

1. Ineligibility of Chinese companies for 3.75% withholding tax rate
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Introduction

The committee recognizes the efforts of the Taiwan government, especially the amendments to the Taiwan Income Tax Act as these address the following issues raised in the 2008-2009 position paper:

- **Loss Carry Forward (LCF) period:**

The LCF period has been extended from 5 years to 10 years.

- **Reduction of the corporate**

income tax rate: Effective from January 1, 2010, a unitary corporate income tax rate of 20% will be applied.

- **Reduction of personal income**

tax rates: The progressive personal income tax rates of 6%, 13%, and 21% have been reduced by 1 percentage point to 5%, 12%, and 20% respectively, while no changes were made to the 30% and 40% rates.

Also, the government has taken initiatives to address the following issues which have been raised in previous position papers:

- **Interpretation of Taiwan sourced service income and the basis of imposing withholding tax:**

The Ministry of Finance (MoF) is revisiting its position on this issue by introducing the "Principle for Determining Taiwan Sourced

Income under Article 8 of the Taiwan Income Tax Act".

- **Alternative Minimum Tax (AMT) treatment of overseas securities gains:** Although our recommendation made in the 2008-2009 position paper has not been adopted, the MoF is introducing guidelines on the treatment of overseas income under AMT rules.

While progress has been made, issues regarding outdated tax deduction's limits for entertainment expenses, personal income tax paid on expatriate's behalf by the employer, and tax administration efficiency remain unresolved. Although these issues are not repeated this year, we hope to see the government working continuously to resolve these outstanding issues. The committee remains concerned about the deductibility of offshore insurance premiums paid abroad and therefore repeat this issue in this year's position paper, together with several new issues.

1. Ineligibility of Chinese companies for 3.75% withholding tax rate

This issue is being raised for the first time by this committee. Based on relevant tax regulations, the government specifically precludes Chinese companies from being eligible for the 3.75% withholding tax rate (deemed profit

rule) provided under Article 25 of the Taiwan Income Tax Act. This rule is applicable to profit-seeking enterprises whose headquarters are located outside the territories of the Republic of China that engage in the provision of technical services, among other things, in the territories of the Republic of China.

To a Taiwanese company that obtains technical services from a Chinese company, from a commercial perspective, the arrangement is in substance no different from those made with other companies located in other countries. However, without the opportunity to seek a reduced withholding tax rate, the withholding tax costs for obtaining such services from Chinese companies would be higher.

RECOMMENDATION

The government has recently enacted Article 12-1 of the Tax Collection Act, which provides that "interpretations of laws involving tax matters should be made based on the spirit of statutory taxation doctrine and should consider the economic meaning and the equality principle behind substance-over-form taxation in light of the legislative purpose of the respective law." Following the spirit and content of this new law, we recommend that the government remove the preclusion on Chinese companies' eligibility for the 3.75% withholding tax rate.

2. Deductibility of insurance premiums paid to foreign insurance companies

In last year's position paper, we voiced the concern that many multinational

corporations (MNCs) in Taiwan find it difficult to claim deductions for insurance premiums paid to offshore insurance companies due to the pre-approval requirement provided under Article 83 Subparagraph 6 of the Income Tax Assessment Rules for Profit-Seeking Enterprises. Pursuant to the said article, for the purpose of seeking pre-approval, MNCs need to prove that either the same type of insurance is not available in Taiwan or special circumstances exist that require them to seek insurance from offshore insurers.

According to an old ruling no. 770044898, dated 22 March 1988, the legislative intent of the strict deduction rules is to keep insurance business inside Taiwan. This legislative intent does not promote equality between local insurers and offshore insurers and thus may be in contravention of the WTO's mission of non-discriminatory treatment and the opening of national markets to international trade.

Moreover, according to the deduction rules, pre-approval from the Financial Supervisory Commission (FSC) needs to be obtained in order to claim deductions for offshore insurance expenses. As indicated by the cumbersome procedures set forth below, such pre-approval is practically impossible to obtain.

1. MNCs need to conduct a screening process to:

- Identify local insurers who offer the same type of insurance through website research (e.g., the Taiwan Insurance Institute) or liaison with relevant insurance associations
- Collect evidence during the screening process.

This implies that thousands of insurance products launched in

Taiwan should be looked at and matched with the MNC's own insurance policy in order to assess whether or not the same type of insurance is available in Taiwan. This is a time-consuming process and it entails a wealth of knowledge in insurance products which most MNCs would not have.

2. MNCs need to:

- Persuade local insurers who offer the same type of insurance one by one to issue a statement declaring that they refuse to offer the desired insurance policy; and
- Obtain statements from all of these insurers.

