TAX MANAGEMENT
PORTFOLIOS™

FOREIGN INCOME

Business Operations in the Republic of Korea

by

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TAX MANAGEMENT
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FOREIGN INCOME

Business Operations in the Republic of Korea

PORTFOLIO DESCRIPTION

Tax Management Portfolio, *Business Operations in the Republic of Korea,* No. 7210, deals with the taxes and tax problems most likely to be encountered by foreign firms doing business in the Republic of Korea.

The Detailed Analysis provides a summary of the Korean tax system and detailed treatment of the major taxes affecting business: the individual and corporate income taxes and the value added tax. Tax presence is discussed separately, in detail, because of its importance as a threshold issue.

The Worksheets include corporation tax forms and tax rates.

This Portfolio may be cited as Kim and Choi, 7210 T.M., *Business Operations in the Republic of Korea.*

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TABLE OF ABBREVIATIONS

AFCST	Agricultural and Fishery Communities Special Tax
ARL	Assets Revaluation Law
BOK	Bank of Korea
CC	Commercial Code
CTL	Corporation Tax Law
FETL	Foreign Exchange Transactions Law (formerly known as FEML, Foreign Exchange Management Law)
FETR	Foreign Exchange Transaction Regulation
FIPL	Foreign Investment Promotion Law
FSC	Financial Supervisory Commission
FSCMA	Financial Investment Services and Capital Markets Act
FSS	Finance Supervisory Service
FTC	Fair Trade Commission
FTL	Foreign Trade Law
IGTL	Inheritance and Gift Tax Law
ITCL	International Tax Coordination Law
ITL	Income Tax Law
KCC	Korean Commercial Code
LSA	Labor Standards Act
LTL	Local Tax Law
LTILL	Local Tax Incentive Limitation Law
MOEL	Ministry of Employment and Labor
MOSF	Ministry of Strategy and Finance (formerly known as MOFE, Ministry of Finance and Economy)
MOKE	Ministry of Knowledge and Economy (formerly known as MOCIE, Ministry of Commerce, Industry and Energy, and now known as MOTIE, Ministry of Trade, Industry and Energy)
MOTIE	Ministry of Trade, Industry and Energy
MRFTL	Monopoly Regulation and Fair Trade Law
NTBL	National Tax Basic Law
NTS	National Tax Service
PDWA	Protection of Dispatched Workers Act
PFPEA	Protection of Fixed-Term and Part-Time Employees Act
TILL	Tax Incentive Limitation Law (formerly TERCL, Tax Exemption and Reduction Control Law)

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DETAILED ANALYSIS

I. The Republic of Korea: General Background

A. Political System and Governmental Organization

The Republic of Korea (also referred to in this work as "Korea") exercises sovereignty over that portion of the Korean peninsula lying south of the cease-fire line of 1953.

The Western legal system currently in effect in Korea is relatively new. The Japanese imposed their system of codes (translated from French and German during the Meiji Restoration) upon the Korean people during the period of occupation from 1910 to 1945. After liberation from the Japanese, the Koreans translated, recodified and revised the Japanese statutes and added a large volume of their own statutory law.

The government of Korea is described as a democratic republic. The government is divided into three branches — executive, legislative and judiciary — which are more or less independent of each other.

The president is elected by universal direct suffrage for a single term of five years. The president appoints the prime minister, with the consent of the National Assembly. On the recommendation of the prime minister, the president appoints a State Council that has from 15 to 30 members.

The National Assembly consists of 246 members, popularly elected from separate districts, and 54 members selected on a proportional basis by the political parties which get at least 3% of the votes in an election.

B. Statutes/Sources of Law

The Western legal system currently in effect in Korea is relatively new. The Japanese imposed their system of codes (translated from French and German during the Meiji Restoration) upon the Korean people during the period of occupation from 1910 to 1945. After liberation from the Japanese, the Koreans translated, recodified and revised the Japanese statutes and added a large volume of their own statutory law, that includes constitutional law, civil law, criminal law, a Korean commercial code, litigation procedures law and other laws regarding administration, economy and society as a whole.

C. Court System and Arbitration

There are three levels of courts: the District Courts, the High Courts and the Supreme Court. In addition, a Constitutional Court has jurisdiction over constitutional matters, impeachment and other specific areas delineated in the Constitution.[1] The Patent Court, the Family Court, the Administrative Court and the Bankruptcy Court handle cases related to specific matters, such as intellectual property rights and administration issues.

Act No. 1767 of March 16, 1966, introduced the arbitration law in Korea, and it has been amended several times since.[2] Arbitration refers to the procedure through which judicial disputes are settled by an arbitrator's award by agreement between the parties. An arbitral award has the same effect as a final and conclusive judgment of a court and may be enforced compulsorily. In principle, there are three arbitrators and the procedure for appointing the arbitrators is determined by agreement between the parties involved.

[1] For more detail on the structure of the Korean government, along with links to additional sources, see the Library of Congress' legal research guide for the Republic of Korea at www.loc.gov/law/help/guide/nations/southkorea.php.

[2] For more details on arbitration rules in Korea, see https://elaw.klri.re.kr/eng_service/lawView.do?hseq=38889&lang=ENG.

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II. Operating a Business in Korea

A. Foreign Investment Regulations

The Foreign Capital Inducement Law (FCIL), which was in effect for more than 16 years, was replaced by the Foreign Investment Promotion Law (FIPL) with effect from November 17, 1998. Portfolio investments are governed by the Foreign Exchange Transactions Law (FETL).

An applicant may request pre-confirmation of eligibility for the tax exemptions before beginning the stock subscription process of filing a foreign investment report.

The discussion that follows relates to the FIPL. (On May 24, 1999, the tax-related provisions of the FIPL were moved to Chapter 5 of the Tax Incentive Limitation Law (TILL), pursuant to a restructuring of the Ministry of Strategy and Finance or MOSF (formerly the Ministry of Finance and Economy or MOFE) and the Ministry of Knowledge and Economy or MOKE (formerly the Ministry of Commerce, Industry and Energy or MOCIE, now the Ministry of Trade, Industry and Energy or MOTIE.)) Note, however, that for foreign investment for which an exemption application is filed on or after January 1, 2019, the FIPL income tax exemption no longer applies. See XV, below.[3]

1. General

Foreign investment is generally allowed unless specifically restricted under the FIPL or another statute. The Korean government has repeatedly announced its long-term policy of liberalizing foreign investment. In furtherance of this policy, the system for granting foreign investment approval has been shifted from a system of general prohibition to a system of general permission. Before 1984, foreign investment was prohibited except where specifically permitted. From 1984 until 1991, foreign investors could apply for investment approval unless their investment was specifically prohibited, but approval was still discretionary and subject to the imposition of conditions. Under the current system, most categories of investment fall within what is referred to as the "report" system. Under this system, the foreign investor's report is deemed to be accepted unless the MOSF or the Bank of Korea (BOK) responds within a fixed period of time (generally 30 days). The MOSF or BOK can refuse to accept a report only after the matter is considered by the MOSF's Foreign Invested Business Committee. Effective March 1, 1991, the minimum foreign investment requirement was newly introduced and at the time was 50 million *won*, the minimum amount of paid-in capital then required for the formation of a *chusik hoesa* (joint stock company; see III, D, below). In the case of multiple investors, each investor had to make a minimum investment of 25 million *won.*

Effective April 1998, the investment rules were further relaxed to permit the purchase by a foreign investor of shares of its Korean partner's stock and to remove restrictions on investment in areas previously reserved for small businesses.[4]

Effective October 2010, the minimum foreign investment threshold as well as the minimum investment amount per investor is 100 million *won.*

Foreign persons (domestic corporations in which foreign persons hold majority ownership are considered to be foreign persons) may not own or lease land without the approval of the relevant local authority.

A foreign person not resident in Korea may apply to the MOKE or its designee, or may make an investment by reporting to one of 17 Korean banks or 21 foreign banks in Korea under the FIPL.[5] Investment can be made in this way in most categories of manufacturing, foreign trading and distribution businesses. No investment can be made when the investment falls in a prohibited or restricted category. Prohibited categories include government administration, education, religion and political party activities. Restricted categories currently include public-power generation, meat wholesaling, telephone business and freight forwarding. Table 2 of the Regulation Concerning Foreign Investment and Technology Inducement sets out the restricted categories, specifies conditions that must be met, sets out a schedule for future liberalization and specifies foreign ownership restrictions.[6]

Under the FIPL, the MOSF has announced a list of high technology and industry support services that qualify for tax benefits in relation to capital investments or technology inducement agreements. These include the manufacture of composite materials, specialty chemicals, chemicals and gas used in semiconductors, software development services, industrial design services, and engineering used in social overhead capital projects.[7]

2. Tax Incentives

Tax exemptions are available for investment in one of the areas of high tech or industry support services as listed in the Tax Exemption Regulation on Foreign Investment.[8] Tax incentives currently include tax exemptions and reductions for certain foreign investments, as described at XV, P, below. Either the Korean subsidiary (which may or may not be in the form of a joint venture company) or the foreign investor is required to file a tax exemption application by the end of the fiscal year in which the business commencement date falls. Effective January 1, 2010, no exemption applies to payments under the Technology Inducement Agreement following the repeal of Art. 121-6 of the Tax Incentive Limitation Law. As noted above, however, for foreign investment for which an exemption application is filed on or after January 1, 2019, the FIPL income tax exemption no longer applies.

[3] Addendum to Government Organization Law, Law No. 5982 (1999).

[4] Small and Medium Enterprise Production and Cooperation Law Enforcement Decree, Presidential Decree No. 14697 (1995), as last amended by Presidential Decree No. 14909 (1996), Art. 4.

[5] Ministry of Knowledge and Economy (MOKE) Notice No. 2011-170, Regulation Concerning Foreign Investment and Technology Inducement, Sept. 1, 2011. MOKE is now MOTIE.

[6] MOKE, Regulation Concerning Foreign Investment and Technology Inducement (2011). MOKE is now MOTIE.

[7] Ministry of Strategy and Finance (MOSF) Notice No. 2010-24 of Oct. 1, 2010.

[8] MOFE Decree No. 1999-14 (May 29, 1999), as last amended by MOFE Decree No. 2010-24 (Nov. 1, 2010).

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B. Currency and Exchange Controls

Effective April 1, 1999, the FETL replaced the Foreign Exchange Management Law (FEML). Under the FETL, most foreign exchange transactions are free from restrictions, but the MOSF retains the authority to impose such restrictions as it deems necessary. Emergency measures may be invoked by the MOSF in the case of natural disaster, war, significant and extremely volatile economic circumstances, and other similar circumstances.[9]

In principle, residents and nonresidents are to report foreign exchange transactions for monitoring purposes.[10]

In general terms, all currency and credit transactions between a resident and a nonresident are permitted unless specifically restricted by the decrees and regulations promulgated under the FETL. Domestic Korean corporations and the Korean branch offices of foreign corporations are residents for foreign exchange control purposes.[11] A foreign national is deemed to be a resident of Korea for foreign exchange control purposes if he works at a place of business in Korea, engages in business in Korea, or maintains a domicile or residence in Korea for six months or more.[12] The term "domicile," although not defined in the FEML, is defined in Article 18 of the Korean Civil Code as the "base" of a person's life. The term "residence" is not defined by statute, but is generally considered to refer to a place where a person is staying.

There are no foreign exchange restrictions on payments for trade in goods or services. The Foreign Exchange Transaction Regulations (FETR), however, require banks to provide certain payment information to the National Tax Service and the Korea Customs Service.[13] Payments in the nature of a donation are subject to per-person and per-instance limits. Transactions of a capital nature such as loans, lease payments, and guarantee payments are subject to reporting or approval by a bank, the Bank of Korea (BOK) or the MOSF.

Comment: As foreign exchange flow has become less restricted, control over withholding of tax at source has become less regulated. Payors are no longer required to obtain a tax clearance certificate from the district tax office before remitting foreign exchange payments.

The FEMR was revised with respect to payments and receipts for trades, services and capital transactions, including portfolio inbound investments, effective July 1, 1998. These changes were later reflected in the FETR (April 1, 1999).

First, most restrictions on import and export credit terms have been removed. In the past, imports on credit terms were restricted to discourage imports and to control domestic liquidity. Most of these restrictive provisions have now been abolished. Imports can now be paid for by a resident in *won* through a bank without government approval. Further, there is no restriction on payment for imports after the receipt of the goods. In case of payment for imports before receipt of the goods, there is no restriction for up to one year. However, if payment occurs more than one year before receipt, a BOK report is required.

In case of export advances, the receipt of payment after the shipment of goods is allowed for up to three years without restriction for transactions between the parent company and a branch, unless payment occurs after three years in which case a BOK report is required. For all other types of transactions, no restrictions exist. For payments received prior to the shipment of goods, a BOK report is required if the advance payment is made more than one year before shipment of the goods. Although there are limited restrictions on export advances, there can be tax ramifications, for example, imputed interest on transactions between related parties.

Second, under the revised FETR, a resident is to report to a foreign exchange bank when borrowing foreign currency from an overseas lender, or to the MOSF if the loan exceeds US$30 million.[14]

Third, nonresidents no longer need to use a designated foreign exchange bank when making portfolio investments in the form of debt or equity securities.[15] Investments evidenced by promissory notes and commercial paper are permitted.

Fourth, it has been made easier for the Korean branch of a foreign company to repatriate liquidation proceeds. A foreign corporation may repatriate liquidation proceeds by reporting to the designated foreign exchange bank.[16] There are no restrictions on the remittance of operating funds into Korea, but remittances are to be reported by the designated foreign exchange bank to the BOK by the end of February of the calendar year following the date of remittance.[17]

C. Protection of Intellectual Property Rights

Effective May 4, 1980, Korea became a member of the Paris Convention for the Protection of Industrial Property, extending reciprocal protection for patent and trademark rights to Korean nationals and to the nationals of countries that are members of the Paris Convention. To bring the Korean statutes into conformity with the Convention, the Korean Patent Law, Utility Model Law, Design Law, and Trademark Law were all amended, effective September 1, 1981, amended again effective September 1, 1990, and then, to implement the General Agreement on Tariffs and Trade/Trade-Related Aspects of Intellectual Property Rights (GATT/TRIPs), further amended effective July 1, 1996.[18] Subsequently, with the passing of the respective free trade agreements with the European Union and the United States, the Korean Patent Law, Utility Model Law, Design Law, and Trademark Law were amended on two further occasions (effective as of July 1, 2011, and as of March 15, 2012, respectively) to bring such laws into conformity with the free trade agreements.

The term of a patent is 20 years from the Korean filing date.[19] Effective July 1, 1987, chemical substances are

[9] Foreign Exchange Transactions Law (FETL), Art. 6.
[10] FETL, Arts. 15 and 16.
[11] FETL Enforcement Decree (FETL-ED), Art. 10.
[12] FEML-ED, Art. 10 (1), Item 4.
[13] Foreign Exchange Transaction Regulations (FETR), Art. 4-8.
[14] FETR, Art. 7-14.
[15] FETR, Arts. 7-32, 7-36 and 7-38.
[16] FETR, Art. 9-37(1).
[17] FETR, Art. 9-34(2).
[18] *See* S.K. Chang, "A Brief Sketch on the Amended Statutes of the Korean Industrial Property Rights," in *Introduction to the Law and Legal System of Korea* 675–702 (S. H. Song, Ed., 1983).
[19] Patent Law, Art. 88.

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patentable. The Patent Law encompasses patents for mechanical, electrical or chemical inventions covering processes, machines, articles of manufacture, or compositions of matter, as well as improvements of the same. A utility model is covered by the Utility Model Law and a design patent is covered by the Design Law.

The term of a trademark is 10 years from the registration date and may be renewed indefinitely.[20] Although prior use is not required, use is required after registration. Failure to use a trademark may subject it to cancellation. The licensing of trademarks is permitted, and, since 1998, it has not been necessary to register licenses.[21]

The Copyright Law was enacted effective July 1, 1987.[22] The act protects the works of foreign authors as Korea accedes to international treaties providing reciprocal protection for the works of Korean nationals. Korea acceded to the Universal Copyright Convention effective October 1, 1987. In the absence of treaty coverage, foreign works are entitled to protection if first published in Korea or if published in Korea within 30 days after publication abroad, or if created by a foreign incorporated entity having its principal office in Korea. If the term of protection afforded by the foreign author's home country has expired, the Copyright Law would not afford protection of the works of the foreign author in Korea. The life of a copyright is the life of the author plus 50 years.[23] However, for works created after July 1, 2013, the life of the copyright will be extended to 70 years after the death of the author pursuant to an amendment of the Copyright Law effective July 1, 2013.

D. Fair Trade and Antitrust

The Korean Monopoly Regulation and Fair Trade Law (MRFTL) came into effect on April 1, 1981, and was entirely revised in 1990.[24] The most recent amendment to the MRFTL was on December 2, 2011.[25]

The Fair Trade Commission (FTC) is responsible for enforcing and administering the MRFTL[26] and nine other competition-related laws. The FTC is charged with advancing four mandates: promoting competition, strengthening consumers' rights, creating a competitive environment for small and medium enterprises, and restraining concentration of economic power. The FTC also has the authority to regulate certain market-controlling price maintenance activities and other matters.

The MRFTL prohibits the abuse of a market dominant position including unfair pricing, unfair output restriction, unfair business interference, unfair obstruction of entry, and unfair exclusion of competitors.[27] In determining whether an enterprise has a market dominant position, the MRFTL presumes market dominance if any enterprise in a relevant area of trade: (i) has a market share of more than 50%; or (ii) has, combined with two or fewer enterprises, a market share above 75%, where each of the relevant enterprises has a market share of at least 10%. Once the presumption is triggered, the burden shifts to the respondent to demonstrate that it does not enjoy market dominance.

There are also restrictions on business combinations in restraint of competition in the market[28] and on unfair collaborative and unfair business practices.[29]

The FTC is authorized to permit cartels for the purpose of (i) industrial rationalization, (ii) promoting research and technology development, (iii) overcoming economic depression, (iv) promoting industrial restructuring, (v) rationalizing terms of trade, and (vi) improvement of competitiveness of small and medium-sized corporations.[30] However, to qualify for one of the foregoing safe harbors, the enterprises involved must have first obtained the approval of the FTC to engage in such collaborative behavior. Without such prior approval, an enterprise involved in unfair collaborative acts may not seek protection under the MRFTL.[31]

Perhaps of greatest interest to foreign business people are the provisions dealing with "international agreements." Until April 1, 1995, prior clearance from the FTC was required for technology license agreements, copyright license agreements and import agency agreements. This requirement has been repealed. Nevertheless, a person may request the FTC to review an international agreement, including intellectual property license agreements, copyright agreements, know-how license agreements, franchise agreements, joint R&D agreements, import agency agreements and joint venture agreements, to determine in advance whether it has unfair provisions.[32]

The MRFTL restricts corporate acquisitions by large company groups. Once a group has been designated a "large company group," as defined under the MRFTL, certain mergers and acquisitions are tightly regulated. For example, a company that belongs to a large company group may not acquire stock in subsidiary companies which own stocks of the company.[33]

Reporting requirements are also imposed on certain extraterritorial mergers and acquisitions that might have effects in Korea. One or both of the parties, as the case may be, to such a merger or acquisition is to file a business combination report with the FTC.[34] The FTC applies the filing requirements if the following conditions are met: (i) one party's total assets or sales are 200 billion *won* or more on a worldwide basis and the other party's total assets or sales are 20 billion *won* or more; and (ii) the total sales in or into Korea of each of the parties to the transaction (as determined by total affiliated company sales in Korea, not necessarily limited to the company at issue) are 20 billion *won* or more.[35]

[20] Trademark Law, Law No. 4210, Jan. 13, 1990, as amended, Art. 42.

