Bringing in Revenues for Nation-building

REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE

BAGONG PILIPINAS

January 16, 2025

REVENUE MEMORANDUM CIRCULAR NO. 005-2025

SUBJECT: **Amends Certain Provisions of Revenue Memorandum Circular Nos. 11-2024, 12-2024, 13-2024 and 19-2024, Provide Clarifications/ Transitory Provisions and to Align them with the Provisions of Republic Act No. 11976, otherwise known as the "Ease of Paying Taxes Act", its Implementing Rules and Regulations and Other Issuances**

TO: **All Internal Revenue Officials, Employees and Others Concerned**

This Circular is issued to update certain provisions of Revenue Memorandum Circular (RMC) Nos. 11-2024, 12-2024, 13-2024 and 19-2024, by integrating clarifications/ transitory provisions in line with Republic Act No. 11976, otherwise known as the "Ease of Paying Taxes Act" (EOPT Act), its Implementing Rules and Regulations and other issuances.

COVERAGE:

1. **RMC No. 11-2024** – Clarifies the tax treatment of lease accounting by lessees under Philippine Financial Reporting Standard 16 in relation to Sections 34(A), 34(K), 106, 108, 179, 194 of the Tax Code, as amended, Revenue Regulations (RR) No. 19-86, as amended, and RR No. 02-98, as amended;

2. **RMC No. 12-2024** – Clarifies the treatment of foreign currency transactions for financial reporting and internal revenue tax purposes;

3. **RMC No. 13-2024** – Clarifies the treatment of retirement benefits expense for financial reporting and tax purposes; and

4. **RMC No. 19-2024** – Clarifies the tax treatment of interest expense paid or incurred on indebtedness in connection with the taxpayer's profession, trade or business and other related matters.

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AMENDMENTS/ALIGNMENT WITH EOPT ACT:

PROVISIONS AFFECTED BY EOPT ACT	AMENDMENTS
RMC No. 11-2024 (Lease Accounting by Lessees)	
Q6: What shall be the income tax treatment of initial direct costs paid by the lessee in relation to the lease of an asset? **A6:** For purposes of taxation, Initial Direct Costs shall be defined as payments which are directly related to the negotiation and execution of a lease agreement. The initial direct cost paid or incurred by the lessee in relation to the lease agreement shall be claimed as outright expenses in the year it was paid or incurred subject to substantiation and withholding requirements pursuant to Section 34 of the Tax Code, as amended.	**Q6: What shall be the income tax treatment of initial direct costs paid by the lessee in relation to the lease of an asset?** **A6:** For purposes of taxation, Initial Direct Costs shall be defined as payments which are directly related to the negotiation and execution of a lease agreement. The initial direct cost paid or incurred by the lessee in relation to the lease agreement shall be claimed as outright expenses in the year it was paid or incurred subject to substantiation requirements pursuant to Section 34(A)(1)(b) of the Tax Code of 1997, as amended. Furthermore, the same shall be subject to withholding tax pursuant to Section 9 of the Ease of Paying Taxes (EOPT) and Section 7 of RR No. 4-2024, as provided below: "**SECTION 7.** ***Withholding of Tax at Source.*** Section 2.57.4 of RR No. 2-98, as amended, shall now read as follows: *'Sec. 2.57.4. Time of Withholding. – The obligation of the payor to deduct and withhold the tax under Section 2.57 of these Regulations arises at the time an income has become payable. The term "payable" refers to the date the obligation becomes due, demandable or legally enforceable. The obligation of the payor to deduct and withhold the tax arises at the time an income payment is accrued or recorded as an expense or asset, whichever is applicable, in the payor's books, or at the issuance by the seller of the sales invoice or other adequate document to support such payable, whichever comes first.'* It was however clarified under RMC No. 60-2024 that the non-withholding of tax will no longer be a ground for the disallowance of the claimed deduction/expense for taxable year covering January 1, 2024 onwards.

