

[BIR REVENUE MEMORANDUM CIRCULAR NO. 30-2008, April 01, 2008]

CLARIFYING THE TAXABILITY OF INSURANCE COMPANIES FOR MCIT, BUSINESS TAX, AND DOCUMENTARY STAMP TAX PURPOSES

The primary and predominant business activity of an insurance company is the writing of insurance or the reinsuring of risks underwritten by insurance companies which are subject to the supervision by the Insurance Commission.

Section 2 of Presidential Decree No. 612 (PD 612), otherwise known as the "The Insurance Code" defines the term "doing an insurance business" or "transacting an insurance business" to include: "(a) making or proposing to make, as insurer, any insurance contract; (b) making or proposing to make, as surety, any contract of suretyship as a vocation and not as merely incidental to any other legitimate business or activity of the surety; (c) doing any kind of business, including a reinsurance business, specifically recognized as constituting the doing of an insurance business within the meaning of this Code; (d) doing or proposing to do any business in substance equivalent to any of the foregoing in a manner designed to evade the provisions of this Code. X x x"

In proposing to indemnify another against any loss, damage or liability arising from an unknown or contingent event through the issuance of insurance policies, these companies engaged in the insurance business receive, as consideration for the services rendered, "premium" payment from the insured/policyholder.

The insurance business may pertain to life insurance or non- life insurance business.

Life insurance company is a company which deals with the insurance on human and insurance appertaining thereto or connected therewith. The service likewise includes soliciting group insurance, and health and accident insurance policies which the company is nevertheless authorized to pursue as part of its business activity. Group insurance is essentially a single insurance contract that provides coverage for many individual In its original and most common form, group insurance provides life or health insurance coverage for the employees of one employer. In an accident insurance, the insured's F-neficiary has the burden of proof in demonstrating that the cause of death is due to the covered peril. Once the fact is established, the burden then shifts to the insurer to show any excepted peril that may have been stipulated by the parties. An accident insurance js not thus to be likened to an ordinary life insurance where the insured's death, regardless of the cause thereof, would normally be compensable.

Non-life insurance company, on the other hand, is one which solicits insurance on the security of property such as: marine, fire and casualty insurance companies; surety fidelity, indemnity and bonding companies; and such other persons as may

be authorized by the Insurance Commission.

Determination of the Minimum Corporate Income Tax For Life and Non-Life Insurance Companies. - For purposes of computing the gross income on the 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 1997 National Internal Revenue Code (Tax Code), as amended, of life and non- life insurance companies, their gross revenue shall include direct premium and reinsurance assumed (net of returns, cancellations); miscellaneous income; investment income not subject to final tax; released reserve; and, all other items treated as gross income under Section 32 of the said Tax Code, as amended.

Their costs of services or direct cost and identifiable direct revenue-related deductions shall refer to those incurred costs which are exclusively related or otherwise considered indispensable to the creation of the revenue from their business activity as an insurance company, including the generation of investment income not subject to final taxes, and shall be limited to the following:

01. Claims, losses, maturities and benefits net of reinsurance recoveries;
02. Additions required by law to reserve fund; and
03. Reinsurance ceded.

Taxability of the Various Business Activities of Life Insurance Company for Business Tax and Documentary Stamp Tax. -

(a) Business Tax. - While it may be said that the core revenue source of a life insurance company is the generation of premiums from undertaking life insurance contracts, its business undertakings have slowly evolved and expanded through the years such that aside from the premiums earned from its main activity, its other ancillary services have likewise brought forth other types of revenue like rental income, management fee, interest income, other investment income, renewal and/or re-issuance fees, reinstatement fees, penalties and the like.

With regard to these types of income, the business tax (i.e., whether premium tax, VAT or Gross Receipts Tax) to be imposed will depend on the nature of the activity pursued by the life insurance company in producing such type of income.

(1) Direct Writings/Premiums-Generally, for the premiums received by a life insurance company in undertaking its insurance activities, the same are subject to premium tax at the rate of five percent (5%) on its direct writings/premiums pursuant to Section 123 of the Tax Code, as amended, to wit:

"SEC. 123. Tax on Life Insurance Premiums. — There shall be collected from every person, company or corporation (except purely cooperative companies or associations) doing life insurance business of any sort in the Philip-nines a tax of five percent (5%) of the total premium collected, whether such premiums are paid in money, notes, credits or any substitute for money; but premiums refunded within six (6) months after payment on account of rejection of risk or returned for other reason to a person insured shall not be included in the taxable receipts; nor shall any tax be paid upon reinsurance by a company that has already paid the

tax; nor upon premiums collected or received by any branch of a domestic corporation, firm or association doing business outside the Philippines on account of any life insurance of the insured who is a nonresident, if any tax on such premium is imposed by the foreign country where the branch is established nor upon premiums collected or received on account of any reinsurance, if the insured, in case of personal insurance, resides outside the Philippines, if any tax on such premiums is imposed by the foreign country where the original insurance has been issued or perfected; nor upon that portion of the premiums collected or received by the insurance companies on variable contracts [as defined in Section 232(2) of Presidential Decree No. 612], in excess of the amounts necessary to insure the lives of the variable contract owners.

