REPUBLIC OF THE PHILIPPINES
DEPARTMENT OF FINANCE
BUREAU OF INTERNAL REVENUE

Quezon City

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REVENUE MEMORANDUM CIRCULAR NO. 62-2021

SUBJECT : Clarifications on Certain Provisions of Revenue Regulations No. 5-2021 Relative to Corporate Income Taxation

TO : All Internal Revenue Officers and Others Concerned

With the recent promulgation of Revenue Regulations (RR) No. 5-2021, the RR implementing the income tax provisions under Republic Act No. 11534, otherwise known as Corporate Recovery and Tax Incentives for Enterprises Act (CREATE), the Bureau has received from both internal and external stakeholders several concerns and issues. To address these, this Revenue Memorandum Circular, in question and answer format, is hereby issued.

Q1 One of the conditions that must be satisfied to qualify for the reduced corporate income tax rate of twenty percent (20%) is that the total assets should not be more than P 100,000,000, exclusive of the land. Are the total assets net of depreciation and allowance for bad debts, if any?

A1 Yes, total assets shall be net of depreciation and allowance for bad debts, if any. Further, the land where the business entity's office, plant and equipment are situated is excluded in computing for the total assets.

Q2 In relation to the preceding question, what shall be excluded? Is it the acquisition cost or the fair market value of the land?

A2 If the cost of acquisition of the land is reflected in the Financial Statements (FS), that cost shall be excluded in determining the total assets. But if the land is reflected in the FS at its fair market value (FMV), such FMV shall be excluded in the computation of the total assets, for purposes of determining if the corporation is qualified to the reduced corporate income tax rate of twenty percent (20%).

Q3 Is the cost/value of all the land used in business excluded in determining the total assets of the corporation for purposes of qualification to the reduced corporate income tax rate of Twenty percent (20%)?

A3 No, the value of the land which shall be excluded is <u>limited</u> to that particular land where the business entity's office, plant and equipment are situated during the taxable year for which the twenty percent (20%) income tax is imposed. Thus, if the land is being held primarily for sale to customers or land held for investment purposes, the value of these types of land should <u>not be excluded</u> in the determination of the business entity's total assets.

Q4 How to determine the value of the land that shall be excluded in computing for the total assets if only a portion of the floor area of the building is devoted to the entity's office and the rest of the usable floor area are on lease?

A4 In order to determine the value of the land that shall be excluded in the computation of total assets, the percentage of the floor area devoted to the entity's office shall be multiplied with the total value of the land. For example, the building has an area of 5,000 square meters, where 1,000 square meters pertain to the entity's office, while the 4,000 square meters are rented out. If the value of the land is Php 10,000,000.00, the value to be excluded in the computation of total assets shall be Php 2,000,000.00. To further illustrate: 1,000/5,000 square meters x Php 10,000,000.00 = Php 2,000,000.00.

Q5 If the taxpayer's business is banana plantation or leasing of land, will the value/cost of these lands be excluded for purposes of determining the total assets?

A5 No, as discussed in Item A3, the value of the land which shall be excluded is limited to that particular land where the business entity's office, plant and equipment are situated during the taxable year for which the twenty percent (20%) income tax is imposed. Thus, the value of the land being used as banana plantation or being leased should NOT be excluded in the determination of the total assets for purposes of qualification to the 20% corporate income tax rate.

Q6 Are private educational institutions distributing dividends to shareholders taxable at the regular corporate income tax rates of either twenty-five (25%) or twenty percent (20%)?

A6 Yes, because the law is very specific that the preferential rate of Ten Percent (10%) or One Percent (1%) starting from July 1, 2020 to June 30, 2023 shall be imposed to Proprietary Educational Institution, which is defined as "any private schools which are <u>non-profit</u>, maintained and administered by private individuals or groups, with an issued permit to operate from Department of Education (DepEd) or Commission on Higher Education (CHED) or Technical Education and Skills Development Authority (TESDA), as the case may be, under existing regulations".

Q7 Did the CREATE law prescribe a new tax treatment for proprietary educational institution and private hospital?

A7 No, the CREATE law did not prescribe new tax treatment for proprietary educational institutions and private hospital since it is already provided in the Tax Code of 1997, as amended. The CREATE Act merely reduced the tax rate, from 10% to 1%, effective July 1, 2020 to June 30, 2023 for such institutions which are non-profit.