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PROVISIONS AFFECTED BY EOPT ACT	AMENDMENTS
Q7: What shall be the income tax treatment of expenses paid or incurred by the lessee which are properly for the account of the lessor? A7: The amounts paid by the lessee for certain expenses, which are properly for the account of the lessor as indicated in the contractual agreement between the parties, shall be allowed as deductions during the year the same has been paid or accrued pursuant to Section 34 of the Tax Code, as amended. Provided, however, that lessor shall issue invoices/receipts in the name of the lessee (e.g., realty tax, association dues, etc.)	**Q7: What shall be the income tax treatment of expenses paid or incurred by the lessee which are properly for the account of the lessor?** A7: The amounts paid by the lessee for certain expenses, which are properly for the account of the lessor as indicated in the contractual agreement between the parties, shall be allowed as deductions during the year the same has been paid or accrued pursuant to Section 34 of the Tax Code of 1997, as amended, which shall be properly substantiated with invoices issued by the lessor in the name of the lessee. Thus, it will form part as gross sales of lessor and allowable as deduction on the part of the lessee.
Q12: What are the business tax implications relative to leases? A12: For business tax purposes, the following guidelines shall still be observed: 1. The corresponding input VAT shall only be creditable to the lessee upon payment of the rentals, which shall be evidenced by a VAT Official Receipt pursuant to Section 110 in relation to Section 113 of the Tax Code, as amended. XXX XXX XXX	**Q12: What are the business tax implications relative to leases?** A12: For business tax purposes, the following guidelines shall still be observed: 1. The corresponding input VAT shall only be creditable to the lessee **for the amount of rentals paid incurred/accrued**, which shall be evidenced by **a VAT Invoice** pursuant to Section 110 in relation to Section 113 of the Tax Code, as amended. XXX XXX XXX
Q13: What are the withholding tax implications of leases? A13: For contracts considered as leases, only the actual rental paid or accrued shall be subject to five percent (5%) Expanded Withholding Tax (EWT) pursuant to Section 2.57.2 (B) of RR No. 02-98, as amended. Hence, only the actual rental paid or accrued shall be considered as the tax base for EWT purposes, without regard to the depreciation expense from the ROUA. XXX XXX XXX	**Q13: What are the withholding tax implications of leases?** A13: The 5% withholding tax under Section 2.57.2 (B) of RR No. 02-98 shall be based on the amount payable which refers to the value paid/accrued or recorded as an expense or asset, whichever is applicable in the payor's book or at the issuance by the seller of the sales invoice or other adequate document to support such payable whichever comes first pursuant to Section 7 of RR No. 4-2024. XXX XXX XXX

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PROVISIONS AFFECTED BY EOPT ACT	AMENDMENTS
RMC No. 12-2024 (FOREX Transactions)	
Q17: What will be the basis for the reportable amount of transactions denominated in foreign currency for taxes other than income tax (e.g., Value Added Tax (VAT), Gross Receipt Tax (GRT), Other Percentage Tax (OPT), Excise Tax, Documentary Stamp Tax (DST), etc.)?	**Q17: What will be the basis for the reportable amount of transactions in foreign currency for taxes other than income tax (e.g., Value Added Tax (VAT), Other Percentage Tax (OPT), Excise Tax, Documentary Stamp Tax (DST), etc.)?**
A17: Foreign Currency transactions are converted into Philippine Peso using the prevailing spot rate on the date of transaction. This is the basis of the reportable transactions of taxes other than income tax (e.g., VAT, GRT, OPT, Excise, DST, etc.)	**A17:** For taxes other than income tax (e.g., VAT, OPT, Excise, DST, etc.), the basis of the reportable amount for foreign currency transactions shall be the Philippine Peso-converted amount using the prevailing spot rate on the date of transaction. In determining the date of transaction, the enactment of RA 11976 or EOPT Act shall be taken into consideration which provides the revised bases for the reportable amounts for VAT, OPT and withholding taxes, as follows:
For VAT purposes, the reportable amount for sale of goods or properties shall be the gross selling price or the gross value in money as supported by a corresponding sales invoice; while for sale or exchange of services, including the use or lease of property, it shall be the gross receipts as supported by a corresponding official receipt.	For VAT purposes, the reportable amount for sale of goods, properties and sale or exchange of services shall be the gross sales as supported by a corresponding VAT invoice[1];
For GRT and OPT, the reportable amount shall be the gross quarterly sales or receipts depending on the type of transaction subject to the said taxes.	For OPT, the reportable amount shall be the gross quarterly sales depending on the type of transaction subject to the said taxes[2];
For Excise, the reportable amount shall be the excise taxes imposed and based on weight or volume capacity or any other physical unit of measurement *(specific tax)* and imposed and based on selling price or other specified value of the goods *(ad valorem tax)* generally before the removal/release of the excisable products.	For Excise, the reportable amount shall be: a) **Specific tax**. The excise taxes imposed based on weight or volume capacity or any other physical unit of measurement. b) **Ad valorem tax**. The excise tax shall be based on selling price or other specified value of goods before the removal/release of the excisable products;
For DST, the reportable amount shall be based on the value of the documents subject to stamp tax.	For DST, the reportable amount shall be based on the value provided in the documents subject to stamp tax; and
For withholding taxes, in general, the reportable amount shall be the value of the taxable income payment at the time it is paid or payable or when it	For withholding taxes, in general, the reportable amount shall be the value of the taxable income payment at the time it has

[1] Revenue Regulations No. 3-2024.
[2] Ibid.

