

CHAPTER I

A GENERAL DESCRIPTION OF TAXATION

I. Tax System

Following the teachings of the late Dr. Sun Yat-Sen, the political system of our country is based on a separation of power between central government and local government, and this therefore is the concept underlying our tax system. Thus, in the Act Governing the Allocation of Government Revenues and Expenditures, taxes are either classified as national taxes, municipality, county, or city taxes. National taxes are allocated to the central government, while municipality taxes, as well as county and city taxes, are allocated to the local governments of special municipalities, counties, and cities. With independent sources of revenue, each of the various levels of governments under this definition can, at the same time, adjust their local finances by helping one another in either sharing their resources or allocating them in accordance with an overall plan.

According to the Act Governing the Allocation of Government Revenues and Expenditures as amended and promulgated in 1999, current taxes are classified as follows:

A. National taxes consist of income tax (individual income tax and profit-seeking enterprise income tax), estate and gift tax, customs duties, business tax, commodity tax, tobacco and alcohol tax, securities transactions tax, futures transactions tax, and mine concession tax. Ten percent of total revenue from income tax and commodity tax and 40% of total revenue from business tax, after subtracting the prizes awarded to invoice lottery winners, shall be allocated by the central government according to an overall plan of the special municipality and county (or city).

In the case of a special municipality, 50% of total revenue from the estate and gift tax it collects shall be allocated to the district.

In the case of a county (city), 80% of total revenue from the estate and gift tax it collects shall be allocated to the county (city) government.

B. Municipality and county (city) taxes consist of land taxes (land value tax, agricultural land tax, and land value increment tax), house tax, vehicle license tax, deed tax, stamp tax, and amusement tax. Of these, land value increment tax shall have 20% of its total revenue redistributed by the central government among counties according to an overall plan.

In the case of a special municipality directly under the central government, municipality taxes take the place of the county and city taxes mentioned above; the total revenue of these taxes goes to the special municipality governments.

Instead of being collected as monopoly revenues, tobacco and alcohol taxes have, since 1st January, 2002, been levied separately and classified as a national tax according to the Act Governing the Allocation of Government Revenue and Expenditures.

Eighteen percent of total revenue from the tobacco and alcohol tax is allocated to the special municipalities and counties in Taiwan Province based on the proportion of population, and 2% of it is allocated to Kinmen and Lienchiang Counties in Fukien Province.

There are sixteen statutory tax items, levied by the two levels of government. Those taxes that come under the category of direct taxes according to conventional taxation theories are income tax, mine concession tax, estate and gift tax, securities transactions tax, futures transactions tax, land tax, house tax and deed tax; the remainder are indirect taxes, such as customs duties, commodity tax, business tax, stamp tax, amusement tax, and tobacco and alcohol tax.

II. Tax Structure

The proportions of direct and indirect taxes in a nation's total revenue are often taken as criteria in judging its tax system; theoretically, direct taxes adapt better to the ability of the people to bear the burden and are in accordance with the principle of taxation according to ability-to-pay. Furthermore, direct taxes interfere less with the allocation of resources in a private economy, and this is more in keeping with the requirements of economic efficiency. Consequently, direct taxes have been regarded in conventional taxation theories as good taxes, and their proportion of state revenue has been held as a measure by which to judge whether a taxation system is progressive or regressive.

For years it has been the objective of our taxation policy to build a tax system with direct taxes at its core. According to data presented in the Yearbook of Tax Statistics compiled by the Ministry of Finance (MOF), the proportion of direct taxes in total tax revenue rose from 54.8% to 58.5% between 2003 and 2010, while that of indirect taxes declined from 45.2% to 41.4%, and the proportion of direct taxes in that period thus increased by 3.7%.

However, in recent years, it has been suggested in some taxation theories that direct taxes with progressive rates have an adverse effect on people's inclination to work and to invest. As a result, many countries began to lower their marginal rates of income tax and we also followed suit. At the same time, our tax structure continues to be adjusted in a rational way, which indicates that our tax system and tax structure have gradually become comparable to those in countries such as the OECD nations.

