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

January 23, 2006

REVENUE MEMORANDUM ORDER NO. 4-2006

Subject: Prescribing Guidelines and Procedures in the Conduct of Benchmarking and Adapting/Implementing the Performance Benchmarking Method in the Revenue District Offices

To : All Revenue Officials, Officers and Others Concerned

I. Background

The downward trend in revenue collections due to numerous incidents of registered taxpayers not filing their tax returns and paying their taxes correctly brought about the necessity of instituting a systematic program that would level the playing field among taxpayers engaged in similar line of industry, in accordance with Section 5(E) of the National Internal Revenue Code, as amended, in relation to Section 6 (C) of the same Code.

In this connection, performance benchmarking of taxpayers by line of industry where the best performers, among taxpayers within the same line of industry or business, will be identified using profit margin rate, Net VAT Due and Income Tax Due in relation to gross sales/receipts, could be an excellent tool in increasing taxpayers' voluntary compliance.

Monitoring and evaluation of tax payments through the use of performance benchmarking will determine/identify taxpayers within industry groups who are paying below the minimum amount or set benchmarks for tax compliance purposes.

II. Objectives

This Order is issued:

1. To enhance taxpayers' voluntary compliance by setting up a standard in measuring taxpayers' compliance with regard to Income Tax Due and Net VAT Due of taxpayers engaged in the same line of industry;

2. To prescribe policies, guidelines and procedures in the implementation of benchmarking activities in the districts in accordance with Sections 5(E) and 6 (C) of the NIRC; and

3. To effectively monitor the accomplishments of the Regional and Revenue District Offices regarding benchmarking activities.

III. Definition

For the purpose of this Order the following definitions shall be used as reference terms:

1. Benchmark – a point of reference for measurement of or a standard by which to measure the performance/compliance of taxpayers in a particular industry using one's profit margin rate, Net VAT Due and Income Tax Due in relation to gross sales/receipts.

2. Benchmarking – the process of determining and comparing the performance level of taxpayers in a given line of industry as far as Net VAT Due and Income Tax Due are concerned in relation to gross sales/receipts vis-à-vis profit margin rate for the purpose of setting an industry standard of taxpayers' performance/compliance.

3. Mean – the average or sum of all values in a distribution divided by the number of values in the distribution. It is used to approximate the expected value or statistical industry norm.

4. Weighted Average Method – a method of computation wherein the benchmark or average is derived by taking into account the proportional relevance of each component, rather than treating each component equally. It is calculated by multiplying each number by a weight, adding these together and then dividing the total by the sum of the weights.

   To illustrate, in a weighted average method of inventory valuation using the periodic method, the weighted unit cost is computed as follows:

Date	Units	Unit Price	Amount
Jan. 1	100	1.30	P 130
Jan. 18	300	1.36	408
July 4	150	1.40	210
Oct. 28	150	1.50	225
	700		P 973

Weighted Unit Cost 973 /700 = 1.39

5. Tax Type – kind of tax, such as income tax (IT), value-added tax (VAT), etc.

6. Industry – a group of companies engaged in the production of similar goods or services.

7. Area – refers to district/s or town/s or city/cities comprising a BIR revenue district.

8. Taxpayer Class – kind of taxpayer, whether individual or corporation.

IV. Coverage

This Order shall cover all types of taxpayers per line of industry. To get an impact on collection, initial coverage will be the top 200 taxpayers of each industry per district based on gross sales as reflected in the tax returns, or actual gross sales/receipts as determined from sources within and outside the Bureau, whichever is higher. The number of taxpayers will be increased until all taxpayers of all industries shall have been fully covered. All should be completed on or before end of calendar year 2008.

V. General Policies

1. All Regional Directors and Revenue District Officers shall cause the implementation of benchmarking activities in their respective regions;

2. A Regional Committee is hereby created to assist in monitoring/coordinating benchmarking activities and/or to prepare and consolidate management reports as hereinafter provided;

3. Benchmarking shall be separate for corporations and individuals;

4. Benchmarking shall be on a per area (district or town/cities component of district), per line of industry, and per tax type basis and shall be done in the districts by preparing a profile of taxpayers per taxable year (Annex "A"). Based on tax returns and data from other sources within and outside the Bureau, Revenue District Officers shall determine the specific industry target/coverage to be benchmarked;

5. Priority industries for benchmarking covering taxable year 2004 are the following:

   5.1 Manufacturing (Flour, Softdrinks, Sugar, Cement and Plastic)
   5.2 Hardware
   5.3 Restaurants
   5.4 Shipping
   5.5 IT Providers
   5.6 Telecommunication
   5.7 Call Centers

5.8 Logistics Providers (Arrastre, Stevedoring, Freight, Trucking and Courier Services)
5.9 Construction
5.10 Petroleum

6. In cases where Letters of Authority have been issued to taxpayers subject of benchmarking, the RDO shall not close the case without taking into consideration the prescribed benchmarks;

7. Revenue District Officers shall submit a Monthly Report on the Status of Benchmarking Activities (Annex "B") to the Regional Director thru the Regional Committee created for this purpose on or before the 5th day of the following month.

   The Regional Committee shall consolidate the reports of the districts and submit a Consolidated Report on Benchmarking Activities (Annex "C") to the Deputy Commissioner for Operations, copy furnished the Assessment Service, on or before the 10th day of the following month.

