

August 25,1998

REVENUE REGULATIONS NO. 9-98

SUBJECT: Implementing Republic Act No. 8424, “ An Act Amending the National Internal Revenue Code, as amended” Relative to the Imposition of the Minimum Corporate Income Tax (MCIT) on Domestic Corporations and Resident Foreign Corporations

TO: All Internal Revenue Officers and Others Concerned

Pursuant to Section 244, in relation to Section 27(E) and Section 28(A)(2), these Regulations are hereby promulgated to govern the imposition of the minimum corporate income tax on domestic and resident foreign corporations.

Sec 2.27(E) MINIMUM CORPORATE INCOME TAX (MCIT) ON DOMESTIC CORPORATION-

(1) Imposition of the Tax- A minimum corporate income tax (MCIT) of two percent (2%) of the gross income as of the end of the taxable year (whether calendar or fiscal year, depending on the accounting period employed) is hereby imposed upon any domestic corporation beginning the fourth (4th) year immediately following the taxable year in which such corporation commenced its business operations. The MCIT shall be imposed whenever such corporation has zero or negative taxable income or whenever the amount of minimum corporate income tax is greater than the normal income tax due from such corporation.

For purposes of these Regulations, the term, “**normal income tax**” means the income tax rates prescribed under Sec. 27(A) and Sec. 28(A)(1) of the Code at 34% on January 1, 1998; 33% effective January 1, 1999; and at 32% effective January 1, 2000 and thereafter.

In the case of a domestic corporation whose operations or activities are partly covered by the regular income tax system and partly covered under a special income tax system, the MCIT shall apply on operations covered by the regular income tax system. For example, if a BOI-registered enterprise has a “registered” and an “unregistered” activity, the MCIT shall apply to the unregistered activity.

(2) Carry forward of excess minimum corporate income tax- Any excess of the minimum corporate income tax (MCIT) over the normal income tax as computed under Sec. 27(A) of the Code shall be carried forward on an annual basis and credited against the normal income tax for the three (3) immediately succeeding taxable years.

Illustration on how to carry forward excess minimum corporate income tax –

Year	Normal Income Tax	MCIT	Excess of MCIT Over the Normal Income Tax
1998	P50,000	P75,000	P25,000
1998 amount of tax payable		<u>P75,000</u>	
1999	P60,000	P100,000	P40,000
1999 amount of tax payable		<u>P100,000</u>	
2000	P100,000	P60,000	

Computation of Net Amount of Tax Payable in 2000:

Amount of tax payable		P100,000
Less:		
1998 excess MCIT	(25,000)	
1999 excess MCIT	<u>(40,000)</u>	<u>P65,000</u>
Net amount of tax payable		P35,000

The taxpayer shall pay the MCIT whenever it is greater than the regular or normal corporate income tax which is imposed under Sec. 27 (A) of the Code. The comparison between the normal income tax payable by the corporation and the MCIT shall be made at the end of the taxable year. Thus, under the example, the taxpayer will pay the MCIT of P75,000 since this amount is greater than the normal income tax of P50,000 in 1998.

In 1999, the firm will also pay the MCIT since the MCIT of P100,000.00 is greater than the normal income tax P60,000.

In the year 2000, where the normal or regular corporate income tax of P100,000.00 is greater than the MCIT of P60,000.00, the firm will pay the normal income tax.

The corporation can credit the excess of its MCIT over the normal income tax for 1998(i.e. P25,000) and 1999 (i.e. P40,000), or a total amount of P65,000 from the amount of normal income tax which is payable by the firm in the year 2000. Thus, the amount of income tax payable by the firm is P35,000 after deducting P65,000 from P100,000.

The excess MCIT is creditable against the normal income tax within the next three (3) years from payment thereof. Thus, in the illustration above where the corporation had an excess MCIT of P25,000 over its normal income tax in 1998, the and only when the normal income tax is greater than the MCIT. The excess MCIT cannot be claimed as a credit against the MCIT itself or against any other losses.