A tax structure adjusts itself to the economic system and development of the country,

however, at the same time, the objectives of a governmental taxation policy and the design of the tax system are also important factors in guiding the adjustments. For the last forty years, we have made establishing an equitable and rational tax system and raising the proportion of income tax in total revenue the goals of our effort in tax reform. In practice, our tax structure has already undergone changes along those policy lines. The following table shows changes in our tax structure with respect to the four major tax categories: income tax, property tax, sales tax, and others.

Tax Structure

Tax Item	Unit: %		
	2003	2010	% Change
Income Tax	32.9	36.4	+3.5
Individual Income Tax	15.8	18.8	+3.0
Profit-Seeking Enterprise Income Tax	17.1	17.6	+0.5
Property Tax	12.7	12.0	-0.7
House Tax	3.8	3.6	-0.2
Land Tax	8.9	8.4	-0.5
Sales Tax	34.7	31.9	-2.8
Business Tax	15.8	16.5	+0.7
Stamp Tax	0.6	0.6	0.0
Commodity Tax	11.7	9.3	-2.4
Customs Duties	6.6	5.5	-1.1
Others	19.7	19.7	0.0
Financial Enterprises Business Tax	1.8	1.3	-0.5
Health and Welfare Surcharge on Tobacco	0.8	2.1	+1.3
Other Taxes	17.1	16.3	-0.8
Total	100	100	

III. Tax Revenues

Owing to economic development, social progress, and population growth, there has been an increasing demand for services to be provided by the government, and with the expansion of government functions, the magnitude of government expenditure has continued to grow. According to data presented in the Yearbook of Financial Statistics, the percentage ratio of tax revenues to general government net revenues for the period between 2002 and 2009 was on average 70.2%, the highest being 76.7% for the fiscal year 2008, and the lowest 62.6% for the year 2003. There has been remarkable growth in the absolute value of tax revenues (excluding monopoly revenues, financial enterprises business tax, and the health and welfare surcharge on tobacco), which came to a total of NT\$1,483.5 billion in 2009 as

compared with NT\$1,190.9 billion in 2002, an increase of 24.6%.

There have also been notable changes during the last decade in the contribution ratios of tax revenues among government at all levels as a result of changes in the social environment, as well as in the Act Governing the Allocation of Government Revenues and Expenditures. For example, of the total tax revenues for the fiscal year 2002, the central government took 80.1%, the municipality and county (or city) governments 17.1%, while for the fiscal year of 2009, the central government took 80.9%, and the municipality and county (or city) governments 16.0%.

IV. Tax Burden

The magnitude of the tax burden on the public has been not only a principal basis in reference to which financial authorities determine their taxation policies, but also an indicator by which international comparisons are made between tax burdens in different countries. This burden directly affects the disposable income and indirectly the consumption level and the standard of living of the people. Thus, in order to enhance public welfare, countries with taxes as their principal source of revenue all take light taxation as the goal of their taxation policies. The magnitude of the tax burden of the people has thus become one of the set of indicators by which the economic well-being of a nation is assessed.

The tax burden of the people can be measured by the proportions of total tax revenues to the gross domestic product (GDP). In the decade between 2001 and 2010, the proportion of total tax revenues to GDP averaged 12.7%. The ratio was 12.7% in 2001, while in 2010 it was 12%, with the lowest point being 11.7% in 2003. The overall tax burden, however, still remains relatively low among the nations of the world.

If we compare the tax burden of our people with that of people in noted industrial countries, for example in the USA and Japan, the proportions of total revenues to GDP according to data for 2007 were 21.7% in the USA and 18.0% in Japan, both higher than our 13.4% for the same year.

Considering the present levels of our economic development and national income, the current level of the tax burden can be called reasonable and there is a potential capacity for additional taxation in the future.

