April 10, 2018

BIR RULING NO. 620-18

Section 32 (B) (6) (a) of the Tax Code of 1997, as amended; BIR Ruling No. 177-2011; BIR Ruling No. 199-2011

Misamis Occidental II Electric Cooperative, Inc.
Circumferential Road, Ozamiz City 7200

Attention: *AAA*

Gentlemen :

This refers to the request for exemption from income tax and, consequently, from withholding tax, on the retirement benefits of the following employees of Misamis Occidental II Electric Cooperative, Inc. (MOELCI-II), to wit:

Name	Date Hired	Date Retired	Age	Length of Service
BBB	_____	_____	___	___
CCC	_____	_____	___	___
DDD	_____	_____	___	___
EEE	_____	_____	___	___
FFF	_____	_____	___	___

It is represented that MOELCI-II has an Upgraded Retirement Plan for Coop Employees and Officials embodied in Resolution No. 08, s. 99 which provides for the optional and compulsory retirement benefits for the company's employees and officials. Section I (A) and (B) of said Plan provide:

"A. Optional Retirement:

Coop employees shall be eligible for optional retirement under this circumstance:

Age: less than 60 yrs,

1. An employee who had served the coop 9 years and below, who intend to separate from the service shall be entitled to a separation pay of 100% of the

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basic salary for one month for every year of service rendered.

2. An employee who had served the coop 10 years and above shall be entitled to a separation pay base under Contents No. II

B. Compulsory Retirement:

Upon reaching the age of 60 years old, the retirement shall be compulsory.

xxx xxx xxx

Coop officials who had served the electric cooperatives for a period of at least 5 years are entitled to gratuity benefits."

In reply, please be informed that under Section 1 of Republic Act (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, it is provided, *viz.*:

> *"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) 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."*

The aforesaid provision allows the retirement of an employee upon reaching the retirement age as may be provided under the applicable collective bargaining agreement (CBA) or other employment contract entered into by and between the employer and the employees of the company, and the parties to the CBA or 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 ("Labor Code").

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As previously noted, MOELCI-II maintains a retirement plan providing for the optional and compulsory retirement benefits for the company's employees and officials. Thus, said plan governs the retirement benefits of the above-named employees in the absence of a showing that the benefits provided under the said plan are less beneficial than those provided under the Labor Code.

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

> *"Section 32. Gross Income. —*
>
> *(B) Exclusions from Gross Income. — The following items shall not be included in gross income and shall be exempt from taxation under this Title:*
>
> xxx xxx xxx
>
> *(6) Retirement Benefits, Pensions, Gratuities, etc. —*
>
> *(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: Provided further, that the benefits granted under this subparagraph shall be availed of by an official or employee only once. x x x . . ., shall not be included in gross income and shall be exempt from taxation."*
> (underscoring supplied)

Accordingly, the retirement benefits of the above-named employees shall only be exempt from income tax if the conditions set forth under Section 32 (B) (6) (a) of the Tax Code of 1997, as amended, are satisfied, to wit: (1) the employee had been in the service of the same private firm for at least ten (10) years; (2) he is at least fifty (50) years old at the time of retirement; and (3) the tax exempt retirement benefits have not been previously availed of by the employee. (*BIR Ruling No. 154-13* dated April 29, 2013) In view thereof, please determine if the above employees have previously availed of the tax exemption under the afore-quoted provision. The submitted documents only show the age and length of service rendered by the employees. They still have to prove compliance with the other requisite, that is, that the tax exempt retirement benefits have not been previously availed of by the employees.

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 of the employees 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

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said leave credits. (*BIR Ruling No. 154-13* dated April 29, 2013)

It must be understood that the payment to the retired employees of salaries and the 13th month pay and other benefits in excess of the Php82,000 [1] threshold shall be subject to income tax, and consequently to withholding tax, under Section 2.78.1 (A) (3) (a) and (A) (7) of RR 2-98,as amended.

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,

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

Footnotes

1. 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.

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