respect to exchange, sell and otherwise dispose of, alone or in syndicates or otherwise in conjunction with others, and generally deal in and with all or any kinds of shares of stocks and other securities, without necessarily engaging in stock brokerage and financing business and in the business of an investment house.

On the other hand, FEHI, HFSC, MC, SMBI, and TRC (collectively referred to as the "Absorbed Corporations"), are corporations duly established and existing under the laws of the Philippines primarily to purchase, sell and dispose of, and generally deal in all kinds of shares of stock and other securities, without necessarily engaging in stock brokerage and financing business and in the business of an investment house.

The Absorbed Corporations are the main holding companies for SM Group's Retail operations involving food and department stores and leading local brands such as Ace Hardware, Watsons, Toy Kingdom, SM Appliances, Our Home, Baby Company, Kultura, Sports Central, Pet Express, and other specialty retailers.

SMRI and the Absorbed Corporations deemed it necessary and advisable to merge the corporations into one, with SMRI as the surviving corporation, since it will be both value and earnings accretive given the stores' competitive position, complementary retail portfolio and strong growth potential arising from the increase in diversity and retail footprint. Additionally, consolidation of the retail assets of the companies owned and/or controlled by the SM Group will result in simplification of the corporate structure and increase in organizational efficiencies and synergies. Thus, the Board of Directors and stockholders of SMRI and the Absorbed

Corporations in their respective meetings held on February 29, 2016, unanimously approved the Plan of Merger.

Pursuant to the Plan of Merger, SMRI shall increase its authorized capital stock in the amount of (, consisting of) shares with a par value of er share, to support the issuance of shares of stock to the current shareholders of the Absorbed Corporations.

On July 7, 2016, the Securities and Exchange Commission ("SEC") approved the Plan and Articles of Merger and the amendment of the Articles of Incorporation of SMRI amending its principal address and increasing its authorized capital stock to

Under the approved Plan and Articles of Merger, the merger shall become effective on the date of approval by the SEC of: (1) the increase in the authorized capital stock of SMRI; and (2) the Absorbed Corporation's Articles and Plan of Merger by the issuance of the Certificate of Filing of the Articles and Plan of Merger. Accordingly, the merger took effect on July 7, 2016 ("Effectiv e Date of Merger").

Also, pursuant to the approved Plan and Articles of Merger, SMRI shall issue a total of 4,965,208 new shares to the shareholders of the Absorbed Corporations, as follows:

1. 505,571 shares to the shareholders of FEHI;
2. 985,734 shares to the shareholders of HFSC;
3. 1,150,387 shares to the shareholders of MC;
4. 1,136,507 shares to the shareholders of SMBI; and
5. 1,187,009 shares to the shareholders of TRC.

The authorized capital stock, total number of issued and outstanding shares, the par value of each shares, and the total paid-up capital of each of SMRI and the Absorbed Corporations as set forth in their respective audited financial statements filed with the SEC together with the Plan and Articles of Merger are as follows:

SMRI

	Number of Shares	Type of Shares	Amount (at alue per share)
Authorized Capital Stock	15,000,000	Common	F
Subscribed Capital Stock	12,837,170	Common	F
Paid-Up Capital	12,837,170	Common	P

FEHI

	Number of Shares	Type of Shares	Amount (at par value per share)
Authorized Capital Stock	500,000	Common	F
Subscribed Capital Stock	500,000	Common	F
Paid-Up Capital	500,000	Common	P

HFSC

	Number of Shares	Type of Shares	Amount (at par value per share)
Authorized Capital Stock	360,000	Common	P
Subscribed Capital Stock	360,000	Common	F
Paid-Up Capital	360,000	Common	F

MC

	Number of Shares	Type of Shares	Amount (at par value per share)
Authorized Capital Stock	550,000	Common	
Subscribed Capital Stock	550,000	Common	
Paid-Up Capital	550,000	Common	

SMBI

	Number of Shares	Type of Shares	Amount (at par value per share)
Authorized Capital Stock	450,000	Common	P
Subscribed Capital Stock	450,000	Common	P
Paid-Up Capital	450,000	Common	P

TRC

	Number of Shares	Type of Shares	Amount (at par value per share)
Authorized Capital Stock	500,000	Common	P
Subscribed Capital Stock	500,000	Common	P
Paid-Up Capital	500,000	Common	P

Beginning on the effective date of the merger and upon approval of its increase of authorized capital stock, the authorized capital stock and issued and outstanding capital stock of SMRI are as follows:

Type of Share	Authorized	Issued and Outstanding	Par Value	Amount
Common	20,000,000 shares	17,802,378 shares	P100	

Based on the foregoing representations, you now request for confirmation of the following:

1. The statutory merger of SMRI and the Absorbed Corporations qualifies for non-recognition of gain or loss for income tax purposes in accordance with Sections 40 (C) (2) in relation to 40 (C) (6) (b) of the Tax Code of 1997, as amended. Therefore, no gain or loss shall be recognized by SMRI and the Absorbed Corporations on the transfer of all assets and assumption of liabilities pursuant to the Articles and Plan of Merger, and SMRI and the Absorbed Corporations will not be subject to income tax, withholding tax, or capital gains tax on the transfer.