[21] Trademark Law, Law No. 5355, Aug. 22, 1997, removed Art. 73(1)(1).

[22] In relation to computer programs, the Computer Program Protection Law was separately enacted effective July 1, 1987, but was later integrated into the Copyright Law effective July 23, 2009.

[23] Copyright Law, Law No. 10807, June 30, 2011, as amended, Art. 39.

[24] Law No. 4198 (1990).

[25] Law No. 11119 (2011).

[26] Monopoly Regulation and Fair Trade Law (MRFTL), Art. 35.

[27] MRFTL, Arts. 3-2 and 4.

[28] MRFTL, Arts. 7 and 12.

[29] MRFTL, Arts. 19 through 24.

[30] MRFTL, Art. 19; MRFTL Enforcement Decree (MRFTL-ED), Arts. 24 through 31.

[31] MRFTL-ED, Art. 24.

[32] MRFTL, Art. 33. The FTC promulgated guidelines, "Types and Criteria of Unfair Business Practices in International Agreements," on Apr. 21, 1998. However, the guidelines were abolished on Aug. 21, 2009.

[33] MRFTL, Art. 9.

[34] MRFTL, Arts. 7 and 12.

[35] MRFTL-ED, Art. 18.

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E. Labor Law

All of the provisions of the Labor Standards Act (LSA) apply to employers with five or more employees. Some of its provisions apply to employers with fewer than five employees, as specified by presidential decree.[36]

The LSA establishes minimum standards. Any terms of an employment contract that do not meet its requirements are null and void, and are deemed automatically replaced by the pertinent LSA provisions. The LSA's scope is broad. The following is a brief summary of its salient provisions:

(i) Wages must be paid directly, regularly, and in full, once or more per salary pay period on a fixed day;

(ii) Each employer must maintain a register of employees and a wage ledger in a prescribed form;[37]

(iii) No employee may be dismissed, suspended, transferred or punished without just cause;[38]

(iv) An employee must be given 30 days notice of dismissal or 30 days wages in lieu of notice;[39]

(v) Employees must be paid 70% of their average wages during suspension due to business reasons, unless the suspension is for "unavoidable reasons," verified as provided by the LSA;[40]

(vi) The employer must pay compensation for job-related illness or injury;[41] and

(vii) An employer must pay severance pay to terminated employees at the rate of at least 30 days average wages (a defined term) for each year of continuous service. No discrimination in severance pay is allowed on the basis of sex, nationality, religion or social status. Severance pay is due on termination for any reason (i.e., death, retirement, resignation or discharge).

A workplace having 10 or more employees is required to file rules of employment with the local labor office. The rules must set forth, among other things, working hours, leave, rest periods, holidays, shift schedules, compensation, promotion, retirement, employee expenses, employee education, safety and health rules, accident compensation, commendations and penalties.[42]

The Male-Female Equal Employment Treatment Law, which prohibits sex discrimination in employment, came into effect on April 1, 1988.[43]

Minimum wage requirements are set pursuant to the Minimum Wage Law.[44]

Effective March 13, 1997, the LSA was revised to provide for (among other things): severance pay in the form of an annuity; flexible working hours over a 44-hour week; layoffs permitted for reasonable cause; and provision for part-time employees.

The Protection of Fixed-Term and Part-Time Employees Act (PFPEA)[45] was enacted on July 1, 2007, to enhance labor flexibility in the market and extended protection against discrimination to non-regular workers. Under the PFPEA, a fixed-term employee who has worked for the same employer for more than two years is presumed to be a regular employee with an indefinite term contract. Further, part-time employees enjoy the same protections as regular workers with respect to termination and, in most cases, prorated benefits. Their wages, period of employment and working hours must be specified in writing.

The Trade Union and Labor Relations Adjustment Act was also revised, effective as of July 1, 2011, to provide for multiple unions in a workplace from the effective date.

The regular work week has 40 hours. This requirement was applied first to companies engaged in certain industries and employing a certain number of employees, but as of July 1, 2011, it applies to all workplaces having five employees or more.

A pension system was instituted pursuant to the National Pension Law, effective January 1, 1988.[46] Employers hiring one or more persons must subscribe to the National Pension Plan.[47] Employers and employees are each required to contribute 4.5% of the standard monthly wage (a defined term).

An employer of one or more persons is required to subscribe to the medical care insurance program under the Medical Care Insurance Law.[48]

An employer of one or more persons is required to subscribe to the governmental Industrial Accident Compensation Insurance plan. Certain types of employers are exempt from this requirement. In general, an employer must provide medical care and/or compensation to an employee injured on the job or who becomes ill as a result of employment.[49]

Under the Unemployment Insurance Act,[50] all employers are required to subscribe to the government's unemployment insurance program. The premium for unemployment coverage is 1.1% of salary, half of which is borne by the employer and half by the employee. The premium for the "employment stability fund" and the "vocational skills development fund" varies depending on the number of employees, ranging from 0.25% to 0.8% of salary, all of which is borne by the employer.

Korea has entered into social security agreements with Australia, Austria, Belgium, Bulgaria, Canada, China, (former) Czechoslovakia, Denmark, France, Germany, Hungary, India, Iran, Ireland, Italy, Japan, Mongolia, the Netherlands, Poland, Romania, Slovakia, the United Kingdom, the United States, and Uzbekistan, covering the Korean National Pension Plan and analogous benefit systems in the other contracting states. The agreements with Australia, Austria, Belgium, Bulgaria, Canada, (former) Czechoslovakia, Denmark, France, Germany,

[36] LSA, Art. 11; Labor Standard Act Enforcement Decree (LSA-ED), Art. 7.
[37] LSA, Arts. 41 and 48.
[38] LSA, Art. 23.
[39] LSA, Art. 26.
[40] LSA, Art. 46.
[41] LSA, Arts. 78 through 92.
[42] LSA, Art. 93.
[43] Law No. 3989 (1987), as amended.
[44] Law No. 3927 (1986), as amended.
[45] Law No. 8074 (2007), as amended.
[46] Law No. 3902 (1986), as amended.
[47] National Pension Law Enforcement Decree (NPL-ED), Art. 19.
[48] Law No. 4728 (1994), as amended.
[49] Law No. 4826 (1994), as amended.
[50] Law No. 4644 (1993), as amended.

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Hungary, India, Ireland, Poland, Romania, Slovakia, and the United States, are totalization agreements. The agreements with China, Iran, Italy, Japan, Mongolia, the Netherlands, the United Kingdom, and Uzbekistan provide only for the elimination of dual coverage.

Temporary employment agencies licensed by the Ministry of Employment and Labor (MOEL) are now authorized to dispatch employees to the workplace of another employer up to two years under the Protection of Dispatched Workers Act (PDWA).[51] The presidential decree of the PDWA specifies 32 categories of employment (e.g., drivers, security guards, cleaners, telephone switchboard operators, cooks, parking lot attendants, delivery men, telemarketers, etc.) in which dispatched workers under labor supply arrangements may be employed. If an employer uses dispatched workers for jobs not included in the 32 permitted categories, for more than two years or from the labor supply agency which is licensed by MOEL, the service recipient employer will be obligated to hire such improperly deployed dispatched workers.

F. Imports and Exports

Effective January 1, 1997, the import license and export license system was fundamentally revised, eliminating the requirement for import and export licenses except where required by the provisions of an international convention, or to protect the environment, and for certain other specified reasons. Payment terms continue to be regulated under the FETL. Foreign traders must obtain a registration number from the Korean Traders' Association.

The procedures for importing and exporting are regulated under the Foreign Trade Law (FTL)[52] and the FETL. In addition, World Trade Organization (WTO) agreements apply. Korea became a member of the WTO on January 1, 1995. The FTL specifies certain “free trades” that are to be under the trader's responsibility and thus not regulated.[53]

Traders are required to obtain an ID number from the Korea International Trade Association, submitting a valid tax registration certificate.[54] All imports and exports are processed through the Korea Customs Service Electronic Data Interchange (EDI) system. As a general matter, imports do not require approval, but advance approval is required for specified products, such as certain pharmaceuticals and electronic gauges.[55]

Note: Since the establishment of the Free Trade Agreement (FTA) Roadmap in 2003, Korea has actively engaged in FTA negotiations with over 50 countries, becoming one of the most prominent advocates for FTAs in the world. With Korea's free trade agreements with the European Union and the United States in effect as of July 2011 and March 2012 respectively, only several months away from each other, the momentum for change in the international trade dynamics involving Korea has reached its pinnacle. As a consequence, the need for the affected industries to formulate business strategies based on reliable projections and accurate assessments has never been stronger.

G. Securities Regulations

1. General

Since May 25, 1998, foreign investors have been free to invest in stocks, bonds, derivatives and money market instruments. These liberalization measures were introduced with the object of helping overcome the financial crisis of 1997. Before joining the OECD in October 1996, Korea's original timetable for fully liberalizing its financial markets was set for year-end 2000. But with the sudden onset of the financial crisis, the process of liberalization and market opening was accelerated with the subsequent adoption of the IMF program in December 1997.[56]

The purchase of shares of a Korean company for purposes of participating in its management is regulated under the FIPL;[57] the domestic market for publicly traded securities is regulated under the Financial Investment Services and Capital Markets Act (FSCMA), pursuant to which the Korean Exchange (KRX) was established.

The Korean Stock Price Index (KOSPI) is an index of shares of all companies listed on the KRX and is computed on an aggregate value basis. Under this method, the market capitalization of all listed companies is aggregated and, subject to certain adjustments, this aggregated amount is expressed as a percentage of the aggregate market capitalization of all listed companies as of the base date of January 4, 1980.

With certain exceptions, daily upward and downward movements in share prices of any category of shares are limited under the KRX rules to 15% of the previous day's closing price.

The brokerage commission rate on equity transactions may be determined by the transacting parties. However, securities companies currently charge commissions on equity transactions at a maximum rate of 0.5% of the sales amount, as a matter of custom.

Subject to certain exceptions, a securities transaction tax is imposed at the rate of 0.5% (in the case of transactions outside the KRX) or 0.3% (in the case of transactions on the KRX) of sales proceeds.

2. Securities Related Organizations

Two main types of regulators oversee the Korean securities market. One group consists of government regulatory bodies: MOSF and the Financial Supervisory Commission (FSC). The FSC's executive arm is the Finance Supervisory Service. Under the FSC, the Securities and Futures Commission (SFC) was set up to oversee the securities and futures market.

The other group is composed of self-regulatory organizations, such as the Korea Financial Investment Association (KOFIA) and the KRX.

[51] Law No. 5512 (Feb. 20, 1998), in effect since July 1, 1998.

[52] Law No. 3895 (1986), as entirely amended by Law No. 5211 (1996), as subsequently amended.

[53] Foreign Trade Law (FTL), Art. 10.

[54] Foreign Trade Management Regulation, Art. 24.

[55] FTL, Art. 11(1).

[56] The Korea Securities Dealers Association, “Securities Market in Korea,” (Feb. 1999), pp. 145-146. In 2009 the Korea Securities Dealers Association (KSDA) was integrated into the Korea Financial Investment Association: http://eng.kofia.or.kr/index.do.

[57] Known, as of Feb. 1, 1997, as the “Foreign Investment and Foreign Capital Inducement Law,” which was replaced by the Foreign Investment Promotion Law (FIPL), effective Nov. 17, 1998.

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The Korea Securities Finance Corporation (KSFC) is the central source of securities credit in Korea. The Korea Securities Depository (KSD) is to serve as a sole central securities depository in Korea, conducting the clearing and settlement of securities by maintaining accounts and making book entries without the actual movement of paper certificates.

3. Foreign Investment in Korean Securities

In principle, foreign investors may purchase any type of securities. However, acquisition of stock issued by companies belonging to certain industries, such as the telecommunications, printed press, broadcasting industries, etc., is subject to a ceiling amount and, in other cases (such as the Korea Gas Corporation), there may be restrictions in the articles of incorporation of such domestic companies limiting the amount of investment by foreign investors.

The FSCMA provides that the acquisition of listed stock by a foreign investor shall be acquired, in principle, only through the KRX with limited exceptions. If an exception is applicable, the acquirer must obtain prior approval from the FSC by claiming that an exception applies.

Securities purchased by foreign investors are to be deposited with securities companies, the KSD, foreign exchange banks or foreign depository institutions that are internationally recognized.

Since May 3, 1996, the KOSPI stock price index futures market has been open to investors, including foreign investors.[58]

Hostile takeovers of Korean companies by foreigners have been allowed since May 1998 by a revision to the then Foreign Investment and Foreign Capital Inducement Law. Before February 1998, if any foreign person purchased 10% or more of a listed company's shares, it was required to obtain prior approval from the company's board of directors. In February 1998, this regulation was relaxed and the previous board approval remained necessary only when an acquisition of shares exceeded one-third of the company's total outstanding shares. In May 1998, the board approval requirement was repealed.[59] Under the FIPL a foreign investor should still file a foreign capital report in advance with an authorized bank when it purchases 10% or more of the total voting shares of an existing Korean company or purchases any percentage interest with a view to influencing the operations of the Korean company.[60]

4. Investment Procedures

A foreign investor that wishes to invest in domestic securities traded on the KRX must register with the Financial Supervisory Service (FSS) prior to making any investment. On registration, an investment registration card is issued. The card must be presented each time the foreign investor opens a brokerage account with a securities company. A foreign person may appoint one or more standing proxies to exercise shareholders' rights, apply to change a name in the shareholders' register, place an order to sell or purchase shares, or engage in any other matters relating to the foregoing if the foreigner does not engage in these activities itself.

A foreign investor that intends to acquire shares must open a foreign currency account and a *won* account with a designated foreign exchange bank.[61]

No governmental approval is required for foreign investors to receive or retain in Korea dividends from, or the *won* proceeds of the sale of, any shares. Such funds must be deposited in a *won* account. Funds in an investor's *won* account may be transferred to its foreign currency account without restriction and can be repatriated without restriction. In addition, funds in the *won* account may be used for future investment in securities.

[58] Korea Securities Dealer Association, Securities Market in Korea (Feb. 1999), p. 150.

[59] *Id.*

[60] FIPL, Art. 6(1); Foreign Investment Promotion Law Enforcement Decree (FIPL-ED), Art. 2(2).

[61] Foreign Exchange Transactions Regulations (FETR), Arts. 7-36 through 7-39.

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III. Forms of Doing Business in Korea

The presence of a foreign enterprise in Korea usually takes one of four forms: an agency, a liaison office, a branch or a subsidiary.[62]

A. Agency

The appointment and maintenance of an agent in Korea are primarily matters of contract. Nevertheless, a principal is required to pay a terminated agent "reasonable compensation" for business developed by the agent if such business development will benefit the principal after the termination of such agent, unless the termination is based on the agent's breach.[63]

Subject to the statutes that regulate all contracts (e.g., Civil Code and the Monopoly Regulation and Fair Trade Law (MRFTL)), the relationship with an agent can be defined by an agency agreement. Exclusive and nonexclusive arrangements as well as territorial restrictions are possible. The rules for determining the circumstances under which an agent binds its principal are set forth in Articles 114 through 136 of the Civil Code.

Whether the activities of an agent may subject the principal to Korean taxation is an issue of Korean tax law subject to relevant treaties (see V, A, below).

B. Liaison Office

The term "liaison office" is not found in the Korean Commercial Code or Civil Code, but is generally used to refer to an office that engages in nontaxable liaison activities of a preliminary or auxiliary nature. If such an office maintains liaison status, it must report its existence to a foreign exchange bank, although it is not required to be registered with the recording office of a district court.[64]

A liaison office may be used only for conducting liaison activities exclusively for the legal entity of which it is a part. It may not engage in any activities for profit. Permissible activities include: the purchase of goods; storing or displaying goods not for sale; advertising; the collection and supply of information; scientific research; and arranging for goods to be processed by other persons, so long as such activities are conducted for the entity of which the liaison office is a part.[65] Although a liaison office may conduct liaison-type activities on behalf of its own entity, if it conducts such activities on behalf of another party, including an affiliate, it will lose its liaison status and will have to be registered as a taxable branch office.

Since a liaison office does not conduct income-producing activities, it is not subject to the income or corporation tax and need not file tax returns.

However, a liaison office does have certain obligations to cooperate with the government. It must, first of all, withhold taxes when paying income subject to withholding taxes to corporations or individuals. Second, a liaison office must file reports of payment schedules within prescribed time limits when paying certain income to corporations or individuals. From 2022 onwards, a liaison office must also file a report on the operation of the office by February 10 of each fiscal year, including information on the lease, employees and operating funds, status of the headquarters of the foreign corporation, etc. To meet these obligations, the liaison office may obtain a nontaxpayer's identification number from the tax office, although this is not legally required. A liaison office does not have an obligation to collect value added tax (VAT) for services it provides on behalf of its own entity.

Comment: Lack of a court registry may cause some legal and practical problems for a liaison office. The representative of a liaison office that is not registered with the court must, in many cases, act in his or her individual capacity and not as the representative of a juridical entity. To avoid this problem, an enterprise may wish to register its liaison office with the court even though this is not legally required.

C. Branch Office

A branch office is required to report its existence with a foreign exchange bank and must also register with a local district court and local tax office.[66] Licenses for particular business activities are also required.

Branch offices, other than those offices registered as branches that engage only in liaison-type activities for their own entities, constitute taxable domestic business entities. See V, below.

D. Subsidiary

Until recently, when forming entities in Korea, the two most popular types of entities chosen by foreign and domestic companies as well as foreign investors have been *chusik hoesa* and *yuhan hoesa*, each of which is described in detail below. However, with the amendment of the Commercial Code, which took effect on April 15, 2012, a new type of entity, the *yuhan chaekim hoesa*, modeled after the limited liability company in the United States, became available. All of the entity types set forth above provide limited liability to the shareholders or members having equity interest in the relevant entities and, therefore, the liability of the shareholders or members of the entities are limited to the capital amounts they have invested in such entities.

Comment: The Commercial Code has other forms of company such as *hapmyung hoesa* and *habja hoesa*. These forms originated from *offene Handelsgesellschaft* and *Kommanditgesellschaft*, respectively, under German law. Since the members are to take unlimited liability on company business, foreign corporations are not allowed to use these forms of company.

1. Chusik Hoesa (CH) and Yuhan Hoesa (YH)

When establishing an entity in Korea, foreign investors have preferred to use a joint-stock company — the *chusik hoesa* — because it is considered more prestigious than a private company — the *yuhan hoesa* — which is associated principally with small family-owned businesses. However, because of certain advantages of using a *yuhan hoesa* (e.g., ability to con-

[62] *See* Kim, "Legal Forms of Doing Business in Korea," 2 *Korean J. Comp. L.* 58 (1974).