(3) Relief from the Minimum Corporate Income Tax under Certain Conditions – The Secretary of Finance, upon recommendation of the Commissioner, may suspend imposition of the MCIT upon submission of proof by the applicant-

corporation, duly verified by the Commissioner's authorized representative, that the corporation sustained substantial losses on account of a prolonged labor dispute or because of "force majeure" or because of legitimate business reverses.

(4) Definition of Terms

(a) **"Gross Income" defined** – For purposes of the minimum corporate income tax prescribed under this Subsection, the term **"gross income"** means gross sales less sales returns, discounts and allowances and cost of good sold. **"Gross sales"** shall include only sales contributory to income taxable under Sec. 27(A) of the Code. **"Cost of goods sold"** shall include all business expenses directly incurred to produce the merchandise to bring them to their present location and use.

Passive incomes which have been subject to a final tax at source shall not form part of gross income for purposes of the minimum corporate income tax.

For a trading or merchandising concern, **"cost of goods sold"** means the invoice cost of goods sold, plus import duties, freight in transporting the goods to the place where the goods are actually sold, including insurance while the goods are in transit.

For a manufacturing concern, **"cost of goods manufactured and sold"** means all costs of production of finished goods, such as raw materials used, direct labor and manufacturing overhead, freight cost, insurance premiums and other costs incurred to bring the raw materials to the factory or warehouse.

In the case of sales of services, the term **"gross income"** means gross receipt less sales returns, allowances, discounts and cost of services. **"Cost of services"** means all direct costs and expenses necessarily incurred to provide the services required by the customers and clients including (a) salaries and employee benefits of personnel, consultants and specialists directly rendering the service, and (b) cost of facilities directly utilized in providing the service such as depreciation or rental of equipment used and cost of supplies: Provided, however, that **"cost of services"** shall include interest expense except in the case of banks and other financial institutions. The term **"gross receipts"** as used herein means amounts actually or constructively received during the taxable year; Provided, that for taxpayers employing the accrual basis of accounting, the term **"gross receipts"** shall mean amount earned as gross income.

(b) The term **"substantial losses from a prolonged labor dispute"** means losses arising from a strike staged by the employees which lasted for more than six (6) months within a taxable period and which has caused the temporary shutdown of business operations.

(c) The term **"force majeure"** means a cause due to an irresistible force as by "Act of God" like lightning, earthquake, storm, flood and the like. This term shall also include armed conflicts like war or insurgency.

(d) The term **"legitimate business reverses"** shall include substantial losses sustained due to fire, robbery, theft or embezzlement, or for other economic reason as determined by the Secretary of Finance.

(5) Specific Rules for determining the Period When a Corporation Becomes Subject to the MCIT -

For purposes of the MCIT, the taxable year in which business operations commenced shall be the year in which the domestic corporation registered with the Bureau of Internal Revenue (BIR).

Firms which were registered with BIR in 1994 and earlier years shall be covered by the MCIT beginning January 1, 1998.

Firms which were registered with BIR in any months in 1998 shall be covered by the MCIT three calendar years thereafter (i.e. after the lapse of three calendar years from 1998). For example, a firm which was registered in May 1998 shall be covered by the MCIT in 2002.

The reckoning point for firms using the fiscal year shall also 1998. For example, a firm which registered with the BIR on July 1, 1998 shall be subject to an MCIT on his gross income earned for the entire fiscal year ending in the year 2002.

Transitory Rule for determining the MCIT for 1998 on firms which are taxable on a fiscal year basis. For firms using the fiscal year basis and whose first taxable period under the minimum corporate income tax covers month/months in 1997 shall be computed using an apportionment formula. The ratio to be applied is the number of months in 1998 to twelve (12) months (i.e. the total number of months in a fiscal year).

Illustration. Firm A registered with the BIR in July 1994. It becomes subject to the MCIT in 1998. Since it is using a fiscal year as basis of its taxable period, a part of the tax base for the MCIT was earned by the corporation in 1997 prior to the imposition of the MCIT (i.e. gross income from July to December 1997). The MCIT which is due from the firm is computed using the gross income of the form for 1998 (January to June) which is computed on an apportionment basis as follows:

Gross income of the firm for the entire fiscal year

Multiply: 0.50 (i.e. ratio of 6 months in 1998 to 12 months covering FY 97-98)

Equals: Tax base of the MCIT for 1998

Multiply; 2% (i.e. MCIT tax rate)

Equals: MCIT for 1998.