2. The transfer of shares of stock which are legally and beneficially owned by the Absorbed Corporations to SMRI, as the surviving corporation, pursuant to the merger occurs by operation of law, in as much as the shares of stock are deemed transferred without further act or deed. Accordingly, it is not subject to documentary stamp tax (DST) under the Tax Code of 1997, as amended.

3. No DST shall be due on either the surrender of shares for cancellation as a result of the transfer of assets and assumption of liabilities by SMRI.

4. The transfer of properties by the Absorbed Corporations to SMRI will not give rise to any liability for donor's tax since there is no intention to donate

on the part of the Absorbed Corporations and that the merger was undertaken purely for legitimate business purposes.

5. The transfer of assets from the Absorbed Corporations to SMRI pursuant to the merger is not subject to value-added tax (VAT) and any unused input tax of the Absorbed Corporations as of the effective date of the merger shall be absorbed by SMRI as the surviving corporation pursuant to Section 106 of the Tax Code of 1997, as amended, and as implemented by Section 4.106-8(b)(3) of Revenue Regulations (RR) No. 16-2005, as amended.

In reply thereto, please be informed as follows:

1. The merger of SMRI and the Absorbed Corporations is a merger within the contemplation of Section 40 (C) (2), in relation to Section 40 (C) (6) (b) of the Tax Code of 1997, as amended, because SMRI shall acquire/assume all the assets and liabilities of the Absorbed Corporations and the same is necessary and advisable since it will be both value and earnings accretive given the stores' competitive position, complementary retail portfolio and strong growth potential arising from the increase in diversity and retail footprint. Additionally, consolidation of the retail assets of the companies owned and/or controlled by the SM Group will result in simplification of the corporate structure and increase in organizational efficiencies and synergies. Hence, said merger is being undertaken for a bona fide business purpose and not for the purpose of escaping the burden of taxation.

The merger of SMRI and the Absorbed Corporations qualifies for non-recognition of gain or loss for income tax purposes in accordance with Section 40 (C) (2) of the Tax Code of 1997, as amended, and that no gain or loss shall be recognized by the Absorbed Corporations, as the transferors of all assets and liabilities, to SMRI pursuant to the Articles and Plan of Merger.

Accordingly, no gain or loss shall be recognized by SMRI, as the transferee, on its receipt of the assets and liabilities of the Absorbed Corporations pursuant to and as a consequence of the merger.

The basis of the shares of stocks to be received by shareholders of the Absorbed Corporations upon the exchange shall be the same as the basis of the properties, stocks or securities exchanged, decreased by (1) the money received, and (2) the fair market value of the other property/ies received and increased by (a) the amount treated as dividend of the shareholders and (b) the amount of any gain that was recognized in the exchange[1].

The basis of the property transferred in the hands of the transferee (SMRI) shall be the same as it would be in the hands of the transferors (Absorbed Corporations) increased by the amount of the gain, if any, recognized to the transferor on the transfer.[2]

If the amount of the liabilities assumed plus the amount of the liabilities to which the property is subject exceed the total of the adjusted basis of the property transferred pursuant to such exchange, then such excess shall be considered as a gain from the sale or exchange of a capital asset or of property which is not a capital asset, as the case may be.[3]

The substituted basis of the properties transferred by the Absorbed Corporations to SMRI should strictly comply with the rule that cash and other cash items will be excluded from the computation of the adjusted basis of the properties transferred for purposes of determining whether liabilities assumed and to which the property is subject do not exceed the adjusted basis of the property transferred, pursuant to No. IV (A) (2) of Revenue Memorandum Ruling (RMR) No. 2-2002 dated June 10, 2002.