[63] Korean Commercial Code, Art. 92-2.

[64] FETR, Art. 9-33(1).

[65] CTL, Art. 94(4).

[66] FETR, Art. 7-77(2)(1).

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trol the change of equity holders, flexibility in respect of corporate structure such as no mandatory requirement to have a board of directors or an auditor, fewer requirements for disclosure of a company's financial/accounting information, etc.), some foreign investors have chosen to use *yuhan hoesas.* In addition, a *yuhan hoesa* can be an attractive alternative in case it is preferable to have a company treated as a partnership or branch for U.S. tax purposes. In particular, under the so-called "check-the-box" regulations of the United States, it may be possible to elect to treat a *yuhan hoesa* as a partnership or branch for U.S. tax purposes, and such election would not be possible in the case of a *chusik hoesa*, which is expressly mentioned in the relevant regulations as an ineligible entity. However, for Korean tax purposes, a *yuhan hoesa* is taxed at the entity level as well as the owner level.

2. Yuhan Chaekim Hoesa (YCH)

As of April 15, 2012, a new type of entity called the *yuhan chaekim hoesa* was introduced in Korea. A YCH acknowledges limited liability of its members while providing greater flexibility in terms of corporate formalities, management and corporate structure. While there are certain restrictions on the transfer of a membership interest in a YCH under the Commercial Code, the membership interest in the YCH may be freely transferred if the articles of incorporation of the YCH allow such transfer. In addition, there is no minimum capital amount required for establishing a YCH. Also, similar to a *yuhan hoesa,* there is no mandatory requirement to have a board of directors or an auditor and the members of a YCH may take any action by written consent in lieu of a formal meeting.

Furthermore, unlike a *chusik hoesa* or a *yuhan hoesa*, a YCH can be managed by an entity (as opposed to an individual) and can be converted to a *chusik hoesa* upon approval by its members. In terms of taxation, unlike limited liability companies in the United States, under the current Korean tax law, a YCH is not treated as a pass-through entity and, therefore, is taxed at the entity level as well as at the owner level.

3. Incorporation Process

After the execution of the articles of incorporation, a foreign investor has to file a foreign investment report with a foreign exchange bank in Korea and hold the first meeting of shareholders/members to appoint directors and/or a corporate representative. Thereafter, the foreign investor must register the new entity with the court registry and the local tax office. To register with the local tax office, the new entity must have a lease agreement in place.

For a *chusik hoesa*, *yuhan hoesa* and *yuhan chaekim hoesa*, there is no minimum capital required. Nevertheless, regardless of the corporate entity form, to qualify as a foreign direct investment under the Foreign Investment Promotion Law, a foreign investor should, among others, invest a minimum amount of 100 million *won* (approximately US$ 87,000).

4. Liquidation

The process of liquidating a *chusik hoesa* and other corporate entities, including the YCH, is governed by the provisions of the CC. The directors of the company become liquidators by operation of law, unless otherwise specified in the articles of incorporation or unless other liquidators are appointed by the shareholders.[67]

The liquidators must register with the commercial recording office of the district court[68] and must report to the court the cause of dissolution, the date of dissolution, and the names and addresses of the liquidators within two weeks after appointment.[69]

The liquidators must prepare a statement of assets and liabilities and a balance sheet for review by the company auditor, approval by the shareholders and submission to the court.[70]

Notice of liquidation is required to be given to each creditor known to the company by specific notice, and to unknown creditors by public notice published twice during a two-month period beginning within two months after the liquidators are appointed. Creditors must be given a period of not less than two months to report their claims.[71] During this period, no claim may be paid except with court approval.[72]

After the period for reporting claims has elapsed, the liquidators must pay the reported claims and distribute the remaining assets among the shareholders in proportion to their holdings.[73] Although this is not required by statute, as a matter of practice, the plan for distribution is submitted for shareholder approval.

The liquidators must prepare and submit to the shareholders for approval the financial statements showing transactions carried out up to the completion of liquidation.[74] When approval is granted, the liquidators are discharged.[75]

The completion of the liquidation must be registered with the commercial recording office of the district court within two weeks from the date on which shareholder approval is obtained.[76]

The books and "important documents" pertaining to the business and the liquidation of the company must be preserved for 10 years from the date on which the completion of the liquidation is registered with the commercial recording office. Accounting vouchers and similar records must be kept for at least five years.[77]

Income arising from a liquidation is subject to corporation tax. The income to be recognized on liquidation is computed by deducting the book value of shareholders' equity, as of the date of registration of the liquidation, from the value of the remaining assets.[78] This income must be reported to the tax office within three months from the date on which the value of the remaining assets is determined.[79] Corporation tax at ordinary rates is payable when the return is filed.[80] The date on which the val-

[67] CC, Art. 531.
[68] CC, Arts. 253 and 542.
[69] CC, Art. 532.
[70] CC, Art. 533.
[71] CC, Art. 535.
[72] CC, Art. 536.
[73] CC, Art. 538.
[74] CC, Art. 540(1).
[75] CC, Art. 540(2).
[76] CC, Arts. 264 and 542.
[77] CC, Art. 541.
[78] CTL, Art. 79(1).
[79] CTL, Art. 84(1)(1).
[80] CTL, Arts. 83 and 86.

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ue of the remaining assets is determined is the date on which all assets have been sold or distributed to the shareholders.[81]

The liquidator is required to withhold tax on dividends deemed to arise as a result of the distribution of proceeds that exceed basis.[82] The liquidator, as a withholding agent, has a secondary liability for any taxes of the liquidating company that he fails to withhold and pay to the tax office.[83]

5. Mergers

A merger causes the dissolution of one or more companies. The details of a merger are required to be stipulated in a written agreement, which must be approved by the shareholders of the companies involved.[84] The CC distinguishes between mergers by way of acquisition and mergers through which a new entity is created. The matters required to be included in agreements for the two categories of merger are listed in the statute.[85]

In the case of merger by acquisition, the directors of the surviving company must convene a general meeting of shareholders or directors to report on the merger as soon as the procedures have been completed for notifying creditors and consolidating or disposing of stock.[86]

If a new company is to be created, an inaugural general meeting of shareholders of the new company is to be convened without delay after completion of the procedures for notifying creditors and consolidating or disposing of shares.[87]

A merger must be registered with the commercial recording office of the district court that has jurisdiction over the head office of the surviving or newly created corporation within two weeks of the general shareholders' meeting. Branches must be registered within three weeks of that meeting.[88] An action challenging a merger may be brought by any shareholder, director, statutory auditor, liquidator, administrator in bankruptcy, or creditor of any company involved in the merger within six months of the registration of the merger.[89]

A simplified procedure for merger applies if unanimous consent was obtained from the merged company, or if the surviving company ends up owning 90% or more of the stock of the merged company.[90] There may be a small-scale merger when the surviving company issues 10% or less of its total stock to the merged company's shareholders or boot paid in an amount that is 5% or less of the surviving company's total assets.[91] In the case of both these types of merger, a board of directors, rather than the shareholders, may approve the merger plan.

Effective July 1, 2010, a merger in principle is considered a taxable transfer of assets and liabilities of the merged company to a surviving company or a new company. However, if certain requirements are satisfied, any such gain from the transfer can be deferred until the surviving company or the new company sells or depreciates the assets. Unlike in the case of a liquidation of a company, the liquidation income, if any, is no longer taxable in case of a merger. If the value of consideration received by the shareholders of the merged company exceeds the cost basis of the shares in the merged company, the difference is considered divided income. However, as in the case of the gain on the transfer of assets, if certain requirements are satisfied, there is no deemed dividend income issue.

The surviving company or the new company incorporated as a result of the merger is liable for the payment of taxes attributed to the merged company.[92]

6. Insolvency Regimes

A new consolidated insolvency law called the Debtor Rehabilitation and Bankruptcy Law (DRBL) became effective on April 1, 2006. The DRBL repealed the four previous insolvency-related laws and consolidated the proceedings thereunder into the following two insolvency regimes: (a) rehabilitation proceedings under Chapter 2 of the DRBL primarily for the rehabilitation of insolvent business entities; and (b) bankruptcy proceedings under Chapter 3 of the DRBL for the liquidation of insolvent business entities and individuals. As such, under the DRBL, there are mainly two proceedings for the insolvency of business entities: (i) Chapter 2 rehabilitation proceedings and (ii) Chapter 3 bankruptcy proceedings.

In line with the international efforts for harmonization of cross-border insolvency regimes, the DRBL discarded the principle of territoriality that was applicable under the previous insolvency laws and adopted the so-called modified principle of universality.[93] In addition, the DRBL includes new provisions in Chapter 5, which address, among other matters, the recognition and enforcement of foreign insolvency proceedings in Korea, the outbound effect of Korean insolvency proceedings on assets located in a foreign country and the rule of payment adjustment in concurrent insolvency proceedings (the hotchpot rule).

Korea offers another insolvency-related law called the Corporate Restructuring Promotion Law (CRPL). This law took effect on May 19, 2011, with certain changes to its predecessor, which expired on December 31, 2010. Generally, the CRPL applies only to debt owed by an insolvent company to certain Korean financial institutions (including Korean branches of certain foreign financial institutions) which are rescheduled pursuant to out-of-court workout arrangements governed by the CRPL.

a. Rehabilitation Proceedings Under Chapter 2 of the DRBL

A debtor company, creditors holding claims amounting to 10% or more of the debtor company's paid-in capital or shareholders holding 10% or more of the debtor company's total issued and outstanding shares, may file for the commencement of the rehabilitation proceeding against the debtor company. A

[81] Corporation Tax Law Enforcement Decree (CTL-ED), Art. 124(3).
[82] CTL, Art. 16(1)(4).
[83] National Tax Basic Law (NTBL), Art. 38.
[84] CC, Art. 522.
[85] CC, Arts. 523 and 524.
[86] CC, Art. 526.
[87] CC, Art. 527.
[88] CC, Art. 528(1).
[89] CC, Art. 529.
[90] CC, Art. 527-2.
[91] CC, Art. 527-3.
[92] CTL-ED, Art. 127(2).
[93] It is understood that the DRBL has adopted legislation based on the UNCITRAL Model Law on Cross-Border Insolvency.

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rehabilitation proceeding commences only when the court issues a separate commencement order in response to the filing.[94]

Upon commencement of the rehabilitation proceeding, in principle, the court will appoint a receiver.[95] In general, the court will appoint the existing management (e.g., a representative director) of the debtor company to act as the receiver in the rehabilitation proceedings, unless the insolvency of the debtor company was caused by the existing management, in which case the court will appoint an independent receiver. The receiver has the power to conduct all of the debtor's business and manage all of its property, subject to the court's supervision.

When an application for the commencement of a rehabilitation proceeding has been filed with the court, the court may issue, upon petition by an interested party or at its discretion, a preservation order within seven days from the filing and will determine whether to commence the rehabilitation proceeding.

Upon commencement of the rehabilitation proceedings, the receiver will prepare lists of claims held by the creditors. In Chapter 2 rehabilitation proceedings, creditors are classified into three basic categories: (i) creditors with unsecured rehabilitation claims; (ii) creditors with secured rehabilitation claims; and (iii) creditors with common benefit claims. Creditors with either secured or unsecured rehabilitation claims are subject to rehabilitation proceedings and generally may not receive payment or repayment of their respective claims (with certain exceptions, including set-off of claims that are exercised within certain periods permitted under the DRBL) other than as provided for in the rehabilitation plan.

A rehabilitation plan may call for rescheduling of the debtor's debt over a period not to exceed, in principle, 10 years, except when corporate debentures are issued pursuant to the rehabilitation plan. Any secured rehabilitation claims and unsecured rehabilitation claims which are not recognized under the court-approved rehabilitation plan would be irrevocably extinguished even if the rehabilitation proceedings are subsequently terminated. If payment under the court-approved rehabilitation plan has commenced, the court shall, upon petition by an interested party or at its discretion, terminate the rehabilitation proceedings early, unless there is an impediment to the implementation of the rehabilitation plan.

If it becomes apparent, either before or after the court approves the rehabilitation plan, that the debtor cannot be rehabilitated, the court may, in its sole discretion or upon request by the receiver or a creditor, issue an order to discontinue the rehabilitation proceedings. Once the rehabilitation proceedings are discontinued due to the debtor's failure to comply with the rehabilitation plan, the court may declare the debtor bankrupt and liquidate the debtor.

[94] The court is required to render its decision on whether to commence a rehabilitation proceeding within one month after the filing of a petition for commencement of a rehabilitation proceeding.

[95] If the debtor is an individual, a small- or medium-size company, etc., the court may choose not to appoint a receiver in its discretion. In such case, the existing management maintains control of the company as if it were appointed as a receiver.

b. Bankruptcy Proceedings Under Chapter 3 of the DRBL

Bankruptcy proceedings governed by Chapter 3 of the DRBL are court-administered proceedings designed to liquidate an insolvent debtor's assets. The bankruptcy proceedings are analogous to Chapter 7 proceedings of the U.S. Bankruptcy Code.

The bankruptcy proceedings formally begin upon adjudication by the court that the debtor is "bankrupt" after the filing of a petition for the bankruptcy proceeding by the debtor company itself or by its creditors. The adjudication of bankruptcy also has the effect of staying all creditors that have unsecured bankruptcy claims from exercising or otherwise enforcing their claims against the bankruptcy estate (with certain exceptions, including set-off claims that are permitted by the DRBL). Even before the formal adjudication of bankruptcy, the court is empowered to issue preservation orders preventing creditors that have unsecured bankruptcy claims from enforcing their claims.

The bankruptcy trustee appointed by the court will be vested with the exclusive right to manage and dispose of the bankruptcy estate, and to conduct an investigation and assessment of the bankruptcy estate.

Subject to certain statutory limitations and approval by the court, the bankruptcy trustee has the power to liquidate the bankruptcy estate, and to determine the manner and timing of such liquidation. The bankruptcy trustee distributes the proceeds from the liquidation of the bankruptcy estate to the creditors according to the priority of their claims and, with regard to the claims of the same priority, in proportion to their claim amounts. The distribution then proceeds in several stages, and when the bankruptcy estate has been fully realized, the bankruptcy trustee will make the final distribution.

In bankruptcy proceedings, creditors are generally divided into creditors with bankruptcy estate claims and creditors with unsecured bankruptcy claims. Unsecured bankruptcy claims are subject to the bankruptcy proceedings and repaid from the distributions made by the bankruptcy trustee. However, bankruptcy estate claims are repaid from time to time from the bankruptcy estate. Unlike rehabilitation proceedings, enforcement of security interest in the debtor's assets is not subject to bankruptcy proceedings except for certain procedural limitations. Thus, the proceeds recovered from such enforcement may be applied to the repayment of the secured claims regardless of the bankruptcy proceeding.

E. Partnerships

The Korean entity closest to a partnership, as this term is understood in the United States, is the *chohap* under the Civil Code. Members of the c*hohap* bear unlimited liability. Few Korean businesses, except for small ventures, are conducted in this form. A *chohap* is not a legal entity for tax purposes, but contracts that bind the *chohap* members may be made in the *chohap* name. *Chohaps* are formed and regulated almost entirely by contract. Corporations may be members of a *chohap*. *Chohap* assets are held in common, each member having an undivided interest in each asset. Another contractual arrangement called *ikmyung chohap*, similar to a silent partnership, consisting of silent partner(s) with limited liability and general partner(s) with unlimited liability, is regulated under the Korean Commercial Code.

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Beginning on April 15, 2012, under the Korean Commercial Code, a new type of entity called the *hapja chohap*, modeled after the U.S. limited partnership, was introduced in Korea. The *hapja chohap* consists of general partner(s) and limited partner(s). It must be registered with the commercial recording office of the district court. However, like the *chohap*, the *hapja chohap* is not a juridical entity.

All *chohaps*, *ikmyung chohaps* and *hapja chohaps* are subject to a separate tax regime for partnerships introduced effective January 1, 2009. See XV, Q, 4, below.

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IV. Tax System and Principal Taxes

A. In General

The Korean tax system has undergone frequent revisions in recent years. Tax reforms have been instituted in 1976, 1981, 1999 and almost every year thereafter. The 1976 legislation created a value added tax (VAT) and special consumption tax to replace eight taxes that had previously been applied to business activities. In 1996, the Income Tax Law (ITL), which governs income taxes of individuals, was extensively revised. In 1999, the Corporation Tax Law (CTL) was entirely rewritten and the Tax Exemption Reduction and Control Law (TERCL) was replaced by the Tax Incentive Limitation Law (TILL).

Currently, the principal taxes affecting business enterprises in Korea are the corporation tax, the individual income tax, the VAT, customs duties, and the local income tax surcharge levied on the corporation tax and on the individual income tax.

The taxation of real estate was previously regulated by three statutes that had been introduced in 1990: the aggregate land tax, the land excess profits tax, and the recovery of benefits from development tax. The land excess property tax was repealed in 1998 after the Constitutional Court struck down portions of it.[96] In 2005, in connection with a general policy of reforming taxes affecting real estate, the aggregate consolidated real estate tax was introduced as a national tax, while the aggregate land tax (a local tax) was integrated into a property tax under the Local Tax Law (LTL).[97]

The authors focus their attention on the corporation tax, the individual income tax and the VAT, the three taxes of primary concern to entrepreneurs in Korea. Taxes affecting real estate and the gift and estate taxes are also covered. The customs tax system, although important to business enterprises, is beyond the scope of this work.

Tax collections constitute the Korean government's largest source of revenue. Of these, the taxes on goods and services produce the most revenue, followed by the taxes on income.

1. National Taxes

The national taxes listed below are levied by the central government.

Direct Taxes	**Indirect Taxes**
Individual income tax	VAT
Corporation tax	Individual excise tax[98]
Inheritance and gift tax	Transportation energy environment tax
Aggregate real estate tax	Liquor tax
Assets revaluation tax (repealed, but portions are grandfathered)	Stamp tax
	Securities transaction tax
	Customs duties
	Agricultural and fishery communities special tax
	Education tax

2. Local Taxes

Local taxes are levied by the following administrative districts: Special Cities (Seoul, Pusan, Taegu, Taejeon, Incheon, Ulsan and Kwangju); Provinces; Special City Precincts (*ku*); and ordinary Cities and Counties (*kun*). Local taxes are categorized as either "ordinary" taxes or "earmarked" taxes. Effective from January 1, 2011, certain previous local taxes were combined into other taxes or abolished.

3. Special City Taxes

Ordinary Taxes	**Earmarked Taxes**
Acquisition tax	Regional resources and facility tax
Leisure tax	Education tax
Tobacco consumption tax	
Local consumption tax	
Inhabitant tax	
Local income tax	
Automobile tax	

4. Provincial Taxes

Ordinary Taxes	**Earmarked Taxes**
Acquisition tax	Regional resources and facility tax
Registration and license tax	Education tax
Leisure tax	
Local consumption tax	

5. Precinct Taxes

Ordinary Taxes	**Earmarked Taxes**
Registration and license tax	
Property tax	

6. City and County Taxes

Ordinary Taxes	**Earmarked Taxes**
Inhabitant tax	
Property tax	
Automobile tax	

[96] Decision 92 Hunba 49, 52 (1994).