VI. Guidelines and Procedures

1. All RDOs shall observe the following steps in the conduct of benchmarking:

   1.1 Plan and determine the specific industry and covered taxpayers to be benchmarked;

   1.2 Collect/gather relevant data & information (ITR/VAT Returns)

      1.2.1 Sort out data by area (district or town or city), by line of industry, by class of taxpayer and by tax type;

      1.2.2 Submit a profile of taxpayers' return data per report on Annex "A" hereof.

   1.3 Determine benchmark based on Net VAT Due which is computed as follows:

      Net VAT = Output Tax – Input Tax claimed per return

      Not included in the computation of claimed input tax is the input tax credit carry-over or carried forward to the next accounting period and input tax on capital goods as illustrated below:

      Example 1

      Given:

Annual Sales subject to 10% VAT	P 2,000,000
Domestic Purchases – Goods	300,000

Domestic Purchases - Services	200,000
Domestic Purchase - Capital Goods	100,000

Computation:

Output Tax 2,000,000 x 10%		P 200,000
Less: Input tax for benchmarking purposes		
300,000 x 10%	30,000	
200,000 x 10%	20,000	50,000
Net VAT		P 150,000

Example 2
Given:

Annual Sales subject to 10% VAT	P 1,000,000
Domestic Purchases – Goods	500,000
Domestic Purchases – Services	500,000

Computation:

Output Tax 1,000,000 x 10%		P 100,000
Less: Input tax for benchmarking purposes		
500,000 x 10%	50,000	
500,000 x 10%	50,000	100,000
Net VAT		P 0

Example 3

Given:

Annual Sales subject to 10% VAT	P 1,000,000
Domestic Purchases – Goods	1,000,000
Domestic Purchases – Services	1,000,000
Domestic Purchase - Capital Goods	500,000
Input Tax Carried Over from the last quarter of the previous year	25,000

Analysis of Quarterly VAT Return for 4 quarters:

Particulars	**Amount**	**Output Tax**	**Input Tax**
Annual Sales	P1,000,000	P 100,000	
Input Tax Carried Over from previous quarter			P 25,000
Domestic Purchases - Goods	1,000,000		100,000
Domestic Purchases - Services	1,000,000		100,000
Domestic Purchases – Capital Goods	500,000		50,000

Conclusion:

Under the facts and prevailing circumstances, the Quarterly VAT Returns shall reflect an Allowable Input Tax of only 70% of Output Tax or P 70,000. Thus, the Net VAT due and paid per return is P 30,000, without prejudice to the carry-over to the next quarter/taxable period of unutilized Input Tax.

1.4 Compute for the benchmark per tax type (Income Tax, Value Added Tax, Percentage Tax), per industry, per area and per taxpayer class by determining the mean through the use of the weighted average method:

1.4.1 Analyze Gross Profit Margin, number of taxpayers belonging to the same group with the same profit margin. Consider the gap for each margin. Include in the analysis VAT and IT compliance in relation to gross sales or revenues.

1.4.2 Establish performance benchmark, by industry, on Gross Profit Rate, ratios of Net VAT Due and Income Tax Due to gross sales or revenues. Take into consideration the area, taxpayer class and the trend in the industry.

2. After establishing the benchmark ratios, RDOs shall prepare their recommendations and plan of actions to be submitted to the Regional Director for consideration and approval;

3. RDOs shall implement the following programs and strategies:

3.1 Conduct a tax dialogue by industry;

3.2 Send letters to taxpayers informing them of their tax compliance as shown from benchmark data/analysis or tax compliance in relation to sales/revenues;

3.3 Consider the reply/feedback received from taxpayers and make the necessary adjustment or correction, if appropriate:

3.3.1 Taxpayers who will voluntarily comply in accordance with benchmarking may amend their ITR/VAT Returns, provided no Letter of Authority has been issued yet;

3.3.2 Taxpayers who failed to comply as a result of the benchmarking shall be subjected to any of the following:

- Inventory Stocktaking
- Surveillance
- Audit & Investigation
- Tax Compliance Verification Drive

3.3.3 Evaluate results and realign strategies, if needed.

3.4 Assess and collect the deficiency taxes found due as a result of the above activities in VI.3.3.2;

3.5 Taxpayers who failed to pay the corresponding deficiency taxes shall be recommended for appropriate administrative and/or legal action/judicial action.

4. The RDOs shall integrate the use of benchmarking method with other tools and initiatives:

4.1 Utilize third party information, the RELIEF System and other tools within and outside the Bureau in the determination of gross sales/receipts, where applicable;

4.2 Adjust benchmark rate/ratio after incorporating deficiency taxes paid or assessed without protest;

4.3 Periodically review the statistical method utilized to arrive at the benchmarks.

VII. Composition and Functions of the Regional Committee on Benchmarking

1. The Regional Director shall create a Committee, composed of the following:

Chairman: Regional Director

Members: Assistant Regional Director
Chief, Assessment Division
Technical Staff/Reviewer
Revenue District Officer Concerned

Secretariat: Revenue personnel to assist in the encoding/consolidation of reports

2. The Chairman shall call and preside a regular meeting of the Committee to update/brief the district officers and determine their course of actions on issues raised by all concerned;

3. The Committee shall assist the Regional Director in monitoring and/or coordinating the benchmarking activities of the districts;

4. The Committee Secretariat shall consolidate and submit the required reports; and

5. The Committee shall perform other responsibilities, as may be required.

VIII. Sanctions

Appropriate cases will be filed against taxpayers who will be found to have supplied fabricated data or incorrect information just to meet the benchmark requirements, in violation of Sections 254, 255, 256 and 257 of the Tax Code.

IX. Effectivity

This order shall take effect immediately.

(Original Signed)
JOSE MARIO C. BUÑAG
Commissioner of Internal Revenue

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