

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

December 31, 2002

**REVENUE MEMORANDUM CIRCULAR NO. 4-2003**

**SUBJECT:** Clarifying Items That Would Constitute Gross Receipts and Costs in Determining “Gross Income” on Services for the Purpose of Computing the Minimum Corporate Income Tax (MCIT) Pursuant to Sections 27(E) and 28(A)(2) of the National Internal Revenue Code of 1997.

**TO :** All Internal Revenue Officers and Other Concerned

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This Circular is hereby issued to clarify what items should comprise gross receipts and corresponding cost of services for purposes of computing the gross income on sale of services which shall be the basis of the 2% Minimum Corporate Income Tax (MCIT) imposed under Section 27(E) and Section 28(A)(2) of the National Internal Revenue Code (NIRC) of 1997.

**Gross Receipts and Cost of Services Per Industry.** - For purposes of applying the MCIT, the ‘gross receipts’ and ‘cost of services’ of taxpayers engaged in the following types of services, or any other kind but of a similar nature, shall be determined as follows:

- (i) **Banks and non-bank financial intermediaries performing quasi-banking activities** pursuant to Sec. 22(V), (W), and (X) of the NIRC of 1997. Their gross receipts shall mean actual or constructive receipts from interests, commissions, and discounts from lending activities, and all other items treated as gross income under Section 32 of the NIRC of 1997 that are not subject to final withholding income tax. Their cost of services shall refer to those incurred directly and exclusively for the following activities:
01. Lending/investment of funds;
  02. Obtaining of funds from the public through the receipt of deposits; and,
  03. Trading of foreign exchange and other financial instruments.

and shall be limited to the following:

01. Salaries, wages and other employee benefits of personnel directly engaged in any of the said activities;
02. Interest expense except interest charged by or paid to the head office on funds considered/classified as *assigned capital* of the branch;
03. PDIC premium payments; and,
04. BSP supervision fee.

- (ii) **Insurance and pension funding companies** refer to those engaged in life and non-life insurance business as defined under the Insurance Code and pre-need companies, including health maintenance organizations. Their gross receipts shall mean actual or constructive receipts representing: net retained premiums (gross premiums net of returns, cancellations, and premiums ceded)/gross premium or collection from planholders; membership fees (in the case of HMOs); miscellaneous income; investment income not subject to final tax; *released reserve* and, in the case of pre-need companies, gross withdrawals from the trust funds set up independently as mandated by the Securities and Exchange Commission (SEC); and, all other items treated as gross income under Section 32 of the Tax Code. Their costs of services shall refer to those incurred directly and exclusively in the insurance and pre-need business, including the generation of investment income not subject to final taxes, and shall be limited to the following:
01. Salaries, wages and other employee benefits of personnel directly engaged in said activities;
  02. Commissions on direct writings/agents of pre-need companies;
  03. Claims, losses, maturities and benefits net of reinsurance recoveries; and,
  04. Net additions required by law to reserve fund (for insurance companies) and in the case of pre-need companies, contributions to the trust funds to be set up independently as mandated by the SEC.
- (iii) **Finance companies and other financial intermediaries not performing quasi-banking activities** refer to those engaged in the business of extending credit facilities to consumers and to industrial, commercial, or agricultural enterprises, including lending investors. Their gross receipts shall mean actual or constructive receipts representing interests, discounts, and all other items treated as gross income under Section 32 of the NIRC of 1997 that are not subject to final withholding income tax. Their costs of services shall refer to those incurred directly and exclusively in their lending, financing and generating of investment income not subject to final taxes, and shall be limited to the following:
01. Salaries, wages and other employee benefits of personnel directly doing such functions; and,
  02. Interest expense.
- (iv) **Brokers of securities (excluding banks).** Their gross receipts shall mean actual or constructive receipts for engaging in the business of effecting transactions in securities for the account of others. Their costs of services shall refer to those incurred directly and exclusively for such activity, and shall be limited to the following:

01. Salaries, wages and other employee benefits of personnel directly engaged in said activities;
02. Philippine Stock Exchange (PSE) terminal fees;
03. Communication charges related to trading/sales of securities;
04. Research fees such as access to Bloomberg and Reuters stock data;
05. Commissions paid to its agents who are not employees of the brokerage firm; and,
06. Settlement/processing costs of trades, commonly known as “exchange dues.”

(v) **Customs, insurance, real estate, immigration and commercial brokers.** Their gross receipts shall mean actual or constructive receipts in the form of brokerage fees, commissions and remuneration as such broker. Their costs of services shall refer to those incurred directly and exclusively for brokering activities, and shall be limited to the following:

01. Salaries, wages and other employee benefits of personnel directly engaged in brokering activities; and,
02. Commissions paid to its agents who are not employees of the brokerage firm.

(vi) **General engineering and/or building contractors** refer to those engaged in contracting business in connection with fixed works requiring specialized engineering knowledge and skill (e.g. reclamation works, railroads, highways, streets roads, tunnels, airports), or with any structure built, for the support, shelter and enclosure of persons, animals, chattels, or movable property of any kind, requiring in its construction the use of more than two unrelated building trades or crafts, or to do or superintend the whole or any part thereto (e.g. sewers and sewerage, disposal plants and systems, parks, playgrounds, refineries). Their gross receipts shall mean actual or constructive receipts representing the contract price, including the amount charged for materials supplied with the services. Their costs of services shall refer to those incurred directly and exclusively for such activities, and shall be limited to the following:

01. Cost of materials used in construction;
02. Salaries, wages and other employee benefits of site laborers and supervisors;
03. Health insurance, workers compensation and general liability insurance of site laborers and supervisors;
04. Fees and costs paid to sub-contractors;
05. Costs of performance bonds on the particular contract;
06. Depreciation/amortization, rentals, repairs and maintenance of equipment directly used in the said activities;

07. Costs of moving equipment and materials to and from the contract site;
08. Costs of design and technical assistance; and,
09. Supplies and tools directly used in the said activities.