[97] Law No. 7332 (Jan. 5, 2005) on the Local Tax Law (LTL), which integrated the previous aggregate land tax into a property tax, and Law No. 7328 (Jan. 5, 2005) introduced the Aggregate Consolidated Real Estate Tax Law.

[98] On Dec. 31, 2007, the name of the law was changed from Special Excise Tax to Individual Excise Tax, while the subject matter of the tax remained unchanged. The excise tax still applies to jewelry, high-class watches, automobiles, fuel oil and gas, golf course fees, and casino and horse race fees.

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Local income tax
Tobacco consumption tax

B. Administration of the Tax System

The Tax Bureau of the Ministry of Strategy and Finance (MOSF) is responsible for drafting tax laws, negotiating international tax treaties and preparing the tax revenue section of the national budget.

The National Tax Service (NTS), an agency of the MOSF, is in charge of the assessment and collection of internal taxes. There are seven regional tax offices, 135 district tax offices under the NTS. (Before 2000, the NTS was called the National Tax Administration, or NTA.)

During the course of a tax audit, a taxpayer may ask his attorney to be present. After a field audit is complete, but before issuing a tax payment notice, the tax inspectors issue a notice of outcome of tax audit. Upon receipt of the notice of outcome of tax audit, the taxpayer may bring the matter to the district, regional or national tax office by filing a review of adequacy of tax imposition (RATI).[99] Effective January 1, 2009, the separate committees that dealt with RATI cases and administrative appeals at the district, regional and national levels have been consolidated into a single National Tax Deliberation Committee.[100]

If tax is assessed by a Tax Payment Notice, the appeal of a contested tax assessment may begin at the district tax office level or at the level of the regional office of the NTS, or the taxpayer may ask for a review directly from the NTS. Alternatively, the taxpayer has the right to file an appeal with the Tax Tribunal, an independent agency of the Prime Minister's Office separate from the NTS. If the decision of the NTS Appeal Bureau or the Tax Tribunal is adverse to the taxpayer, the taxpayer may file an action with the Administrative Court, at which point the issue will be reviewed *de novo.* An appeal from the Administrative Court may be taken to the High Court and then to the Supreme Court.[101]

An alternative procedure is to appeal a tax assessment directly to the Board of Audit and Inspection, an independent agency directly under the president. An unfavorable ruling before this body may be reviewed by the Administrative Court with a right of appeal to the High Court and the Supreme Court. This appeal procedure is not often used. The primary function of the Board of Audit and Inspection is to investigate the operations of other government bodies. Its power to review tax assessments is only a small part of its authority. The Tax Tribunal, on the other hand, is involved exclusively in the hearing of tax appeals.

A taxpayer is entitled to interest at the statutory rate (currently at 1.2% p.a.) on any refunds found to be owed to the taxpayer. Interest runs from the due date of the payment, or actual payment date, whichever is later, until the date a vested right to the refund is created at law.[102]

In addition to the remedial procedures available under Korean law, a resident taxpayer may request the NTS Assistant Commissioner (International), the competent authority of Korea, to initiate the mutual agreement procedure (MAP) (also referred to as "competent authority assistance procedure") if the taxpayer believes that a foreign tax authority in a jurisdiction with which Korea has a tax treaty in force has taken a position in contravention of the provisions of the treaty.[103] Pursuant to this procedure, the taxpayer may request that the district tax office delay issuance of a tax payment notice, or extend the time to pay tax after a tax payment notice has been issued. Further, the limitation period for taxpayers to make appeals to NTS or the Tax Tribunal is tolled while the case is pending at the mutual agreement procedure. (It should be noted that, effective May 2006, taxpayers no longer need to file a request pursuant to Article 50(1) of the International Tax Coordination Law (ITCL).) The settlement at the competent authority level must be enforced, irrespective of the running of the statute of limitations, within one year from the date notice of outcome of its tax audit to a taxpayer before issuing a tax payment notice. This gives the taxpayer an opportunity to file a request for review of adequacy of tax imposition with the district, regional or national tax office within 30 days after receipt of the settlement.[104] Furthermore, a provision was added in Article 43 of the ITCL to provide the legal basis for mandatory binding arbitration arrangements. The rule goes into effect when the relevant tax treaty provides for such arbitration mechanism.

The competent authority must inform the taxpayer of the result within 15 days from the day following the closing date of the MAP. The taxpayer must then inform the NTS, within two months from the date of receipt of the notification, as to whether the taxpayer (i) consents to the terms mutually agreed to by the competent authorities and (ii) withdraws the court appeal if the taxpayer had both filed an appeal with the court and requested a MAP. If the taxpayer (i) refuses to consent to the terms mutually agreed to by the competent authorities, (ii) does not withdraw the court appeal, or (iii) does not notify the NTS as required by the deadline, the taxpayer is deemed to withdraw the MAP application.

The tax assessment authority is required to issue a notice of tax audit result upon completion of the tax audit.[105]

Effective October 1, 2008, the NTS introduced an advance ruling procedure for specific transactions.[106] Different from traditional rulings, the NTS response is to be binding on the NTS, as well as on the applicant. An applicant, including a foreign company that does not have a fixed place of business, should file a form application with the NTS on a real name basis and is required to make complete disclosure of all the relevant facts, including documents. In principle, each response is to be disclosed on the NTS website, but an applicant may request that disclosure be delayed if reasonable grounds exist for a delay.

[99] National Tax Administration Notification (May 1996); NTBL, Art. 81-7.
[100] NTBL, Art. 66-2.
[101] NTBL, Art. 56(2) and Administrative Litigation Law, Law No. 3754 (1984), as amended, Art. 18(1).
[102] NTBL, Art. 52.
[103] ITCL, Arts. 42–51.
[104] NTBL, Art. 26-1(2); ITCL, Art. 51
[105] NTBL, Art. 81-12 (1).
[106] Regulation No. 1699.

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V. Taxation of Corporations

A. Domestic and Foreign Corporations

The Corporation Tax Law (CTL) was extensively revised, effective January 1, 1999. In the process, most of the section numbers in the law and the regulations were changed. The new CTL added provisions concerning mergers, corporate divisions and asset-for-asset exchanges.

1. Corporate Entities

In addition to the CTL itself, both the Commercial Code (CC)[107] and the National Tax Basic Law (NTBL)[108] contribute to the definition of taxable juridical persons. The CTL uses the term "juridical person" (*pobin*), without defining it, so it is necessary to refer to the CC to establish the scope of this term.

Traditionally, there have been four types of juridical persons under the CC: joint stock company (*chusik hoesa)*; limited company (*yuhan hoesa*); general partnership company (*hapmyung hoesa*); and limited partnership company (*habja hoesa*).[109] The most common form is the joint stock company (*chusik hoesa*, a translation of the Japanese, *kabushiki kaisha*, to which the *chusik hoesa* is similar). A fifth type, the *yuhan chaekim hoesa*, modeled after the limited liability company in the United States, has been in effect since April 15, 2012. (See III., above.)

Comment: Although the limited company (*yuhan hoesa*) is not often used, it has distinct advantages for a foreign investor and should be considered in Korean business planning, especially for joint ventures. In contrast to the rules applying in the case of a *chusik hoesa*, the transfer of limited company ownership units may be restricted by contract, changes in capital structure are comparatively easy, duration may be limited and actions may be taken with the written consent of the members of the board. In addition, a *yuhan hoesa* and *yuhan chaekim hoesa* (but not a *chusik hoesa*) may qualify for U.S. partnership treatment. See III.D., above. A *yuhan hoesa* is not required to be audited by an independent auditor, nor does it have to disclose its financial statements. A *chusuk hoesa* whose assets exceed 12 billion *won* is (with certain exceptions) required to be audited and the audited financial statements must be disclosed. From fiscal year beginning on or after November 1, 2019, a *yuhan hoesa* is also subject to an external audit.

The NTBL treats other entities, in addition to the entities described in the CC, as corporations for tax purposes. These are associations, foundations and other organizations designated by presidential decree.[110] To date, presidential decrees have added "associations, foundations and other organizations established with the permission of the appropriate authorities" and "non-profit foundations with property."[111] These provisions constitute general definitional terms and are applicable to the income tax and corporation tax laws.[112]

Comment: It should be noted that trusts and estates, which are taxable entities under U.S. law, are not included in the definition of corporations under the CTL.[113] Under Korean law, trust income is imputed to the beneficiary or settlor of the trust.[114] Estates are not taxed as entities. However, from 2021, a trust with certain qualifications can elect to be treated as a corporation and thus distributions of trust income will be treated as an income deduction.

The English word "corporation" is used in this work (instead of the phrase "juridical person") to refer to taxable entities.

2. Domestic Versus Foreign Corporations

A domestic corporation subject to the corporation tax is defined as any corporation with its head office or main business office in Korea.[115] A foreign corporation is any corporation with its head office or main place of business in a foreign country.[116] Effective January 1, 2006, any corporation with its place of effective management in Korea is defined as a domestic corporation. By virtue of this revision, a company incorporated in a "convenient jurisdiction" that has most of its management function conducted in Korea will be treated as a domestic corporation, and will be subject to Korean tax on its worldwide income.[117] This is a rule of domestic law that may be overridden by an applicable tax treaty.

B. Taxation

1. Taxation of Worldwide Income

Domestic corporations are taxable on "income accruing during the business year."[118] Foreign corporations, on the other hand, are taxable on income from Korean sources only.[119] The inference is therefore that domestic corporations are taxable on income from non-Korean sources.

The CTL definition of income for domestic corporations is comprehensive. The income of each business year is defined as gross income minus allowable deductions.[120] The term "gross income" refers to "revenues accruing from transactions that increase the value of the net assets of the corporation."[121] Amounts from capital transactions are not included in the definition of "revenues."

A 1973 case defines "revenues" to mean all amounts, other than amounts from capital transactions, that increase the "assets" as carried on the books of the corporation.[122] Such amounts do not include "unrealized appreciation," except for certain items prescribed in the law.

There are at least two reasons for concluding that "unrealized appreciation" is generally not taxed under the CTL. First, taxable revenue is limited to revenue accruing from "transac-

[107] Law No. 1000 of 1962, as amended.
[108] Law No. 2679 of 1974, as amended.
[109] CC, Art. 170.
[110] NTBL, Art. 13(1).
[111] National Tax Basic Law Enforcement Decree (NTBL-ED), Art. 8.
[112] NTBL, Art. 2(1).
[113] NTBL, Art. 1.
[114] NTBL, Art. 5.
[115] CTL, Art. 1(1).
[116] CTL, Art. 1(3).
[117] CTL, Art. 1(3).
[118] CTL, Arts. 2(1) and 3(1).
[119] CTL, Art. 2(1)(2).
[120] 131 CTL, Art. 14(1).
[121] CTL, Art. 15(1).
[122] Supreme Court Case No. 72 Nu 140 (June 29, 1973).

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tions."[123] The term "transactions" is not defined in the statute, but it would seem to require some kind of transfer or dealing. The second reason to conclude that "unrealized appreciation" is not taxed under the CTL is that increases in the book value of an enterprise have been specifically taxed under another statute, the Assets Revaluation Law (ARL), described below. Furthermore, assets may not be adjusted upward, except for inventories, portfolio securities, foreign currency assets and liabilities, and certain derivatives.[124]

As a general matter, until 2000, the ARL[125] applied a flat 3% tax to increases in the appraised value of an "enterprise."[126] Such increases were not to be deemed "profits" under the provisions of other laws, decrees and regulations.[127]

In short, one may conclude, with certain reservations, that the Korean CTL includes within the concept of income all accretions to wealth accruing from "transactions." Certain specified items of income, such as income from trust property, are exempted from taxation, but these items still fall within the definition of income.[128]

The concept of income under the CTL is different from the concept of income under the Income Tax Law (ITL). An accretion to wealth is not income of a resident individual unless it falls within one of the categories set out in the statute. A corporation, on the other hand, is taxable on all net accretions to wealth accruing from transactions except those excluded or exempted by specific statutory provisions.

One result of this scheme is that gains on all transfers are taxable in the hands of a domestic corporation unless exempted, but only gains on those transfers listed are taxable in the hands of a resident individual. For example, a resident individual is not taxed on gains from transfers of listed company stock unless the individual holds at least 3% of the company's stock or the market value of the stock is at least 10 billion *won*. Individuals are subject to a tax on capital gains from the transfer of non-listed company stock.[129] Individual investors are thus favored slightly over corporate investors in this respect. Income from virtual assets is considered as "ordinary income" for corporations and, therefore, is taxable. However, it is not regarded as taxable income for individuals, non-resident companies and non-resident individuals until December 31, 2024. From January 1, 2025, income from virtual assets will be considered as "other income" for such persons and, therefore, subject to 20% withholding tax, which may be modified depending on the applicable tax treaty.

2. *Accounting Methods*

a. *Financial and Tax Accounting*

All Korean corporate entities are required to follow generally accepted accounting principles in reporting to their shareholders. Generally accepted accounting principles are described in the Business Accounting Standards promulgated by the Financial Supervisory Commission (FSC), with the advice and consent of the Securities and Futures Commission (SFC).[130] The FSC, which operates the SFC, has delegated the responsibility of developing accounting principles to the Korea Accounting Principles Board of the Korea Accounting Institute.[131]

Article 112 of the CTL requires that all corporations practice double-entry bookkeeping for tax purposes, and the details of tax accounting are spread throughout the Presidential Decrees and Regulations under the CTL. As a matter of practice, most Korean companies maintain a single set of books to be used for both financial reporting and tax purposes. Expenses not accounted for in the books are generally not allowed as deductions from taxable income. Adjustments must be made in those situations in which the principles of tax accounting and financial accounting conflict. For example, penalty taxes may be reported as expenses for financial accounting purposes, but they are not tax-deductible items. Generally accepted accounting principles apply specifically to the timing of the recognition of income and expenses, and the valuation of assets and liabilities for tax purposes.[132]

Effective from 2011, accounting standards acceptable under the CTL include generally accepted accounting principle (GAAP) and International Financial Reporting Standards (IFRS).

b. *Timing of Recognition of Revenue and Expenses*

Korean corporations are required to account for revenue and expenses on an accrual basis. For tax purposes, recognition is determined by reference to the time at which legal rights and obligations are fixed. The rules for the recognition of revenue and expenses are set forth in detail in Article 40 of the CTL.

In the case of sales of goods and commodities, revenue is to be recognized when the goods are delivered.[133] This may be the date on which the goods are held at the delivery site, or if applicable, the date of completion of inspection.[134]

Contracts for the transfer of property in Korea frequently specify a down payment of approximately 10% of the purchase price to be followed by a 40% payment, with a final payment of the balance. In such cases, revenue is to be recognized at the time of the last payment, or the time when the transfer of title is registered, whichever is earlier.[135] In the case of installment contracts for the transfer of property, revenue and corresponding expenses are to be recognized when the payments are re-

[123] CTL, Art. 3(1); CTL-ED, Art. 11(4).

[124] CTL, Arts. 18(1) and 42; CTL-ED, Art. 73-78.

[125] Law No. 1691 of 1965, as amended, which allows revaluation up to the end of 2000 (Law No. 5531 (Apr. 1998)).

[126] Assets Revaluation Law (ARL), Arts. 5(1) and 13; Art. 38, which provided the requirement of a 25% price index increase was abolished in April 1998.

[127] ARL, Art. 27.

[128] CTL, Art. 51.

[129] ITL, Art. 94(3) and (4); Income Tax Law Enforcement Decree (ITL-ED), Art. 157(4).

[130] Authority for these regulations is found in the External Audit of Joint Stock Companies Law, Art. 13 (Law No. 3297 of 1980, as amended).

[131] Revision to the Law Concerning External Audit of Chusik Hoesa, Law No. 6108 (Jan. 2000).

[132] CTL, Art. 43.

[133] CTL-ED, Art. 68(1)(1).

[134] Corporation Tax Law Enforcement Regulation (CTL-ER), Art. 33.

[135] CTL-ED, Art. 68(1)(3).

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ceived or are to be received, whichever is earlier.[136] However, if the taxpayer recognized the income from installment contracts on an installment basis on its books, then revenue and expenses should be recognized on an installment basis for tax purposes as well. Installment contracts are defined as contracts that provide for two or more payments over a period of no less than one year from the delivery date to the last installment payment date.

Income and expenses for construction, production or the rendering of services (including, among others, advance order contracts) are to be recognized on a percentage of completion method.[137] The percentage of completion is a fraction, the numerator of which is actual expenses incurred in a fiscal period and the denominator of which is the estimated total cost and expenses anticipated at the outset of the contract, as computed pursuant to the Construction Business Accounting Standards.[138] When actual expenses cannot be determined because of a lack of accounting records or because of insufficient information or in case of an advance order contract that is performed by a certain qualified Special Purpose Company which adopts the IFRS, a taxpayer must recognize revenues and expenses in the year in which the products of the work are delivered to a customer.[139]

Interest, discounts, and other forms of consideration from the lending of funds earned by financial institutions are recognized when received, except for those received in advance (which are recognized at the time the funds are advanced).[140] However, accrued interest, except for certain minor exceptions, is recognized if it is accrued on the books. Interest, etc., received by non-financial institutions is recognized according to the timing of income recognition as specified in the Income Tax Law.

c. Fiscal Years

Until 1980, most Korean companies used the calendar year as their fiscal year. Under Article 12 of the External Audit Joint Stock Companies Act, the FSC of the Ministry of Finance (MOF) was authorized to make a recommendation to selected companies to change their fiscal years with a view to spreading out the collection of tax revenues. In response to these recommendations, many companies have changed their fiscal years. The fiscal year is set out in a company's articles of incorporation. Although it is theoretically possible to have a fiscal year of less than 12 months, most Korean companies select a 12-month period as their fiscal year.

A corporate taxpayer may change its fiscal year by filing a change report with the relevant district tax office within three months after the end of any fiscal year.[141] For example, a calendar year taxpayer wishing in 2014 to change its fiscal year from a calendar year to a fiscal year ending September 30 must file a change report by the end of March 2015. The first new fiscal period will then be from January 1, 2015, to September 30, 2015.

d. Reporting by Entity

Basically, a separate reporting by each corporation is required. However, effective from January 1, 2010, consolidated reporting is permitted to the extent that a parent company owns 90% (100% before 2023) of the subsidiaries, upon approval by the director of the relevant tax office.[142] The parent company must own 90% of voting and non-voting stock, except for stock owned by employees pursuant to an employee stock ownership plan, up to 5% of all outstanding shares of stock. All qualified subsidiaries are to be included. The election is irrevocable for the year in which made and for four years thereafter. After this period, the taxpayer may revoke the election by filling an application three months before the new fiscal year starts.[143]

e. Accounting for Leases

For leases that are entered into during the fiscal year commencing on or after January 1, 2011, tax accounting for leases is the same as that under the accounting principles. Leases falling within the definition of financing leases under the accounting principles are to be accounted for as capital assets under the tax law as well. All other leases fall within the category of operating leases for which the payments may be charged to expenses over the lease term. For leases entered into before 2011, the tax criteria for financing leases and for operating leases differed from the accounting criteria, which created unnecessary complexities for taxpayers.

