

CHAPTER V

INCOME TAXATION OF TRUSTS

I. General Description

The term “trust” refers to the legal relationship in which the settlor transfers or disposes of a right to property, thereby allowing the trustee to administrate or dispose of the trust property according to the stated purpose of the trust either for the benefit of a beneficiary or for a specified purpose. The Trust Act was promulgated on 26th January, 1996. The MOF also augmented stipulations to the Income Tax Act in order to address income taxation problems resulting from the trust system, so as to supply more force to the provisions of the Trust Act to create a complete and stable trust system. The stipulations were revised and published on 13th June, 2001.

II. Taxation Principles of Trust Benefits

A. Creation of a Trust

Where the settlor of a trust deed is a profit-seeking enterprise and the beneficiary of the whole or any part of the trust benefits designated is not the settlor him, her, or itself, then the said beneficiary shall include the value of his, her, or its entitlement to such trust benefits in the aggregate amount of his, her, or its annual income for income tax assessment under the Income Tax Act in the year the trust deed takes effect.

B. Change of Beneficiary

Where the settlor of a trust deed is a profit-seeking enterprise and the designated beneficiary of the whole or any part of the trust benefits is the settlor him, her, or itself, in the case that the beneficiary is replaced by a person other than the settlor during the term of such a trust relationship, the new aforesaid beneficiary shall include the value of his, her, or its entitlement to such trust benefits in the aggregate amount of his, her, or its annual income for income tax assessment under the Income Tax Act in the year such a change of beneficiary takes place.

C. Addition of Trust Property

Where the settlor of a trust deed is a profit-seeking enterprise, in the case that any person other than the settlor is added thereto as a beneficiary to the trust benefits, thereby resulting in an increase in the value of the trust property during the term of the trust relation, the new said beneficiary shall include the increased portion of the value of his, her, or its entitlement to such trust benefits in the aggregate amount of his, her, or its annual income for income tax assessment under the Income Tax Act in the year the increase in the value of the trust property takes effect.

D. A Non-Specific or Non-Existent Beneficiary

Where a beneficiary of a trust deed is non-specific or non-existent, the trustee shall be considered as the taxpayer for that trust deed and shall include the value of the entitlement to such trust benefits, as calculated in accordance with the applicable withholding tax rate (20%), in his or her annual income tax return, filed within the fixed period under the Income Tax Act in the year the trust deed, a change of the beneficiary, or the increase to the value of the trust property takes effect.

III. Exemption for Trust Deeds

Where the trust property is transferred or otherwise disposed of based on any of the following trust relationships, such a trust property shall be exempt from income tax:

- A. Between the settlor and a trustee, due to the creation of a trust deed;
- B. Between the original trustee and a new trustee, upon a transfer of the trustee during the term of the trust relationship;
- C. Between a trustee and a beneficiary, upon delivery of the trust property by the trustee according to the purposes of the trust stated during the term of the trust relationship;
- D. Between the settlor and the trustee or between the trustee and the beneficiary, due to the termination of the trust relationship; or
- E. Between the settlor and the trustee due to a failure of establishment of the trust deed, or invalidation, cancellation, or nullification of the trust deed.

IV. Taxation of Income Arising from Trust Property

The income arising from the management or disposal of the trust property by the trustee shall be subject to the following income tax assessment:

- A. Separate accounting books and records shall be established and maintained by the trustees for use in keeping details of the received and disbursed transactions. Each disbursement must be supported by the appropriate documents or receipts.
- B. With regard to the revenue derived from the trust property, the trustee shall calculate the amount of various categories of income accrued and to be payable to each trust beneficiary in the year of such income derivation, following deductions for costs, necessary expenses, and losses incurred. Each beneficiary shall include the portion of the trust benefits in his, her, or its annual income tax return for income tax assessment.
- C. Where there are two or more beneficiaries entitled to the trust benefits, the trustee shall calculate the amount of such income to be distributed to beneficiaries in accordance with the proportions for distribution as explicitly stated in the trust deed or the deductive proportions. However, if the proportions to be distributed are either unknown or cannot be deduced, the income derived from the trust property shall be calculated on an average basis.

- D. Where the beneficiary is non-specific or non-existent yet, the taxpayer for the amount of income derived from the trust property for that year shall be the trustee of the trust property, and a withholding tax shall be paid at the applicable withholding rate and declared in the annual income tax return filed within the fixed period under the Income Tax Act. With regard to the withholding tax already declared and paid, the amount of such tax withheld may be deducted from the amount of income tax payable by the taxpayer.
- E. In the case where a trustee fails to comply with the provisions set out in the preceding Sub-Sections B through D, the collection authority-in-charge shall assess the amount of income of the trust beneficiary concerned based on the relevant information available, and levy the income tax accordingly.
- F. With regard to a charitable trust conforming to the requirements set out in the Income Tax Act (see V. below), the benefits from the trust actually distributed to the trust beneficiaries shall be included in their respective annual incomes for income tax assessment for the year such benefits were distributed.
- G. With regard to mutual trust funds, securities investment trust funds, futures trust funds, or any other trust funds approved by the Financial Supervisory Commission, Executive Yuan, the trust benefits actually distributed to the trust beneficiaries shall be included in their respective annual incomes for income tax assessment for the year such benefits were distributed.

