

Basic Introduction to Levying of the Income Tax on Cross-Border Electronic Services by a foreign profit-seeking enterprise

1. In line with and the promulgation of the new VAT system that foreign suppliers selling cross-border electronic services to domestic purchasers shall register for business and file VAT in our country, the Ministry of Finance (hereafter MOF) promulgated a new income tax interpretive rule Decree Tai-Cai-Shui-Zi No. 10604704390 on January 2, 2018 to clearly regulate levying, reporting and paying of the income tax on cross-border electronic services by a foreign profit-seeking enterprise. According to annual income tax principle, the income tax regime became effective from taxable year 2017. The basic introduction is described below:

1.1 Recognition of revenue sources from the R.O.C.

According to the Guidelines for the Determination of Sources of Income in the R.O.C. in accordance with Article 8 of the Income Tax Act, and considering the connections between the electronic services and national economy, the following shall be recognized as income from sources in the R.O.C.:

1.1.(1) Where a foreign profit-seeking enterprise produces or manufactures a product (e.g., stand-alone software, e-book, etc.) outside of the R.O.C., and after changing the method of presentation of the product, the enterprise transmits, downloads, and saves the product into a computer or mobile device via the Internet or other electronic means so as to offer electronic services to buyers within the R.O.C., the sales amounts collected therefrom are not regarded as income from sources in the R.O.C. However, if the product is provided with the assistance and involvement of a person or profit-seeking enterprise of the R.O.C., the sales amounts collected therefrom shall be recognized as income from sources in the R.O.C.

1.1.(2) Where, via the Internet or other electronic means, a foreign profit-seeking enterprise offers real-time, interactive, handy, and continuing electronic services (e.g., online games, online films and series, online music, online video, online advertisements, etc.) to domestic buyers within the R.O.C., the sales amounts collected therefrom shall be recognized as income from sources of the R.O.C.

1.1.(3) Where, via the Internet or other electronic means, a foreign

profit-seeking enterprise selling services which are delivered by physical locations (e.g., accommodation services, automobile renting services) and the locations of delivering services or running the business are outside of R.O.C., the sales amounts collected therefrom are not regarded as income from sources in the R.O.C., whether or not it is through the assistance of a foreign platform operator¹.

1.1.(4) Where a foreign platform operator provides an Internet-based platform on which onshore and offshore sellers and buyers conduct transactions, if one of the transaction parties is a person, profit-seeking enterprise, organization, institution, or entity within the R.O.C., the sales amounts collected from the seller and buyer shall be recognized as income from sources in the R.O.C.

2. Calculation of the taxable income

Pursuant to the criteria set forth above, in the case of foreign profit-seeking enterprises selling cross-border electronic services, their income from sources in the R.O.C. may be eligible for the following deductible costs and expenses, and their taxable income in the R.O.C. shall be calculated based on the applicable profit contribution ratio :

2.1 Deductible costs and expenses

2.1.(1) Where the accounting books and documents are provided, the taxable income amount shall be the verified gross revenue from sources in the R.O.C. after the deduction of related costs and expenses.

2.1.(2) Where the accounting books and documents are not available, but contracts, major business items, onshore and offshore transaction flows, and other sufficient evidence are provided allowing the taxation authority to verify the applicable major business item, the taxable income amount shall be calculated as the gross revenue from sources of the R.O.C. multiplied by the net profit ratio of the profit standard of the same trade concerned applicable to the foreign profit-seeking enterprise. Where the business type of the foreign profit-seeking enterprise is recognized as the type "offering platform electronic services," the applicable net profit ratio is 30%.

2.1.(3) For foreign profit-seeking enterprises not meeting the 2.1.(1) and

¹ A foreign platform operator is a foreign profit-seeking enterprise offering platform electronic services. It establishes platforms on the Internet (online virtual stores) for both domestic and/or overseas buyers and sellers to conduct transactions via the Internet or other electronic devices as well as collect service fees from platform users.

2.1.(2) above, their taxable amount shall be calculated based on a net profit ratio of 30%.

2.1.(4) If the actual net profit ratio verified by the taxation authority is higher than the ratio verified based on the first and second item above, the actual net profit ratio shall be applied.