Comment: The foregoing rules apply to domestic leases. In the case of cross-border leases, there is no specific rule for distinguishing a financing lease from an operating lease. The MOF has taken the position that the difference between gross lease payments and the market value of the subject equipment should be treated as a royalty.[144] The NTS (then known as the NTA) has ruled[145] that operating lease payments to a nonresident lessor not having a permanent establishment (PE) in Korea may include an interest portion that, in the case of a lessor resident in the United States, should be subject to Article 13 (Interest) of the Korea-United States tax treaty.[146] Other NTS rulings concerning foreign lessors include a decision that a financing lease should generate business profits not subject to a withholding tax, under Article 8(1) of the Korea-United States tax treaty,[147] that payment of rental for catalysts used in a petrochemical plan should be business profits under Article 8(5) of the Korea-United States tax treaty,[148] and that a Panamanian company's income from bare boat charter to a Korean company

[136] CTL-ED, Art. 68(2).

[137] CTL-ED, Art. 69(1), effective for any contract executed on or after Jan. 1, 1999.

[138] CTL-ER, Art. 34(1).

[139] CTL-ED, Art. 69(2), proviso; and CTL-ER, Art. 34(3).

[140] CTL-ED, Arts. 70(1)(1) and 111(2).

[141] CTL, Art. 7(1).

[142] CTL, Chapter 2-3.

[143] CTL, Arts. 1(6) through (10), 2(4), 3(2), 8(4), 18(9), 21(7), 63(4), 76-8 through 76-22, and 113(5).

[144] Ministry of Finance ruling, Kukjo 22601-762, July 16, 1985.

[145] Convention Between the Government of the United States of America and the Government of the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and the Encouragement of International Trade and Investment, signed on June 4, 1976 (the "Korea-United States tax treaty").

[146] Korea Tax Accountants' Institute, Sokpo Chose Charyo, No. 92-30, p. 221 (July 29, 1992); NTA Ruling, Kukil 22601-266 (May 21, 1992).

[147] Woiin 22601-2699 (Sept. 7, 1985).

[148] Kuki 22601-214, Apr. 22, 1992.

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with a title transfer at the end of the term should be viewed as business profits in its entirety.[149]

Assets purchased under long-term installment payment terms can be depreciated, irrespective of whether the taxpayer has ownership of the assets.[150] This provision provides an opportunity for double-dipping, where the lessee and lessor are in different countries and may both depreciate the same assets.

The Korea-United Kingdom tax treaty[151] treats leases of commercial, industrial or scientific equipment as royalties and permits a 2% (2.2% including surtax) withholding tax. The Korea-Germany tax treaty[152] follows the same pattern. For payments of income on leasing of commercial, industrial or scientific equipment made on or after January 1, 2013, if a relevant treaty treats such payment as royalty, a 20% rather than 2% domestic withholding rate applies. Thus, the final withholding rate would be the lesser of 20% or the treaty withholding rate.[153]

3. Calculation of Gross Income

Income for each fiscal year is defined as gross income minus expenses. Gross income is further defined as any revenue from transactions that increases the net worth of the corporation.[154]

Article 17 of the CTL excludes certain capital transactions from the definition of gross income. These items are: (i) the excess of paid-in capital over the par value of shares; (ii) gains from any reduction of paid-in capital; (iii) gains from mergers; (iv) gains from corporate divisions; and (v) gains from comprehensive transfer or exchange of shares.

Article 18 of the CTL excludes certain additional items from the definition of gross income. These items are: (i) gains from the revaluation of assets (excluding the revaluation allowed by Article 42 of the CTL, namely the revaluation of inventory, portfolio securities, foreign exchange assets, any liabilities and certain derivatives); (ii) gross income that has previously been recognized; (iii) increases in value arising from revaluation under the ARL and the revaluation difference resulting from the devaluation of certain land that has been revalued once; (iv) refunds of corporation tax and local income surtax; (v) interest accrued on national or local tax refunds; (vi) output value added tax (VAT) (representing amounts of VAT collected from customers and to be paid over to the tax office); (vii) income from relinquishment of debt; and (viii) income from donated asset to the extent of loss carryover.

The regulations allow holding companies, as defined under the fair trade law,[155] and general companies a deduction on the dividends received. The deduction rate of the latter used to be smaller than the one of the former. However, starting with dividends received from 2023, the same dividend deduction rate applies to both of them, as follows:

Ownership ratio	Deduction rate %
0-19%	30%
20-49%	80%
50% and above	100%

From January 1, 2023, dividends received by companies from foreign entities may benefit from a 95% tax exemption. This rule applies to dividends received from 10% or more owned subsidiaries held for at least six months. The 95% exemption rule does not apply to dividends received:

- By companies subject to the controlled foreign company (CFC) regime on the undistributed income of the CFC;
- From hybrid instruments; and
- By a special purpose investment vehicle for which foreign tax credit under article 57-2 of the CTL applies.

Direct and indirect tax credit allocable to the exempt dividends will not be granted.

4. Deductions from Gross Income

a. Summary of Business Expenses

Business expenses are deductible unless specifically not allowable. For fiscal years beginning on or after January 1, 1999, the following categories of expenses are specifically not allowed:

(i) Expenses arising from the following capital transactions:[156]

- Appropriated surplus, previously treated as deductible expenses (excluding performance bonuses paid in the form of treasury stock acquired pursuant to Article 165-2 of the Financial Investment Services and Capital Markets Act (FSCMA), and distributed through an employee stock association, and certain qualified stock options);[157] and
- Discounts on the issuance of capital stock.

(ii) Certain expenses arising from the payment of public imposts and levies:

- Corporation tax (including corporation tax paid to foreign governments that is eligible for a foreign tax credit), local income surtax, tax penalties and input tax under the Value-Added Tax Law (representing VAT paid by the corporation for goods and services purchased by it; see XIV., below);
- Special consumption tax, liquor tax and traffic tax accrued on products that have left the factory, but have not been sold, excluding such tax included in the sales price;

[149] Kuki 46017-702, Dec. 26, 1996.

[150] CTL-ED, Art. 24(3).

[151] Convention Between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital Gains, signed on Oct. 25, 1996 (the "Korea-United Kingdom tax treaty").

[152] Agreement Between the Federal Republic of Germany and the Republic of Korea for the Avoidance of A Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and on Capital, signed on Mar. 10, 2000 (the "Korea-Germany tax treaty").

[153] International Tax Coordination Law or ICTL, Art. 29.

[154] CTL, Art. 15(1).

[155] Under the Fair Trade Law, a holding company is a company where 50% or more of its assets consists of shares in subsidiaries in which the holding company has a stake of 30% or more.

[156] CTL, Art. 20.

[157] CTL-ED, Art. 20(1).

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• Fines, penalties (*kwataeryo, kasangum*) and expenses owing from the disposition of delinquent taxes; and

• Public imposts and fines imposed on the nonperformance of legal obligations or the violation of rules, not including fees that must be paid pursuant to law.[158]

(iii) Losses arising from the appraisal of assets except as specifically permitted by law (examples of losses that are specifically permitted are losses from the valuation of inventory, securities portfolios, foreign exchange assets and liabilities, and certain derivatives).[159]

(iv) Depreciation in excess of allowable depreciation, as prescribed by Presidential Decree.[160]

(v) Certain excessive and unjust payments as defined by Presidential Decree:[161]

• Excessive salary (bonuses paid to officers, directors and auditors of joint stock companies, and executive members and directors of partnerships and limited companies), if not supported by an internal regulation of the corporation,[162] and severance payments to officers in excess of certain limitations;[163]

• Excess benefits (except for company picnic expenses, the employer portion of national medical insurance premiums, unemployment insurance premiums and group retirement fund insurance premiums);[164]

Comment: The Ministry of Strategy and Finance (MOSF) had issued a ruling to the effect that the charges of a foreign parent to its Korean subsidiary in connection with the grant or exercise of options pursuant to a stock option plan of the parent were not deductible in Korea.[165] For accounting purposes, a Korean company was to record a stock option using either an intrinsic value-based or a fair value-based method when the option was granted. The fair value of a stock option could be computed using a financial model, such as the Black-Scholes Model.[166]

The then-MOFE's rule was repealed pursuant to Article 19 of the Presidential Decree of CTL in February 2009. Thus, a Korean subsidiary may claim a deduction to the extent of the fair value of stock issued as a result of the exercise of a stock option over what the employee pays. However, this rule applies only to charges for certain qualified foreign companies.

• Travel, education or training expenses for shareholders not employed by the corporation;

• Certain disproportionate expenses paid by a corporation in connection with a joint business or project with related corporations;[167] and

• Expenses not related to business, as further defined by Presidential Decree.

(vi) Non-business expenses:[168]

• Expenses unrelated to the business of the enterprise as specified by Presidential Decree (for example, expenses arising from the acquisition and management of assets not related to the business of the enterprise, and interest payments on loans taken out for the purpose of acquiring assets not related to the business of the enterprise); and

• Expenses incurred on the acquisition and maintenance of assets that are primarily used by persons other than the corporation, such as shareholders or shareholder officers.

(vii) Certain interest expenses:[169]

• Interest paid to unidentified lenders;

• Interest on certain construction loans during the construction period as prescribed by Presidential Decree and interest on loans with respect to which the lender is undisclosed (interest incurred during the construction or acquisition of assets should be capitalized rather than being treated as a current expense); and

• Interest on loans attributable to the holding of non-business assets or advances extended to related parties.

(viii) Certain insurance company reserves,[170] i.e., certain reserves set up by an insurance company for future distributions to policyholders, as specified by Presidential Decree.

(ix) Punitive damages[171]

• For fiscal years starting from January 1, 2018, punitive damages payments for violation of certain laws that exceed the actual damages incurred are non-deductible. If the actual damages incurred are unclear, 2/3 of the damages payment is treated as non-deductible.

b. Specific Deductions

The categories of expenses set out in (1) to (9), below, are specifically identified as deductible.

(1) Depreciation, Amortization and Depletion

The Enforcement Decrees and Regulations prescribe detailed rules for calculating the useful life and rate of depreciation of the fixed assets of a corporation. A table of depreciation rates appears in Worksheet 6.

Article 26 of the Corporation Tax Law Enforcement Decree (CTL-ED) recognizes three methods for depreciating as-

[158] CTL, Art. 21.
[159] CTL, Art. 22.
[160] CTL, Art. 23.
[161] CTL, Art. 26; CTL-ED, Arts. 43-48.
[162] CTL-ED, Art. 43.
[163] CTL-ED, Art. 44.
[164] CTL-ED, Art. 45.
[165] *Chaepo~bin* 46012-82, Apr. 23, 2002.
[166] KASB Interpretation No. 39-35 (1999).
[167] For fiscal years beginning on or after January 1, 2008, this exception affects only corporations related to each other by investment.
[168] CTL, Art. 27.
[169] CTL, Art. 28.
[170] CTL, Art. 30.
[171] CTL, Art. 21-2.

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sets: (i) the straight-line method; (ii) the declining balance method; and (iii) the unit of production method. (The CTL uses only one term, which may be translated as "depreciation," to refer to depreciation, amortization and depletion. The term "depreciation" is used here in this general sense.) Under the declining balance method, a fixed percentage rate determined based on the useful life of the asset concerned is applied to the declining balance of the book value of the asset. Under the unit of production method, the volume of a mineral actually extracted during a fiscal year is compared to the estimated total volume of the minerals to be extracted, and a *pro rata* amount of the total book value of the mineral rights concerned represents the depreciation (depletion) of the mineral right for the fiscal year involved.

Assets subject to depreciation are categorized and assigned depreciation methods as follows: (i) buildings and intangible assets — straight-line method; (ii) tangible assets (except for those used in mining) — straight-line method or declining balance method; (iii) mining rights — unit of production method or declining balance method; and (iv) tangible assets used in mining — straight-line method, declining balance method or unit of production method.[172]

The method of depreciation is determined when a corporation files its first tax return. If the corporation fails to select a method for depreciating its assets, the tax authorities will designate the method as follows: tangible fixed assets will be depreciated using the declining balance method; buildings will be depreciated using the straight-line method; intangible fixed assets will be depreciated using the straight-line method; mining rights will be depreciated using the unit of production method; and fixed assets used for mining will be depreciated using the unit of production method.[173]

The depreciation method may be changed within the ambit of the rules described above with the approval of the tax office in the following situations: (i) pursuant to a merger; (ii) if 20% or more of the shares of a domestic corporation are acquired by a foreign investor under the Foreign Investment Promotion Law (FIPL); (iii) when a taxpayer has purchased substantially all of a business that uses a different method; (iv) when it is necessary to change the depreciation method because of changes in the economic situation or the international market; or (v) when a company first adopts IFRS.[174]

Under the post-1998 rule, the CTL-ED provides useful lives by asset and by business line. All depreciable assets are grouped by asset, such as buildings, experimental equipment, and machinery, and equipment by industry classification. Each group of assets should be tested in determining allowable depreciation for a particular fiscal year. Under the previous rule introduced in 1995, depreciation was to be calculated separately for: (i) each asset group having the same useful life; (ii) assets that were written off when they should have been capitalized; and (iii) experimental and research assets.[175] Pre-1999 depreciable assets are to be depreciated under the new grouping rule.[176]

Taxpayers are free to select the useful life of any asset acquired after 1994, provided it is within 25%, up or down, of the basic useful life specified by MOSF Decree[177] (see Worksheet 6, generally, and for cases in which the 25% range does not apply, namely to experimental and research assets, and intangible assets).

The useful life of each asset is to be reported to the district tax office with the tax return for the first year of incorporation or for the year in which the asset is brought into use.[178] Assets purchased during the first half of a fiscal year are depreciated over the entire year. With respect to pre-1999 assets, a taxpayer had to file a report on useful life when he filed his 1999 corporation tax return.[179] Assets purchased during the second half of a fiscal year are depreciated over six months. Any second-hand assets start with a new useful life, irrespective of the expired useful life in the previous owner's hands.[180]

If the useful life of an asset is not reported by the taxpayer, the tax authorities apply the designated basic useful life. A 50% departure from the designated basic useful life may be approved where the taxpayer can show the following:

(i) The occurrence of serious wear, tear, corrosion or destruction due to the geographical or environmental characteristics of the location of the asset;

(ii) Where a taxpayer has been in business for three years or more, a current year utilization ratio significantly exceeding the average of such ratio for the most recent three years (the utilization ratio is either the actual production volume over the possible annual production volume or the number of actual operation days over the number of possible operation days for a year); or

(iii) Development, the expanded use of production technology and new production requiring accelerated depreciation for an existing facility.[181]

To apply for the 50% adjustment, the taxpayer should submit to a commissioner of the relevant regional tax administration an application for approval within three months after business commences or not later than three months before the end of the fiscal year for which the adjustment is to apply.[182]

Salvage value for purposes of computing allowable depreciation expenses is 10% of the acquisition cost plus any increase in book value computed pursuant to the ARL. No salvage value may be claimed for assets purchased after 1994. For assets subject to the fixed percentage of declining balance method, a 5% salvage value is built into the formula in arriving at an annual depreciation rate. The salvage value may be added to depreciation in the year in which the net book value, after deduction of accumulated depreciation expense, becomes 5% or less.[183]

The rules for determining which expenses are to be capitalized and which expenses are to be deducted from revenue in the current year are set forth in Article 31(2) of the CTL-ED

[172] CTL, Art. 26(1).
[173] CTL, Art. 26(4).
[174] CTL-ED, Art. 27(1).
[175] Pre-1999 CTL-ED, Art. 54.
[176] CTL-ED, Art. 27(1).
[177] CTL-ED, Art. 28(1)(2).
[178] CTL-ED, Art. 49(2).
[179] Addendum to Dec. 1998 CTL-ED revision, Art. 12(1).
[180] Old CTL-ED, Art. 58 was repealed as of January 1, 1999.
[181] CTL-ED, Art. 29.
[182] CTL-ED, Art. 29(2).
[183] CTL-ED, Art. 26(6) and (7).

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and Article 17 of the Corporation Tax Law Enforcement Regulation (CTL-ER). The general rule is that repair expenses made for purposes of restoring assets to their original state or for maintaining the efficiency of assets are regarded as deductible revenue expenditure, whereas repair expenses intended to extend the useful life of assets or to increase their value are regarded as capital expenditure.[184]

Expenditure on the purchase of items amounting to less than one million *won* per transaction may be treated as revenue expenditure if the expenditure is entered as expenses on the books when paid.[185] The following items are excepted from this special treatment, however: assets held in large quantities due to the nature of the business; and assets required for commencing or expanding the business.[186]

Test equipment or tools, and certain other assets may be expensed currently when brought into use. Other assets in this category include motion pictures, tools, furniture, electric appliances, gas equipment, tools and equipment for households, clocks, special equipment, and sign boards.[187]

From January 1, 2016, the deductibility of certain passenger vehicle expenses is limited, with the excess being deemed as non-business related.

The following expenses qualify under the new rules: Expenses incurred in acquiring and maintaining passenger vehicles, including depreciation, lease payments, fuel, repairs, insurance, taxes and interest expenses on finance leases. Passenger vehicles directly used to produce income for certain businesses, however, are excluded from the new deductibility criteria (e.g., passenger vehicles used by leasing companies or transportation companies).

The deductible portion of the expenses is calculated as follows:

• An "employee-use only" automobile insurance policy is required to deduct any of the qualifying expenses listed above. To maximize eligible deductions, a travel log is also recommended for each vehicle to substantiate the business-use percentage (calculated as a proportion of mileage travelled for business over total mileage). An "employee-use only" automobile insurance policy is an insurance policy that insures the vehicle only where it is used by a director or an employee of a company for the company's business and includes existing automobile insurance policies that are renewed for "employee-use only" on or after April 1, 2016.

• The following table outlines the methodology used to calculate the deductible portion of passenger vehicle related expenses under the new rules.

Conditions	Deductible Portion
Employee-use only automobile insurance policy does not exit	Nil
Employee-use only automobile insurance policy exists but a travel log is not maintained	Up to 15 million *won* per year
Employee-use only automobile insurance policy exists and a travel log is maintained	Actual expenses) x (Business-use percentage as substantiated by the travel log)

In addition to the overall limitation on the deductibility of vehicle expenses, the per vehicle cap for business-use depreciation expenses is 8 million *won* per year, with any excess carried forward to subsequent years.

The base amount of deductible depreciation subject to the 8 million limit is calculated as follows:

- Depreciation x business-use percentage as substantiated by travel log

- Where a travel log is not maintained, the business-use percentage will be 100% if the total vehicle related expenses are 10 million *won* or less. Where the total vehicle related expenses exceed 10 million *won*, the business-use percentage is calculated by dividing 10 million *won* by the total vehicle related expenses.

• Where the vehicle is leased, a portion of the lease payment (excluding insurance and taxes) will be deemed as depreciation subject to the 8 million *won* limit.

