Taiwan Imposes VAT on Cross-Border E-Commerce Sales of Digital Services and Goods

Beginning May 1, 2017, foreign businesses selling digital content and services to consumers in Taiwan must register as tax entities, issue government invoices, and timely report and pay VAT.

I. EXECUTIVE SUMMARY

On December 28, 2016, President Tsai Ing-Wen signed and promulgated into law a set of amendments to the Value-Added and Non-Value-Added Business Tax Act ("Business Tax Act"), which will require foreign enterprises without a fixed place of business in Taiwan selling services electronically to Taiwan consumers to register as a taxpaying entity and pay value-added tax ("VAT") on sales. The scope of the amendment is broad, and will cover not only services such as travel booking and ride-sharing, but also digital goods such as music, movies, books, mobile apps, and online games. Foreign enterprises that must apply for tax registration and comply with the law are those with NTD $480,000 in annual sales. Changes will take effect on May 1, 2017, after which businesses that fail to register or collect and pay VAT may be fined cumulatively until they comply. The current VAT rate applicable to most products and services sold in Taiwan is 5%.

The amendments are aimed at leveling the playing field between domestic and foreign e-commerce companies such as Uber, Agoda, and Booking.com, as well as providers of digital content and applications such as Google, Spotify, Netflix, and Amazon, which had previously been exempt from the obligation to collect and pay VAT. While the new law appears to present some practical enforcement difficulties, foreign e-commerce firms can expect more efforts by Taiwan authorities in the future to protect domestic competitiveness.

II. BACKGROUND

Generally, all goods and services sold in or imported into Taiwan are subject to a VAT of 5% under the Business Tax Act.[1] VAT is generally collected and paid by the seller on behalf of the purchaser at the time of sale, although buyers of services provided by foreign businesses without a fixed place of business in Taiwan are in principle obligated to voluntarily pay VAT to the tax authority. A seller's VAT obligation is tracked by Government Uniform Invoices ("GUI") that must be issued to the purchaser at the time of the sale. Under the law before it was amended, sales of services below NTD $3,000 by foreign enterprises without a fixed place of business in Taiwan were exempt from VAT.

[1] The Business Tax Act also imposes a Non-Value-Added Tax ranging between 0.1% to 25% on a handful of disparate business categories, such as small businesses, financial services, agricultural wholesale, and night clubs.

Relationship to the Income Tax

Taiwan profit-seeking enterprise income tax is only imposed on businesses with a fixed place of business in Taiwan. Therefore, foreign e-commerce firms without a business need to physically operate in Taiwan are not subject to Taiwan income tax. This has not changed from prior law. Generally, Taiwan taxes the income of enterprises organized in any form operating through a fixed place of business at 17% for amounts at or above NTD $120,001, with an additional 10% profit retention tax on earnings that have not been distributed by the end of the following year. Profit-seeking enterprises residing in Taiwan (currently those formed or headquartered in Taiwan) are taxed on their worldwide income, subject to a credit for foreign income taxes paid, while non-resident enterprises (e.g., branches of foreign companies) are taxed only on their Taiwan-source income.

III. THE E-COMMERCE AMENDMENTS

The recent amendments to the Business Tax Act adds foreign enterprises with no fixed place of business within Taiwan selling electronic services to Taiwan individuals to the definition of "business entities" under the Act.[2] Business entities are required to register with tax authorities, calculate the amount of business tax due on sales, file a return, pay taxes, or appoint a Taiwan tax-filing agent to handle such obligations.[3] In contrast to other types of foreign businesses with no Taiwan presence, the business engaged in e-commerce, not the purchaser, is the party with the legal obligation to pay tax.[4]

Definition of "Electronic Services"

Electronic services" is not defined in the law and has not been clarified by regulation, but the Taxation Administration's press releases make clear that digital content and applications such as music and games, which might otherwise be thought of as goods, are squarely intended to be covered by the amendment. Providers of services such as online travel booking and mobile ride-sharing are all the more so within the coverage of the amendment; indeed, many such companies were invited to comment on the amendment during its drafting.

