REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE

Quezon City

Section 32(B)(6)(b), NIRC of 1997, as amended.
BIR Ruling No. 404-13; **BIR Ruling No. 386-13;** **BIR Ruling No. 018-15;**
#133-2016 4-15-2016

Millennium Challenge Account - Philippines
2/F Development Academy of the Philippines Building
San Miguel Avenue, Ortigas Center
Brgy. San Antonio, Pasig City

Attention: Ms. Ma. Victoria E. Añonuevo
Managing Director and CEO

Gentlemen:

This refers to your letter dated November 25, 2015, requesting in behalf of MILLENIUM CHALLENGE ACCOUNT - PHILIPPINES (MCA-P for brevity), for the issuance of a Confirmatory Ruling that the separation benefits to be received by employees affected on account of retrenchment are exempt from income and withholding tax.

It is represented that MCA-P, with Taxpayer's Identification No. (TIN) is a Philippine government corporation duly organized by virtue of Executive Order No. 879 with principal office address at 2nd Floor Development Academy of the Philippines Building, San Miguel Avenue, Ortigas Center, Barangay San Antonio, Pasig City. MCA-P is the accountable entity tasked to manage the USD : to the Republic of the Philippines under the Millennium Challenge Compact (the "Compact") entered into by the United States Government, acting through the Millennium Challenge Corporation ("MCC"), and the Republic of the Philippines, acting through its government (the "Government"), represented by its Department of Finance ("DOF").

The primary goal of the Compact is to reduce poverty in the Philippines through economic growth (the "Compact Goal"). The Compact entered into force on 25 May 2011 and will terminated after the lapse of five years, or on 25 May 2016 (the "Compact End Date"). The closure of the Compact Program will result in the separation from service of MCA-P employees for reasons beyond their control. After the Compact End Date, MCA-P will be precluded from using Compact funds to engage in project management activities. On Compact End Date, MCA-P intends to downsize its workforce by releasing personnel whose services are not critical during the Closure Period. Notice of Retrenchment was sent to the Department of Labor and Employment (DOLE) which resulted in the Establishment Termination Report duly received by DOLE-Papamamarisan Field Office on March 1, 2016.

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In reply, please be informed that any amount received by an official or employee or by his heirs from the employer as a consequence of separation of such official or employee from the service of the employer because of death, sickness or other physical disability or for any cause beyond the control of the said official or employee is exempt from taxes regardless of age or length of service pursuant to Section 32 (B) (6) (b) of the Tax Code of 1997. 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 law requires the presence of two (2) conditions in order that the employee benefits may be granted tax exemption, namely (1) the employee is separated from the service of the employer due to death, sickness or other physical disability or for any cause beyond the control of the said official or employee; and (2) the employer pays benefits to the official or employee or his heirs as a consequence of such separation.

Accordingly, this Office hereby holds that any and all amount to be received by your fifty two (52) employees, namely:

1. Bernabe, Grace M.
2. Borbon, Rogelio G.
3. Contreras, Dianina Rose L.
4. Ditalo, Fidevic A.
5. Fernando, Maria Christina P.
6. Honrade, Yevgeny L.
7. Manalo, Juanito R.
8. Nicolita, Jiffy R.
9. Ranada, Reynaldo V.
10. Perina, Rodel T.
11. Porcadilla, Maria Lycel
12. Salcedo, Dick Bon P.
13. Tantiado, Marie Antoinette T.
14. Baddiri, Elien D.
15. Repulda, Joni A.
16. Robles, Hazel S.
17. Serrano, Michael G.
18. Macariola, Maria Elena T.
19. Yuvienco, Claricel M.
20. Villanueva, Francisco Z.
21. Gange, David V.
22. Agda, Rogelio G.
23. Alvarez, Ruby U.
24. Anonuevo, Ma. Victoria
25. Arias, Rodolfo L.
26. Austria, Renevic M.
27. Barcenas, Belinda E.
28. Bugtas, Bianca E.
29. Camacho, Gianfrancis S.
30. Demabildo, Arnold C.
31. Dumlao, Julie Ann A.
32. Fernandez, Bernardo C.
33. Gatarin, Grace R.
34. Gutierrez, Bingle B.
35. Hasan, Radzmier H.
36. Justiniano, Jimmy D.
37. Lesigues, Amy A.
38. Mayor, Jansen M.
39. Moll, Andres K.
40. Nacario, Dennis Lorne S.
41. Navida, Criste Z.
42. Nicdao, Warren Paul A.
43. Ocampo, Jason N.
44. Orozco, Edith A.
45. Paras, Anna Fatima T.
46. Parcia, Mark Anthony M.
47. Peniano, Pia Hyacynth Z.
48. Salazar, Rossana L.
49. Santos, Loreta M.
50. Santos, Ofelia D.
51. Saracho, Andres B.
52. Tan, Eleanora E.

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who are affected by the retrenchment program are exempt from income tax and consequently from the withholding tax prescribed by Section 79, Chapter XIII, Title II of the Tax Code of 1997, as implemented by Revenue Regulations No. 2-98, as amended. The payment of salaries, however, is subject to income tax and consequently to withholding tax. (BIR Ruling No. 404-13 dated November 7, 2013)

Moreover, pursuant to Section 2.78.1 (A) (7) of RR 2-98, as amended, commutation and payment of monetized unused vacation leave credits not exceeding ten (10) days during the year are not subject to income tax and consequently to the withholding tax. Conversely, the cash equivalent of vacation leave exceeding ten (10) days is subject to tax. However, this same principle cannot apply to sick leave credits since an employee must actually go on sick leave to be able to avail of said leave credits. (BIR Ruling No. 386 dated October 22, 2013).

It is, however, understood that this exemption does not include the payment of the separated employees' salaries and the payment of the 13th month pay and other benefits in excess of the Php82,000.00 pursuant to Republic Act (R.A.) No. 10653, "An Act Adjusting the 13th Month Pay and other Benefits Ceiling Excluded from the Computation of Gross Income for Purposes of Income Taxation, Amending for the Purpose Section 32 (B), *Chapter VI of the National Internal Revenue Code of 1997, as Amended.*" R.A. No. 10653 is being implemented by Revenue Regulations No. 3-2015. The amount of P82,000 shall apply to the 13th month pay and other benefits paid or accrued beginning January 1, 2015.

Lastly, the separation from the service must be the direct result of actual retrenchment implemented and not due to the employees' voluntary resignation or separation or qualification to the compulsory/optional retirement program of the company.

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 as null and void.

Very truly yours,

(SGD.) KIM S. JACINTO-HENARES
Commissioner of Internal Revenue

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