

Taiwan CFC Rules

Taiwan's Controlled Foreign Corporation ("CFC") rules became effective on 1 January 2023.

CFC stands for controlled foreign corporation. In order to better protect Taiwan's tax base and align with international tax trends, Taiwan introduced CFC rules effective from 1 January 2023 to curb tax leakage arising from complex international tax planning structures.

Definition of CFC

A foreign enterprise registered in a low-tax-burden country or jurisdiction will be deemed a CFC if more than 50% of its paid-in capital is owned, directly or indirectly, by a Taiwan tax resident individual together with related parties, or by a Taiwan profit-seeking enterprise together with its related parties.

Even if the ownership percentage is less than 50%, a foreign enterprise will still be deemed a CFC if it is effectively controlled by a Taiwan tax resident individual together with related parties, or by a Taiwan profit-seeking enterprise together with its related parties, directly or indirectly.

Low-tax burden country or jurisdiction

A low-tax-burden country or jurisdiction refers to any jurisdiction meeting one of the following criteria:

- The corporate income tax rate in the foreign country or jurisdiction is no more than 70% of Taiwan's corporate income tax rate (i.e., $20\% \times 70\% = 14\%$).

The Ministry of Finance ("MOF") has published a list of jurisdictions meeting this criterion (Appendix 1).

- The foreign country or jurisdiction adopts a territorial tax system, meaning it does not tax offshore-source income, or taxes such income only upon remittance.

The MOF has published a list of jurisdictions meeting this criterion (Appendix 2).

Definition of Related Parties

The definition of related parties is broad. Further details are set out in Article 3 of the Regulations Governing the Application of Accrued Income from Controlled Foreign Companies for Profit-Seeking Enterprises.

Scope

Article 43-3 of the Income Tax Act requires profit-seeking enterprises to include profits earned by CFCs when computing taxable income for the year. However, for purposes of computing interim corporate income tax payable, CFC income is not required to be included (Tax Ruling No. 11204543460).

Any foreign corporation meeting the definition of a CFC under the above rules is subject to

inclusion. Where both the CFC rules and Place of Effective Management ("PEM") rules apply, the PEM rules take precedence over the CFC rules.

Please note that a substance-over-form principle applies. Accordingly, shares held through nominees or similar arrangements must be taken into account when determining CFC ownership and control.

General Exemption

CFC rules do not apply if the CFC conducts substantial operating activities.

This requires that the CFC maintain a fixed place of business in its jurisdiction of registration and employ personnel who carry out substantive business operations locally. In addition, passive income (such as rental income, royalties, and interest) must account for less than 10% of the sum of operating income and non-operating income.

As noted above, where income has already been recognized under the PEM rules, the same income is not required to be reported again under the CFC rules.

Tax Computation (Individual)

CFC income is computed as follows:

CFC income = Income earned by the CFC for the year – required legal reserve – prior-year losses

Taxable CFC income is calculated based on the actual ownership percentage and the weighted average holding period.

If the total computed CFC income for a tax-filing household is less than TWD 1 million, reporting is not required.

If the current year's earnings of a single CFC are less than TWD 7 million, reporting is not required. However, where a tax-filing household holds multiple CFCs and the aggregate CFC income

exceeds TWD 7 million, the full amount must be reported.

Treatment of CFC Losses

Computed CFC losses may be carried forward for up to 10 years, provided that:

- the losses arise in or after tax year 2023, i.e., after the CFC regime became effective;
- the relevant supporting documentation (including CFC financial statements) has been duly prepared and audited by a CPA; and
- such losses have been reported and recognized by the competent tax authority.

Such losses may only be used to offset CFC income derived from the same invested entity.

Where accumulated losses of a CFC are offset against paid-in capital, the offset losses may not be carried forward for CFC loss reserve purposes.

CFC income is subject to taxation only once. It is not required to be reported again upon dividend distribution unless the amount distributed exceeds the CFC income previously reported.

For capital gains arising from the disposal of CFC shares, taxable income is computed as follows:

Taxable capital gain = Selling price – cost of shares – residual CFC income previously reported × disposal percentage

CFC income earned by individuals is subject to Alternative Minimum Tax ("AMT") computation.

Tax Computation (Profit Seeking Enterprise)

CFC income is computed as follows:

CFC income = Income earned for the year - required legal reserve – losses from prior years

Taxable CFC income is calculated based on the actual ownership percentage and the weighted average holding period.