V. Tax Organization

A. Central Government

The MOF, as the highest administrative organ of taxation, lays down taxation policies, enacts tax laws and oversees the levy and collection of taxes. Under the MOF, there are the Taxation Agency, Department of Customs Administration,

Taxation and Tariff Committee, Financial Data Center, and Training Institute. The Taxation Agency is in charge of drafting, enacting, and interpreting inland tax codes (for taxes other than customs duties and mine concession tax), as well as overseeing the levy and collection of inland taxes. The Department of Customs Administration is in charge of drafting, enacting, and interpreting tariff codes, as well as overseeing the collection of customs duties under the direction of the MOF. The Taxation and Tariff Committee is in charge of the research and planning of inland taxes and customs duties. The Financial Data Center is in charge of filing, checking, and examining the inland tax data of the whole country. The Training Institute is in charge of the pre-job and on-the-job training of public finance personnel. Except for the Department of Customs Administration, which is an internal staff unit of the MOF, all the above organs are directly subordinated to the MOF, while serving at the same time as staff units for the Minister of Finance.

National taxes of the central government are levied in two broad categories: customs duties and inland taxes. Customs duties are the responsibility of the Directorate-General of Customs, under which are the customs offices of Keelung, Taipei, Taichung, and Kaohsiung, with branches and sub-branches, and which may, as determined by local conditions and the volume of business, set up collection offices as local level customs units. Inland tax collection comes directly under central government control. Five national tax administrations are in charge of the collection of national taxes in different locations: Taipei, Kaohsiung, and Northern, Central, and Southern Taiwan Province. In the past, the collection of business tax was entrusted to the municipality and county (or city) governments. However, the collection of the aforesaid tax was assumed by the national tax administration as of January, 2003 in order to promote efficiency in collection and improve the cross-auditing of tax information related to the business tax and the profit-seeking enterprise income tax.