• Any deductible depreciation in excess of the annual limit may be carried forward and deducted in subsequent years when the depreciation for that year is less than 8 million *won*.

• Any loss on disposal of a passenger vehicle is also subject to the annual 8 million *won* deductibility limit.

• If the lease period expires or the vehicle is disposed of, any excess depreciation or loss on disposal carried forward may be deducted at 8 million *won* per year beginning the following fiscal year, with any balance remaining on the 10th anniversary of expiry of the lease period or disposal being deductible outright in that fiscal year.

Under the new rule, passenger vehicles must be depreciated using the straight-line method assuming a useful life of five years.

(2) Accrued Severance Pay and Pension Payments

(a) Severance Payments

On termination of employment, Korean employees are entitled by statute and by contract to lump-sum severance payments. The Labor Standards Act (LSA) provides that employers with five or more full-time employees must establish a plan in accordance with which not less than 30 days of average wages or salary times the number of years in employment must be paid as severance pay on termination of employment. This establishes minimum severance pay for qualifying employers, but it is a common practice for employers to contract with their employees to pay severance pay in excess of this minimum. Severance pay is paid to an employee in a lump sum at the time of termination of employment. (See X.B., below, for a dis-

[184] CTL-ED, Art. 31(2).
[185] CTL-ED, Art. 31(4).
[186] CTL-ED, Art. 31(4).
[187] CTL-ED, Art. 31(6).

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cussion of the taxation of an individual in receipt of such payments.)

Severance payments may be deducted by the corporation in the year in which they are paid.[188] A corporation may elect to accrue severance liabilities, except for employees covered by a defined contribution plan, subject to certain limitations. Deductions for such accruals are limited to 5% of the wage and salary income actually paid during the fiscal year concerned to employees (including officers). The accumulated amount of such deductions, less severance pay paid to the terminated employees (including officers) during a fiscal year, however, may not exceed 30% of the severance pay that would be payable if all of the employees entitled to severance pay were to terminate at the end of the fiscal year concerned.[189] This 30% threshold is to be reduced by 5% each year beginning in 2011 until it reaches zero in 2016. Additional deduction for pension reserves under the defined benefit plan will be granted in the case of pension reserves made on or after January 1, 2011, under the Retirement Pension Plan. Previous reserves required to be set aside under a severance insurance scheme were replaced by pension reserves under the defined benefit plan.

Accrued severance pay may be transferred by an employer company to a successor company on the transfer of substantially all of the business or on a statutory merger or division.[190]

A corporation may elect to contribute to a defined contribution plan instead of adopting a defined benefit plan in which case the contribution itself is treated as a deductible expense.[191] Since 1994, the severance pay provisions have applied to officers as well as other employees.[192]

(b) Pension Plan Payments

Since April 1, 1999, every employed and self-employed person in Korea has been required to contribute 9% of his or her earnings, up to 4,210,000 *won* (from July 2015) per month, to a pension plan (the "National Pension"). Employers are required to pay half of the contribution.[193] The "Severance Payment Conversion" portion of the contribution under the National Pension is regarded as part of accrued severance pay.[194] Individuals not working in a workplace with at least five employees are required to join a community pension plan.

Foreign employees in a place of work with five or more employees must subscribe to a pension plan.[195] Such foreign employees are not entitled to a refund of their pension plan contributions until they have stayed in Korea for a total of 15 years from the date of initial subscription to the pension plan.

In the absence of an agreement between Korea and the country of domicile of a foreign employee, the employee may be required to contribute to two retirement systems at the same time. The Agreement on Social Security between Korea and Canada, which contains a "totalization" feature, came into effect on May 1, 1999. Since April 1, 2001, the United States and Korea have had an Agreement on Social Security that includes a waiver for an employee of a company of one state assigned to an office in the other state for five years or less. Similar agreements were made with several other countries, including Canada, China (PRC), Germany, Hungary, Italy, Japan, Mongolia, The Netherlands, the United Kingdom and Uzbekistan.[196]

The law provides that treaty provisions may supersede the effect of the statute.[197]

(3) Bad Debt Expenses

Bad debt expenses are deductible for tax purposes only in limited circumstances and only if the taxpayer can show that the debt is in fact uncollectible. The following are deemed to be circumstances in which a debt may justifiably be considered uncollectible: (i) the bankruptcy of the debtor; (ii) judicial garnishment or attachment of the debtor's assets; (iii) criminal punishment of the debtor for a crime connected with the debt; (iv) the closure of the business operations of the debtor; (v) the death or disappearance of the debtor; (vi) the running of the statute of limitations applicable to an action on the debt; (vii) the designation of a debt as uncollectible pursuant to a corporate reorganization plan or composition plan as finalized pursuant to the Corporation Reorganization Law (CRL) or the Composition Law; and (viii) the stopping of foreclosure with respect to a debt by the court for failure of the bids to exceed a court-determined upset price pursuant to claims under Article 616 of the Civil Procedure Act.[198] The circumstances listed above at (i) through (v) do not conclusively establish that a debt is uncollectible. A debt must fall within one of these five categories and, in addition, the creditor must prove to the satisfaction of the tax office that the debt is uncollectible. The circumstances listed above at (vi), (vii) and (viii), on the other hand, are deemed to be conclusive evidence that a debt is uncollectible. The applicable statutes of limitations are as follows: most business debts, except for sales of goods, five years;[199] claims against a transport agent or a warehouse-keeper, one year;[200] bills and notes, three years;[201] checks, generally six months;[202] and loans and advance payments, generally 10 years.[203]

Comment: As a practical matter, the only time these regulations are useful to a corporation is when the applicable statute of limitations has run or when a debtor is in a corporate reorganization or composition proceeding, or has been declared bankrupt. Since 1998, when the Korean economy experienced a liquidity crisis and the volume of non-performing debts of financial institutions became substantial, Korean corporations have been forced to deal with this issue.

[188] CTL, Art. 33(1) and (2).

[189] CTL-ED, Art. 60(1) and (2); 50% reduced to 40%, effective for fiscal years beginning on or after January 1, 1999, then to 30%, effective January 1, 2010.

[190] CTL, Art. 33(3).

[191] CTL-ER, Art. 23(1).

[192] CTL, Art. 33(1).

[193] National Pension Law (NPL), Art. 75 and National Pension Law Enforcement Decree (NPL-ED), Table 1.

[194] CTL-ED, Art. 60(3).

[195] NPL, Art. 102(1).

[196] Refer to the National Pension Service's English website at http://english.nps.or.kr.

[197] NPL, Art. 102(3).

[198] CTL, Art. 34; CTL-ED, Art. 62.

[199] CC, Art. 64.

[200] CC, Arts. 121(1) and 166(1).

[201] Bills and Notes Law, Arts. 70 and 77.

[202] Checks Law, Art. 51.

[203] CC, Art. 162.

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A bad debt allowance may be claimed as an expense to the extent of the greater of:

(i) 1% of accounts receivable during a fiscal year (2% in case of specified banking institutions, including Korean branches of foreign banks);

(ii) Actual bad debt write-offs over the opening balance of accounts receivable for the year concerned; or

(iii) In the case of specified banking institutions, an allowance guideline as set by the government's finance authority.

Eligible accounts receivable include those account arising from most business transactions.[204] The bad debt allowance established in each fiscal year must be reversed in the following fiscal year and a new allowance established.

In line with a decision of the Korean Supreme Court,[205] a guideline has been promulgated permitting foreign banks to allocate bad debt allowances between tax-exempt and taxable lending activities.[206] This rule applies to loans made before 1991, when foreign banks were exempt from tax on interest and commissions from foreign currency loans.

The NTS has issued a series of rulings confirming that no deduction is allowed in connection with a debt-to-equity swap under a plan of reorganization.[207] The rulings follow Interpretation of Korea Accounting Standards No. 55-67. For accounting purposes, fair market value applies, but the tax rules continue to disallow a deduction until the debts are canceled, forgiven or relinquished. One exception is the allowing of a deduction for the difference between the original value and the present value of a claim that has been adjusted by virtue of an extension of the repayment term.[208]

(4) Donations

The term "donation" is defined to include: (i) property transferred for no consideration to a person other than a person in a special relationship to the taxpayer, as defined in Article 35(2) of the CTL-ED, where the transfer has no direct connection with the trade or business of the transferor corporation; and (ii) the difference between the fair value and the value at which property is actually transferred to a person not in a special relationship with the transferor corporation. Fair value, for this purpose, is value within 30% of actual market value.[209]

Donations are further categorized as 50% deductible, deductible within prescribed limits and non-deductible.

Fifty percent deductible (previously, fully deductible) donations may be made: (i) to the national or local governments; (ii) for national defense or war relief; and (iii) for disaster relief.[210] Effective from January 2011, the scope of 50% deductible donations expanded to include donations to certain designated nonprofit organizations, hospitals, educational institutions, and research institutions. Also, effective from July 1, 2011, donations to certain Korean schools overseas qualified under the Act on Educational Support to Korean Nationals Overseas are fully deductible.

Donations to qualified institutions, other than donations mentioned above to be 50% deductible, such as social welfare, cultural, educational, religious or medical research institutions, are subject to a limit of 10% of income for the fiscal period after deduction of the 50% deductible donations and loss carryforwards.[211] The excess is carried forward for 10 years (for five years for taxable year filed on or before December 31, 2018). Also, effective from 2011, donations to certain designated foreign institutions, such as institutions supporting Korean nationals residing in foreign countries, international cooperation institutions, etc., are deductible.

Donations not falling in any of the above categories are not deductible.[212]

(5) Business Promotion Expenses

"Entertainment expenses", renamed as "business promotion expenses" with effect from 2024, includes any business promotion expense, gratuity, or other expense of a similar nature, regardless of how it is denominated, connected with the trade or business of corporations.[213] "Confidential expenses" are no longer allowed, effective for fiscal years beginning on or after December 31, 1999.[214]

Comment: The category of confidential expenses was provided in the law in deference to certain social customs and business practices. A corporation did not have to prove that such expenditure was actually made or demonstrate for what specific purposes the funds were expended. This category gave businesses some leeway in their dealings with other businesses. On December 17, 1998, Korea ratified the Organisation for Economic Co-operation and Development (OECD) Convention on Combating Bribery of Foreign Public Officials in International Business Transactions. The National Assembly has also passed legislation implementing the OECD Convention, the Act on Preventing Bribery of Foreign Public Officials in International Business Transactions.[215] The repeal of the category of confidential expenses is in line with this international trend.

Business promotion expenses may not exceed the sum of: (i) 12 million *won* per year (36 million *won* for a small company); and (ii) the following rate of revenue:

Revenue from	Revenue to	%
0	10 billion	0.2
10 billion	50 billion	0.1
Above 50 billion		0.03

[204] CTL-ED, Art. 61.

[205] 81 Nu 241, Dec. 14, 1982.

[206] Corporation Tax Basic Guideline, Art. 6-1-32(54), renumbered as Art. 92-129(3) in November 2001.

[207] NTS ruling *Seo~I*, 46012-11089, May 24, 2002; *Po~bin* 46012-301, May 23, 2002.

[208] CTL-ED, Art. 19-2(5), effective December 2001.

[209] CTL-ED, Art. 35(2); when actual market value is unclear, an independent appraisal is necessary (CTL-ED, Art. 89).

[210] CTL, Art. 24(2); such donations should be allowed as deductions provided the taxpayer has taxable income rather than a loss, before the claim is taken into account.

[211] CTL, Art. 24(1).

[212] CTL, Art. 24(1), text.

[213] CTL, Art. 25(4).

[214] Addendum to CTL Revision of Dec. 28, 1998, Art. 9.

[215] Law No. 5588 (1998).

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Any business promotion expense that exceeds 30,000 *won* must be paid by credit card to be accepted as a qualifying business promotion expense, subject to the general limitation for deductions.[216] Effective January 1, 2009, a payment for congratulations or condolences has a limit of 200,000 *won* per instance. In addition, supporting documentation is not required for entertainment expenses paid in those countries in which a credit card is not commonly used.[217]

(6) Foreign Exchange Gains and Losses

Gains or losses from foreign exchange transactions realized during the fiscal year may be credited or charged to current income or expense.[218]

For banks, gains or losses from the translation of monetary foreign currency assets or liabilities must be recognized as income or expense for the current year. Gains or losses from valuation of currency swap and currency forward are recognized as current income or expense on an election basis. The exchange rate to be used is the average of the telegraphic transfer buying and selling rates, namely, the Basic Rate for U.S. dollars and the Arbitrated Rate for other currencies, as defined by Article 1-2(6) of the Foreign Exchange Transaction Regulations.[219] (In the Korean foreign exchange market, U.S. dollars are traded against *won* currency only, from which a market rate is generated, leading to a Basic Rate. The rates for translating *won* to currencies other than U.S. dollars are formulated from this market rate, leading to Arbitrated Rates.) Monetary foreign currency assets and liabilities include foreign currency on hand, and receivables and payables that must be settled in foreign currency under contracts.[220] Securities held may be either monetary assets or nonmonetary assets, depending on their nature and the reason for holding them. Nonmonetary foreign currency assets and liabilities are to be translated at the exchange rate prevailing on the date on which they were acquired or assumed.[221]

On an election basis, non-banks can recognize gain or loss from translation of monetary foreign currency assets and liabilities, currency swap or forward contracts for the purpose of hedging as income or expense in the current year.

An overseas branch's financial statements may be translated into *won* using one of three methods: (i) cash and bank deposits, receivables and payables may be translated at a year-end rate (all other balance sheet items being translated at the rate prevailing on the transaction date, income statement items at the rate prevailing on the transaction date, and journal entries at the rate prevailing on the voucher entry date); (ii) all balance sheet items may be translated at the year-end rate and all income statement items at the average rate prevailing for the fiscal year concerned; or (iii) both the balance sheet items and the income statement items may be translated at the year-end rate. The exchange rate to be used is an average of the buying and selling rates. Once a method is elected, no change is allowed. Gains or losses arising from either the second or the third method are not added to taxable income.[222]

(7) Deferred Charges

Certain items that are normally expensed must be capitalized and amortized over artificial useful lives, typically better to match expenses with revenues.

The categories of expenses for which charges must be deferred (and the deferral periods) are defined as follows:

(i) Development expenses: expenses that are incurred in the course of applying research findings or relevant knowledge necessary to develop a plan or design, in order to achieve substantial advancement in a process, system or service prior to commencement of commercial production or use (no more than 20 years); and

(ii) The right to use a facility after the donation of the facility to an authority: the right arises after the donation of certain facilities to the government, a local government unit or a nonprofit public corporation as set forth in Article 73 of the TILL (special deduction for donations made to a public-interest organization) or in Article 36 of the CTL-ED (deduction for donations made to enumerated nonprofit organizations) (the period of use).

Comment: Certain expenses, such as attorney's fees incurred before the commencement of operations, may not be deducted unless the incorporators provide in the articles of incorporation for such expenses to be borne by the corporation. The category of pre-incorporation expenses is limited to registration fees and taxes paid in the course of registering a corporation. A court appointed inspector is required to examine and approve other pre-incorporation expenses for which the incorporators may seek reimbursement.

For accounting purposes, there is no longer a deferred charge category. Intangible assets also include development expenses that will generate future income with certainty, and rights to use assets on an exclusive basis.[223] Intangible assets are to be amortized using the straight-line or production use method over a reasonable period, which must not exceed 20 years. An exception to the 20-year limit may be made if this is supported by a statute, decree or contract that demonstrates the economic life is longer than 20 years.

The right to use a radio frequency, airport facility, or other government facility is to be amortized over the term of the contract.[224]

(8) Valuation of Inventory

Inventory is classified as either securities held for resale, or other inventory.

Two methods are available for valuing inventory:

[216] CTL, Art. 25(2); CTL-ED, Art. 41.

[217] CTL ED, Art. 41.

[218] CTL-ED, Art. 76.

[219] CTL-ED, Art. 76(1). Before the introduction of the new rules, effective for fiscal years beginning on and after Jan. 1, 1995, the rate of exchange applicable to the translation of foreign currency credits and liabilities into *won* was, for the translation or collection of foreign currency credits, the foreign exchange buying rate and, for the translation or payment of foreign currency liabilities, the foreign exchange selling rate.

[220] Business Accounting Principle, Art. 68(2), which is generally effective for fiscal years beginning on or after Dec. 12, 1998.

[221] Business Accounting Principle, Art. 68(2).

[222] CTL Basic Guideline, Art. 2-11-10(17), renumbered as Art. 42-76(4) in November 2001.

[223] Business Accounting Principle, Art. 20, as announced on December 12, 1998.

[224] CTL-ED, Art. 26(1).

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(i) The cost pricing method; and

(ii) The lower of cost or market pricing method.

Under the cost pricing method, cost may be determined using any of the following methods:

(i) Specific identification;

(ii) First in, first out (FIFO);

(iii) Last in, first out (LIFO);

(iv) Weighted average;

(v) Moving average; or

(vi) Cost computed from retail price.[225]

Comment: A corporation may choose a monthly, quarterly or semi-annual interval for employing the LIFO, weighted average, or moving average methods.[226]

For securities, only the cost pricing method is applicable regardless of whether they are securities held as inventory or are listed. However, for securities held by certain collective investment vehicles, only the market pricing method is applicable with certain exceptions.

A corporation must file a report with the local tax office designating the method of inventory valuation and securities valuation it will use with its first corporation tax return. A corporation wishing to change its method of valuation must file a report no later than three months before the end of the fiscal year for which the change is to be effective.[227]

In the event that the taxpayer fails to designate the method of valuation of inventory as required above, or employs a method other than the one reported, or changes the method of valuation without reporting the change as required by law, the tax authorities may value the inventory using the following methods: (i) in the case of securities, the weighted average cost pricing method; (ii) in the case of real property held for resale, the specific identification cost pricing method; and (iii) in the case of all other inventory, the FIFO method.

(9) Interest Expense

Business interest expense is generally deductible in the year of accrual. Interest is not deductible, however, to the extent that it is attributable to loans that are deemed to have been used in holding the following kinds of assets:

(i) The construction of facilities such as buildings or factories;

(ii) Real property that was not used for a business purpose within the grace period (expenses associated with such interest are not deductible) (five years for bare land and two years for other real property);[228]

(iii) Real property recharacterized as non-business use within the grace period; and

(iv) Advances extended to a person in a special relationship.[229]

Effective January 1, 2005, the domestic thin capitalization rules were repealed. However, such rules continue to apply on a cross-border basis (see XIII.B., below).[230]

5. Taxable Income and Tax rates

Gross income minus deductible expenses yields either net operating loss, or income for the fiscal year.

Comment: The term "income for the fiscal year" is a term of art in the Korean statute, a translation of Korean *kaksaob-nyondo soduk*. This term is important for various allocation purposes under the Korean statute.

