

Newsletter No 38 (EN)

Recent Developments in Taiwanese Business Law
May 2005

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I. Introduction

As we recently extended our services to Vietnam and Taiwan, in the following we would like to keep you informed about current legal changes in Taiwan.

II. Tax Law

1. Income tax of branches of “profit-seeking enterprises”

Unlike the corporate tax system in Germany, the profit-seeking enterprise tax is imposed not only on corporations and cooperative organizations, but also on sole proprietors and partnerships. Regarding sole proprietors and partnerships, individual income tax is levied in addition to the profit-seeking enterprise tax and double taxation avoided through a special imputation credit system.

The tax rate of 25 % (2004) is the maximum rate in a progressive tax structure. The rate is applicable on income in excess of TW\$ 100,000 (approx. EUR 1,250).

Where the head office of a profit-seeking enterprise is located outside the territory of Taiwan, for instance in Germany, but the enterprise has a permanent establishment (PE) or a business agent within the territory of Taiwan, profit-seeking enterprise income tax shall be levied on that part of the business profits derived from operating within the territory of Taiwan. The PE or agent shall have the obligation to pay tax and shall be responsible for filing a tax return for the fiscal year (as of assessment period 2005 = calendar year) and paying income tax. The tax return has to be filed within the period from 1 May to 31 May of each year, e.g. for assessment period 2004 until 31 May, 2005.

Remunerations paid by a branch of a foreign company in Taiwan to the parent company in Germany for the provision of services shall be deemed as the in-

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come of the parent company from source in Taiwan. The income derived from sources in Taiwan has to be reported in the tax return of respective PE or agent. Any omission or under-reporting of income derived from such a branch is subject to a fine of no more than twice the amount of the evaded taxes.

Irrespective of the above, according to the transfer pricing regulations in Taiwan, a PE in Taiwan which pays remunerations to its foreign parent company needs to provide proof to the fiscal authorities that the transfer pricing of such payment is in conformity with “arm’s length transaction principles” and that such transaction is reasonably categorized and recognized within the entire enterprise. Otherwise the authorities may adjust the amount in accordance with the regular business practice and add the respective amount to the taxable income.

2. Stock Options

The income of stock options granted to employees in Taiwan by foreign companies as a consequence of work performed in Taiwan shall be subject to income tax. Pursuant to the latest Explanation of the Ministry of Finance in Taiwan in April 2004, the time of receiving stock warrant income or any convertible bond income shall be the exercise date.

Regarding an employee, however, who is not a national of Taiwan and/or resident in Taiwan for less than 183 days during the same taxable year, the income with respect to the realization of stock warrants has not to be declared in his tax return and is separately subject to a 20 % withholding tax, irrespective of the actual residence on the exercise date of the stock warrant.

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3. Stock Interests

The draft Amendment of Article 24 of the Taiwanese Income Tax Act states that income of branches of foreign companies, e.g. a PE of a German corporation, derived from interest of short-term commercial papers (interest on public debts, corporate bonds, financial, various kinds of short-term commercial papers, deposits and other loans) by a profit-seeking enterprise shall not be added to the amount of income of the profit-seeking enterprises, but withheld with a flat rate of 20 % instead.

4. Value-Added and Non-Value Added Business Tax

Business tax, in the form of value-added or non-value-added tax, is generally levied on the sale of goods or the provision of services within the territory of Taiwan and the import of goods. In other words, any transaction of goods or services within the territory of Taiwan including importation is subject to business tax. Concerning trade through the internet the National Tax Administration recently declared that the trade will be subject to business tax provided that the trade value exceeds NT\$ 60,000 (approx. EUR 1,500) for three to four transactions through internet per month with the exemption to the trade value for each transaction is no more than NT\$ 1,000 (approx. EUR 25).

Another exemption applies to individual persons selling used merchandise, daily consumables or auctioning second-hand goods, provided that the goods are not stocks (in this case the sale is subject to business tax), Art. 3 Value Added and Non-Value-Added Business Tax Act.

III. Labour Law

According to Article 46 of the Employment Service Act 2003 the scope of work a foreign worker may be employed for in Taiwan is limited to:

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- specialized or technical work
- Director/Manager/Business executive positions if the business is invested in or set up by overseas Chinese or foreigners with the authorization of the Government of Taiwan
- teachers at schools, colleges or universities established for foreign residents or foreign languages teachers
- sport coach and athletes
- religious, artistic and show business workers
- crew members of vessels
- marine fishing/netting workers
- household assistants
- work designated by the Central Competent Authority with respect to major national construction projects or economic or social development needs
- other specialized work as approved by the competent authority or due to a lack of such specialists in Taiwan and business necessity to hire the specialist

Furthermore the competent authority has to consult the respective authority dealing with the field of work with respect to qualifications of the foreign worker. Another precondition of the employment of foreigners is a written employment contract with a limited duration. In case no duration has been determined the duration is deemed to expire with the underlying work permit.

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IV. Corporate Law and Partnerships

1. Broadened Scope of Application of Limited Partnerships

A partnership under Taiwanese Law has only one form of partners, and the partner is unlimited liable towards any obligations of the company. Taiwan's Council for Economic Planning and Development and the Ministry of Economics are currently drafting a bill regarding a Limited Partnership Act that will enhance the flexibility of corporate operations in Taiwan. It is especially envisaged to enlarge this form of partnership with limited liability from venture capital, which the drafting is originally aimed at, to such professions as accountants, lawyers and architects, thus relieving them the risk of bearing unlimited liability.

2. Determination of the promoters of a Company limited by shares

The Taiwanese Supreme Court recently held referring to the foundation of a company limited by shares that despite the fact that Article 129 of the Company Act states that the promoters shall draw up the articles of incorporation and shall affix thereon their respective signature or personal seals, it does not deal with the questions who the promoters actually are. To determine the promoter it also has to be taken into account whether respective persons de facto engage in the foundation process.

The determination of the promoters of a Company can be a vital issue where there are "sleeping promoters", especially when the promoters are imposed heavy obligations and liability pursuant to company law, the Security Act and related financial laws in Taiwan. For instance, if a person knew the set-up of a company, contributed capital, but did not attend the founding meeting or sign on the memorandum of association, he shall still be deemed as the promoter and

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shall be jointly and severally liable for the consequences of his acts in forming the company and all expenses incurred.

V. Restrictions on Foreign Investment in Securities

In general, except a few industries on which upper limits of foreign investments apply, off-shore institutional foreigners are granted the right to hold up to 100 % of the total outstanding shares in companies listed in the local market. Therefore, a German investor may invest directly in Taiwanese securities without any investment ceiling.

As of 2003 all foreign investors can invest in the securities market after simply registering with the Taiwanese Stock Exchange and obtaining an investment ID. However, it is necessary for them to appoint a local agent or representative to undertake matters such as opening accounts for trading in Taiwanese securities, applying to exchange, convert into, or subscribe to domestic corporate bonds; applying for exchange settlement, paying taxes and exercising rights in purchased securities.

Foreign institutional investors which hold shares in public companies are also prohibited from handing the proxies printed and distributed by the companies to solicitors or consigned agents.

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