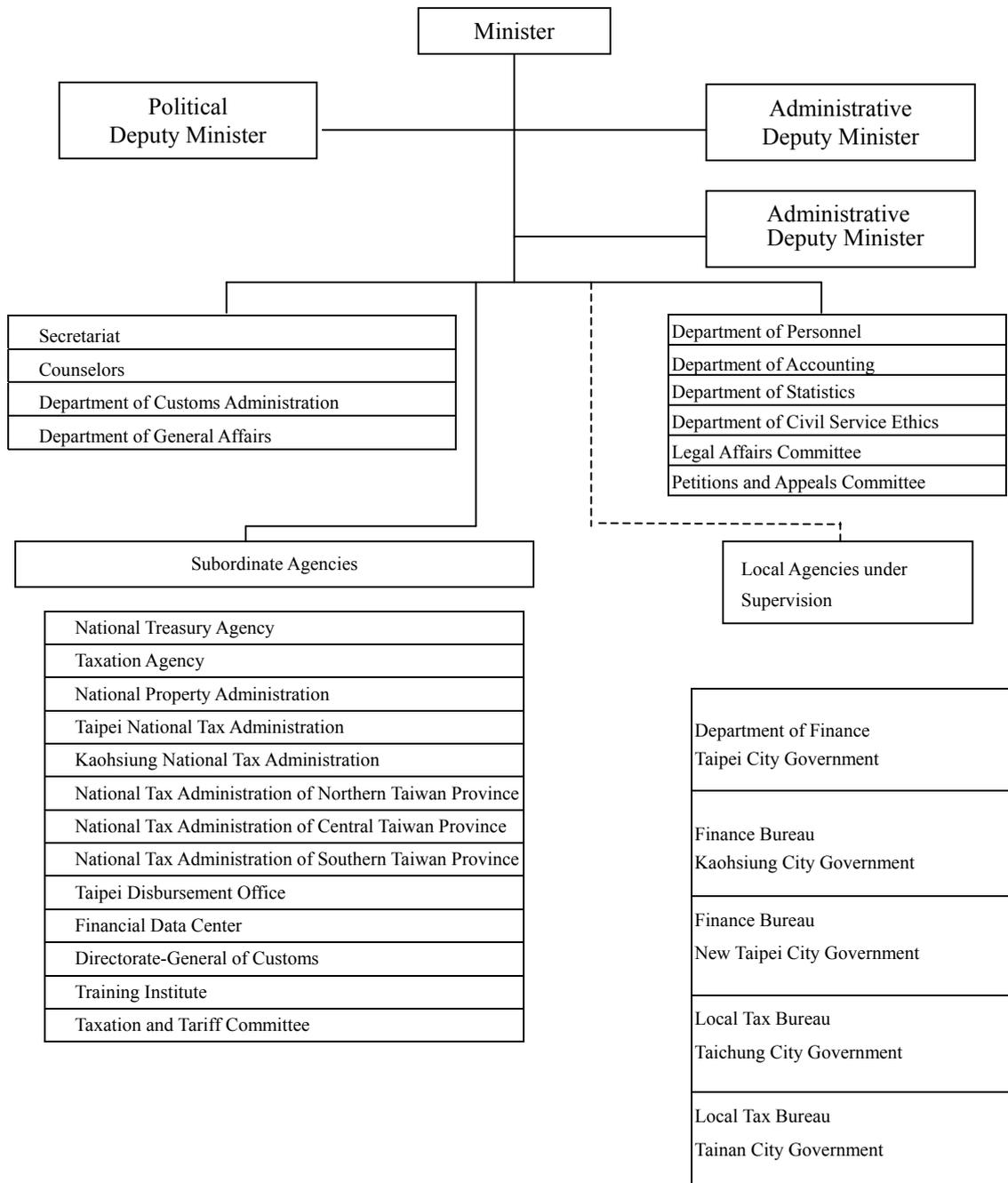
B. Municipality Governments

Municipality tax bureaus are the branches in charge of the levying of municipality taxes. Under the municipality tax bureaus are the municipality tax offices in charge of the collection of municipality taxes. The tax offices may, in view of the administrative divisions and economic development of an area, set up branch offices as local level tax collection units.

C. County (or City) Governments

County (or city) governments under the provincial government all have their own tax offices in charge of the collection of county and city taxes, respectively. These tax offices may, in view of the administrative divisions and business conditions of the area, set up branches as local level collection units. County and city tax offices are subordinate organs of the county and city governments concerned, performing tax collection tasks on orders from the magistrate of the county or the mayor of the city, and are directed and supervised by the county and city government concerned, as well as the Finance Bureau.

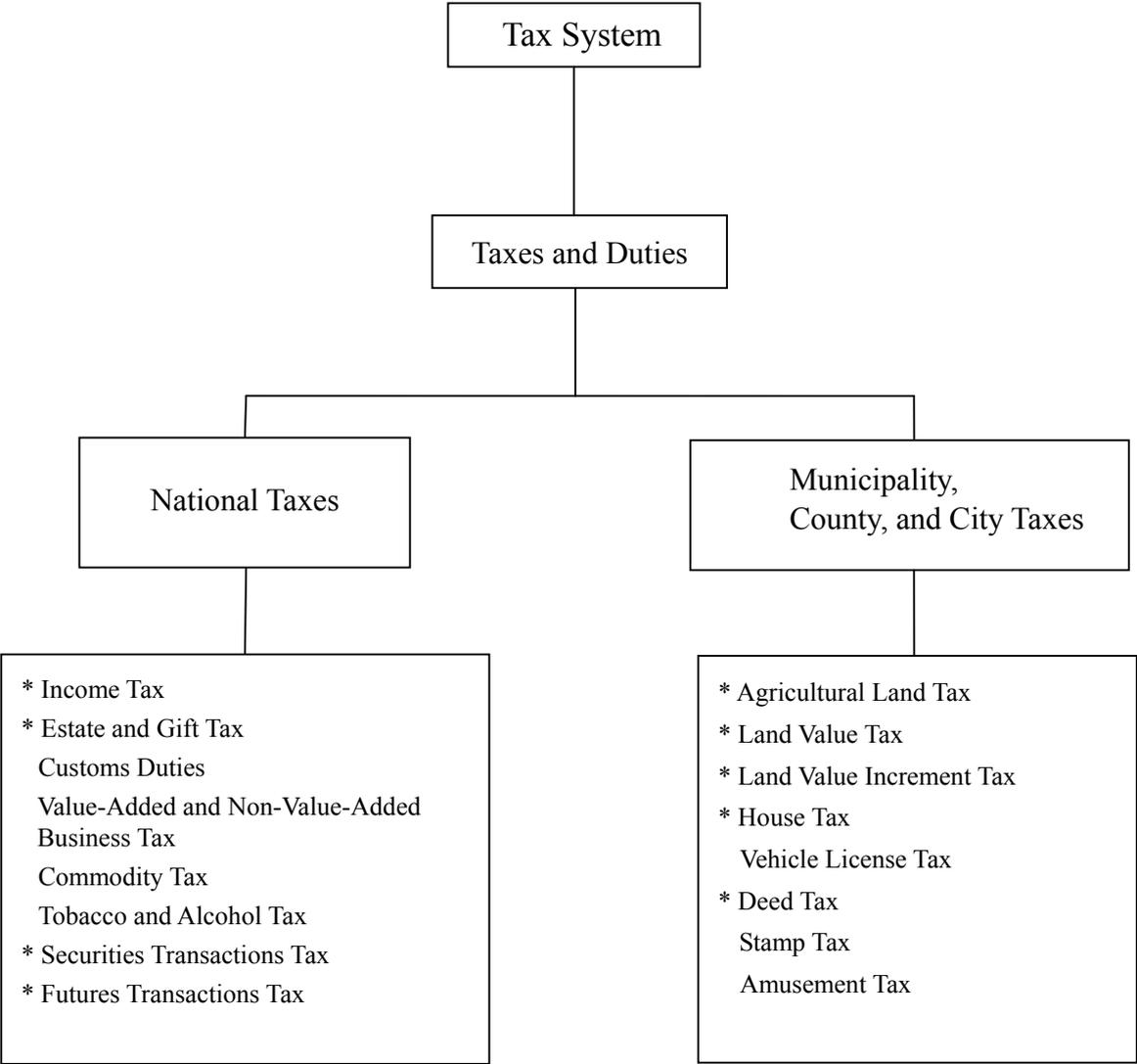
Chart A: The Organization of the Ministry of Finance



