REPUBLIC OF THE PHILIPPI

DEPARTMENT OF FINANCE

BUREAU OF INTERNAL REVENUE

Quezon City

Sec. 40 (C)(2)&(6)(b) of the Tax Code, as amended	
BIR Ruling No. 214-2012; BIR Ruling No. 100-2017; BIR Ruling No. 75-2018	
S40M- 319-2022	
JUN 29 2022	

BDB LAW
Du-Baladad and Associates
20th Floor, Chatham House, Rufino cor. Valero treets
Salcedo Village, Makati City

Attention: **Atty. Benedicta Du-Baladad**
Managing Partner

Gentlemen:

This refers to your request on behalf of your clients, Innodata Knowledge Services, Inc. ("IKSI") and Content Online Services, Inc. ("COSI") for confirmation that the merger of COSI, as the absorbed corporation, with IKSI, as the surviving corporation, qualifies as a tax-free merger under Section 40 (C)(2) and (6)(b) of the National Internal Revenue Code of 1997 ("Tax Code"), as amended.

IKSI (formerly: Innodata XML Content Factory, Inc.) is a corporation duly registered with the Securities and Exchange Commission (SEC) under SEC Registration No. with TIN . located at HVG Arcade I.T. Park, Brgy. Subangdaku, Mandaue City, Cebu. IKSI is engaged in the export of all forms of electronic information processing, particularly in the areas of data capture, conversion and imaging, utilizing state of the art technology, including without limitation extendible mark-up language as a device for extracting information. It has an authorized capital stock of Pesos (P) divided into . ( ) shares with par value of P1.00 per share, of which N ( ) shares have been duly subscribed and fully paid.

COSI, on the other hand, is likewise a domestic corporation with SEC Registration No. with its principal place of business is at G. marine I.T. Center, Alternate Road, Legaspi City, Albay. It is engaged in the business of electronic information processing services particularly in the areas of data capture, conversion and imaging and the development of software and other tools to assist in the efficient and effective discharging of its services. COSI has an authorized capital stock of Pesos (P. divided into and ( )) shares with a par value of P10.00 per share, of which . and (shares have been duly subscribed and fully paid.

The management of both corporations agreed and deemed it wise and prudent to merge the operations of the two (2) corporations, with IKSI as the surviving corporation. The

9.

merger is desirable and advantageous to the two (2) corporations and their respective stockholders considering their business objectives, including, without limitation, the following:

1. as the constituent corporations are engaged in the same or related type of business, the merger will consolidate their related businesses;

2. the integration of the administrative facilities of the constituent corporations will result in economies of scale and efficiency in management, operations and rendition of services to customers; and

3. the merger will make possible the more productive use of the properties of the constituent corporations.

Pursuant to the articles and plan of merger, which was approved by the SEC on December 8, 2011 and with effective date on January 1, 2012, all the rights, business, powers, privileges, immunities, franchises and assets of the absorbed corporation (COSI) such as real or personal, tangible or intangible, and all receivables due on whatever account, including subscription to shares and choses in action, and all and every other interest of, belonging to or due to the absorbed corporation shall be deemed transferred to the surviving corporation without further act or deed. Likewise, the surviving corporation shall assume all obligations, debts, loans, payables and liabilities. The total amount of assets transferred from COSI to IKSI exceed the total amount of liabilities transferred and assumed by IKSI.

On the effective date of merger (January 1, 2012), the stockholders of the absorbed corporation shall surrender their shares in the absorbed corporation, and in exchange thereof, the surviving corporation shall issue its own shares.

Based on the foregoing representations, you now request confirmation of your opinion that –

1. *Income Tax.* The merger between IKSI and COSI is a statutory and tax-free merger under Section 40(C)(2) and (6)(b) of the Tax Code, as amended. Accordingly, no gain or loss shall be recognized on the transfer of assets and liabilities of COSI to IKSI. The basis of the transferred assets and liabilities in the hands of IKSI shall be the same as it would be in the hands of COSI.

2. *Value-added Tax.* The transfer of assets of COSI to IKSI is not subject to VAT pursuant to Section 4.106-8(b)(3) of Revenue Regulations (RR) No. 16-2005, otherwise known as the Consolidated Value-Added Tax Regulations of 2005.

3. *Documentary Stamp Tax.* The transfer of assets and liabilities of COSI to IKSI pursuant to the merger is not subject to DST in accordance with Section 199(m) of Republic Act (RA) No. 9243, otherwise known as an Act Rationalizing the Provisions on the Documentary Stamp Tax (DST) of the Tax Code of 1997, as amended, as implemented by Revenue Regulations No. 13-2004.