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PROVISIONS AFFECTED BY EOPT ACT	AMENDMENTS
is accrued or recorded as an expense or asset, whichever comes first.	become payable, accrued or recorded as an expense or asset, whichever is applicable, in the payor's books, or at the issuance by the seller of the sales invoice or other adequate document to support such payable, whichever comes first.
RMC No. 19-2024 (Interest Expense)	
Q1: When can interest expense be claimed as a deduction from gross income? **A1:** Interest paid or incurred within a taxable year on indebtedness in connection with the taxpayer's profession, trade or business shall be allowed as a deduction from gross income, subject to certain limitations, when the following requisites, provided in Section 34 (B)(2) of the National Internal Revenue Code (NIRC) of 1997, as amended, and as implemented by Revenue Regulations (RR) No. 13-2000 and Section 7(B) of RR No. 5-2021, are met: 1. The indebtedness must be that of the taxpayer; 2. The interest must have been stipulated in writing; 3. The interest must be legally due; 4. The interest payment arrangement must not be between related taxpayers as mandated in Sec. 34 (B)(2)(b), in relation to Sec. 36(B), both of the NIRC of 1997, as amended; 5. The interest must not be incurred to finance petroleum operations; 6. The interest was not treated as "capital expenditure" if such interest was incurred in acquiring property used in trade, business or exercise of profession; and 7. The interest shall be reduced by an amount equivalent to twenty percent (20%) of interest income subjected to final tax. However, if the final withholding tax rate on interest income of twenty percent (20%) will be adjusted in the future, the interest reduction shall be adjusted accordingly. In addition, the taxpayer must have withheld the appropriate tax in order to claim the interest expense as a deduction from the gross income (refer to Q9).	**Q1: When can interest expense be claimed as a deduction from gross income?** **A1:** Interest paid or incurred within a taxable year on indebtedness in connection with the taxpayer's profession, trade or business shall be allowed as a deduction from gross income, subject to certain limitations, when the following requisites, provided in Section 34 (B)(2) of the National Internal Revenue Code (NIRC) of 1997, as amended, and as implemented by RR No. 13-2000 and Section 7(B) of RR No. 5-2021, are met: 1. The indebtedness must be that of the taxpayer; 2. The interest must have been stipulated in writing; 3. The interest must be legally due; 4. The interest payment arrangement must not be between related taxpayers as mandated in Sec. 34 (B)(2)(b), in relation to Sec. 36(B), both of the NIRC of 1997, as amended; 5. The interest must not be incurred to finance petroleum operations; 6. The interest was not treated as "capital expenditure" if such interest was incurred in acquiring property used in trade, business or exercise of profession; and 7. The interest shall be reduced by an amount equivalent to twenty percent (20%) of interest income subjected to final tax. However, if the final withholding tax rate on interest income of twenty percent (20%) will be adjusted in the future, the interest reduction shall be adjusted accordingly. The requirement to withhold taxes in order to claim the interest expense as a deduction from the gross income was repealed under Section 5 of the EOPT Act, as implemented by Section 6 of RR No. 4-2024.

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PROVISIONS AFFECTED BY EOPT ACT	AMENDMENTS
	As clarified in RMC No. 60-2024,[3] the non-withholding of tax will no longer be a ground for the disallowance of the claimed interest expense for taxable year covering January 1, 2024 onwards. However, the obligation of the payor to withhold tax and remit the same under Q9 remains, pursuant to Section 9 of the EOPT_Act and as implemented by Section 7 of RR No. 4-2024, *to wit* "**SECTION 7. *Withholding of Tax at Source.*** Section 2.57.4 of RR No. 2-98, as amended, shall now read as follows: *'Sec. 2.57.4. Time of Withholding. – The obligation of the payor to deduct and withhold the tax under Section 2.57 of these Regulations arises at the time an income has become payable. The term "payable" refers to the date the obligation becomes due, demandable or legally enforceable. The obligation of the payor to deduct and withhold the tax arises at the time an income payment is accrued or recorded as an expense or asset, whichever is applicable, in the payor's books, or at the issuance by the seller of the sales invoice or other adequate document to support such payable, whichever comes first.'*

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CLARIFICATIONS/TRANSITORY PROVISIONS:

I. RMC NO. 12-2024 (FOREX TRANSACTIONS)

Q1: Is the use of average rate for a period under Philippine Accounting Standards (PAS) 21 for Foreign Currency Transactions permitted both for Financial Reporting and Tax purposes?

