REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE
Quezon City

REVENUE MEMORANDUM CIRCULAR NO. 39-2014

SUBJECT: Clarifying the Tax Treatment of Payouts by Employee Pension Plans

TO : All Internal Revenue Officers and Others Concerned

There are pension, stock bonus and profit-sharing plans that are permitted by their charters to disburse benefits (i.e., dividends) to the beneficiary-employees. As a general rule, Section 60(A) of the National Internal Revenue Code (NIRC) of 1997, as amended, subjects the income of any kind of property held in trust to income tax. By way of exception, Section 60(B) exempts from income tax an employee's trust which forms part of a pension, stock bonus or profit-sharing plan of an employer for the benefit of some or all of his employees subject to the following conditions:

1) Contributions are made to the trust by such employer, or employees, or both for the purpose of distributing to such employees the earnings and principal of the fund accumulated by the trust in accordance with such plan; and

2) Under the trust instrument it is impossible, at any time prior to the satisfaction of all liabilities with respect to employees under the trust, for any part of the corpus or income to be (within the taxable year or thereafter) used for, or diverted to, purposes other than for the exclusive benefit of his employees.

As an exception to the above exception, Section 60(B) subjects to income tax, in the year in which so distributed, any amount actually distributed to any employee or distributee to the extent that it exceeds the amount contributed by such employee or distributee.

Prescinding from the foregoing, the entire amounts of benefits paid by a pension, stock bonus or profit-sharing plan of an employer for the benefit of employees are taxable on the part of the employees in the year so distributed. This tax treatment, however, does not apply to payouts representing a return of an employee's personal contributions to the fund and to retirement benefits exempt under Section 32(B)(6)(a) of the NIRC.

Illustrations. —

Situation No. 1. Non-contributory Pension Plan. — ABC Labor Union represents all the daily paid employees of VCC Corporation. As a result of their collective bargaining agreement, ABC Labor Union and VCC Corporation established a provident fund. The plan sets forth the terms and conditions of membership therein and the benefits to be provided. Under the terms of the agreement, VCC Corporation is obligated to establish a trust fund and

to make contributions thereto at specified rates. The daily paid employees of VCC Corporation are not allowed to contribute to the provident plan.

a. The provident fund distributed dividends to the covered employees. As a result, the entire amount of the dividends is subject to income tax on the part of the covered employees in the year so distributed.

b. Mr. Q, an employee covered by the provident plan, resigned from VCC Corporation. He received benefits from the provident plan that do not qualify as tax-exempt separation or retirement benefits. These benefits are subject to income tax on the part of Mr. Q to the extent of the entire amount received in the year so distributed.

Situation No. 2. Contributory Pension Plan. — Same facts as *Situation No. 1*, except that in this situation, the daily paid employees of VCC Corporation are allowed to contribute up to Twenty Thousand Pesos (Php20,000) each year to the provident plan.

a. The provident fund distributed dividends to the covered employees. The dividends do not constitute a return of the employees' voluntary contributions. As a result, the entire amount of the dividends is subject to income tax on the part of the covered employees in the year so distributed.

b. Ms. M, an employee covered by the provident plan, contributed a total of Sixty Thousand Pesos (Php60,000) to the provident fund. Upon her resignation from VCC Corporation, she received benefits from the provident plan in the amount of Three Hundred Thousand Pesos (Php300,000) that do not qualify as tax-exempt separation or retirement benefits. Of this amount, Sixty Thousand Pesos (Php60,000) constitutes a return of her contribution to the provident fund. The entire amount of Two Hundred Forty Thousand Pesos (Php 240,000) that Ms. M received in excess of her contribution (or Three Hundred Thousand Pesos [Php300,000] less Sixty Thousand Pesos [Php60,000]) is subject to income tax on the part of Ms. M in the year so distributed.

All other issuances inconsistent herewith are hereby repealed or modified accordingly.

All concerned are hereby enjoined to be guided accordingly and give this Circular as wide a publicity as possible.

This Circular shall take effect immediately.

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