In reply thereto, please be informed as follows:

1. The foregoing merger of COSI and IKSI is a merger within the contemplation of Section 40 (C)(2)(a) in relation to Section 40(C)(6)(b) of the Tax Code, as amended, for the following business reasons: (1) the constituent corporations are engaged in the same or related type of business, the merger will consolidate their related businesses; (2) the integration of the administrative facilities of the constituent corporations will result in economies of scale and efficiency in management, operations and rendition of services to customers; and (3) the merger will make possible the more productive use of the properties of the constituent

9k

S40M- 319-2022
JUN 29 2022

corporations. Hence, the merger of COSI and IKSI is being undertaken for a *bona fide* business purpose and not for the purpose of escaping the burden of taxation.

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

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

On the other hand, the bases of the shares of stocks to be received by the shareholders of COSI upon the exchange shall be the same as the bases 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. (*Sec. 40 (C) (5) (a) of the Tax Code, as amended*)

The basis of the properties transferred in the hands of the transferee (IKSI) shall be the same as it would be in the hands of the transferor (COSI) increased by the amount of the gain, if any, recognized to the transferor (COSI) on the transfer. (*Sec. 40 (C) (5) (b), supra*)

Finally, 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 properties transferred pursuant to such exchange, then such excess shall be considered as a gain, on the part of the transferor, from the sale or exchange of a capital asset or of property which is not a capital asset, as the case may be. (Sec. 40 (C) (4) (b), *supra*)

The substituted basis of the properties transferred by COSI to IKSI shall 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.

Accordingly, the allocated shares and liabilities, and the substituted basis of the assets transferred by COSI to IKSI, based on COSI's audited financial statements as of December 31, 2011 shall be as follows:

	Amount (in Php)	**Allocated Liabilities**	**Allocated Shares**	**Substituted Basis (in Php)**
Cash				
Trade and other receivables				
Other current assets				
Property and equipment – net				
Deferred tax assets – net				
Other non-current assets -net				
TOTAL				

gu f

S40M-

Liability	Amount (in Php)
Trade and other payables	
Microsoft license obligations (current)	
Microsoft license obligations (non-current)	
Post-employment benefit obligation	
TOTAL	

2. The transfer of properties of COSI to IKSI as a consequence of the merger shall not be subject to any output tax, pursuant to Section 4.106-8(b)(3) of Revenue Regulations (RR) No. 16-2005, as amended by RR No. 4-2007, as further amended by RR No. 10-2011, and last amended by RR No. 4-2021. The conveyance of properties to effectuate a merger is not made in the course of business but by operation of law pursuant to the merger. Thus, any unused input tax as of the effective date of merger will be absorbed by IKSI, as the surviving corporation pursuant to Section 4.106-8(b)(3) of RR No. 16-2005, as amended by RR Nos. 4-2007; 10-2011 and 4-2021.

3. No DST is due on the transfer of assets made pursuant to the Plan of Merger under Section 199 (m) of the Tax Code, as amended by Republic Act (RA) No. 9243, in relation to Section 40 (C) (2) of the Tax Code, as amended. *(BIR Ruling No. S40-0427-2020 dated July 30, 2020)*

However, a DST at the rate of P1.00[1] on each P200 par value, or fractional part thereof, shall be imposed on the original issuance of shares by IKSI to the stockholders of COSI as a consequence of the merger as provided under Section 174 of the Tax Code, as amended.

4. The retained earnings of COSI 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, as amended. *(BIR Ruling No. 1422-18 dated December 7, 2018)*

In order that the above-described reorganization can be considered as merger under Section 40 (C) (2) and (6) (b) of the Tax Code, as amended, 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

---

[1] The Plan of Merger was approved by SEC on December 8, 2011

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 merger occurred a copy of the request for ruling filed with, and the corresponding ruling issued by, the Bureau of Internal Revenue, both duly stamp-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 merger occurred a statement to the effect that they hold such assets/shares acquired in a merger and the year in which such merger occurred, and in the taxable years until the subject properties are subsequently transferred to another transferee.

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

The parties shall cause to annotate at the back of the Transfer Certificates of Title and/or Certificates of Stock, the date the merger was executed, the original/historical/adjusted costs 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 Corporate Secretary of this condition shall be penalized under Section 275 of the Tax Code, as amended. It is further 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 Revenue, proof of annotation of the original/historical/adjusted bases of the properties and/or real properties involved in the transfer and certified true copies by the Corporate Secretary, of

S40M-319-2022
JUN 29 2022

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

052154

K-1
gps(innodata-content online merger)