



TAX LAW FOR BUSINESS
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VAT on exchange of property for shares of stocks

The Bureau of Internal Revenue (BIR) issued Revenue Regulations (RR) 10-2011 on dated July 1 amending the value-added tax (VAT) regulations specifically applicable on exchanges of goods and pieces of property for shares of stocks of another company. Under the new regulations, all goods and property exchanged for shares of stocks are now subject to 12-percent VAT, except when the goods or property, or the transferor is specifically exempt.

The VAT law, as amended by Republic Act (RA) 9337, provides that any person who, in the course of trade or business, sells or barter, exchanges, leases goods or properties, xxx shall be subject to VAT. The phrase "in the course of trade or business" was defined as the regular conduct or pursuit of a commercial or an economic activity, including transactions incidental thereto xxx".

It further provides under the "Exempt Transactions" that, in case of sale of real property not primarily held for sale to customers or held for lease in the ordinary course of trade or business, the same shall be exempt from VAT.

However, when RR 04-2007 was issued amending Section 4.109-1(B)(p) of RR 16-2005 (Consolidated VAT Regulations implementing RA 9337), the BIR clarified that "even if the real property is not primarily held for sale to customers or held for lease in the ordinary course of trade or business but the same is used in the trade or business of the seller, the sale thereof shall be subject to VAT being a transaction incidental to the taxpayer's main business." The latter provision was presumably added by the BIR to be consistent with the applicability of VAT even to transactions that may only be incidental to the main trade or business of the seller.

In contrast, however, Section 4.106-8 of RR 16-2005, as amended by RR 04-2011, provides that in transactions affecting a change or cessation of status as VAT-registered persons, "the VAT shall not apply to goods or property existing as of the occurrence of the following:

(1) Change of control of a corporation by the acquisition of the controlling interest of such corporation by another stockholder or group of stockholders. The goods or property used in business or those comprising the stock-in-trade of the corporation, having a change in corporate control, will not be considered sold, bartered or exchanged despite the change in the ownership interest in the corporation.

(2) Change in the trade or corporate name of the business.

(3) Merger or consolidation of corporations.”

In the illustration given for the first scenario, the exchange of real property held for sale or for lease for shares of stock of a merchandising company, whether it results in a corporate control or not, is subject to VAT. However, in case of transfer of real property for shares of stock wherein both parties to the transaction are real-estate dealers, and the transferor gains control of the transferee-corporation, the transaction is exempt from VAT.

With the issuance of RR 10-2011, the BIR amended the foregoing provision to read as:

“The VAT shall not apply on goods or property, which are originally intended for sale or for use in the course of business existing as of the occurrence of the following:

(1) Change of control of a corporation by the acquisition of the controlling interest of such corporation by another stockholder (individual or corporate) or group of stockholders. The goods or property used in business (including those held for lease) or those comprising the stock-in-trade of the corporation, having a change in corporate control, will not be considered sold, bartered or exchanged despite the change in the ownership interest in the corporation.

However, the exchange of goods or property, including the real-estate property used in the business or held for sale or for lease by the transferor, for shares of stock, whether resulting in corporate control or not, is subject to VAT.

(2) Change in the trade or corporate name of the business.

(3) Merger or consolidation of corporations.”

Hence, the applicability of VAT on the earlier illustration was modified, holding that the exchange of real property held for sale or lease for shares, whether resulting in a corporate control or not, is subject to VAT.

Taking into account the latest amendment, it seems that exchange of property for shares of stock, whether it results in a corporate control as contemplated under Section 40 (2) of the 1997 Tax Code, and regardless of the nature of the business of the parties involved in the transaction, shall now be subject to VAT.

Although it would seem that these amendments had clarified the BIR position, still their validity and applicability remain dubious or uncertain. Two questions remain unanswered: Does the BIR’s interpretation constitute administrative legislation?

Are the exchanges under the foregoing instances considered acts of business reorganization and not the VATable transfer contemplated by law?

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