———— Administration System

----- Supervision System

Chart B: The Tax System



* Direct Taxes

Chart C: Total Tax Revenue for the Years from 2006 to 2010

Unit: NT\$ million

Item	2006		2007		2008		2009		2010	
	Amount	Ratio %								
Total	1,600,804	100.0	1,733,895	100.0	1,760,438	100.0	1,530,282	100.0	1,622,244	100.0
Taxes	1,556,652	97.2	1,685,875	97.2	1,710,617	97.2	1,483,518	96.9	1,565,847	96.5
Customs Duties	79,567	5.0	81,859	4.7	80,426	4.6	68,827	4.5	89,484	5.5
Income Tax	646,218	40.4	730,160	42.1	834,988	47.4	640,967	41.9	590,387	36.4
Profit-Seeking Enterprise Income Tax	311,888	19.5	382,634	22.1	445,245	25.3	334,163	21.8	285,701	17.6
Individual Income Tax	334,330	20.9	347,526	20.0	389,744	22.1	306,804	20.0	304,686	18.8
Commodity Tax	159,201	9.9	149,037	8.6	126,660	7.2	127,879	8.4	150,777	9.3
Tobacco and Alcohol Tax	51,042	3.2	50,415	2.9	49,506	2.8	45,349	3.0	44,516	2.7
Business Tax	236,931	14.8	246,137	14.2	243,961	13.9	223,503	14.6	268,214	16.5
Land Value Tax	54,660	3.4	59,009	3.4	59,127	3.4	59,054	3.9	63,044	3.9
Land Value Increment Tax	76,547	4.8	74,682	4.3	56,955	3.2	53,313	3.5	73,313	4.5
Others	252,486	15.8	294,576	17.0	258,994	14.7	264,626	17.3	286,112	17.6
Financial Enterprises Business Tax	26,644	1.7	28,131	1.6	29,706	1.7	21,853	1.4	21,602	1.3
Health and Welfare Surcharge on Tobacco	17,508	1.1	19,888	1.1	20,115	1.1	24,911	1.6	34,795	2.1

Chart D: The Annual Percentage of Direct and Indirect Taxes of Total Tax Revenues for 2003 to 2010

Due to government efforts to improve the tax structure and strengthen the income tax collection system, the relative importance of direct taxes as a percentage of total tax revenue has grown annually. In the year 2003, the percentage of direct taxes to total revenues was 54.8%, and in the year 2010 it was 58.5%, an increased of 3.7%.

