Republic of the Philippines
COURT OF TAX APPEALS
Quezon City

EN BANC

COMMISSIONER OF INTERNAL REVENUE, Petitioners,	**CTA EB CASE NO. 1257** (CTA Case No. 8428)
-versus-	Present: DEL ROSARIO, P.J., CASTAÑEDA, JR. BAUTISTA UY CASANOVA FABON-VICTORINO MINDARO-GRULLA COTANGCO-MANALASTAS RINGPIS-LIBAN, JJ.
THE HONGKONG SHANGHAI BANKING CORPORATION LIMITED – PHILIPPINE BRANCH, Respondent.	Promulgated: SEP 09 2016 2:35 p.m.

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RESOLUTION

MINDARO-GRULLA, J.:

This resolves petitioner's "Motion for Reconsideration" of the Decision dated May 17, 2016 of this Court en banc, the dispositive portion of which states:

> ***"WHEREFORE,*** *premises considered, the petition is* ***DENIED*** *for lack of merit. The Decision of the Third Division of this Court in CTA Case No. 8428, promulgated on October 13, 2014 and its Resolution, promulgated on December 10, 2014, are hereby* ***AFFIRMED***. *No pronouncement as to costs.*
>
> ***SO ORDERED***."

In assailing this Court's Decision, petitioner raised this sole issue:

"I.

THE HONORABLE COURT ERRED WHEN IT CANCELLED THE DEFICIENCY INCOME TAX ASSESSMENT AGAINST RESPONDENT ON THE SALE

OF "GOODWILL" OF ITS MERCHANT ACQUIRING BUSINESS FOR TAXABLE YEAR 2008 IN THE AMOUNT OF P342,886,095.88."

Petitioner maintains its arguments previously raised before the Division of this Court and the Court en banc. Petitioner insisted that the intention of respondent was to sell its Merchant Acquiring Business for a consideration of P899,342,921.00. Likewise, petitioner insisted that the creation of GPAP-Philippines was to circumvent the law to classify the transaction as a tax free exchange instead of a sale of the POS terminals and the goodwill which is an ordinary asset subject to 35% income tax.

The Court received respondent's comment on August 1, 2016.

We resolve to deny the motion.

After a careful examination of petitioner's "Motion for Reconsideration", the Court finds that the issues and arguments raised in said motion had already been sufficiently passed upon and fully discussed not only by the Third Division's Decision dated October 13, 2014 and its Resolution dated December 10, 2014 but also by this Court en banc's Decision dated May 17, 2016.

To reiterate, HSBC-Philippines and GPAP-Singapore agreed to recognize and value the goodwill of the Merchant Acquiring Business in the Share Sale and Purchase Agreement at P885,378,821.00. However, while goodwill was recognized and valued, the same cannot be sold or purchased independently of the Merchant Acquiring Business. As to whether said goodwill is an ordinary asset and subject to 35% income tax, we rule in the negative.

The gain or the loss is ordinary when the property sold or exchanged is not a capital asset. Goodwill is not an ordinary asset as it is not among the exceptions on the definition of capital asset. A capital asset is defined negatively in Section 39(A)(1) of the 1997 NIRC, as amended[1]; to wit:

> *(1) Capital Assets. - The term 'capital assets' means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property used in the trade or business, of a character which is subject to the allowance for depreciation provided in Subsection (F) of Section 34; or real property used in trade or business of the taxpayer."*

Thus, We find that the Court's Division aptly ruled that it is a capital asset subject to capital gains tax, to wit:

> *For easy reference, Section 27(A) of the 1997 NIRC, as amended, provides:*
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> > *"SECTION 27. Rates of Income Tax on Domestic Corporations. - (A) In General. - Except as otherwise provided in this Code, an income tax of thirty-five percent (35 %) is hereby imposed upon the taxable income derived during each taxable year from all sources within and without the Philippines by every corporation, as defined in Section 22(B) of this Code and taxable under this Title as a corporation, organized in, or existing under the laws of the Philippines: Provided, That effective January 1, 1998, the rate of income tax shall be thirty-four percent (34%); effective January 1, 1999, the rate shall be thirty-three percent (33%); and effective January 1, 2000 and thereafter, the rate shall be thirty-two percent (32%)."*
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> *And Section 22(Z) of the Code clearly defines an "ordinary income," as follows:*
>
> > *"(Z) The term 'ordinary income' includes any gain from the sale or exchange of property which is not a*