If the current-year earnings of a CFC are less than TWD 7 million, reporting is not required.

However, where multiple CFCs are held and the aggregate CFC income exceeds TWD 7 million, the full amount must be reported.

Treatment of CFC Losses

Computed CFC losses may be carried forward for up to 10 years, provided that the losses arise after the implementation of the CFC regime, are properly documented, and have been audited and recognized by the competent tax authority.

Such losses may only be used to offset CFC income derived from the same invested entity.

Losses accumulated by a CFC prior to tax year 2023 may not be carried forward or deducted against CFC income recognized under the CFC regime.

Where accumulated losses of a CFC are offset against paid-in capital, the offset losses may not be carried forward in the CFC loss reserve computation.

Computed CFC income is subject to taxation only once and is not required to be reported again in the year of dividend distribution unless the amount distributed exceeds the CFC income previously reported.

For capital gains arising from the disposal of CFC shares, taxable income is computed as follows:

Taxable capital gain = Selling price – cost of shares – residual CFC income previously reported
× disposal percentage

Implications of Non-Compliance

Under Article 41 of the Tax Collection Act:

A taxpayer who evades tax payment by fraud or other unrighteous means shall be sentenced to imprisonment for no more than five (5) years, and shall be subject to a fine of no more than ten million New Taiwan Dollars (NT\$10,000,000).

A taxpayer committing an offense as described in the preceding paragraph, and the tax evasion amount is over ten million New Taiwan Dollars (NT\$10,000,000) for an individual or over fifty million New Taiwan Dollars (NT\$50,000,000) for a profit-seeking enterprise, shall be sentenced to imprisonment of not less than one year but not more than seven years, and shall be subject to a fine of not less than ten million (NT\$10,000,000) but not more than one hundred million New Taiwan Dollars (NT\$100,000,000).

Our Approach

Historically, tax haven entities have often been used as part of international tax planning structures. With the introduction of the CFC rules, existing group structures may no longer be tax efficient or compliant.

We assist clients in evaluating whether their current group structures remain appropriate in light of the CFC regime. If you have any questions or concerns, please do not hesitate to contact any member of our tax team.

Contact



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Appendix 1 – Countries with Corporate income tax rates lower than 70% of Taiwan’s income tax rate

- Anguilla
- Barbados
- Bermuda
- Bonaire, Sint Eustatius and Saba
- Bosnia and Herzegovina
- British Virgin Islands
- Cayman Islands
- Commonwealth of The Bahamas
- Democratic Republic of Timor-Leste
- Guernsey
- Hungary
- Isle of Man
- Jersey
- Kingdom of Bahrain
- Kyrgyz Republic
- Macao
- Principality of Andorra
- Principality of Liechtenstein
- Republic of Bulgaria
- Republic of Cyprus
- Republic of Kosovo
- Republic of Moldova
- Republic of North Macedonia
- Republic of Palau
- Republic of Paraguay
- Republic of the Marshall Islands
- Republic of Vanuatu
- State of Qatar
- Turks and Caicos Islands

Appendix 2 - Foreign countries/jurisdictions that impose taxes on a territorial basis

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- Belize
- Brunei Darussalam
- Curaçao
- Democratic Republic of the Congo
- Federated States of Micronesia
- French Guiana
- French Polynesia
- French Republic
- French Southern Territories
- Georgia
- Gibraltar
- Guadeloupe
- Hong Kong
- Kingdom of Eswatini
- Malaysia
- Martinique
- Mayotte
- New Caledonia
- Oriental Republic of Uruguay
- Palestine
- Plurinational State of Bolivia
- Principality of Monaco
- Republic of Botswana
- Republic of Chad
- Republic of Costa Rica
- Republic of Djibouti
- Republic of El Salvador
- Republic of Guatemala
- Republic of Guinea-Bissau
- Republic of Honduras
- Republic of Kenya
- Republic of Malawi
- Republic of Namibia
- Republic of Nauru
- Republic of Nicaragua
- Republic of Niger
- Republic of Panama
- Republic of Seychelles
- Republic of Singapore
- Reunion
- Saint Barthelemy
- Saint Martin (French Part)
- Saint Pierre and Miquelon
- State of Eritrea
- State of Kuwait
- State of Libya
- Syrian Arab Republic
- Tuvalu
- United Arab Emirates
- Wallis and Futuna
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