(6) Manner of filing and payment – The minimum corporate income tax (MCIT) shall be paid on a taxable year basis. It shall be covered by a tax return designed for the purpose which will be submitted together with the corporation's annual final adjustment income tax return. Domestic corporations shall not be required to pay the minimum corporate income tax on a quarterly basis, the provisions of Sec. 75 of the Code notwithstanding.

(7) Accounting treatment of the excess minimum corporate income tax paid – Any amount paid as excess minimum corporate income tax shall be recorded in the corporation’s books as an asset under account title “deferred charges-minimum corporate income tax”. This asset account shall be carried forward and may be credited against the succeeding the taxable year/s in which the same has been paid. Any amount of the excess minimum corporate income tax which has not or cannot be so credited against the normal income taxes due for the 3-year reglementary period shall lose its creditability. Such amount shall be removed from “deferred charges-minimum corporate income tax” account by a debit entry to “retained earnings” account and a credit entry to “deferred charges-minimum corporate income tax” account since this tax is not allowable as deduction from gross income it being an income tax.

Illustration on the accounting treatment of the excess minimum corporate income tax paid – Assume that ABC Corporation commenced business operations in calendar year 1991. It is already more than four (4) years in operation as of calendar year 1998 hence, subject to the minimum corporate income tax beginning taxable year 1998. Assume, further, that its income taxes during the years from 1998 to year 2005 are as follows:

YEAR	NORMAL INCOME TAX	MCIT	EXCESS OF MCIT OVER NORMAL INCOME TAX
1998	P 25,000	P100,000	P75,000
1999	130,000	150,000	20,000
2000	200,000	190,000	-
2001	-	300,000	300,000
2002	10,000	50,000	40,000
2003	15,000	60,000	45,000
2004	8,000	40,000	32,000
2005	1,000	50,000	49,000

In this case, ABC Corporation shall not be allowed to carry forward and credit the 1998 excess MCIT against the income tax liability for 1999 since the 1999 MCIT is greater than the normal income tax for said year. However, for year 2000, where the normal income tax is greater than the computed MCIT, ABC Corporation shall be allowed to apply the excess MCIT of 1998 and 1999 amounting to P95,000 (P75,000 plus P20,000) against the normal income tax liability of P200,000.

The excess MCIT for the year 2001 (P300,000) may only be credited against normal income tax liabilities for the succeeding three years from 2002 to 2004. However, since the normal income tax liabilities for these succeeding years are less than the respective MCITs, the excess MCIT for the year 2001 of P300,000 loses its creditability by the year 2005 hence, must be removed and deducted from the “Deferred charges – MCIT” account and be charged to “Retained Earnings” account.

Illustrative accounting entries to record excess MCIT –

(a) For taxable year 1998 when MCIT is greater than the normal income tax liability of the company

1998

- | | |
|---|----------|
| (1) Debit: Provision for income tax | P25,000 |
| Credit: Income tax payable | P25,000 |
| To record income tax liability using the normal income tax rate | |
| (2) Debit: Deferred Charges-MCIT | P75,000 |
| Credit: Income Tax payable | P75,000 |
| To record excess MCIT (P100,000 – 25,000) | |
| (3) Debit: Income Tax Payable | P100,000 |
| Credit: Cash in Bank | P100,000 |
| To record payment of income tax due for 1998 | |

(b) For taxable year 2000 when excess MCIT (1998 and 1999) is applied against normal income tax liability

2000

- | | |
|--|----------|
| (1) Debit: Provision for income tax | P200,000 |
| Credit: Income Tax Payable | P200,000 |
| To record income tax liability using the normal income tax rate | |
| (2) Debit: Income tax payable | P95,000 |
| Credit: Deferred Charges-MCIT | |
| (P75,000 plus P20,000) | P95,000 |
| To record application of excess MCIT against normal income tax liability for taxable year 2000 | |
| (3) Debit: Income Tax Payable | P105,000 |
| Credit: Cash in Bank | P105,000 |
| To record payment of income tax due (P200,000 less P95,000) | |

(c) For taxable year 2005 when the expired portion of excess MCIT (P300,000) for taxable year 2001 is closed to the retained earnings amount due to its non-application.