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[1] Sec. 40 (C)(5)(a) of the Tax Code of 1997, as amended.
[2] Sec. 40 (C)(5)(b), supra
[3] Sec. 40 (C)(4)(b), supra

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Accordingly, the allocated shares and the substituted basis of the properties transferred by the Absorbed Corporations based on their respective audited financial statements as of July 7, 2016 shall be as follows:

FEHI

Assets	Amount	Allocated Liabilities	Allocated Shares	Substituted Basis
Cash and cash equivalents		-	71,528	
Receivables		124,152,934	293,375	
Available for investments		57,840,279	136,677	
Other non-current assets		1,688,787	3,991	
Total		**183,682,000**	**505,571**	

Liabilities	Amount
Accounts payable and accrued expenses	-
Dividends payable	
Total	

HFSC

Assets	Amount	Allocated Liabilities	Allocated Shares	Substituted Basis
Cash and cash equivalents		-	1,424	
Receivables		201,089,708	525,209	
Available-for-sale investments		175,778,920	459,101	
Total		**376,868,628**	**985,734**	

Liabilities	Amount
Accounts payable and accrued expenses	
Dividends payable	
Total	

MC

Assets	Amount	Allocated Liabilities	Allocated Shares	Substituted Basis
Cash and cash equivalents		-	200,423	
Receivables		376,802,672	679,698	
Available for sale investments		147,851,589	266,703	
Other non-current assets		1,974,739	3,562	
Total		**526,629,000**	**1,150,387**	

Liabilities	Amount
Accounts payable and accrued expenses	
Dividends payable	
Total	

SMBI

Assets	Amount	Allocated Liabilities	Allocated Shares	Substituted Basis
Cash and cash equivalents		-	170,226	
Receivables		364,412,537	682,247	
Available for sale investments		149,802,122	280,457	
Other non-current assets		1,910,591	3,577	
Total		**516,125,250**	**1,136,507**	

Liabilities	Amount
Accounts payable and accrued expenses	
Dividends payable	
Total	

TRC

Assets	Amount	Allocated Liabilities	Allocated Shares	Substituted Basis
Cash and cash equivalents		-	197,160	
Receivables		370,001,746	699,981	
Available for sale investments		151,283,575	286,203	
Other non-current assets		1,937,179	3,665	
Total		**523,222,500**	**1,187,009**	

Liabilities	Amount
Accounts payable and accrued expenses	
Dividends payable	
Total	

2. No DST is due on the surrender by the shareholders of the Absorbed Corporations of their shares in the Absorbed Corporations for cancellation pursuant to the merger under Section 199 (m) of the Tax Code of 1997, as amended, in relation to Section 40 (C) (2) of the Tax Code of 1997, as amended.

On the other hand, pursuant to Section 174 of the Tax Code of 1997, as amended, DST at the rate of P1.00[4] or each par value, or fractional part thereof, shall be imposed on the original issuance of shares by SMRI in favor of the shareholders of the Absorbed Corporations as a consequence of the merger.

3. 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 the Absorbed Corporations to donate to SMRI their assets since the transaction is purely for a legitimate 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.

4. The transfer of assets/properties of the Absorbed Corporations to SMRI as a consequence of the merger is not subject to VAT pursuant to Section 105 of the Tax Code of 1997, as amended. The transfer of assets/properties to effectuate a merger is not made in the course of business but by operation of law pursuant to the merger.

[4] Old DST rate is used since the transaction took place prior to the effectivity of RA No. 10963 or the TRAIN Law.

Furthermore, the assets/properties transferred by the Absorbed Corporations to SMRI do not include goods or properties that are used in business, that are held for sale or for lease by the transferors, that are originally intended for sale or for use in the course of business, nor that are of any character or nature subject to VAT.

5. The excess and unutilized creditable withholding taxes (CWT) of the Absorbed Corporations as of the effective date of the merger, which form part of the assets to be transferred by the Absorbed Corporations to SMRI as a consequence of the merger, may be applied as a tax credit by SMRI against its income tax due for the taxable year 2016, the effective date of the merger being July 7, 2016, and in the succeeding taxable years, or may be the subject of a claim for refund or issuance of a tax credit certificate (TCC).

6. The excess and unexpired Minimum Corporate Income Tax (MCIT) of the Absorbed Corporations as of the effective date of the merger shall be carried forward and credited against the regular corporate income tax due of the surviving corporation, SMRI, for the three (3) immediately succeeding taxable years pursuant to Section 27(E)(2) of the Tax Code of 1997, as amended. Since the excess and unexpired MCIT of the Absorbed Corporations are among the rights, privileges, property and/or interest of the Absorbed Corporations, their excess and unexpired MCIT shall be transferred to and vested in SMRI on the effective date of the merger. Thus, the Absorbed Corporations' excess and unexpired MCIT shall be carried forward and credited against the regular corporate income tax of SMRI subject to the three-year-carry-forward period reckoned from the date of payment of the Absorbed Corporations of their MCIT.

