February 26, 2021

BIR RULING NO. OT-038-21

Sec. 32 (B) (6) (a) & (b), NIRC of 1997, as amended; BIR Ruling No. 1151-18

AAA

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Dear AAA,

This refers to your letter request for clarification on the following:

1. Whether or not your retirement benefits are exempt from payment of tax; and

2. Whether or not the requirement under Sec. 2.78.1 (B) (1) (a) (iv) of Revenue Regulations (RR) No. 2-98, as amended, applies to an employee who has previously availed of a tax exemption pursuant to retrenchment.

As represented, you were employed by the Philippine Associated Smelting & Refining ("PASAR or "the Company") on April 16, 2003. On August 18, 2012, you retired at the age of sixty (60) years old after nine (9) years and four (4) months of service to the Company. At the time of your retirement, you were holding a managerial position in the Company. While PASAR has a retirement plan under its Collective Bargaining Agreement with the Union, the same is applicable to the rank and file employees only.

In reply, please be informed that Section 32 (B) (6) (a) of the National Internal Revenue Code of 1997 (Tax Code), as amended states that:

"SEC. 32. Gross Income. —

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(B) Exclusions from Gross Income. — The following items shall not be included in gross income and shall be exempt from taxation under this Title:

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(6) Retirement Benefits, Pensions, Gratuities, etc. —

(a) Retirement benefits received under Republic Act No. 7641 and those received by officials and employees of private firms, whether individual or corporate, in accordance with a reasonable private benefit plan maintained by the employer: Provided, That the retiring official or employee has been in the service of the same employer for at least ten (10) years and is not less than Fifty (50) years of age at the time of his retirement: Provided, further, That the benefits granted under this subparagraph shall be availed of by an official or employee only once. x x x"

Based on the above-quoted provision, if the company maintains a private retirement plan which have been determined by the Bureau of Internal Revenue (BIR) as a "reasonable retirement benefit plan," the retirement benefits that will be received by the employees shall be exempt from income tax, provided that the two (2) conditions are met, *viz.*: (1) the employee had been in the service of the same private firm for at least ten (10) years; and (2) he is at least fifty (50) years old at the time of retirement. In the absence of a retirement plan or agreement providing for retirement benefits of employees in the company, the provisions of Republic Act (RA) No. 7641 shall apply. Section 1 of RA No. 7641, amending the Labor Code of the Philippines, provides:

"SEC. 1. Article 287 of Presidential Decree No. 442, as amended, otherwise known as the Labor Code of the Philippines, is hereby amended to read as follows:

ART. 287. Retirement. — Any employee may be retired upon reaching the retirement age established in the collective bargaining agreement or other applicable employment contract. In case of retirement, the employee shall be entitled to receive such retirement benefits as he may have earned under existing laws and any collective bargaining agreement and other agreements: Provided, however, That an employee's retirement benefits under any collective bargaining and other agreements shall not be less than those provided herein.

In the absence of a retirement plan or agreement providing for retirement benefits of employees in the establishment, an employee upon reaching the age of sixty (60) years or more, but not beyond sixty-five (65) years which is hereby declared the compulsory retirement age, who has served at least five (5) years in the said establishment, may retire and shall be entitled to retirement pay equivalent to at least one-half (1/2) month salary for every year of service, a fraction of at least six (6) months being considered as one whole year.

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Unless the parties provide for broader inclusions, the term one-half (1/2) month salary shall mean fifteen (15) days plus one-twelfth (1/12) of the 13th month pay and the cash equivalent of not more than five (5) days of service incentive leaves."

In this case, since there is no separate retirement benefit plan for managerial employees, the retirement benefits set forth under RA No. 7641 shall apply, *i.e.*, at least one-half (1/2) month salary for every year of service of an employee who has reached the age of sixty (60) years or more, but not beyond sixty-five (65) years, and rendered at least five (5) years of service in the company. The retirement benefits of employees who met the age and length of service requirement under R.A. No. 7641 shall be exempt from withholding income tax by express provision of Section 32 (B) (6) (a) of the Tax Code, as amended.

Since you are more than sixty (60) years of age and have more than five (5) years in the service of the company, you meet the age and length of service requirement under R.A. No. 7641. Thus, your retirement benefits received under RA No. 7641 are exempt from income tax, and consequently to the withholding tax.

With regard to the query as to whether or not Section 2.78.1 (B) (1) (a) (iv) of RR No. 2-98, as amended, applies to an employee who has previously availed of a tax exemption pursuant to retrenchment, we rule in the negative. Section 2.78.1 (B) (a) and (b) provides as follows:

"Sec. 2.78.1. Withholding Tax on Compensation. —

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(B) Exemption from withholding tax on compensation. — The following income payments are exempted from the requirement of withholding tax on compensation but may be subject to income tax depending on the nature/sources of income earned by the individual recipient.

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(1) Remunerations received as an incident of employment as follows:

(a) Retirement benefits received under Republic Act 7641 and those received by officials and employees of private firms, whether individual or corporate, under reasonable private benefit plan maintained by the employer which meet the following requirements:

(i) The plan must be reasonable;

(ii) The benefit plan must be approved by the Bureau;

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(iii) The retiring official or employee must have been in the service of the same for at least ten (10) years and is not less than fifty (50) years of age at the time of retirement; and

(iv) The retiring official or employee shall not have previously availed of the privilege under the retirement benefit plan of the same or another employer.

(b) Any amount received by an official or employee or by his heirs from the employer due to death, sickness or other physical disability or for any cause beyond the control of the said official or employee, such as retrenchment, redundancy, or cessation of business.

The phrase 'for any cause beyond the control of the said official or employee' connotes involuntariness on the part of the official or employee. The separation from the service of the official or employee must not be asked for or initiated by him. The separation was not of his own making. Whether or not the separation is beyond the control of the official or employee, being essentially a question of fact, shall be determined on the basis of prevailing facts and circumstances. It shall be duly established by the employer by competent evidence which should be attached to the monthly return for the period in which the amount paid due to the involuntary separation was made.

Amounts received by reason of involuntary separation remain exempt from income tax even if the official or the employee, at the time of separation, had rendered less than ten (10) years of service and/or is below fifty (50) years of age.

Any payment made by an employer to an employee on account of dismissal, constitutes compensation regardless of whether the employer is legally bound by contract, statute, or otherwise, to make such payment."

The requirement that the employee must not have previously received retirement benefits pursuant to RA No. 7641 or from a reasonable private benefit plan of the same or another employer does not apply to a retiring employee who has previously received separation benefits and availed of a tax exemption pursuant to retrenchment. There is no double availment in case of separation benefit and retirement benefit considering that they are covered by separate provisions of the Tax Code.

This ruling is being issued on the basis of the foregoing facts as represented. However, if upon investigation, it will be ascertained that the facts are different, then this ruling shall be considered null and void.

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Very truly yours,

(SGD.) CAESAR R. DULAY
Commissioner of Internal Revenue

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