REVENUE MEMORANDUM CIRCULAR NO. 13-2024 issued on January 22, 2024 clarifies the treatment of retirement benefits expense for financial reporting and tax purposes.

The Table below shows the differences between the recording and treatment of income and expenses relating to employee retirement benefits under the Philippine Financial Reporting Standards (PFRS)/Philippine Accounting Standards (PAS) and the National Internal Revenue Code of 1997, as amended.

Particulars	PFRS	Taxation	
		RA No. 4917	**RA No. 7641**
1. Employee benefit expense	Employee benefit expense comprises of: 1. Service costs 2. Net interest costs	Contribution to a tax qualified plan is deductible expense	Actual retirement benefits paid is a deductible expense
2. Current service costs	Recognized in profit or loss as part of employee benefit expense	Contribution for normal cost is deductible in full	Not applicable
3. Past service costs	Recognized in profit or loss as part of employee benefit expense	Contribution for past service liability is recognized as deductible expense over ten years	Not applicable
4. Gain or loss on settlement	Recognized in profit or loss as part of employee benefit expense	Not applicable	
5. Return on plan assets	Included in the employee benefit costs	Exempt from income tax	Not applicable
6. Remeasurement gains and losses	Remeasurement gains and losses are recognized in other comprehensive income	Not applicable	
7. Actuarial Valuation Method	Actuarial valuation for accounting	Actuarial valuation for funding	Not applicable

The accounting for the post-employment benefits are employee benefits that are payable after the completion of employment. The most common form of a post-employment benefit is the retirement benefit given by employer to its employees. The accounting for the post-employment benefit depends on whether it is classified as a defined contribution plan or a defined benefit plan.

Accounting for a defined contribution plan is straight-forward. When an employee has rendered service to an entity during a period, the entity recognizes the contribution payable to a defined contribution plan in exchange for that service as an expense unless another Standard requires it to be included in the cost of an asset.

Defined contribution plans are accounted for as a defined benefit plan based on Q&A 2013-03 as provided by the Philippine Interpretations Committee of the Philippine Financial and Sustainability Reporting Standards Council. A major reason for this is that the mandatory minimum retirement benefit under RA No. 7641 is in nature, a defined benefit plan.

Any post-employment benefit plan other than a defined contribution plan is a defined benefit plan. Accounting for defined benefits plans requires a valuation prepared by an actuary using a projected unit credit method. This includes attributing benefit to periods of service and making actuarial assumptions.

The amount of employee benefit cost can be disaggregated into: (1) employee benefit expense recognized in profit or loss; and (2) remeasurement gains and losses recognized in other comprehensive income. Employee benefit expense is recognized in profit or loss: (1) the service costs; and (2) the net interest costs.

Service cost is comprised of: (a) Current service costs; (b) Past service costs; and (c) Settlement gain or loss. Current service cost is the increase in the present value of the defined benefit obligation resulting from employee service in the current period. Past service cost, on the other hand, is the change in the present value of the defined benefit obligation resulting from a plan amendment or curtailment. A settlement occurs when an employer enters into a transaction that eliminates all further legal or constructive obligations for part or all of the benefits provided under a defined benefit plan. A gain or loss on settlement arises when there are differences between the present value of the defined benefit obligation being settled and the settlement price. (PAS 19.109).

The net interest cost/income represents the increase in the net defined benefit liability/asset due to passage of time. This is determined by multiplying the net defined benefit liability/asset by the discount rate taking into account any changes in the net defined benefit liability/asset during the period resulting from contributions or benefit payments. (PAS 19.123, 123A).

Employee benefit expense is recognized in profit or loss unless another Standard requires it to be included as cost of an asset.

Remeasurement gains and losses may occur because the reality may differ from the actuarial assumptions. Also, changes in assumptions used to determine the net defined asset/liability can also give rise to remeasurement gains and losses. Remeasurements of the net defined benefit liability/asset comprise:

a. Actuarial gains and losses;
b. The difference between the actual return on plan assets and the interest income; and
c. The effect of the asset ceiling. (PAS 19.8, 127)

Remeasurement gains and losses are generally recognized as "Other Comprehensive Income".

The amount of expense that can be claimed as deduction for Income Tax purposes will depend primarily on whether the employer has a retirement benefit plan that is registered with the BIR and declared as reasonable within the contemplation of Section 32 (B) (6) (a) of the Tax Code ("Tax Qualified Plan").

If the employer's retirement benefit plan meets the requirements under Republic Act (RA) No. 4917, evidenced by a Certificate of Tax Qualification issued by the BIR, the employer may deduct the following contributions to the retirement fund pursuant to Section 34(J) of the Tax Code:

a. contributions to the Retirement Fund during the taxable year to cover the pension liability accrued during that year ("Normal Cost"); and
b. contributions to the Retirement Fund during the taxable year in excess of the Normal Cost but only if such amount: (i) has not theretofore been allowed as a deduction; and (ii) is apportioned in equal parts over a period of ten (10) consecutive years beginning with the year in which the transfer or payment is made.