2005

- | | |
|--|----------|
| Debit: Retained Earnings | P300,000 |
| Credit: Deferred Charges-MCIT | P300,000 |
| To record the expired portion of Deferred Charges-MCIT | |

(8) Exceptions – The minimum corporate income tax (MCIT) shall apply only to domestic corporations subject to the normal corporate income tax prescribed under these Regulations. Accordingly, the minimum corporate income tax shall not be imposed upon any of the following:

(a) Domestic corporations operating as proprietary educational institutions subject to tax at ten percent (10%) on their taxable income; or

(b) Domestic corporations engaged in hospital operations which are nonprofit subject to tax at ten percent (10%) on their taxable income; and

(c) Domestic corporations engaged in business as depository banks under the expanded foreign currency deposit system, otherwise known as Foreign Currency Deposit Units (FCDUs), on their income from foreign currency transactions with local commercial banks, including branches of foreign banks, authorized by the Bangko Sentral ng Pilipinas (BSP) to transact business with foreign currency deposit system units and other depository banks under the foreign currency deposit system, including their interest income from foreign currency loans granted to residents of the Philippines under the expanded foreign currency deposit system, subject to final income tax at ten percent (10%) of such income.

(d) Firms that are taxed under a special income tax regime such as those in accordance with RA 7916 and 7227 (the PEZA law and the Bases Conversion Development Act, respectively).

Sec. 2,28(A)(2) MINIMUM CORPORATE INCOME TAX (MCIT) ON RESIDENT FOREIGN CORPORATION – A minimum corporate income tax of two percent (2%) of the gross income from sources within the Philippines is hereby imposed upon any resident foreign corporation, beginning on the fourth (4th) taxable year (whether following the taxable year in which the corporation commenced its business operations, whenever the amount of the minimum corporate income tax is greater than the normal income tax due for such year.

In computing for the minimum corporate income tax due from a resident foreign corporation, the rules prescribed under Sec. 2.27(E) of these Regulations shall apply: Provided, however, that only the gross income from sources within the Philippines shall be considered for such purposes.

Exceptions – The minimum corporate income tax shall only apply to resident foreign corporations which are subject to normal income tax. Accordingly, the minimum corporate income tax shall not apply to the following resident foreign corporations:

(a) Resident foreign corporations engaged in business as “international carrier” subject to tax at two and one-half percent (2 ½%) of their “Gross Philippine Billings”;

(b) Resident foreign corporations engaged in business as Offshore Banking Units (OBUs) on their income from foreign currency transactions with local commercial banks, including branches of foreign bank, authorized by the Bangko Sentral ng Pilipinas (BSP) to transact business with Offshore Banking Units (OBU’s), including interest income from foreign currency loans granted to residents of the Philippines, subject to a final income tax at ten percent (10%) of such income; and

(c) Resident foreign corporations engaged in business as regional operating headquarters subject to tax at ten percent (10%) of their taxable income.

(d) Firms that are taxed under a special income tax regime such as those in accordance with RA 7916 and 7227 (the PEZA law and the Bases Conversion Development Act, respectively).

EFFECTIVELY CLAUSE. These Regulations shall apply to domestic and resident foreign corporations on their aforementioned taxable income derived beginning January 1, 1998 pursuant to the pertinent provisions of RA 8424, provided, however, that corporations using the fiscal year accounting period and which are subject to MCIT on income derived pertaining to any month or months of the year 1998 shall not be imposed with penalties for late payment of the tax.

Edgardo B. Espiritu
Secretary of Finance

Recommending Approval:

Beethoven L. Rualo
Commissioner of Internal Revenue