November 15, 2018

BIR RULING NO. 1331-18

Sec. 32 (B) (6) (a) NIRC; BIR Ruling No. 64-13

HS Technologies (Phils.), Inc.
Main Avenue, Cavite Economic Zone Authority (CEZA)
Rosario, Cavite

Attention: *AAA*

Gentlemen :

This refers to your letter dated June 17, 2014 requesting, on behalf of BBB ("BBB"), exemption from income tax on his retirement benefits paid by HS Technologies (Phils.), Inc. (the "Company"), pursuant to Republic Act (R.A.) No. 7641.

Based on the documents submitted, it is shown that BBB, with Tax Identification No. 000-000-000-000, is a Japanese National who was employed by the Company on May 24, 2004; that he has retired from the Company on May 31, 2014 after reaching the age of sixty-six (66) and serving the Company for a continuous period of ten (10) years.

In reply, please be informed that Section 1 of R.A. No. 7641, amending the Labor Code of the Philippines by providing for retirement pay to qualified private sector employees in the absence of any retirement plan in the establishment, provides:

> *"Section 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 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)*

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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." (Underscoring supplied)

The foregoing provision allows the retirement of an employee upon reaching the retirement age as may be provided under the applicable employment contract entered into by the Company and its employees, and the parties to the employment contract may agree on the retirement benefits that will be received by the employees provided that such benefits shall not be less than those provided under the Labor Code of the Philippines. In the absence of a retirement plan or other agreement providing for the retirement benefits of employees in the establishment, the retirement benefits as set forth under Section 1 of R.A. 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. In the absence of a showing that there is a reasonable retirement benefit plan or CBA established by the Company, Section 1 of R.A. No. 7641 shall apply in this case.

As regards the taxability of the subject retirement benefits, Section 32 (B) (6) (a) of the Tax Code of 1997, as amended, states, thus:

"(a) Retirement benefits received under R.A. 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: . . ., shall not be included in gross income and shall be exempt from taxation." (underscoring supplied)

The retirement benefits received by an employee pursuant to R.A. 7641 are exempt from income tax by express provision of Section 32 (B) (6) (a) of the Tax Code of 1997, as amended. In the instant case, BBB retired from the Company on May 24, 2004 at the age of sixty-six (66) and after serving for a period of ten (10) continuous years in the Company, thus, the retirement benefits of BBB, after having complied with the age and length of service requirements set forth in Section 1 of R.A. No. 7641, are not subject to income tax and consequently, to the withholding tax under Section 79, Chapter XIII, Title II of the Tax Code of 1997, as amended. *(BIR Ruling No. 64-2013 dated February 12, 2013)*

Moreover, pursuant to Section 2.78.1 (A) (7) of RR 2-98, as amended, the terminal pay, *i.e.*, 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.

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It is must be understood that the payment to BBB of his salaries and the payment of the 13th month pay and other benefits in excess of the Php82,000.00 threshold shall be subject to income tax, and consequently to withholding tax.

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.) CAESAR R. DULAY
Commissioner of Internal Revenue

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