

Applying a Cost-Plus Approach for Foreign Enterprises in Taiwan

Understanding Taiwan's Transfer Pricing and Tax Compliance Considerations

Many foreign enterprises operating in Taiwan through a local subsidiary or branch adopt a cost-plus approach to determine the Taiwan entity's remuneration. Under this model, the Taiwan company typically provides support, maintenance, or business services to the foreign parent or affiliated company, while the foreign entity sells goods directly to Taiwanese customers and ships from abroad.

1. Common Business Models

Foreign enterprises frequently use one or more of the following arrangements:

1. Support and maintenance services – The Taiwan entity provides after-sales support, installation, maintenance, or technical assistance to Taiwanese customers on behalf of the foreign parent. The foreign parent sells the goods and recognizes the sales revenue.
2. Business services – The Taiwan entity provides marketing, sales promotion, customer liaison, or administrative services to the foreign group. The foreign entity invoices Taiwanese customers and ships the goods directly.
3. Direct shipment with local support – The foreign entity contracts with Taiwanese customers and ships goods from overseas, while the Taiwan entity provides local support functions without taking title to the goods.

In these models, the Taiwan entity generally does not recognize the full sales margin. Instead, it is remunerated on a cost-plus basis, reflecting the service or support functions it performs.

2. Why a Cost-Plus Approach?

A cost-plus approach is often appropriate where the Taiwan entity:

- Performs routine or support functions;
- Does not control significant risks (e.g., inventory risk, credit risk, or market risk);
- Does not own valuable intangibles; and
- Is not the principal in the transaction.

Under this approach, the Taiwan entity's taxable income is generally determined by applying a mark-up to its relevant costs. The mark-up should be arm's length and supported by a transfer pricing report, benchmarking analysis, or comparable uncontrolled transactions.

Other remuneration methods, such as commission-based or hourly-rate arrangements, may also be used. Each method has its own advantages and disadvantages. However, the cost-plus method is generally regarded as the simplest and easiest to administer and manage.

3. Key Tax Considerations

3.1 Transfer Pricing Documentation

Taiwan's transfer pricing regulations require related-party transactions to be conducted on arm's length terms. Companies meeting certain thresholds must prepare a transfer pricing report. Even where not strictly required, maintaining contemporaneous documentation is prudent and can reduce tax risk.

3.2 Corporate Income Tax

The Taiwan entity's profits is subject to Taiwan corporate income tax at 20%.

4. Practical Implementation Points

When implementing a cost-plus model, foreign enterprises should consider the following:

- Define the services clearly – The scope of services, deliverables, and responsibilities of the Taiwan entity should be documented in an intercompany agreement.
- Determine the cost base – Identify which costs are eligible for mark-up, and ensure they are consistent with the functions performed.
- Select an appropriate mark-up – The mark-up should be supported by benchmarking or comparable data.
- Maintain documentation – Keep contracts, invoices, transfer pricing reports, and supporting calculations.
- Review regularly – Business models and intercompany arrangements should be reviewed periodically to reflect changes in functions, risks, and market conditions.

5. How Grant Thornton Taiwan Can Help

Grant Thornton Taiwan has extensive experience assisting foreign enterprises with:

- Designing and documenting cost-plus arrangements;
- Preparing transfer pricing reports and benchmarking analyses;
- Applying for advance rulings under Article 25 and Article 4;
- Assessing permanent establishment risk;
- Advising on withholding tax and compliance obligations; and
- Coordinating with the tax authorities on behalf of clients.

Our team works closely with foreign parent companies, Taiwan subsidiaries, and local advisers to ensure that intercompany arrangements are commercially reasonable, tax-efficient, and defensible on audit.

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