(vii) **Common carriers or transportation contractors.** Their gross receipts shall mean actual or constructive receipts for engaging in the business of carrying or transporting passengers or goods or both, by land, water, or air, for compensation, offering their services to the public, including transportation contracting (e.g. operation of public utility buses, jeepneys, taxi-cabs and cars-for-rent). Their costs of services shall refer to those incurred directly and exclusively for such activities, and shall be limited to the following:

01. Salaries, wages and other employee benefits of personnel directly engaged in the operation of the transportation equipment;
02. Toll fees (representing rental for the use of road);
03. Parking fees (for aircraft, sea craft and motor vehicles);
04. Franchise fees (representing rental for the use of road network);
05. Depreciation/amortization, rentals, repairs and maintenance of:
  - Transportation equipment, and
  - Properties, building and improvements exclusively used as parking for aircrafts, sea crafts or motor vehicles;
06. Fuel and lubricants of motor vehicles, aircraft or sea craft directly used in transporting passengers and/or goods/cargoes;
07. Meals provided to passengers;
08. Cost of safety paraphernalia and other supplies for use by passengers (e.g. life jacket, mask, etc.); and,
09. Annual transportation equipment registration fee.

(viii) **Hotel, motel, rest/pension/lodging house and resort operators.** Their gross receipts shall mean actual or constructive receipts derived from the operation of such hotel, motel, rest/pension/lodging house, resort and other similar places. Their costs of services shall refer to those incurred directly and exclusively for providing rooms and other related facilities (e.g. hotel premises, kitchen, restaurants, recreational facilities, other spaces used by customers, but should not include office premises of administrative staff) for the enjoyment of customers, and shall be limited to the following:

01. Salaries, wages and other employee benefits of housekeeping staff, concierge personnel and other hotel/house/resort attendants;
02. Depreciation/amortization, rentals, repairs and maintenance of building, properties and facilities, and equipment directly used in the said activities;
03. Commissions paid to travel agents for bookings of guests for such establishments;
04. In case the operator also serves food and beverage, its direct costs shall include those allowed to food service establishments; and,
05. Supplies (e.g. hotel room/housekeeping, kitchen and laundry).

(ix) **Food service establishments.** Their gross receipts shall mean actual or constructive receipts derived from the operation of such restaurant, bars, cafes, clubs, caterers, other eating/drinking-places, as well as take-out counters. Their costs of services shall refer to those incurred directly and exclusively in the preparation and serving/selling of foods and drinks and other requirements of the customers, and shall be limited to the following:

01. Cost of raw/cooked foods and drinks prepared and served/sold;
02. Salaries, wages and other employee benefits of personnel directly engaged in the said activities;
03. Depreciation/amortization, rentals, repairs and maintenance of properties, buildings, furniture and fixtures, and equipment directly used in the performance of said activities;
04. Cost of cooking oil, condiments and other ingredients used in cooking the food; and
05. Royalties paid by franchisee.

(x) **Lessors of property.** Those engaged in the business of leasing out properties, such as real properties, equipment, and other movable properties. Their gross receipts shall mean actual or constructive receipts derived from such lease of properties. Their costs of services shall refer to those incurred directly and exclusively for the property leased, and shall be limited to the depreciation/amortization, rentals, real property taxes/charges, and repairs and maintenance, of the properties being leased, as well as salaries of employees and fees of contractors hired to provide maintenance (repairs, cleaning /maintenance of leased properties) and collection services.

(xi) **Telephone and telegraph, electric, gas, and water utilities.** Their gross receipts shall mean actual or constructive receipts derived from the operation of such systems/utilities covered by the law granting the franchise. Their costs of services shall refer to those incurred directly and exclusively for the production and delivery of such systems/utilities, and shall be limited to the following:

01. Salaries, wages and other employee benefits of personnel directly engaged in the said activities;
02. Depreciation/amortization, rentals, repairs and maintenance of properties and equipment directly used in the said activities (i.e., water pipes, electric poles, antennas, etc.);
03. Interconnection fee and/or share of foreign telecommunications administration (FA) for the services they perform;
04. Fuel and lubricants on vehicles or equipment directly utilized in the said activities;
05. Amortization of franchise or development fees;
06. Franchise fees; and,
07. Royalties.

(xii) **Radio and/or television broadcasting.** Their gross receipts shall mean actual or constructive receipts derived from the operation of such radio/television broadcasting covered by the law granting the franchise. Their costs of services shall refer to those incurred directly and exclusively for such production and broadcasting, and shall be limited to the following:

01. Fees of talents hired for production/broadcasting;
02. Salaries, wages and other employee benefits of production and broadcasting personnel;
03. Tapes and other production materials & supplies;
04. Satellite charges & wire services;
05. Film rights royalties & dubbing expenses;
06. Set requirements;
07. Rentals for production equipment & facilities;
08. Rentals for locations used exclusively for production/broadcasting;
09. Costumes, props & prizes; and,
10. Depreciation on production and broadcasting equipment.

The term '*salaries, wages and other employee benefits*' as used herein shall include the following employee benefits: bonuses, Pag-ibig, SSS, Medicare, and HDMF Contributions. If a cost or expenditure is incurred both directly to provide a service required by a client, and indirectly for administration, operation, or sales-promotion purposes, the taxpayer shall be allowed a ratable portion of such cost or expenditure to form part of the "Cost of Services."

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

(Original Signed)  
**GUILLERMO L. PARAYNO, JR.**  
Commissioner of Internal Revenue