2.2 Where a part of the transaction processes of a foreign profit-seeking enterprise selling cross-border electronic services takes place outside of the R.O.C., the profit contribution ratio within the R.O.C. ("domestic profit contribution ratio") shall be determined in accordance with the following:

2.2.(1) Where such foreign profit-seeking enterprise can provide documents supporting a clear division of the onshore and offshore transaction flows as well as the ratio of the contribution attributed to the services performed within the territory R.O.C. (such as the financial statements audited and certified by CPAs, transfer pricing documentation, work planning records or reports, etc.), its domestic profit contribution ratio shall be determined based on the supporting documents provided.

2.2.(2) Where the whole transaction flow is onshore or providing and using services are both within the territory of the R.O.C., the deemed domestic profit contribution ratio is 100%.

2.2.(3) For a foreign profit-seeking enterprise not meeting the 2.2.(1) and 2.2.(2) above, its domestic profit contribution ratio shall be 50%. However, if the actual domestic profit contribution ratio verified by the taxation authority is higher than 50%, the actual domestic profit contribution ratio shall be applied.

3. Rules for reporting and paying taxes

3.1 Where a foreign profit-seeking enterprise has no fixed place of business or business agent within the R.O.C., its cross-border electronic services sold are subject to the tax calculations set forth above, and the income tax shall be collected as follows:

3.1.(1) For income within the withholding tax scope, the tax withholder shall withhold the tax at the time of payment in accordance with the withholding ratio of the "payable amount". However, if a foreign profit-seeking enterprise has applied with the taxation authority in accordance with the above criteria and thereby given an applicable net profit ratio and domestic profit contribution ratio, its payable tax

of the income from sources in the R.O.C. shall be calculated and withheld based on the given net profit ratio and domestic profit contribution ratio.

3.1.(2) For income not within the withholding tax scope, the foreign profit-seeking enterprise shall file the income tax return and make payment in accordance with the regulations concerned by itself or through a tax agent within the period for the taxable year.

3.2 Where a foreign profit-seeking enterprise is a platform operator, the sales amounts it collects shall be subject to the income tax in accordance with 3.1 above. If a part of the sales amounts it collects will be transferred to a foreign non-platform service provider (e.g. foreign online game software supplier), it only actually earn platform service fees. Such foreign platform operator may provide the taxation authority with the relevant contracts and proofs of the transferred sales amounts. If the amounts transferred are recognized as a foreign non-platform service provider's income from sources in the R.O.C., proofs showing the income tax has been paid (such as a certificate of withholding tax) shall also be provided. After deductions of the transferred sales amounts, the platform service fees collected shall be subject to the income tax and tax withholding requirements above. When the foreign platform operator withholds taxes pursuant to 3.1.(1) above, it shall settle all the taxes withheld in the previous month for the national treasury within the first ten days of each month, and shall report the calculation information of the withheld and paid taxes regarding the transferred sales amounts to the taxation authority.

4. Application for a refund of the excessive tax

Effective from 2017, if the withholding tax amount of a foreign profit-seeking enterprise selling cross-border electronic services is different from the actual taxable income amount, net profit ratio, domestic profit contribution ratio, or transferring ratio verified by the taxation authority, it may file an application for a refund of the excessive tax to the taxation authority by itself or through an agent within a period of five years starting from the date the income is received. If any profit-seeking enterprise, organization, institution, or entity having its head office within the territory of the R.O.C. has abused its legal form and made false arrangements in order to be eligible for such taxation rules under this Decree with the intention of avoiding or reducing its tax liability, the tax authorities will reassess the enterprise's income tax accordingly with the actual transactions and economic facts.

5. The MOF clearly regulates recognition of revenue sources from the R.O.C. and reasonably simplifies the process of the relevant cost and cost reduction, the division of profit contribution ratio, and the reporting and paying taxes for foreign profit-seeking enterprises. For the convenience of foreign profit-seeking enterprises selling cross-border electronic services to domestic individuals to file income tax returns in May 2018, the online filing system (“Tax on Cross-Border Electronic Services”) has been established on the eTax Portal, Ministry of Finance (website : <https://www.etax.nat.gov.tw>). The MOF will pay attention to the development trend of the international digital economy tax system, timely research and refine relevant taxation regulations, in order to keep pace with the progression of economic activities and business transaction models to establish a fair, reasonable, and simplified online transaction taxation environment.