If the deduction of deductible expenses from gross income results in a net operating loss, no tax is due. The computation stops at this point, and the taxpayer may carry over net operating loss for 10 years (five years before fiscal year 2008).[231] If the deduction of deductible expenses from gross income results in income for the fiscal year, the taxpayer may then subtract the following items in the following order:

(i) Net operating loss from the previous 10 years. The extended loss carryover rule applies to losses that arise from fiscal years beginning on or after January 1, 2009. Any taxpayer applying the new rule should keep the relevant documents for a period of 10 years, rather than five years;[232]

From January 1, 2016, the 10-year carryforward period remains in place, but the amount of net operating losses (NOL) carryforward that can be deducted in any given year is limited to 80% of the taxable income for such year. The limitation was reduced to 70% for fiscal years starting from January 1, 2018 and to 60% for fiscal years starting from January 1, 2019. The limitation was increased back to 80% in 2023. The limitation applies to all companies other than small and medium-sized enterprises and certain companies designated by the CTL-ED.

Under the CTL-ED, however, the new limit will not apply to the following companies:

- Companies undergoing court rehabilitation procedures,
- Companies undergoing a normalization plan under the Corporate Restructuring Promotion Law,
- Companies undergoing a normalization plan under an agreement with a financial institution,
- ABS-SPC established on or before December 31, 2015.

(ii) Tax-free income attributable to the fiscal year concerned; and

(iii) Income deductions attributable to the fiscal year concerned pursuant to the TILL and other laws.

The resulting sum is defined as "taxable income."[233]

[225] CTL-ED, Art. 74(1)(1).
[226] CTL Basic Guidelines, Art. 2-16-1(29), re-renumbered as Art. 42-74(1) in November 2001.
[227] CTL-ED, Art. 74(3).
[228] CTL, Art. 27.
[229] CTL, Art. 28(1).
[230] CTL, Art. 28(2)–(4).
[231] CTL, Arts. 13 and 14.
[232] CTL, Arts. 13, 76-13(1) and 116(1) proviso.
[233] CTL, Art. 13.

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Income arising from the trust assets of a public interest trust is categorized as "tax-free income," that is, income not included in income for the fiscal year.[234]

A progressive tax rate applies to the taxable income to calculate the corporate income tax, ranging from 9% (for taxable income of up to 200 million won) to 24% (for taxable income exceeding 300 billion won). Please refer to Worksheet 1 for more details on the applicable tax rates.

6. Transactions Between Parties in a Special Relationship

For a discussion of the circumstances under which the tax authorities' may recompute income, see XIII., below.

7. Capital Gains

Gains arising from transfers of capital assets are included in a taxpayer's income for the fiscal year and are taxed at the normal corporate tax rates, with no preferential treatment applying. Instead, to prevent speculation, a special added tax (a capital gains tax) had been added in addition to the normal corporate tax. The tax was levied at the rate of 15% through December 31, 2001. The special added tax was repealed effective January 1, 2002, but a new 10% tax is now imposed on transfers of land and buildings that are located in an area where real property prices have increased substantially as determined by a MOSF Decree.[235] However, as yet, no MOSF Decree has been announced and, consequently, the 10% tax is not being levied.

A 10% tax rate applies to gains from transfers of residential property (40% for transfers of non-registered land). Effective January 1, 2007, gains from transfers of non-business land are subject to a tax rate of 10% (40% for transfers of non-registered land). This tax is to discourage speculation in real property and is to be used for a limited time period. However, the additional taxes on residential property and non-business land do not apply to (i) sales taking place through December 31, 2012, or (ii) sales of property purchased through December 31, 2012. For a small enterprise, the additional tax on residential property does not apply through December 31, 2015.

a. Excess Retained Earnings Tax

To encourage consumption by companies in order to further stimulate consumption in the economy, corporate profits above a defined threshold that are not used for specifically defined purposes (including investments in tangible/intangible assets, increases in salaries, and dividend distributions) are subject to additional taxation. Companies subject to the tax are those with equity capital exceeding 50 billion *won* (excluding small enterprises) and members of conglomerate groups subject to cross-shareholding restrictions.

Companies may elect one of two methods of taxation, which will apply for at least three years after the election.

The initial methods were the following:

A. [Current year income × (base rate of 80%) - (amount of investment + wage increase + dividend payout + mutual cooperation contribution)] × 10%

B. [Current year income × (base rate of 30%) - (wage increase + dividend payout + mutual cooperation contribution)] × 10%

From 2023, this rule only applies to companies in a business group subject to the limitations on cross-capital investment under the Monopoly Regulation and Fair Trade Act, until the fiscal year ending on December 31, 2025.

The excess retained earnings tax initially applied to fiscal years commencing on or after January 1, 2015, through the fiscal year in which December 31, 2017 fell. To encourage the employment of young workers (workers aged 15-29), in calculating the excess retained earnings, a greater weight of 150% applied to wage increases for full time young workers with respect to tax returns filed on or after February 12, 2016. Effective from fiscal years on or after January 1, 2017, the greater weight of 150% was expanded to all workers and 50% weight applied to dividend payout.

In 2017, this rule was moved to article 100-32 of the TILL with some substantive changes. Among others, the applicable tax rate is increased from 10% to 20%, the base rate is decreased from 80% to 65% (in case of method A) and from 30% to 15% (in case of method B), and dividends paid are not counted as a qualified expenditure and thus are no longer deductible from the current year income. The weight for mutual cooperation contribution is increased from 100% to 300%. In 2021, there were additional changes on the basic rate and the rule was extended to the fiscal year in which December 31, 2022 falls. Consequently, the two methods are as follows:

A. [Current year income × (base rate of 70%) - (amount of investment + 150% of wage increase + 300% of mutual cooperation contribution)] × 20%

B. [Current year income × (base rate of 15%) - (150% of wage increase + 300% of mutual cooperation contribution)] × 20%

8. Tax Credits

The Korean CTL does not employ tax credits as business incentives. Corporate tax benefits are specified under a separate law, the TILL (see XV., below). The only tax credits available under the CTL are the foreign tax credits (see XIX.B., below) and the disaster tax credits (see below). (Under the partial integration system, individual shareholders are given partial credit for corporation tax paid by a corporation before the distribution of dividends, see X.B.5., below.)

A company that loses 30% or more of its assets in certain "disasters" may claim a tax credit for the fiscal year during which the disaster occurred, measured against the percentage of total assets lost in the disaster. The tax credit extends both to taxes outstanding on the day of the disaster and to taxes to be paid for the fiscal year in which the disaster occurred.[236]

9. Filing and Payment

A corporate taxpayer must file a tax return and pay corporation tax as set out in subparagraphs a. to h., below.

[234] CTL, Arts. 13(1) and 31.

[235] CTL, Arts. 55-2 and 95-2 (effective Jan. 1, 2002).

[236] CTL, Art. 58.

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a. Corporations Required to File Tax Returns

Filing is required of:

(i) Any domestic corporation having its main office in Korea;

(ii) Any foreign corporation that maintains a domestic place of business in Korea; and

(iii) Any foreign corporation that has domestic-source income from real property.[237]

b. Kinds of Tax Returns to Be Filed

Two types of returns are required: (i) returns for each complete fiscal year; and (ii) returns for each six-month period commencing on the first day of the fiscal year of a corporate taxpayer.[238] The former are referred to as "corporate tax returns," and the latter as "semi-annual tax returns." Whenever a taxpayer's fiscal year exceeds six months, except in the case of the first fiscal year, a semi-annual as well as a corporate tax return must be filed.

c. Documents to Be Submitted

A tax return consists of a corporation tax and taxable income report form, other detailed schedules as specified in Article 82 of the CTL-ER and financial statements prepared in conformity with the Korean Business Accounting Principles. Among the financial statements required are a balance sheet, a profit and loss statement, and a statement of appropriation of earned surplus (or a statement of disposal of deficit).

Effective for fiscal years for which a tax return is filed on or after January 1, 2004, a foreign company's domestic place of business in Korea may not file a statement of appropriation of earned surplus or a statement of disposal of deficit.[239] Effective for fiscal years ending on or after December 30, 2003, a company subject to mandatory external audit is required to attach a cash flow statement.[240]

Corporate taxpayers having transactions with foreign parties in a special relationship, as defined in Article 2(1)(3) of the International Tax Coordination Law (ITCL), during the fiscal year are required to report such transactions on Forms 1 and 8 (see Worksheets 7 and 22), to be filed with the annual return. For a discussion of parties in a special relationship under the ITCL, see XIII., below.[241]

d. Deadline for Submission

A corporate taxpayer is required to file its annual tax return within three months after the end of a fiscal year.[242] Under Article 97-2(10) of the CTL-ER, corporations with revenue of over 7 billion *won* or corporations subject to external audit, etc., are required to have tax adjustments prepared by licensed professionals in order to submit an accurate and honest tax return. Corporations which have been in existence for less than two years and with current year revenue of over 300 million *won* or corporations claiming benefits under the TILL (see XV.B., below) are also required to use licensed professionals.

e. Payment on Filing of Tax Returns

As a general rule, corporation tax must be paid upon the filing of the tax return, and no later than the deadline for filing. A corporate taxpayer may elect to pay the tax on an installment basis if the corporation tax payable exceeds 10 million *won*. In such a case, a portion of the corporation tax may be deferred for one month from the date of filing of the tax return. Certain small corporations, as defined in the statute, may defer payment of tax for two months.[243]

f. Semiannual Tax Returns

A corporate taxpayer is required to file a semi-annual tax return if its fiscal period exceeds six months. Corporation tax payable on filing a semi-annual tax return is based on 50% of the corporation tax paid in the preceding fiscal period. This amount may vary if the preceding period is not a full calendar year. If a taxpayer determines that the amount of corporation tax to be paid based on the 50% rule is greater than the amount of corporation tax based on the actual profit or loss shown on its books for the pertinent six-month period, the taxpayer may file the semi-annual tax return based on its financial statements and pay corporation tax on the taxable income so computed. Filing and payment is required within two months after the end of each six-month period.[244]

g. Special Regime for Diligent Small Companies

Effective for fiscal years ending on or after July 19, 2007, through December 30, 2010, certain diligent small companies were eligible for a special tax regime. (The Korean language term is "small/medium company.") The special regime was repealed effective as of December 30, 2010.

To qualify, a small company was required to have annual revenue of 500 million *won* or less and had to satisfy at least one of the following two conditions: (1) depositing all reported revenues in a bank account; and/or (2) selling to or buying from three or fewer companies. Qualifying companies could apply a simplified computation to determine depreciation, donation and entertainment expenses; could take a 25% tax credit (15% in the Seoul metropolitan area); and, if current revenues were 115% or greater than those in the previous year, could take an additional tax credit from the tax attributable to the excess.[245] Accordingly, a qualifying company could apply a straight-line method of depreciation without electing it over the declining balance method; a useful life of five years applied to all assets (20 years for building and structures); and a first-year purchase was subject to 50% of annual allowable depreciation instead of month-based pro rata depreciation.

[237] CTL, Art. 93(1)(3).
[238] CTL, Arts. 60 and 63, respectively.
[239] CTL, Art. 97(1).
[240] CTL-ED, Art. 97(5).
[241] ITCL-ED, Art. 2, effective for fiscal years beginning on or after January 1, 1996.
[242] CTL, Art. 60, effective for fiscal years beginning on or after January 1, 1999.
[243] CTL, Art. 64; CTL-ED, Art. 101(2).
[244] CTL, Art. 63.
[245] CTL, Arts. 76-2 through 76-6.

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h. Amended Tax Returns

A taxpayer may file an amended tax return showing entitlement to a tax refund or an increase in loss within three years (effective as of fiscal years that included January 1, 2007, from the statutorily determined deadline for filing the initial tax return.[246] On the other hand, an amended tax return showing an additional tax payment or a decrease in loss may be filed at any time before the tax office advises the taxpayer of an adjustment as a result of the redetermination process.[247] Filing an amended tax return may permit the taxpayer to reduce certain tax penalties.[248]

10. Assessment

Liability for corporation tax is fixed at the time when a corporate taxpayer files its tax return. A corporate taxpayer cannot, therefore, request by way of appeal that the government rectify any error made by the taxpayer in its tax return. The only way to rectify such an error is to file an amended tax return.[249]

The government may determine the corporation tax liability of a taxpayer in certain situations, for example, in the event that a taxpayer fails to file a return, if the return is judged to be incomplete or in error, if a report required to be submitted with respect to designated types of transactions (for example, a payment or transaction report)[250] has not been submitted or if the taxpayer has not submitted statutory acquired receipts, such as credit card receipts or VAT receipts and the return appears incorrect or incomplete based on the size or type of the business.

a. Assessment by Examination

In principle, taxable income and corporation tax liability are to be determined based on the accounting books and records kept by a taxpayer. Only in limited circumstances may the government determine taxable income and corporation tax by an estimation method of assessment, as described at b., below.

In making an assessment, the tax authorities may accept the information in the returns and supporting documents filed by a taxpayer (as supplemented by the taxpayer at the request of the tax office) or they may conduct an examination of the books and records of the taxpayer on the taxpayer's premises.

b. Assessment by Estimation

The tax authorities may determine the taxable income and corporation tax liability of a taxpayer by estimation where:

(i) There are no accounting records or other evidence sufficient to determine taxable income, or where important evidence is missing or false;

(ii) The information in the records is clearly false in view of size of the facilities, number of employees, or price of raw materials, products or other goods or services; or

(iii) The information in the records is clearly false in view of the quantity of materials, electricity or other items consumed.[251]

Under the estimation method of assessment, the tax authorities may determine gross revenue based on available information, such as revenue reported by companies in similar industries, or data concerning raw materials used by the taxpayer. Once gross revenue is determined, the tax authorities apply a deemed profit rate in arriving at taxable income. Deemed profit rates are set by industrial category and announced by the National Tax Service (NTS) each year.[252]

c. Effect of Tax Adjustments on Earnings and Profits

Where certain expenses are disallowed or where certain revenues are added to taxable income, earnings and profits are affected.[253]

In the first place, a decision should be made as to whether the tax adjustment (for example, treating expenses as non-deductible) results in a distribution or retention. If the result is a distribution, it must further be determined whether the sum should be treated as deemed salary, deemed dividends, or other income or outlay, depending on the party receiving the benefit from the distribution. Earnings and profits must then be adjusted accordingly.

Transfer pricing adjustments made by the tax authorities pursuant to the rules for parties in a special relationship (see XIII.B., below) may create deemed dividends for foreign shareholders. Such adjustments, however, are not relevant in computing income of a domestic place of business of a foreign corporation.[254]

The regulation on tax adjustments to earnings and profits, Article 94-2 of the CTL-ED, was held to be unconstitutional on the grounds that its enabling legislation, Article 32(5) of the CTL, was excessively broad.[255] Since 1994, Article 32(5) of the CTL has included specific delegation of authority with respect to the treatment of secondary effects. The constitutional defect has, therefore, presumably been corrected. Pursuant to the tax law revision of December 1998, these provisions were renumbered as Article 67 of the CTL and Article 106 of the CTL-ED.

11. Additional Taxes (Penalties)

Failure to comply with the reporting and payment requirements of the CTL results in the imposition of additional tax. The term "additional tax" is a literal translation of the Korean term *kasanse*. Additional taxes under the NTBL constitute penalty taxes imposed for failure to comply with the tax laws.[256]

Most additional taxes are imposed as fixed percentages of the tax due. Time is not a factor in calculating the additional

[246] Effective for tax years including Dec. 29, 2000, and thereafter. Prior to this revision, filing used to be required within one year.

[247] NTBL, Arts. 45 and 45-2.

[248] NTBL, Art. 45.

[249] NTBL, Art. 45.

[250] CTL, Arts. 120 (submission of a payment voucher) and 121 (issuance and submission of *Keisanso*, a simple form receipt, for transactions not subject to a 10% value added tax (VAT)).

[251] CTL-ED, Art. 104.

[252] ITL-ED, Arts. 144 and 145.

[253] CTL, Art. 67; CTL-ED, Art. 106.

[254] Effective for fiscal periods beginning on and after January 1, 1996, notwithstanding the general provisions in CTL, Art. 32(5) and CTL-ED, Art. 94-2(1)(1)(c), ITCL, Art. 13 and ITCL-ED, Art. 23 apply to income adjustments on cross-border transactions. Deemed dividends, capital increases or loans may result. A taxpayer may employ cash movement to avoid such secondary effects.

[255] Constitutional Court Decision, *Taejin Tour Co. v. Pusanjin District Tax Office*, No. 93 Hun-ba 32 en bloc (Nov. 1995)).

[256] NTBL, Arts. 2(4) and 47(1).

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tax, and so additional tax is not in the nature of interest, except for the additional tax on arrears in payment of corporation tax. Additional taxes may be regarded as penalties. Nevertheless, the NTBL expressly provides that additional taxes constitute tax under the relevant laws, and not penalties or interest.[257] In accordance with this principle, the local income tax surcharge is imposed on the additional tax on the corporation tax (prior to 2014[258]) as well as on the corporation tax itself. Thus, while additional taxes may be regarded as civil penalties or sanctions, as a legal matter they are taxes. The statute specifically provides that additional taxes are not deductible for corporation tax purposes.[259]

Additional taxes are levied in the following circumstances:[260]

(i) Failure to file a tax return or any default in complying with the requirement to maintain and keep books of account: 20% of the tax due as calculated by the government (before any credit), or seven-hundredths of 1% (7/10,000) of gross revenue, whichever is greater; or, if the failure to file was caused by an unjust method, 40% of tax or 0.14% (14/10,000) of gross revenue, whichever is greater, effective for fiscal years beginning on or after January 1, 2007;[261]

(ii) Underreporting of income: 10% of the corporation tax on the taxable income not reported or, if the underreporting was caused by an unjust method, 40% of the corporation tax on the taxable income unreported by such unjust method or 0.14% (14/10,000) of gross revenue not reported, effective for fiscal years beginning on or after January 1, 2007;[262]

(iii) Arrears: 8.03% (0.022% per day) for interest accrued from February 15, 2022, is applied by a simple interest method to the tax in arrears. 9.125% (0.025% per day) for interest accrued from February 12, 2019. The rate used to be 10.95% per annum (0.03% per day) for interest accrued up to February 11, 2019, and 18.25% per annum (0.05% per day) in the case of tax returns for fiscal years beginning on or after January 1, 1999, until the fiscal year in which a filing deadline fell before January 1, 2003 (for example, a calendar year taxpayer is subject to the 18.25% rate when the tax office made adjustments to the 2001 tax as a result of a resolution reached in 2006 under the mutual agreement procedures of a tax treaty);[263]

(iv) Arrears in payment of withholding tax: the lesser of (I) 3% of the unpaid withholding tax plus 0.022% (0.025% before February 15, 2022, 0.03% before February 11, 2019) per day of unpaid withholding tax or (II) 10% of the unpaid withholding tax.[264] Before January 1, 2012, the greater of: (I) a penalty of 0.03% per day in arrears up to a maximum of 10% of the unpaid or underpaid withholding tax; or (II) 5% of the unpaid or underpaid withholding tax;[265]

(v) Failure to obtain statutorily designated receipts in a pre-formatted form from suppliers or vendors pursuant to Article 116 of the CTL: 10% of the transaction value in the case of transactions entered into in 2000, and 2% of the transaction value in the case of transactions entered into in 2001 and thereafter;[266]

(vi) Failure to submit a shareholder ledger showing changes or the inclusion of incorrect information in such a ledger: 2% (1% for reporting to be made on or after January 1, 2018) of investment value; effective for submissions due on or after January 1, 2006, the penalty is reduced by half if the required information is submitted within one month after the deadline.[267] Effective for fiscal years for which the report on shareholder ledger change is to be submitted after December 31, 2007, the scope of the shares subject to the report is limited to those held by the controlling shareholder and those shareholders who are in a special relationship with the controlling shareholder.[268] For corporations established on or after January 1, 2012, a shareholder ledger must be submitted to the tax office. Failure to do so is subject to a penalty of 0.5% of the investment amount;[269]

(vii) Failure to comply with the reporting requirements for certain transactions: 2% (1% for reporting to be made on or after January 1, 2018) of the transaction price; the penalty is reduced by half if reporting is made within one month after the deadline, effective for reporting due on or after January 1, 2006;[270] and

(viii) Failure to issue simple receipts (*keisanso*) or to maintain a list of receipts from vendors or suppliers: 1% (effective from January 1, 2012, 2% in case of false receipts) of the transaction value; effective for reports due on or after January 1, 2006, the penalty is reduced by half if the report is filed within one month after the deadline.[271]

On September 1, 2015, the South Korean Ministry of Strategy and Finance and the Ministry of Justice jointly announced an offshore tax evasion amnesty program for resident individuals and corporations to report undeclared foreign income and assets. The program will run from October 1, 2015, to March 31, 2016. Resident taxpayers who voluntarily declare and pay overdue taxes (plus 0.03% interest per day) to a regional tax office will be exempt from all other fines and may receive leniency for criminal acts.