7. It is to be emphasized, however, that the net operating loss carry-over (NOLCO) under Section 34(D)(3) of the Tax Code of 1997, as amended, and as implemented by RR No. 14-2001, of the Absorbed Corporations, if any, is not one of their assets that can be transferred and absorbed by the surviving corporation, SMRI, as this privilege or deduction can be availed of merely by the Absorbed Corporations. Accordingly, the tax-free merger does not cover the NOLCO of the Absorbed Corporations that can be transferred and absorbed by SMRI.

8. The retained earnings pertaining to the individual shareholders of the Absorbed Corporations, are subject to the ten percent (10%) final withholding tax on dividends constructively received by its individual shareholders pursuant to Section 24 (B) (2) of the Tax Code of 1997, as amended.

However, in order that the above-described reorganization can be considered as merger under Section 40(C)(2) and (6)(b) of the Tax Code of 1997, the parties to the merger should comply with the following requirements set forth under RR No. 18-2001:

A. The plan of reorganization should be adopted by each of the corporations, parties thereto, the adoption being shown by the acts of its duly constituted responsible officers and appearing upon the official records of the corporation. Each corporation, which is a party to the reorganization, shall file, as part of its return for the taxable year within which the reorganization occurred a complete statement of all facts pertinent to the non-recognition of gain or loss in connection with the reorganization, including:

   1. A copy of the plan of reorganization, together with a statement executed under the penalties of perjury, showing in full the purposes thereof and in detail all transactions incident to, or pursuant to the plan;

   2. A complete statement of all cost or other basis of all property, including all stocks or securities, transferred incident to the plan;

   3. A statement of the amount of stock or securities and other property or money received from the exchange, including a statement of all

distribution of other disposition made thereof. The amount of each kind of stock or securities and other property received shall be stated on the basis of the fair market value thereof at the date of the exchange;

4. A statement of the amount and nature of any liabilities assumed upon the exchange, and the amount and nature of any liabilities to which any of the property acquired in the exchange is subject.

B. Every taxpayer, other than a corporation, party to the reorganization, who received stock or securities and other property or money upon a tax-free exchange in connection with a corporate reorganization shall incorporate in his income tax return for the taxable year in which the exchange takes place a complete statement of all facts pertinent to the non-recognition of gain or loss upon such exchange, including:

1. A statement of the cost or other basis of the stock or securities transferred in the exchange; and

2. A statement in full of the amount of stock or securities and other property or money received from the exchange, including any liabilities assumed upon the exchange, and any liabilities to which property received is subject. The amount of each kind of stock or securities and other property (other liabilities assumed upon the exchange) received shall be set forth upon the basis of the fair market value thereof at the date of the exchange.

C. Records in substantial form shall be kept by every taxpayer who participates in a tax-free exchange in connection with a corporate reorganization showing the cost or other basis of the transferred property or money received (including any liabilities assumed on the exchange, or any liabilities to which any of the properties received were subject), in order to facilitate the determination of gain or loss from subsequent disposition of such stock of securities and other property received from the exchange.

In addition to the foregoing requirements, the parties shall enclose with their respective income tax returns for the taxable year in which the tax-free exchange occurred a copy of the request for ruling filed with, and the corresponding ruling issued by the Bureau of Internal Revenue, both duly stamped received by the appropriate office of the Bureau of Internal Revenue. Such parties shall include as a note to their respective audited financial statements for the taxable year in which the exchange occurred a statement to the effect that they hold such assets/shares acquired in a tax-free exchange and the year in which such exchange occurred, and in the taxable years until the subject properties are subsequently transferred to another transferee.

Moreover, the absorbed/dissolving corporation/s, its shareholders and the surviving/ transferee corporation shall record in their respective books the mandatory accounting entries stated in **Annex "A"** hereof, pursuant to Revenue Memorandum Order (RMO) No. 17-2016.

Furthermore, the parties shall cause to annotate at the back of the Transfer Certificates of Title (TCT) and/or Certificates of Stock, the date the merger was executed, the original or historical cost of acquisition of the properties or 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 Register of Deeds or by the Corporate Secretary of this condition shall be penalized under Section 269 or 275, as the case maybe, of the Tax Code of 1997, as amended.

Finally, it is required that within ninety (90) days from receipt of this ruling, the parties to the transaction must submit to the Law and Legislative Division, Bureau of Internal

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Revenue, certified true copies by the Corporate Secretary, of duly annotated Certificates of Stock, in respect of the shares of stock of the transferee corporation, including the revised allocation of shares and re-computation of the substituted bases of the properties which shall be in accordance with RMR No. 2-2002.

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

K-1-LMAT

By:
MARISSA O. CABREROS
Deputy Commissioner
Legal Group
Officer-In-Charge

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