A1: No. For tax purposes, foreign currency transactions shall be converted to Philippine Peso using only the spot rate of exchange on the date of transaction.

Conversely, for financial reporting purposes, Paragraph 22 of PAS 21 allows a rate that approximates the actual rate at the date of the transaction (*e.g., an average rate for a week or a month might be used for all transactions in each foreign currency occurring that period*) can be used for practical reasons provided that specific spot rate within the day (opening, closing, high, low or weighted average in a day) has been identified in the sworn statement. However, if exchange rates fluctuate significantly, the use of the average rate for a certain period is inappropriate.

[3] Providing Clarifications and Guidance on Section 6 of Revenue Regulations No. 4-2024 on the Repeal of Section 34 (K) of the National Internal Revenue Code of 1997, as Amended, issued on May 9, 2024.

In the event that in converting foreign currency transactions, the taxpayer used the average rate for a certain period for financial reporting purposes and the spot rate of exchange on the date of transaction for tax purposes, a reconciliation on the foreign exchange (forex) rates used must be prepared and must be available for presentation and submission, together with other supporting documents, during Bureau of Internal Revenue (BIR) audit.

Q2: PAS 21 does not mandate the use of forex rates published exclusively by a specified source for financial reporting purposes. Do taxpayers have an option to choose the source of forex rate to be used in converting foreign currency denominated transactions for tax purposes?

A2: Yes. Q&A No. 4 of RMC No. 12-2024 standardizes the forex rates to be used for tax purposes in converting foreign currency denominated transactions to Philippine Peso. It prescribes the use of forex rates from sources that are widely available to the taxpayers and that can be easily accessed by BIR during tax audits. Taxpayers are given freedom to choose the source of forex rates to be used that are deemed appropriate for their foreign currency transactions as long as the conditions under Q&A No. 4 of RMC No. 12-2024 are met.

Q3: What shall be the spot rate applicable for transactions that occurred prior to the opening of Banker's Association of the Philippines (BAP) Rates at 9 AM like transactions between 6 AM to 8 AM or before 9AM?

A3: For transactions occurring prior to the opening of the BAP Rates, the taxpayer shall use the latest selected spot rate available on the business date immediately preceding the opening of the BAP rates. The use of selected spot rate shall cover the duration up to the cut-off period to avoid multiple use of forex spot rate resulting to various reconciliation. Thus, the duration of the opening/closing spot rate will be up to the next business day. However, if the taxpayer opts to use other or combination of spot rate within the day, such shall be included in the Sworn Statement for submission to BIR concerned office as a guide for proper calculation during audit.

Moreover, the taxpayer shall summarize its foreign currency transactions occurring prior to the opening of the BAP rates, adopting the latest selected spot rate available on the business date immediately preceding the opening of the BAP rates. The summary schedules which is necessary to reconcile the date prior to opening of BAP rate shall be made available for presentation and submission during the BIR audit.

Q4: Is netting or offsetting of forex gains and losses allowed for income tax purposes?

A4: No. The practice of offsetting or netting of separate and distinct transactions, and the accounting and recording of the same and its related/incidental transactions (e.g., forex gains/losses) in the taxpayer's books, is strictly prohibited for tax purposes.

Each transaction is considered a separate taxable event, hence, shall be accounted and taxed separately from other transactions. Regardless if there is an offsetting or netting arrangement between parties, the income and expenses shall be recorded and taxed separately from each other. Moreover, since losses are among those deductions from Gross Income provided under Section 34 of the National Internal Revenue Code of 1997 (Tax Code),as amended, such losses (e.g., forex loss) shall not form part of deduction from Gross Sales.

Q5: What is the deadline for submission of the Notarized Sworn Statement as a Requirement under Q&A No. 4 of RMC 12-2024?

A5: The notarized sworn statement informing the concerned BIR offices of electing the use of forex rates other than BAP published rates shall be submitted within 30 days prior to the start of the taxable year. In case of subsequent change in forex rates used, a new notice shall be submitted to

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the concerned BIR office, which shall be applied from the start of the succeeding taxable year.