V. Stipulations for Charitable Trusts

- A. Where a profit-seeking enterprise provides property for the purpose of formation, contribution, or participation in any of the following charitable trusts, the value of the beneficiaries' entitlement to the benefits under the said charitable trust shall be exempt from income tax assessment:
 - 1. The trustee is a trust business operator as defined by the Trust Business Act.
 - 2. A charitable trust shall not pay special benefits in any manner to any specific person or to any person who may be designated as a specific person, except for payment of expenses which must be made to an incorporated enterprise, in order to meet the objective of the said charitable trust.
 - 3. Trust property which, according to the provisions of the trust deed thereof, shall be transferred to a government authority at a specific level, a public jurist or a charitable trust having a similar objective, upon cancellation or termination of such a trust deed.
- B. With regard to the property provided by any individual or profit-seeking enterprise for creating, contributing to, or participating in a charitable trust conforming to the applicable requirements, the provisions for donations in the Income Tax Act shall govern.

VI. Withholding

- A. With regard to revenue arising from trust property, the withholding agent shall name the trustee of the said trust deed as the taxpayer at the time of payment and complete the tax-withholding process. However, for trust benefits, except for interest from short-term commercial papers and prizes received from government-sponsored lotteries paid by the withholding agent with respect to a charitable trust, such payments shall be exempt from the withholding tax.
- B. When making a withholding tax statement, the trustee of a trust deed shall take the amount of tax withheld from various categories of the trust income accrued and to be payable to a trust beneficiary as the amount of tax withheld for the said trust beneficiary; provided, however, that in the case that there are two or more trust beneficiaries, the trustee shall calculate the tax withheld by each trust beneficiary in accordance with the proportions cited in IV. C above.
- C. Where the trust beneficiary is a non-resident individual or a non-resident foreign business having no fixed place of business in the ROC, the trustee of the said trust deed shall be regarded as the withholding agent, and tax shall be withheld from various income payments to the said trust beneficiary at a withholding rate of 20%; however, withheld tax already paid by the trust beneficiary may be deducted from the withholding tax payable by such trust beneficiary.
- D. When distributing trust benefits to a charitable trust or a trust fund, the trustee shall be considered as the withholding agent who shall complete the withholding process.
- E. The trustee of a trust deed shall, prior to the end of January of each year, prepare documents prescribing the inventory of property, revenue, and expenditure statements, statement of trust benefits accrued and payable to trust beneficiaries, statement of withholding tax, and other relevant documents and submit copies to the collection authority-in-charge. In addition, the withholding (non-withholding) tax statement and relevant vouchers shall be prepared and issued to the relevant taxpayers prior to 10th February of each year. In the case that three national holidays occur in immediate succession in January, the period for the submission of documents shall be extended to 5th February and the period of the issuance of the withholding (non-withholding) tax statement and the relevant vouchers shall be extended to 15th February.

VII. Penalty Provisions

- A. Where the trustee of a trust deed is found to have under-declared or omitted a declaration of any revenue accrued on the trust property, or made a false declaration of any relevant costs, necessary expenses or losses, thus causing an under-calculation of the trust beneficiaries' income; or has failed to accurately categorize the beneficiaries' income, thus causing a reduction in the trust beneficiaries' tax-paying obligations, the trustee shall be liable to a fine in an amount equal to 5% of the amount of under-declared or evaded income of the trust beneficiaries, or the amount of incorrectly categorized income of such

beneficiaries. However, the maximum amount of the fine shall not be more than NT\$300,000, and the minimum amount shall not be less than NT\$15,000.

- B. Where the trustee of a trust deed fails to calculate the amount of trust beneficiaries' income from different categories of income in accordance with the cited proportions, the said trustee shall be liable to a fine in an amount equal to 5% of the deficit between the income amount calculated by the trustee and the income amount calculated in accordance with the applicable proportions. However, the maximum amount of the fine shall not be more than NT\$300,000, and the minimum amount shall not be less than NT\$15,000.
- C. Where the trustee of a trust deed fails to file prior to the deadline, file an accurate withholding tax return, or prepare and issue the relevant documents or withholding (non-withholding) tax statement or any other relevant vouchers, the said trustee shall be liable to a fine in the amount of NT\$7,500; in addition, the said trustee shall be required to file a tax return or to issue the relevant documents within a prescribed time limit. Failure to file or issue prior to the prescribed deadline shall result in a fine imposed on the trustee in an amount equal to 5% of the income accrued on the trust property in the then current year. However, the maximum amount of the fine shall not be more than NT\$300,000, and the minimum amount shall not be less than NT\$15,000.