Q8 Section 5 of RR No. 5-2021 states that "*if the Certification shall state non-utilization of the dividends received, the corresponding tax due on the unutilized dividends shall be declared as taxable income, subject to interest, surcharges and penalties, if any*". Please clarify what should be declared as "taxable income".

A8 The taxable income shall be the unutilized dividends. The provision on RR No. 5-2021 regarding unutilized dividends should be read as "*if the Certification shall state non-*

utilization of the dividends received, the unutilized dividends shall be declared as taxable income, and the corresponding tax due shall be subject to interest, surcharges and penalties".

Q9 What shall be the tax treatment for dividends received by a domestic corporation from a resident foreign corporation (RFC)?

A9 The tax treatment of dividends received by a domestic corporation from RFC will depend on the sources of income of the RFC. Under Section 42(A)(2)(b) of the Tax Code, as amended, "*dividend received from a foreign corporation shall be treated as income derived from sources within the Philippines, unless less than fifty percent (50%) of the gross income of the foreign corporation for the three-year period ending with the close of its taxable year preceding the declaration of such dividends (or for such part of the period as the corporation has been in existence) was derived from sources within the Philippines xxx xxx*".

Illustration:

Corporation X, an RFC, has gross income for the three-year period of P 500,000,000 from sources within the Philippines. However, it also derived gross income from outside of the Philippines, amounting to P 300,000,000. In 2021, it declared dividend amounting to Ten Million pesos (P 10,000,000.00). Five Million pesos (P 5,000,000.00) of which was paid to Corporation Z, a domestic Corporation.

To determine the tax treatment of the dividend received by the domestic corporation, there is a need to determine if the dividend paid by the RFC is sourced within the Philippines or not. In this scenario, it qualified as sourced within the Philippines since the gross income of Corporation X from within is <u>more than</u> fifty percent (50%) of its total gross income. Hence, it is exempt from income tax sans compliance with the conditions imposed under Section 5 of RR No. 5-2021. Conversely, if the gross income of Corporation X from within is <u>less than</u> 50% of its total gross income, then, the dividend received shall be considered as sourced without and, therefore, must comply with the conditions imposed under Section 5 of RR No. 5-2021 to warrant its income tax exemption.

Q10 Illustration "a" under Section 9.B on the Transitory Provisions of RR No. 5-2021 states that the transactions of MVAA Corporation pertain to its fourth year of business operation, hence, MCIT was computed. What was the reckoning date of determining that it is the corporation's fourth year of operation?

A10 The phrase "4th year of business operations" in the illustration should be construed to mean "fourth taxable year immediately following the year in which such corporation commenced its business operation" as indicated under Section 3 of RR No. 5-2021 on MCIT. Thus, if the corporation commenced its business operations in 2017, MCIT <u>may</u> be imposed beginning the year 2021, if it exceeds the regular income tax. The taxable year in which business operations commenced shall be the year in which the corporation is registered with the BIR, as provided under RR No. 9-98.

Q11 Is the additional allowable deduction equivalent to one-half of the actual training expenses applicable only to entities engaged in manufacturing and that such actual training expenses exclude those which pertain to employees under supervisory, managerial, administrative and support functions?

A11 The law provides no distinction as to which type of industry can claim the additional allowable deduction of one-half (1/2) of the value of labor training expenses. There are, however, requirements that must be complied with before this deduction can be claimed. These are:

a) The labor training expenses shall not be more than ten percent (10%) of the Direct Labor Wage;

b) The labor training expenses are incurred for skills development of enterprise-based trainees;

c) The enterprise-based trainees are enrolled in public senior high school, public higher education institutions, or public technical and vocational institutions for the taxable year in which the labor training expenses are claimed;
The training is covered by an apprenticeship agreement under Presidential Decree (PD) No. 442 or the Labor Code of the Philippines; and

d) The Company claiming the additional deduction is granted an authority to offer training program for skills development as certified by the Department of Education (DepED), Technical Education and Skills Development Authority (TESDA) or Commission on Higher Education (CHED), as applicable.

Moreover, since the training is covered by an apprenticeship agreement, it follows that training expenses which pertain to training/s of employees under supervisory, managerial, administrative and support functions should not be included in the computation of the additional allowable deduction of one-half (1/2) of the value of labor training expenses. The resulting amount then shall be subject to a cap of not more than ten percent (10%) of the Direct Labor Wage. The "direct labor" is that portion of salaries and wages which can be identified with and charged directly to a product or to a project or service on a consistent basis. Thus, it does not only apply to a manufacturing industry.

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

CAESAR R. DULAY
Commissioner of Internal Revenue

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