Since RMC No. 12-2024 was issued on January 22, 2024, which is beyond the required period of 30 days prior to the start of the taxable year, taxpayers shall submit the Notarized Sworn Statement to the concerned BIR offices for the selected forex rates for 2024 without penalty/sanction on or before December 31, 2024. In case elected/used forex rates for 2024 with corresponding Sworn Statement is the same for the succeeding year/s, there is no need to resubmit a Sworn Statement for the year 2025.

The template for the **Notarized Sworn Statement** is attached as **Annex "A".**

Q6: What is the timeline for Taxpayers who intends to adopt the standardized forex rates under Q&A No. 4 of RMC 12-2024 on their duly registered Computerized Accounting System (CAS) or Computerized Books of Accounts (CBA)?

A6: Taxpayers that are using duly registered CAS or CBA need to revisit their system in case alignment is needed in terms of their use of forex rates for financial reporting and what is prescribed as source of forex rates under Q&A No. 4 of RMC 12-2024 for tax purposes. In case the adoption of forex rates will have a direct effect on the financial aspect, the system shall be updated/reconfigured following the existing policies and procedures on system enhancement.

In order to provide ample time for system reconfiguration adjustments shall be allowed to be undertaken on or before December 31, 2024. In case, system reconfiguration has not been accomplished within December 2024, a request for extension shall be submitted for approval by the Regional Director or Assistant Commissioner-Large Taxpayers Service (LTS) for a period of not more than six (6) months from December 31, 2024.

II. RMC NO. 13-2024 (RETIREMENT BENEFITS)

Q1: What is the rationale for the exclusion of entities applying Philippine Financial Reporting Standard (PFRS) for Small-Medium Enterprises(SMEs), considering that PFRS for SME allows use of projected unit credit method for Defined Benefit plans?

A1: The RMCs issued by the BIR to address the gaps between the PFRS and the Tax Code only cover the standards under the full PFRS. The PFRS for SMEs and Small Entities were excluded from the coverage since certain standards adopted in the full PFRS are not applicable to PFRS for SMEs and Small Entities. Hence, to avoid any confusion, the BIR initially limited the coverage of the same to full PFRS. Considering however, the manifestation that there are companies (subsidiary, conglomerates, headquarters, branches, etc.) which are required to comply with rules and standards irrespective of classification, SMEs and/or Small Entities may avail of the provisions of RMC No. 13-2024 on an optional basis and to comply with the required disclosure under PFRS.

To clarify the coverage, the following definition from the Securities and Exchange Commission Memorandum Circular No. 5, series of 2018 has been adopted.

(a) Large and/or Publicly Accountable Entities –
For purposes of this Rule, large or publicly accountable entities are those that meet any of the following criteria:
(1) Total assets of more than ₱350 Million or total liabilities of more than ₱250 Million; or
(2) Are required to file financial statements under Part II of SRC Rule 68; or
(3) Are in the process of filing their financial statements for the purpose of issuing any class instruments in a public market; or
(4) Are holders of secondary licenses issued by regulatory agencies.

* Mandatorily covered by RMC No. 13-2024 as Full PFRS Users

(b) Medium-Sized Entities are those that meet all of the following criteria:
   (1) Total assets of more than ₱ 100 Million to ₱350 Million or total liabilities of more than ₱ 100 Million to ₱250 Million. If the entity is a parent company, the said amounts shall be based on the consolidated figures;
   (2) Are not required to file financial statements under Part II of SRC Rule 68;
   (3) Are not in the process of filing their financial statements for the purpose of issuing any class of instruments in a public market; and
   (4) Are not holders of secondary licenses issued by regulatory agencies.

(c) Small Entities are those that meet all of the following criteria:
   (1) Total assets of between ₱3 Million to ₱100 Million or total liabilities of between ₱3 Million to ₱100 Million. If the entity is a parent company, the said amounts shall be based on the consolidated figures;
   (2) Are not required to file financial statements under Part II of SRC Rule 68;
   (3) Are not in the process of filing their financial statements for the purpose of issuing any class of instruments in public market; and
   (4) Are not holders of secondary licenses issued by regulatory agencies.

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* The Medium Sized-Entities and Small Entities may avail of the provisions of RMC No. 13-2024 on an optional basis upon compliance with the requirement on disclosure under existing PFRS issuances.

(d) Micro Entities are those that meet all of the following criteria:
   (1) Total assets and liabilities are below P 3 Million;
   (2) Are not required to file financial statements under Part II of SRC Rule 68;
   (3) Are not in the process of filling their financial statements for the purpose of issuing any class of instruments in a public market; and
   (4) Are not holders of secondary licenses issued by regulatory agencies.