" Xxxxxx xxx"

Re- insurance fees, reinstatement fees, renewal fees as well as penalties paid to the life insurance company which are incidental to or in connection with the insurance policy contracts issued are considered akin to premiums, thus, such types of income are also covered by the above-quoted provision of Section 123, subject to the 5% premium tax for the gross amount received on such fees and/or penalties

(2) Management Fees, Rental Income, or Other Income from Unrelated Services - Management fees, rental income, or any other income earned by the life insurance company from services which can be pursued independently - of the insurance business activity, are thus not subject to the 5% premium tax imposed under Section 123 above but, rather, the same are treated as income for services that are subject to the imposition of VAT pursuant to Section 108 of the Tax Code, as amended, or to the percentage tax imposed under Section 116 of the same Tax Code, as the case may be.

(3) Investment Income-

(3.a) Investment Income Realized from the Investment of Premiums Earned, - income realized from investment activities utilizing the premiums earned by the life insurance company from its policyholders is considered merely a part of, incidental to and is necessary to its main business of contracting insurance services.

Such investment income is considered exempt from the further imposition of business tax since the premiums, which have been the source of the funds invested had already been subjected to the imposition of the 5% premium tax pursuant to Section 123 of the Tax Code, as amended.

(3.b) Investment Income Realized from the Investment of Funds Obtained from Others. - The income earned by the life insurance company whereby it uses the funds solicited and pooled from its policyholders to invest in various marketable securities, instruments, and other financial products, which funds are recognized as liabilities by the life insurance company and which can be withdrawn by the policyholders

anytime, is considered as an income earned from performing a quasi-banking function, thus, subject to the gross receipts tax imposed under Section 121 of the Tax Code, as amended.

(3.c) Manner of Apportionment to Determine Exempt Investment Income and Investment Income Subject to Gross Receipts Tax-As has been discussed above, investment income that is exempt from the imposition of business tax only pertains to that portion of investment income where the source of the funds used in the investment activities comes from the owned funds (i.e., premiums earned) of the life insurance company.

For that portion of investment income whereby the source of the funds used was solicited from the policyholders for purposes other than the payment of the current premiums due to the life insurance company and where such funds solicited are treated by the life insurance company as liabilities, such income is considered to have been earned from performing quasi-banking function, and therefore, subject to the imposition of gross receipts tax pursuant to Section 121 of the Tax Code, as amended.

In order to determine which portion of the investment income earned for the month is exempt and which portion is taxable, the investment income earned for the month shall be allocated between the following:

(i) liability account balance pertinent the other funds solicited from the policyholders as of the end of such month; and

(ii) the total premiums earned for the month. Exempt/Non Taxable Investment Income

= Investment x
for the month

Item (ii) above

Sum of items (i) and (ii)
above

Investment Income Subject to Gross
Receipts Tax

= Investment Income x
for the month

Item (i) above

Sum of items (i) & (ii)
above

Example: "Akim Life Assurance Corp.", a life insurance company, during the month of April, realized an investment income amounting to P1,000,000. The investment funds used in generating this income come from both the premiums earned by the company and the other funds solicited from its policyholders.

For the same month, the premiums earned by the company amounted to P30,000,000 while the liability balance of the end of the said month pertinent to the other funds solicited amounted to P20,000,000.

The exempt portion of the investment income and the portion to be subject to the

gross receipts tax are determined as follows:

Exempt = P1,000,000 x P30,000,000

= P600,000

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Taxable for Gross Receipts Tax = P1, 000,000 x P20, 000,000

P50,000,000

=P400,000

(b) Documentary Stamp Tax. - With respect to life insurance policies issued by the life insurance company, the same is subject to documentary stamp tax pursuant to Section 183 of the Tax Code, as amended, as quoted hereunder:

"SEC. 183. Stamp Tax on Life Insurance Policies. — *On all policies of insurance or other instruments by whatever name the same may be called, whereby any insurance shall be made or renewed upon any life or lives, there shall be collected a documentary stamp tax of Fifty centavos (P0.50) on each Two hundred pesos (P200), or fractional part thereof, of the amount of premium collected.*

For certificates issued, documentary stamp tax is imposed as follows;

SEC. 188. Stamp Tax on Certificates. — *On each certificate of damage or otherwise, and on every other certificate or document issued by any customs officer, marine surveyor, or other person acting as such, and on each certificate issued by a notary public, and on each certificate of any description required by law or by rules or regulations of a public office, or which is issued for the purpose of giving information, or establishing proof of a fact, and not other-wise specified herein, there shall be collected a documentary stamp tax of Fifteen pesos (P15.00).*

For group insurance policies issued, the premium collected therefrom shall be subject to Section 183 above. For the individual certificates issued to each and every em-P'oyee covered by the group insurance policy, the issuance of such certificate shall be subject to Section 188 above.

However, with regard to health and accident insurance coverage provided, the basis or the payment of documentary stamp tax shall be the provision prescribed by Section 185 of the same Tax Code, viz:

"SEC. 185. Stamp Tax on Fidelity Bonds and Other Insurance Policies.

— *On all policies of insurance or bonds or obligations of the nature of indemnity for loss, damage or liability made or renewed by any person, association, company or corporation transacting the business of accident, fidelity, employer's liability, plate, glass, steam boiler, burglar, elevator, automatic sprinkler, or other branch of insurance (except life, marine, inland, and fire insurance), and all bonds, undertakings, or recognizances, conditioned for the performance of the duties of any office or position, for the doing or not doing of anything therein specified, and*