If an employer does not have a Tax Qualified Plan, the rules under RA No. 7641 shall apply. Accordingly, only the actual amount of retirement benefits paid to employees pursuant to RA No. 7641 can be claimed as deduction from the gross income.

Only the: (a) Normal Cost; and (b) contributions to the trust during the taxable year in excess of the Normal Cost but only if such amount (i) has not theretofore been allowed as a deduction, and (ii) is apportioned in equal parts over a period of ten (10) consecutive years beginning with the year in which the transfer or payment is made, are allowed as deductions for Income Tax purposes. Hence, any amount of contribution other than items (a) and (b) above shall not be allowed as deduction from gross income.

In the event that portions of the retirement fund in excess of the amount actuarially determined to cover the benefits of the covered employees are reverted to the employer, said reverted amount shall be reported as income and the applicable taxes thereon shall be paid by the employer concerned.

To apply for tax exemption of the employee retirement benefit plan, the employer shall apply with the BIR, through the Legal and Legislative Division at the National Office, for the issuance of a Certificate of Qualification as a Reasonable Employee's Retirement Benefit Plan within thirty (30) days from the date of effectivity of the retirement benefit plan. Otherwise, penalty shall be imposed upon the employer under the existing rules and regulations. The issued Certificate of Qualification shall be valid until revoked by the BIR.

The following documentary requirements shall be submitted to the BIR relating to the approval and issuance of a Certificate of Qualification:

a. Certified True Copy of the latest Actuarial Valuation Report which must not be more than three (3) years prior to the date of application;
b. Certified True Copy of the Trust Agreement;
c. Duly accomplished BIR Form 17.60 (Retirement Benefit Plan Information Sheet), signed by an authorized officer. BIR Form 17.60 is attached in the Circular as Annex "A;"
d. Certified True Copy of the Retirement Plan Rules and Regulations which must contain the following provisions:
    i. Provision on non-forfeitable rights, that is, upon the termination of the plan or upon the complete discontinuance of contributions under the plan, the rights of the members accrued to the date of such termination or

discontinuance to the extent then funded, or the rights to the amounts credited to the account at such time are non-forfeitable;

ii. Provision that forfeitures must not be applied to increase the benefits any employee would receive, but must be used to reduce the employer's contribution under the plan; and

iii. Provision on impossibility of diversion, that is, that no part of the corpus or income of the Trust Fund shall be used for or diverted to purposes other than for the exclusive benefit of the members-employees and their beneficiaries.

e. Taxpayer Identification Number (TIN) of the Retirement Plan, Certificate of Registration of the Retirement Plan, and BIR Form No. 1901;

f. Secretary Certificate as to adoption/approval of amendments of Retirement Plan/appointment of Trustee; and

g. Payment of fees prescribed under RR No. 11-2001.

The income of the Retirement Fund from its investments are exempt from Income Tax provided all the statutory requirements for a reasonable retirement benefit plan are met and complied with pursuant to Section 60(B) of the Tax Code. A Tax Qualified Plan may invest some or all of its fund without losing its tax-exempt status provided that in such investment activity said funds are not actually used or diverted to purposes other than for the exclusive benefit of the employees or their beneficiaries.

The exemption of the trust income under Section 60(B) of the Tax Code may be denied if the trust:

a. Lends any part of its income or corpus without adequate security and a reasonable rate of interest;

b. Pays any compensation in excess of a reasonable allowance for salaries or other compensation for personal services actually rendered;

c. Makes any part of its services available on a preferential basis;

d. Makes any substantial purchase of securities or any other property for more than adequate consideration in money or money's worth;

e. Sells any substantial part of its securities or other property, for less than an adequate consideration in money's worth; or

f. Engages in any other transaction which results in a substantial diversion of its income or corpus.

to or from the employer or if the employer is an individual, to or from a member of the family of the employer, or to or from a corporation controlled by the employer through the ownership; directly or indirectly, of 50% or more of the total combined voting power of all classes of stock entitled to vote or 50% or more of the total value of shares of all classes of stock of the corporation.

The fund manager should not in any way use the Retirement Fund to invest/deposit in any of the employer's business ventures in keeping with the requirements under Section 5(f) of RR No. 1-68, as amended.

While it is true that there are no specific limitations provided in the law with respect to investments which may be made by the trustee of a Retirement Fund, it is important however, that the said fund be invested in proper and sound investments for the sole benefit of the employees. Considering the potential variability in the business operations of the employer which may adversely affect its capability to contribute to the Retirement Fund, it is deemed best to allow the trustees of a Retirement Fund to use and/or invest said funds in various diverse investments (other than the business ventures of the employer) with the sole objective of accumulating adequate resources to fulfill its obligations. It is important to maintain the separation of fund (or avoid the comingling of funds) of the Retirement Fund from that of the employer, which may be an avenue for evasion of taxes.