[1] China Banking Corporation vs. CIR & Court of Appeals, et. al, G.R. No. 125508, July 19, 2000

capital asset or property described in Section 39(A)(1). Any gain from the sale or exchange of property which is treated or considered, under other provisions of this Title, as 'ordinary income' shall be treated as gain from the sale or exchange of property which is not a capital asset as defined in Section 39(A)(1). The term 'ordinary loss' includes any loss from the sale or exchange of property which is not a capital asset. Any loss from the sale or exchange of property which is treated or considered, under other provisions of this Title, as 'ordinary loss' shall be treated as loss from the sale or exchange of property which is not a capital asset."

Thus, Section 39(A)(1) of the 1997 NIRC, as amended, states:

"SECTION 39. Capital Gains and Losses. –

(A) Definitions. - As used in this Title –

(1) Capital Assets. - The term 'capital assets' means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property used in the trade or business, of a character which is subject to the allowance for depreciation provided in Subsection (F) of Section 34; or real property used in trade or business of the taxpayer."

In the case of Tuason, Jr. v. Lingad, the Supreme Court ruled as follows:

"As thus defined by law, the term 'capital assets' includes all the properties of a taxpayer whether or not connected with his trade or business, except: (1) stock in trade or other property included in the taxpayer's inventory; (2) property primarily for sale to customers in the ordinary course of his trade or business; (3) property used in the trade or business of the taxpayer and subject to depreciation allowance; and (4) real property used in trade or business. If the taxpayer sells or exchanges any of the properties above enumerated, any gain or loss relative thereto is an ordinary gain or an ordinary

loss; the gain or loss from the sale or exchange of all other properties of the taxpayer is a capital gain or a capital loss." (Boldfacing supplied and citations omitted.)

And in the determination of whether a property is a capital or ordinary asset, a careful perusal and weighing of the surrounding circumstances must be made. In the case at bench, after a thorough review of the records of the case, the Court finds respondent's arguments to be without merit.

It is well-settled that a capital gain (or a capital loss) normally requires the concurrence of two conditions: (1) There is a sale or exchange; and (2) the thing sold or exchanged is a capital asset.

Applying the foregoing, and based on the records of the case- the creation of GPAP-Phils to transfer the Merchant Acquiring Business of HSBC by way of additional paid-in capital; the subscription of 139,640 shares of stocks of GPAP-Phils in exchange for HSBC's POS terminals; the subscription of 1 common share of GPAP-Phils in exchange for HSBC' s Merchant Agreements; and the subsequent assignment of the total number of shares of 139,641, subscribed by HSBC to GPAP-Singapore, clearly shows that it is a sale of capital asset, as earlier quoted under Section 39(A)(1) of the 1997 NIRC, as amended, to which petitioner paid the total amount of P89,929,292.10.

Concomitantly, the sale of the Merchant Acquiring Business of HSBC-Philippines at a premium to GPAP-Singapore whereby goodwill was recognized and valued in the Share Sale and Purchase Agreement for P885,378,821.00 is a sale of capital asset since it is not included in stock in trade nor properly included in the inventory at the close of the taxable year, nor is it held primarily for sale to customers in the ordinary course of his trade or business, nor is it a property used in the trade or business, of a character which is subject to the allowance for depreciation provided in subsection (f) of Section 29 of the NIRC, nor is it real property used in the trade or business.

WHEREFORE, premises considered, petitioner's "Motion for Reconsideration" is hereby **DENIED** for lack of merit.

SO ORDERED.

Cielito N. Mindaro-Grulla
CIELITO N. MINDARO-GRULLA
Associate Justice

WE CONCUR:

ROMAN G. DEL ROSARIO
Presiding Justice

Juanito C. Castañeda, Jr.
JUANITO C. CASTAÑEDA, JR.
Associate Justice

LOVELL R. BAUTISTA
Associate Justice

ERLINDA P. UY
Associate Justice

CAESAR A. CASANOVA
Associate Justice

(On Official Business)
ESPERANZA R. FABON-VICTORINO
Associate Justice

AMELIA R. COTANGCO-MANALASTAS
Associate Justice

Ma. Belen
MA. BELEN M. RINGPIS LIBAN
Associate Justice