The difficulty that arises is that even if local insurers offering the same type of insurance refuse to offer the insurance coverage to MNCs, they may not be willing to declare such non-acceptance in writing.

3. MNCs need to submit an application seeking approval from the FSC. The required documents include:

- An application letter.
- Information on the offshore insurance policy.
- Evidence collected from the screening process showing that the desired insurance is not offered by local insurers.
- Non-acceptance declaration from all local insurers who offer the same type of insurance.

The FSC will review the applications on a case by case basis and approve the applications based on its own discretion.

In view of the above cumbersome procedures, many MNCs in Taiwan have given up trying to obtain the FSC's

approval.

RECOMMENDATION

The government should remove the strict criteria only imposed on offshore insurance expenses and apply the same rules to both onshore and offshore insurance expenses.

3. Pre-approval for special allocation basis for head office administrative expenses

This issue is being raised for the first time by this committee. Under Article 70 of the Taiwan Income Tax Assessment Rules for Profit-Seeking Enterprises, the Taiwan branch of an MNC wishing to claim head office administrative expenses (HOAE) should allocate HOAE based on the ratio of its operating revenue over the total revenue of the head office (the revenue ratio method). However, if special circumstances exist necessitating the adoption of an allocation method other than the revenue ratio method, the Taiwan branch should seek pre-approval from the tax authority. In practice, this pre-approval process is often time-consuming and cumbersome due to the large amount of information requested by the tax authorities.

As often required by the relevant regulations of the countries where the head office and other branch offices are located, HOAE should be allocated based on appropriate allocation keys identified according to the nature of the expenses. For example, the allocation keys could be headcount, time spent, revenues, etc.

As these allocation keys are derived through a due diligence process to

properly reflect the cost drivers of the associated expenses, they will be more reasonable and accurate in attributing HOAE to branch offices than the revenue ratio. Therefore, the tax authority should allow Taiwan branches to adopt such cost-driven-based allocation methods where the head offices have the resources to implement them, rather than imposing the pre-approval requirement that may discourage taxpayers from adopting this method. As the tax authority still reserves the right to conduct subsequent audits on the adopted allocation method, removing the pre-approval requirement would not diverge from general taxation principles and practices.

RECOMMENDATION

The government should remove the pre-approval requirement for adopting an allocation method that is different from the revenue ratio.

4. Threshold for advance tax ruling applications

This issue is being raised for the first time by this committee. Currently, the scope for advance tax ruling (ATR) applications is limited to international tax issues relevant to cross-border transactions or investments which meet one of the following conditions:

- Investment amounts of at least NT\$200 million; or the first transaction amount of at least NT\$50 million.
- Investments have major benefits for the Taiwan economy.

Due to the above threshold, smaller enterprises are likely to be excluded from

seeking clarity on tax treatments through ATR. If the above threshold is removed though, it may lead to an increase in applications for ATR, it may reduce the number of potential tax disputes/appeals later on which would require both the enterprise's and the government's additional administrative resources to resolve. Moreover, enterprises would not voluntarily disclose the sensitive background information and spend the time and effort to prepare the required documentations unless they believe the transaction/investment at issue is important. Therefore, we do not expect that the removal of the threshold will lead to many trivial applications.

RECOMMENDATION

The government should remove the threshold on the ATR applications to allow smaller enterprises to seek clarity on tax treatment in advance.

5. Home leave and other benefits for expatriates' family members

This issue has been updated from last year's position paper. With the aim of encouraging foreign professionals to work in Taiwan, on 8 January 2008, the government announced tax ruling no. 09600511821 promulgating certain tax incentives for foreign professionals working in Taiwan. According to this ruling, home leave expenses paid by their employers will not be taxable to foreign professionals. Although it is not conveyed clearly in the tax ruling, we understand that the MoF holds the view that the incentive of non-taxable home leave is not extended

to the professionals' family members (i.e. spouses and children). Without extending the non-taxable treatment of home leave to the expatriate's family members, this ruling does not offer any additional tax incentives to foreign professionals.

Although the government plans to lower the personal income tax rate brackets by one percentage point (i.e. to 5%, 12%, 20%) starting from 2010, compared with neighboring countries such as Hong Kong (17%) and Singapore (20%), Taiwan's personal income tax rate of the highest bracket (40%) is still noticeably higher. Therefore, the government should offer more non-taxable benefits to attract foreign professionals to work in Taiwan.

RECOMMENDATION

The government should offer more tax incentives, such as non-taxable home leave and education allowances for family members to attract foreign professionals to live and work in Taiwan.