Please note that the above entity classification for PFRS purposes is not the same with the taxpayer's classification under Section 21 of the Tax Code which is based on annual Gross Sales.

Q2: In the absence of the actuarial valuation report for funding purposes, can the taxpayer use the current service cost under the actuarial valuation report under PAS 19R as replacement of normal cost?

A2: No. In reiteration of Q&A No. 8 of RMC No. 13-2024, there is a difference in the calculation of service/retirement costs under PAS/PFRS and the Tax Code. The current service cost pertains to the amount that the employee earned for his service in the current reporting period while actuarial valuation is an estimate established by an actuary.

Q3: If the taxpayer contributed to the retirement fund <u>before</u> the date of filing of a Tax Qualified Plan but within the taxable period of the interim period between the date of filing and issuance of certificate of qualification, can the taxpayer claim the contribution up to normal cost as a deductible expense?

A3: No. Employers may deduct their contributions to the retirement fund if they meet the requirements under RA No. 4917, evidenced by a certificate of tax qualification issued by the BIR. Nevertheless, pending employers' application with the BIR, contributions to the retirement fund are allowed to be deducted from the gross income subject to the subsequent issuance of the said certificate (Q&A No.

12, RMC No. 13-2024). Any contributions made by an employer to the retirement fund before the filing of application for tax qualified plan are not deductible from gross income for income tax purposes.

Q4: Can an employee covered by a retirement benefit plan but determined (at the time of retirement) not qualified under the said retirement benefit plan, be covered by RA No. 7641?

A4: No. Under RA No. 7641, "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." It is clear that an employee may only be entitled to the tax-exempt retirement benefits under RA No. 7641 if his/her employer has no existing retirement plan of which the employee is part of. Accordingly, employees covered by a retirement benefit plan (whether determined as reasonable or not by the BIR) may not avail of the tax exemption benefit provided under RA No. 7641.

However, in case the concerned employee is not covered by the retirement benefit plan of his/her employer, or any other retirement plan in the employer's company (e.g. Collective Bargaining Agreement), then such employee may receive the tax-exempt retirement benefits provided under RA No. 7641.

Q5: Is an employee who was not included in the retirement benefit plan of the company but qualified under RA No. 7641, authorized to claim exempt benefit?

A5: Yes, said employee is entitled to claim an exempt retirement benefit under RA No. 7641 since he/she was not included in the retirement benefit plan and no contribution was made in his behalf for income tax deduction purposes.

In addition to the above clarifications, the following are the corrections on the accounting entries provided in Annex B of RMC No. 13-2024:

1. In scenario no. 1, all of the difference between the pension expense of P1,200,000.00 and the deductible pension expense for TY 2023 of P820,000.00 for tax purposes are considered temporary difference because the resulting additional accrual to pension liability of P200,000 will still result in deductible amounts in future periods when the corresponding contribution to the plan is made. Accordingly, corresponding deferred tax assets of P50,000 should also be recognized for such amount (P200,000 x 25%).

   Moreover, there is also a temporary difference for the Remeasurement Loss recognized in Other Comprehensive Income of P100,000 because the resulting additional accrual to pension liability also results in deductible amounts in future periods when the corresponding contribution to the plan is made. Accordingly, corresponding deferred tax assets of P25,000 should also be recognized for such amount (P100,000 x 25%).

2. In scenario no. 2, the illustration concluded that there should be no deferred tax entry. However, the difference between the carrying amount of a net defined benefit liability/asset and its tax base, where tax deduction can be claimed for the actual amount of retirement benefits paid to employees, is a temporary difference because any accruals of retirement liability in excess of benefits paid (or contributions in plan assets not yet paid to employees) will still be deductible in future periods when ultimately settled to employees in the future.

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III. RMC NO. 19-2024 (INTEREST EXPENSE)

Provided below are the clarifications and corrections on the computations and accounting entries for Machines B and C under Illustration B in Annex A of RMC No. 19-2024:

1. Since the interest is incurred by NIRC Company yearly, the computation of capitalized interest and depreciation expense for Machine B under Illustration B are revised as follows:

Year	Value of Machine B	Capitalized Interest	Adjusted Value of Machine B	Depreciation	Balance
1	₱1,000,000.00	₱100,000.00	₱1,100,000.00	₱ -	₱1,100,000.00
2	1,100,000.00	100,000.00	1,200,000.00	-	1,200,000.00
3	1,200,000.00	100,000.00	1,300,000.00	260,000.00	1,040,000.00
4	1,040,000.00	100,000.00	1,140,000.00	285,000.00	855,000.00
5	855,000.00	100,000.00	955,000.00	318,333.33	636,666.67
6	636,666.67	-	636,666.67	318,333.33	318,333.33
7	318,333.33	-	318,333.33	318,333.33	-

