



Taiwan Source Income Defined

Taiwan's Ministry of Finance released an important tax ruling relating to source of income on September 3, 2009 (TaiTsaiSui 09804900430). This article summarizes the content of that ruling.

Background

Taiwan's tax office has been notorious for arguing that just about all payments made by Taiwan entities for services purchased from overseas profit-seeking enterprises are deemed to be Taiwan source income (with a few clearly-defined exceptions). Taiwan's court system generally upholds the views of the tax office. This has resulted in many foreign profit-seeking enterprises being taxed in Taiwan on fees derived from services they performed outside of Taiwan.

Taiwan's Ministry of Finance, recognizing the "source of income" controversy, issued a ruling on September 3, 2009 in order to better regulate the matter.

Summary of the new tax ruling TaiTsaiSui 09804900430:

1. Remuneration for services rendered within the territory of the Republic of China is deemed to be Taiwan source income if any one of the following conditions applies:
 - 1) All services are carried out and completed within the Republic of China.
 - 2) Part of the services are carried out within Republic of China, and part of the services are carried out outside the Republic of China.
 - 3) Although the services are carried out abroad, there is involvement from an individual

or profit-seeking enterprise within the Republic of China to help complete the assignment (e.g. to provide equipment, manpower, technical knowhow or technical resources).

For items 2) and 3) above, if the taxpayer is able to provide proof and supporting documents (such as a CPA-signed audit report, transfer pricing document, work plan, job record or similar document) that show that the profits attributable to those activities carried out in Taiwan can be split out from the overall profits, then the tax officer may elect to assess tax only on profits attributable to Taiwan.

2. Remuneration received by a foreign enterprise for services rendered fully and completely outside the territory of the Republic of China can be deemed to be foreign source income if any one of the following conditions applies:

- 1) The foreign enterprise has no fixed place of business and no business agent in the Republic of China.
- 2) The foreign enterprise has an agent in the Republic of China, but the agent did not act as an agent for the services concerned.
- 3) The foreign enterprise has a fixed place of business in the Republic of China, but the fixed place of business did not participate in the services concerned.



3. Joint research program

In the case of a joint international research project carried out by a Taiwan entity together with other international organizations, payment for the Taiwan entity's share of the research costs can be deemed to be non-Taiwan source income if all of the following conditions can be met:

- Any intellectual property right derived from the project is shared jointly with all the parties involved.
- Payments made by the Taiwan entity are limited to Taiwan's share of the allocated costs.
- The project is likely to result in reasonable benefits for the Taiwan entity.
- There is no royalty payment or other scheme involved to evade income tax.

4. Profits from operation of industry, commerce, agriculture, forestry, fishery, animal husbandry, mining, and metallurgy enterprises within the territory of the Republic of China.

In the case that activities are carried out both in Taiwan's territory and overseas, if a foreign profit-seeking enterprise is able to provide proof and records (such as a CPA-signed audit report, transfer pricing document, work plan, job record or similar document) to show that profits attributable to those activities carried out in Taiwan can be split out from the overall profits, then the tax officer may elect to assess tax only on profits attributable to activities carried out in Taiwan.

If all activities are conducted outside of Taiwan, income earned can be deemed to be foreign source income if any one of the following conditions applies:

- 1) The foreign enterprise has no fixed place of business and no business agent in the Republic of China.
- 2) The foreign enterprise has an agent in the Republic of China, but the agent did not act as the agent for the activities concerned.
- 3) The foreign enterprise has a fixed place of business in the Republic of China, but the fixed place of business did not participate in the activities concerned.

5. Companies and individuals from Mainland China

Companies and individuals from Mainland China having Taiwan source income can also enjoy the benefits listed above.

Comments

Grant Thornton Taiwan welcomes the new tax ruling and believes that the ruling will provide better guidance to profit-seeking enterprises dealing with the "source of income" issue. However, the ruling still leaves room for debate in certain areas. These include:

- It may be difficult for taxpayers to prove, to the satisfaction of tax officers, that all services were performed outside of Taiwan.
- It may be difficult for taxpayers to prove, to the satisfaction of tax officers, that profits attributable to the activities carried out in Taiwan have been split out and computed fairly, given that accounting records and vouchers are kept overseas.

It is important to note that, in addition to the tax ruling explained above, other practical solutions can also be used to address withholding tax issues. These include the S4 full income tax exemption application, the S25 advance ruling application for withholding tax reduction or simply relying on a tax treaty (where applicable) to enjoy lower withholding tax. If in doubt as to which route to take to best address tax planning, please do not hesitate to contact personnel in our tax division.

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