CLARIFYING THE SCOPE OF THE TERM “DIRECT COSTS AND EXPENSES” THAT SHOULD COMPRISE THE “COST OF SERVICES” FOR PURPOSES OF COMPUTING THE GROSS INCOME SUBJECT TO THE 2% MINIMUM COR...

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As provided for by Section 27(E) and Section 28(A)(2) of the 1997 Tax Code, as amended, in computing the gross income subject to the 2% MCIT for sellers of services, y “gross income' means gross receipts less sales returns, allowances, discounts and cost of services. 'Cost of services' shall mean 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 as depreciation or rental of equipment used and cost of supplies: xxx xxx xxx”

As can be gleaned from the above definition of "cost of services" of the sellers of services, "direct costs and expenses" shall only pertain to those costs exclusively and directly incurred in relation to the revenue realized by the sellers of services, in fine, these refer to costs which are considered indispensable to the earning of the revenue such that without such costs, no revenue can be generated.

Thus, expenses and other costs dispensed outside the ambit of what has been defined herein as "direct costs and expenses" are not items allowed for inclusion to "cost of services", for purposes of computing the gross income subject to the 2% MCIT.

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

Adopted: 18 March 2008

(SGD.) LILIAN B. HEFTI
Commissioner of Internal Revenue

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