Threshold for Tax Registration

Foreign businesses with e-commerce sales of services above an annual threshold of NTD $480,000[5] must either register as a taxpayer and file tax returns bimonthly, or appoint a Taiwan agent to carry out their tax obligations, if they do not have a fixed place of business in Taiwan.[6] It is not clear how the tax authorities will audit businesses to determine whether they meet the threshold, but past practice suggests payment processing records of credit card companies may be used for this purpose. Registration must be done prior to commencement of business operations.

Government Uniform Invoices

Businesses that register as a VAT-tax entity will receive a GUI number. All VAT-tax entities must issue GUIs to purchasers at the time of sale, which bear control numbers issued by the government. During the transition period between May 1, 2017 and December 31, 2017, while the government formulates implementation of the law change, overseas e-commerce businesses may self-report taxes due, and will not be required to issue GUIs.

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[2] Art. 6(4).
[3] Arts. 28-1, 38.
[4] Art. 2-1.
[5] 106 年 3 月 22 日台財稅字第 10604539420 號令.
[6] Art. 28-1.

Sales of Services Through Traditional Means or Sales to Legal Entities

For foreign businesses with no fixed place of business in Taiwan selling services to Taiwan other than through electronic channels, or to buyers other than individuals, the law remains the same – i.e., the obligation to compute and pay VAT is on the purchaser.[7] However, services purchased by a business entity solely to conduct business in taxable goods or services are tax-exempt. The obligation to pay VAT on the purchase of goods from abroad remains on the importer, regardless of whether the transaction was conducted electronically or not.

III. ENFORCEMENT

Penalties for Noncompliance

A business entity that fails to register as a VAT-tax entity as required will be fined between NTD $3,000 and 30,000 and given a specified period of time for compliance.[8] Businesses that fail to comply within the allotted time may be fined consecutively for each violation. Furthermore, a business entity that conducts business without registering for VAT may be pursued for taxes owed and fined up to five times the tax due, as well as ordered to suspend business.[9] Those which continue to conduct business after suspension may be fined again.[10] Other fines apply to enforce the timely payment of tax, accurate reporting of sales, the issuance of GUIs and their accuracy, and tax evasion generally. Taiwan agents appointed by foreign e-commerce businesses to be responsible for reporting and paying taxes under the new amendment are also made subject to penalties for non-compliance.

Enforcement Difficulties

It is unclear how the new tax obligation will be enforced against foreign companies without a business need for a permanent establishment in Taiwan, given that tax authorities have finite resources to pursue non-compliant taxpayers, and that courts of one country are generally reluctant to enforce the revenue laws of another. It is also unclear how businesses or the government can accurately determine when sales have been made to persons in Taiwan, as some users will likely attempt to circumvent efforts to collect VAT by using sites directed at other territories, location-disguising services, etc. Nevertheless, businesses that flaunt their tax obligations may be short-sighted in limiting their future potential to expand in Taiwan, as accumulated taxes and penalties cannot be expected to go away.

IV. ACTION REQUIRED

Given the Business Tax Act amendment, foreign companies with no fixed place of business in Taiwan selling digital services to Taiwan individuals should do the following:

- Restructure Transactions. A detailed review of a business's transaction structure should be done by Pamir to identify any opportunities to avoid VAT and withholding obligations. Where desirable, we may recommend that transactions be restructured so that the all or part of the sale of services is outside the scope of the law.

[7] Art. 36.
[8] Art. 45.
[9] Art. 51(1).
[10] Art. 51(4).

- Comply or Appoint Agent. To the extent transactions may not be restructured, businesses must register with tax authorities, incorporate tax calculation and collection into their purchase workflows, implement electronic or paper GUI issuance and compliance in their platforms, comply with record-keeping requirements, and timely file returns and pay taxes due. Alternatively, businesses may appoint a Taiwan agent to comply with registration, filing, and payment obligations, but must still implement tax collection, invoicing, and record-keeping procedures to comply with the law. Pamir can help businesses navigate this foreign terrain.

Where a business need for a fixed place of business or agent in Taiwan exists, tax registration and other requirements would be the responsibility of the branch or agent. Income tax and other obligations would follow from having a permanent establishment in Taiwan. Finally, while it is unclear how tax authorities will overcome practical difficulties in enforcing the new tax obligation against foreign companies without a business need to be physically present in Taiwan, tax evasion is illegal and can entail criminal sanctions and reputational costs. Complete non-compliance is only possible for small businesses that intend to remain small.

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