There is a difference in the calculation of service/retirement costs under Philippines Accounting Standards (PAS)/Philippines Financial Reporting Standards (PFRS) and the Tax Code. The retirement cost for financial reporting purposes is based on the requirements of PAS 19/PFRS which uses the published discount rates for the projected unit credit method (PAS 19.67,83) or accrual method (PFRS for Small Entities 22.393). On the other hand, the retirement cost deductible for tax purposes is based on actuarial valuation for funding requirements that uses the expected return on the fund's actual investments in determining normal costs and past service liability.

The retirement benefit received by a retiring employee is considered as compensation subject to Income Tax and, consequently to Withholding Tax. However, if the retirement benefit is received by a qualified retiring employee pursuant to a Tax Qualified Plan under RA No. 4917, such retirement benefit is exempt from Income Tax and, consequently, from Withholding Tax provided that such retiring employee meets all of the following criteria:

a. must be at least fifty (50) years of age and has served his/her employer for at least ten (10) years; and
b. has not previously availed of the privilege under a retirement benefit plan of the same or another employer.

If the retirement benefit is received by a qualified employee under RA No. 7641, such retirement benefit is exempt from Income Tax and, consequently, from Withholding Tax provided that such retiring employee meets all of the following criteria:

a. must be at least sixty (60) years of age, but not beyond sixty-five (65) years which is declared the compulsory retirement age;
b. has served his/her employer for at least five (5) years, which includes authorized absences and vacations, regular holidays and mandatory fulfillment of military or civic duty; and
c. has not previously availed of the privilege under a retirement benefit plan of the same or another employer.

For the avoidance of doubt, a Certificate of Qualification for Tax Exemption is not required in order to avail of the tax exemption of the retirement benefits received by retirees under RA No. 7641.

While it is true that the age qualification under RA No. 7641 is sixty (60) years or more, but not beyond sixty-five (65) years which is the compulsory retirement age, the employer and qualified employee is not prohibited to continue the employment. In such case, all the retirement benefits received by the qualified employee at the age of his/her actual retirement (in this example is seventy (70) years old) shall be exempt from Income Tax and, consequently, from Withholding Tax: Provided, however, that such qualified employee has: (a) served his/her employer for at least five (5) years, which includes authorized absences and vacations, regular holidays and mandatory fulfillment of military or civic duty; and (b) has not previously availed of the privilege under a retirement benefit plan of the same or another employer since it-must be availed only once.

If such qualified employee has received his/her retirement benefits at the age of sixty-five (65), and was allowed to continue his/her employment thereafter, all income and other benefits he/she received beyond the age of sixty-five (65) shall be considered as compensation that is subject to Income Tax and, consequently, to Withholding Tax. Once the retirement benefit plan is approved by the BIR, the effectivity of the approval is retroacting to the date of effectivity of the retirement benefit plan.

Pending the employer's application with the BIR, the retirement benefits received by any qualified retiring employees shall be exempt from Income Tax and, consequently, from Withholding Tax pursuant to RA No. 4917. However, should the application of the employer for issuance of a Certificate of Qualification be denied by the BIR, the employer/trust shall be directly and solely liable for the deficiency Income Taxes due on the retirement benefits provided to the qualified retiring employees.

Pending the employer's application with the BIR, the contributions of the employers to the retirement fund pursuant to a retirement benefit plan are deductible from the gross income based on Section 34 (J) of the Tax Code. However, should the application of the employer for issuance of a Certificate of Qualification be denied by the BIR, the employer/trust shall be directly and solely liable for the deficiency Income Taxes due on the same.

Under Section 32 (B) (6) (a) of the Tax Code, the retirement benefits to be received by a qualified employee-member of the retirement plan shall be exempt from Income Tax provided the two (2) conditions are satisfied: (a) the employee had been in the service of the same firm for at least ten (10) years; and (b) he or she is already fifty (50) years old at the time of retirement.

The ten (10)-year requirement would be computed only in one company. However, in case of transfer of employees from one participating company to another participating company within a multi-employer plan due to a valid merger, the aggregate years of service to the said companies shall be considered in computing the prescribed ten (10)-year period, provided, however, that said employees did not receive their respective separation pay (an additional pay given to employees who are separated from their employment due to authorized causes as these employees are not at fault since their employment was ended due to legitimate business reasons) from their previous employer/company (the absorbed or acquired company). Considering that the said transfer of employees is outside the control of the concerned employees, it is but just and fair to consider the period of services to both companies.

For this purpose, a "multi-employer plan" refers to a Retirement Plan to which two or more related reporting entities (each of which shall be individually referred to as "Participating Company") contribute for the benefit of its retiring officials and employees. Reporting entities are considered related in this context if they are either a parent, subsidiary, or fellow subsidiary, of any Participating Company/ies.

Pursuant to RR No. 01-83, any amendment to the approved corporate retirement plan should be submitted to the BIR for certification that the amendment/s do not affect the qualification of the approved retirement plan. Also, the prescribed fees under RR No. 11-01 shall be paid to the BIR.

Illustrations and Accounting Entries on retirement benefits are reflected in Annex "B" of the Circular, as guide for recording and reporting of retirement benefit expense.