The revised differences between the accounting and tax treatments for Machine B are as follows:

Year	Interest Expense			Depreciation			Net Difference
	Accounting	Tax	Difference	Accounting	Tax	Difference	
1	₱ -	₱ -	₱ -	₱ -	₱ -	₱ -	₱ -
2	-	-	-	-	-	-	-
3	100,000.00	-	100,000.00	240,000.00	260,000.00	(20,000.00)	80,000.00
4	100,000.00	-	100,000.00	240,000.00	285,000.00	(45,000.00)	55,000.00
5	100,000.00	-	100,000.00	240,000.00	318,333.33	(78,333.33)	21,666.67
6	-	-	-	240,000.00	318,333.33	(78,333.33)	(78,333.33)
7	-	-	-	240,000.00	318,333.33	(78,333.33)	(78,333.33)
							₱ -

There is an automatic gap between the interest expense and depreciation expense accounts due to the loan term, period of preparation of the machine, and useful life of the machine which may be disclosed in the notes to the financial statements. The net difference through years 3 to 5 are temporary differences that are deductible from gross income for tax purposes in subsequent periods.

The following are the revised journal entries to record interest incurred and depreciation for Machine B:

Accounting			Tax		
Years 1 and 2			*Years 1 and 2*		
Dr. PPE – Machine B	₱	100,000.00	Dr. PPE – Capitalized Interest Expense	₱	100,000.00
Cr. Interest Liability		100,000.00	Cr. Interest Liability		100,000.00
Years 3, 4 and 5			*Year 3*		
Dr. Interest Expense	₱	100,000.00	Dr. PPE – Capitalized Interest Expense	₱	100,000.00
Cr. Interest Liability		100,000.00	Cr. Interest Liability		100,000.00
			Dr. Depreciation	₱	260,000.00
			Cr. Accumulated Depreciation		260,000.00
Years 3 to 7			*Year 4*		
Dr. Depreciation	₱	240,000.00	Dr. PPE – Capitalized Interest Expense	₱	100,000.00
Cr. Accumulated Depreciation		240,000.00	Cr. Interest Liability		100,000.00
			Dr. Depreciation	₱	285,000.00
			Cr. Accumulated Depreciation		285,000.00

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Year 5

Dr. PPE – Capitalized	₱	100,000.00
Interest Expense		100,000.00
Cr. Interest Liability		
	₱	318,333.33
Dr. Depreciation		318,333.33
Cr. Accumulated Depreciation		

Years 6 and 7

Dr. Depreciation	₱	318,333.33
Cr. Accumulated Depreciation		318,333.33

2. Similarly, for Machine C, the interest should be capitalized as incurred. Below is the computation of capitalized interest and depreciation expense for Machine C under Illustration B:

Year	Value of Machine B	Capitalized Interest	Adjusted Value of Machine B	Depreciation	Balance
1	₱2,000,000.00	₱200,000.00	₱ 2,200,000.00	₱ 366,666.67	₱1,833,333.33
2	1,833,333.33	200,000.00	2,033,333.33	406,666.67	1,626,666.67
3	1,626,666.67	200,000.00	1,826,666.67	456,666.67	1,370,000.00
4	1,370,000.00	200,000.00	1,570,000.00	523,333.33	1,046,666.67
5	1,046,666.67	200,000.00	1,246,666.67	623,333.33	623,333.33
6	623,333.33	-	623,333.33	623,333.33	-

The revised differences between accounting and tax treatments are as follows:

Year	Interest Expense			Depreciation			Net Difference
	Accounting	Tax	Difference	Accounting	Tax	Difference	
1	₱ 200,000.00	₱ -	₱ 200,000.00	₱ 333,333.33	₱ 366,666.67	₱(33,333.34)	₱ 166,666.66
2	200,000.00	-	200,000.00	333,333.33	406,666.67	(73,333.34)	126,666.66
3	200,000.00	-	200,000.00	333,333.33	456,666.67	(123,333.34)	76,666.66
4	200,000.00	-	200,000.00	333,333.33	523,333.33	(190,000.00)	10,000.00
5	200,000.00	-	200,000.00	333,333.33	623,333.33	(290,000.00)	(90,000.00)
6	-	-	-	333,333.33	623,333.33	(290,000.00)	(290,000.00)
							₱ -

There is an automatic gap between the interest expense and depreciation expense accounts due to the loan term, period of preparation of the machine, and useful life of the machine which may be disclosed in the notes to the financial statements. The net difference through years 1 to 4 are temporary differences that are deductible from gross income for tax purposes in subsequent periods.

