

[BIR REVENUE MEMORANDUM CIRCULAR NO. 19-99, February 25, 1999]

"DEEMED SALE", FOR VAT PURPOSES, OF MERCHANDISE INVENTORIES IN CASES OF MERGERS/CONSOLIDATIONS OF CORPORATIONS

Quoted hereunder is the pertinent portion of BIR Ruling No. S34-263-97 dated October 16, 1997:

"Moreover, for value-added tax purposes, the transfer of the respective assets, including tangible and movable properties, by the 10 ABSORBED CORPORATIONS to USWCI pursuant to the merger shall not be subject to the value-added tax, and any unused input tax of each of the 10 ABSORBED CORPORATIONS as of the date of merger, will be absorbed by USWCI as the surviving corporation, pursuant to Section 5(b)(3) of the Revenue Regulations No. 5-87. (BIR Ruling No. 063-93 dated January 10, 1993; BIR Ruling No. 472-93 dated December 3, 1993)"

It is provided therein that (a) the transferred assets, which include the merchandise inventory of the absorbed corporations, "shall not be subject to the value-added tax" and (b) that the unused input taxes of the absorbed entities shall be transferred for the use or tax credit to the output tax of the surviving corporation.

The Ruling in question enunciated a twin illegality. The absorbed corporation, upon the merger, ceases or retires from doing business, so that its merchandise inventory transferred to the surviving corporation, by clear provision of law, is "deemed sale" for VAT purposes (Section 106, (B) (4), Tax Reform Code). The unused input taxes of the absorbed corporations cannot legally be transferred to the surviving corporation for the latter's use as tax credits to its output VAT. This could only be used as tax credit to the VAT payments of the absorbed corporations and the same is not transferable to a party not privy to the contracts from where the input taxes arose (Section 110 (A) (2) (a) of Tax Code, *supra.*, as implemented by Section 4.104-1 (d) of Revenue Regulations No. 7-95). In other words, only the direct buyers of goods/services to whom the input taxes were "passed on" could avail of the right to tax credit. Under the VAT law, the absorbed entity should pay the VAT on the merchandise inventory, there being a "deemed sale" transaction, after tax crediting the corresponding input taxes, with the right to claim refund, if the input exceeds the output tax. If the output tax is paid, this maybe "passed on" to the surviving corporation for its use as tax credit. BIR Ruling No. S34-263-97 is a flagrant violation of the VAT law, as above pointed out. It was aptly stated by the Supreme Court that —

"x x x that all such issuances must not override, but must remain consistent and in harmony with, the law they seek to apply and implement. Administrative rules and regulations are intended to carry out, neither to supplant nor to modify the law" (Commissioner of Internal