The following are the revised journal entries to record interest incurred and depreciation for Machine C:

Accounting

Years 1, 2, 3, 4 and 5

Dr. Interest Expense	₱	200,000.00
Cr. Interest Liability		200,000.00
Dr. Depreciation	₱	333,333.33
Cr. Accumulated Depreciation		333,333.33

Tax

Year 1

Dr. PPE – Capitalized Interest Expense	₱ 200,000.00
Cr. Interest Liability	200,000.00
Dr. Depreciation	₱ 366,666.67
Cr. Accumulated Depreciation	366,666.67

Year 2

Dr. PPE – Capitalized Interest Expense	₱ 200,000.00
Cr. Interest Liability	200,000.00
Dr. Depreciation	
Cr. Accumulated Depreciation	₱ 406,666.67
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Year 3		
Dr. PPE – Capitalized Interest Expense	₱ 200,000.00	
Cr. Interest Liability		200,000.00
Dr. Depreciation	₱ 456,666.67	
Cr. Accumulated Depreciation		456,666.67
Year 4		
Dr. PPE – Capitalized Interest Expense	₱ 200,000.00	
Cr. Interest Liability		200,000.00
Dr. Depreciation	₱ 523,333.33	
Cr. Accumulated Depreciation		523,333.33
Year 5		
Dr. PPE – Capitalized Interest Expense	₱ 200,000.00	
Cr. Interest Liability		200,000.00
Dr. Depreciation	₱ 623,333.33	
Cr. Accumulated Depreciation		623,333.33
Year 6		
Dr. Depreciation	₱ 623,333.33	
Cr. Accumulated Depreciation		623,333.33

Year 6		
Dr. Depreciation	₱ 333,333.33	
Cr. Accumulated Depreciation		333,333.33

3. Given the foregoing, the revised computation of income tax is as follows:

Year	Net Income before Interest and Depreciation *(a)*	Allowable Interest Expense *(b)*	Depreciation Expense *(c)*	Net Taxable Income *(a – b – c) = (d)*	Income Tax *(d) x 25%*
1	₱ 10,000,000.00	₱ 30,000.00	₱ 533,333.34	₱ 9,436,666.66	₱ 2,359,166.67
2	10,000,000.00	30,000.00	573,333.34	9,396,666.66	2,349,166.67
3	10,000,000.00	30,000.00	883,333.34	9,086,666.66	2,271,666.67
4	10,000,000.00	30,000.00	808,333.33	9,161,666.67	2,290,416.67
5	10,000,000.00	-	941,666.66	9,058,333.34	2,264,583.34
6	10,000,000.00	-	941,666.66	9,058,333.34	2,264,583.34
7	10,000,000.00	-	318,333.33	9,681,666.67	2,420,416.67

Below are the differences between accounting and tax treatments:

Year	Accounting Net Income *(a)*	Taxable Net Income *(b)*	Difference *(a – b)*
1	₱ 9,250,000.00	₱ 9,436,666.66	₱ (186,666.66)
2	9,250,000.00	9,396,666.66	(146,666.66)
3	8,910,000.00	9,086,666.66	(176,666.66)
4	9,076,666.67	9,161,666.67	(85,000.00)
5	9,126,666.67	9,058,333.34	68,333.33
6	9,426,666.67	9,058,333.34	368,333.33
7	9,760,000.00	9,681,666.67	78,333.33
		₱	80,000.00

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capitalize interest expense for tax purposes. The differences must be included as reconciling items in the reconciliation of net income per books against taxable income in the income tax return.

IV. GENERAL TRANSITORY PROVISIONS

The taxpayer using official receipts (manual, POS, CRM, CAS, etc.) shall comply with the provisions of Revenue Regulations No. 7-2024 dated March 22, 2024 and other related issuances.

All revenue issuances and BIR Rulings inconsistent herewith are hereby considered amended, modified or revoked accordingly.

All internal revenue officials/officers, employees and others concerned are hereby enjoined to give this Circular a wide publicity as possible.

This Circular takes effect immediately.

ROMEO D. LUMAGUI, JR.
Commissioner of Internal Revenue

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