Additional taxes may be avoided if the taxpayer is able to give a "justifiable reason" for failure to comply.[272] "Justifiable reasons" have been held to include reasonable reliance by the

[257] NTBL, Art. 47(2).
[258] From 2014, the additional tax is no longer a base for the local income tax surcharge.
[259] CTL, Art. 21(1).
[260] CTL, Art. 76.
[261] NTBL, Art. 47-2(2).
[262] NTBL, Art. 47-3.
[263] NTBL-ED, Art. 27-4.
[264] NTBL, Art. 47-5.
[265] CTL, Art. 76(2).
[266] CTL, Art. 76(5).
[267] CTL, Art. 76(6) and NTBL, Art. 48(2).
[268] CTL, Art. 119.
[269] CTL, Art. 76(3).
[270] CTL, Art. 76(7) and NTBL, Art. 48(2).
[271] CTL, Art. 76(9) and NTBL, Art. 48(2).
[272] NTBL, Art. 48(1).

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taxpayer on a tax ruling arguably relevant to the taxpayer's situation.[273]

12. Special Rules for Mergers and Corporate Divisions

Mergers and corporate divisions are taxable in principle except if they are qualified mergers and divisions, as discussed below:

(i) Prior to July 1, 2010, a surviving company could claim a deduction to the extent of merger appraisal income arising from any increase in the value of the merged company's land and buildings. The surviving company took the appreciated value of the merged company's property, pursuant to generally accepted accounting principles.[274] To qualify for this treatment, both the merging and merged companies had to have been in business for one year or more; at least 95% of the total compensation received from the surviving company by the merged company's shareholders had to consist of stock of the surviving company; and the same business had to be carried on by the surviving company by the end of the year in which the merger took place. The deferred income would be recaptured if the transferred business is discontinued within three years. Effective July 1, 2010, taxable gain upon a merger is defined to be the value of compensation such as stock and/or cash issued or paid by the surviving company to the merged company's shareholders, less net book value of the merged company's assets minus liabilities. The merged company is deemed to transfer its assets and liabilities to the surviving company, whose value shall be the value of the compensation received from the surviving company. Thus, the merged company's liquidation income is based on the excess of the value of the compensation over its book value of assets less liabilities. A surviving company may record the merged company's assets and liabilities at market value. To the extent that the value of compensation exceeds the total market value of the net assets, the surviving company may treat the excess as goodwill and may claim a deduction for the goodwill over five years through tax adjustments. Conversely, the surviving company must recognize income from negative goodwill over five years if the value of compensation is less than the market value of net assets. Only for a qualified merger, the value of the compensation is deemed to be equal to the net book value, resulting in no gain.[275] To be a qualified merger, both the merging and merged companies must have been in business for one year or longer; at least 80% of the total value of compensation received from the surviving company must be in the form of stock of the surviving company (and, effective for mergers effected on or after April 15, 2012, also shares of the parent of the surviving company due to the introduction of triangular mergers in the Korean Commercial Code); the merged company's business must be carried on by the surviving company until the end of the year in which the merger takes place; the new shares issued to old shareholders must be held at least until the end of the fiscal year in which the merger takes place; and effective for mergers taking place on or after January 1, 2018, 80% or more of the employees must be retained until the end of the fiscal year in which the merger takes place .[276] The qualified merger may be subject to recapture if the surviving company ceases the merged company's business within two years (three years for mergers effected through February 1, 2012) from the merger, or the controlling shareholder of the merged company disposes more than 50% of the surviving company's new stock within two years (three years for mergers effected through February 1, 2012) from the merger or, effective for mergers taking place on or after January 1, 2018, if the number of employees of the surviving company becomes less than 80% of the total number of employees of the surviving and merged company within three years.[277] Mergers between a parent and its 100%-owned subsidiary and, effective for mergers on or after January 1, 2017, a merger between brother/sister companies commonly owned 100% by the same Korean parent company, are treated as a qualified merger.

(ii) Prior to July 1, 2010, a surviving company could assume a merged company's loss carryover to be offset against income earned from the merged company's business after the merger when certain conditions as indicated later were satisfied.[278] The same conditions as in (i) applied. In addition, the surviving company's stock issued to the merged company's shareholders had to constitute at least 10% of the total number of outstanding shares of the surviving company. The same recapture rule as in (i) applied. The related-party requirement has been removed, so that a surviving company may set off the merged company's loss carryover against the profits earned from the business of the merged company, even in the case of a related-party merger.[279]

Prior to 2006, a surviving company that had losses while the merged company had profits could not claim its own loss carryover in a reverse merger if the merger was effected by two companies and the merging company had larger losses than the merged company, or the merging company changed its trade name to that of the merged company within two years after the merger was registered. In addition, in the case of a merger that took effect prior to January 1, 2004, the surviving company could not claim its own loss carryover in a reverse merger when the merger was effected by two companies 30% or more of the shares of each of which was owned by one person or 20% or more of the shares of one of which was owned by the other company. A surviving company was required to keep separate books for the business line in which the merged company had engaged. This requirement was relaxed for small-medium companies and for mergers between

[273] *Taehan Semu Hyophoe, Choisin Semu*, p. 6 (Aug. 21, 1992); Supreme Court Decision No. 91 Nu 9848 (Apr. 28, 1992); Seoul High Court, 90 Gu 21423 (Sept. 4, 1991).
[274] CTL, Art. 44.
[275] CTL, Art. 44.
[276] CTL, Art. 44-2.
[277] CTL, Art. 44-3.
[278] CTL, Art. 45.
[279] CTL, Art. 45.

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companies in similar business lines, which need not keep such books separate. The relaxed rule applies to mergers taking place on or after January 1, 2006.[280] Effective for mergers occurring on or after January 1, 2009, no restriction applied to the foregoing reverse merger where the merging company has larger losses than the merged company but should apply such loss to income generated from its own business, not from the business of the merged company.[281] Effective July 1, 2010, a surviving company may assume a merged company's loss carryover to be offset against income earned from the merged company's business after the merger provided the merger is a qualified merger, as defined under (i), above.[282] No other conditions are imposed. A surviving company's losses may not be deducted against the profits of the merged company.[283]

(iii) Prior to July 1, 2010, a resulting new company or merging company could claim a deduction on a corporate division or a division/merger to the extent of appraisal gains arising from the increased value of the original company's land and buildings.[284] To qualify for this treatment, the original company had to have been in business for at least five years; the new company's stock or the merging company's stock had to be distributed to the original company's shareholders on a *pro rata* basis; the original company's shareholders had to receive only stock of the new company or the merging company's stock with no boot (or at least 95% of the compensation received had to be stock in the case of a division/merger); and the new company or the merging company had to continue the business by the end of the fiscal year in which the division or a division/merger took place. The deferred income was recaptured if the business was discontinued within three years of the merger.

Between January 1, 2006, and June 30, 2010, a resulting new company or merging company that was a small-medium company, or was a company engaged in a business line similar to the merged company, could assume the loss carryover of the merged company after a corporate division or a division/merger.[285] Effective July 1, 2010, taxable gain to be recognized by an original company or merged company upon a division or division/merger is defined to be the market value of the compensation including stock less net book value of the original company's assets minus liabilities. A resulting new company or merging company may record the original company's assets and liabilities at market value. To the extent that the value of compensation exceeds the total market value of the net assets, the resulting new company or merging company may record it as goodwill and then claim a deduction for the goodwill over five years through tax adjustments. Conversely, the resulting new company or merging company must recognize income from negative goodwill over five years if the value of compensation is less than the market value of net assets. The value of the compensation is deemed to be equal to the total market value of the net assets, resulting in no gain, only in case of a qualified corporate division or division/merger. To be a qualified division or division/merger, the same conditions as discussed under (i), above, must be met. Therefore, an 80% stock requirement applies instead of 95% in case of division/merger and a 100% stock requirement applies in case of a corporate division. In addition, the *pro rata* requirement continues to apply.[286] The recapture rules in the merger situation in (i), above, and the loss carryover rules in (ii), above, apply in principle in the context of qualifying divisions or division/mergers (loss carryover rules apply only to complete divisions or division/mergers).[287]

(iv) An original company in a drop-down (*mul-jeok-bun-hal*) may claim a deduction to the extent of gains from any increase in the value of the assets dropped down to a new subsidiary in a one-step drop-down (where the original company holds a new subsidiary's stock).[288] The deferred income may be recaptured proportionately as the shares in subsidiaries are disposed of or assets dropped down to the subsidiary are disposed of. All remaining deferred income may be recaptured at once if within two years, the business is discontinued, 50% or more of the shares in the new subsidiary is disposed of or (effective for drop-downs taking place on or after January 1, 2018), if, within three years, the number of employees of the new subsidiary becomes less than 80% of the number of employees of the dropped down business unit one month before the date of registration of the drop-down.

(v) An original company in a taxable corporate division (*in-jeok-bun-hal*) should report income to the extent of compensation received by its shareholders as a result of a corporate division or a division/merger, reduced by the original company's net worth attributed to the business units dropped down to a new or merging company.[289] This rule applies when the original company survives after a corporate division or a division/merger and has similar tax ramifications for the computation of the merged company's liquidation income.

(vi) A surviving company in a merger, a new resulting company in a corporate division, and a merging company in a division/merger may take over the other company's tax attributes in a qualifying merger or qualifying corporate division.[290] All of the timing difference items are transferred to the surviving company, new company or merging company. Conversely, no timing difference items are transferred in case of a taxable merger or taxable corporate division.

[280] CTL, Art. 45.
[281] CTL, Art. 45(1)(3).
[282] CTL, Art. 45(2).
[283] CTL, Art. 45(1).
[284] CTL, Art. 46.
[285] CTL, Art. 48-2.
[286] CTL, Art. 46-3.
[287] CTL, Arts. 46 through 46-5.
[288] CTL, Art. 47.
[289] CTL, Art. 46.
[290] CTL, Art. 46-3(2).

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(vii) A company may defer income arising from an exchange of assets used for at least two years in the same line of business.[291]

(viii) A company may make a tax-deferred contribution in kind to a company, whether upon creation of a new company or upon a capital increase. Effective July 1, 2010, tax-deferral treatment is subject to the following conditions: (I) the eligible company should be in business for five years; (II) the company that received the in-kind contribution must carry out the business through the end of the fiscal year in which the contribution was made; (III) other shareholder companies, if any, with which the eligible company makes the contribution must not be in a special relationship with the eligible company; (IV) the aggregate ratio of shares held by the companies which make such tax-deferred contribution together should be 80% or more of total outstanding shares of the company receiving the contribution; and (V) such shareholders must continue to hold the shares through the end of the fiscal year in which the contribution took place.[292] A recapture rule similar to the drop-down in (iv), above, applies.

13. Capital Registration and License Tax

If a company is incorporated in Korea, it is required to pay a registration and license tax at the rate of 0.48% (including a local education surtax) on its paid-in capital to be registered with the court at the time of its incorporation and subsequent capital increases.

Since the tax base is the paid-in capital, the premium (i.e., additional paid-in capital in excess of the par value) is not subject to a registration and license tax. If a company is established in the Seoul Metropolitan Area, the registration and license tax rate is tripled from 0.48% to 1.44% (applicable to the capital injection upon incorporation and capital increases affected within five years from the date of incorporation).

14. Reporting of Foreign Financial Accounts

Domestic companies and resident individuals must report their financial assets held in foreign countries (including bank accounts, securities accounts, derivatives accounts, and virtual asset accounts) to the tax authorities. This requirement applies only if the aggregate value of the foreign financial accounts exceeds 500 million won at the end of any month during the calendar year. The report for the preceding calendar year must be filed in June of the year following the calendar year.[293]

Failure to file the report in a timely or truthful manner is subject to penalties of up to 20% (capped at 2 billion won). The penalty can be increased or decreased within a 50% range depending on the circumstances for the non-reporting/under-reporting. If the non-reporting/under-reporting amount exceeds 5 billion won, criminal charges of imprisonment of up to two years or fines between 13% to 20% could be applied.[294]

[291] CTL, Art. 50.
[292] CTL, Art. 47-2.
[293] TILL, Art.53.
[294] Tax Criminal Punishment Law, Art.16(1).

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VI. Taxation of Foreign Corporations

A. In General

A foreign corporation that neither maintains a domestic place of business in Korea nor has Korean real property is not required to file a tax return for the fiscal year concerned and is not entitled to deductions from gross income (except in the case of income from the transfer of securities, where certain acquisition costs may be deducted).[295] Such a foreign corporation is taxed by withholding of tax at source by the Korean payor at rates determined by the type of domestic-source income involved.

A foreign corporation maintaining a domestic place of business (i.e., tax presence, see V.A.2., above) in Korea or receiving real property income from Korea is required to file a tax return for each fiscal year, as described at V.B.9., above, including in its return those items of Korean domestic source income attributable to the domestic place of business. This attribution rule is in line with the provisions of most of Korea's tax treaties.[296]

Certain foreign home office expenses are allocable to domestic source income in reasonable proportion based on the value of the assets or revenue related to income from domestic sources as defined under Article 93 of the Corporation Tax Law (CTL).[297]

The allocation may be based on separate criteria for each expense item or alternatively based on the percentage of the gross revenue of the office concerned over the total gross revenue of all the offices throughout the world.[298]

Foreign bank branches are not entitled to deduct the cost of offshore funds where such funds are attributed "to the equity of the bank as a whole." Interest on funds furnished by offshore offices arising from funds other than equity may be allowed as a deduction subject to the thin capitalization rule.[299]

Guidelines have been promulgated for the computation of taxable income attributable to the permanent establishment (PE) of a foreign corporation engaged in supervision, supply or warranty services in Korea.[300] On February 6, 1995, the NTA announced that its previous Guideline on this subject, the "November 1988 Guideline," was not correct, and that henceforth a separate entity approach under an arm's-length principle would apply in determining attributable income. The NTA indicated that the November 1988 Guideline had been based on a formulary apportionment method, which is not acceptable.[301]

B. Domestic Source Income

Income from domestic sources is itemized under Article 93 of the CTL as follows:

Category 1: interest as defined in Article 16(1) of the Income Tax Law (ITL) and interest arising from other types of loans and profits from trusts, received from the national or a local government, a resident individual, a domestic corporation, the domestic place of business of a foreign corporation under Article 94 of the CTL, or any domestic place of business of a nonresident under Article 120 of the ITL, except for interest arising from loans taken out directly by the foreign place of business of a resident person or domestic corporation for use by its foreign place of business, and interest received from a foreign corporation or nonresident that clearly relates to the payor's domestic place of business in Korea and that was deducted from revenues earned from such domestic place of business. From 2023, interest from national bonds and currency stabilization bonds received by a foreign company or non-resident individual without a permanent establishment in Korea is exempt.

Category 2: dividends, as defined in Article 17(1) of the ITL, received from a domestic corporation. Furthermore, income from the sale, cancellation and redemption of collective investment securities (except for income treated as category 10), income from non-qualified collective investment securities, and income from distributions from qualified investment securities, which are to be treated as financial investment income (from income accruing on or after January 1, 2023), distributions from a trust treated as a corporation (from income accruing on or after January 1, 2021), and income from derivative linked bonds (from income accruing on or after January 1, 2023).

Category 3: income arising from the transfer, lease or other disposition of real property or real property rights located in Korea, mining rights, mineral exploration and exploitation rights and quarrying rights acquired in Korea, except for income from transfers under category 7 (see below).

Category 4: income arising from the lease of vessels, aircraft, registered vehicles, heavy equipment and industrial, commercial and scientific equipment to a resident individual, a domestic corporation or the domestic place of business of a foreign corporation under Article 94(1) and (3) of the CTL or the domestic place of business of a nonresident individual under Article 120(1) and (3) of the ITL.

Category 5: income arising from business as further defined by presidential decree: on the authority of this statutory provision, Article 132 (1) of the Corporation Tax Law Enforcement Decree (CTL-ED) was promulgated (referring in turn to Article 19 of the ITL, which specifies the types of businesses from which business income arises for individual income tax purposes) and adds further specific rules applicable to cross-border transactions. These specific rules deal with the following:

- Purchase outside Korea and sale into Korea;
- Manufacture outside Korea and sale into Korea;
- Manufacture in Korea and sale outside Korea;
- Work performed in Korea under a contract for construction, installation, assembly or other work;
- The executing of insurance contracts through certain agents in Korea;
- Advertising;

[295] CTL, Art. 91(1).

[296] Effective January 1, 1991, Korea changed its domestic law to replace the force of attraction rule with the attribution rule. See CTL, Art. 91, which was CTL, Art. 53 before 1999.

[297] CTL-ED, Arts. 129(1)(1) and 130.

[298] NTA Notice No. 18-37 (Nov. 1, 1981).

[299] CTL, Art. 129-3.

[300] NTA Ruling, *Kukil* 22630-487 (Nov. 23, 1988).

[301] *Kukil* 46501-67.

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• International outbound ocean traffic;

• International air traffic; and

• Other cross-border transactions not included in the above categories.[302]

Note: The division of income into domestic-source and foreign-source in the case of these transactions is to be computed as if two independent persons were conducting business, one inside and one outside Korea. Goods are deemed to have been transferred within Korea: (i) if the goods were located in Korea before the transfer or the transaction was managed through the domestic place of business of a foreign corporation; (ii) the contract was concluded in Korea; or (iii) acts important to the transfer took place in Korea, such as the solicitation of orders or negotiation of the contract.[303]

The NTA's internal guidelines, dated August 11, 1995, indicate that the NTA will treat only a portion of income from sales of products to Korea (or marketing income) as domestic-source income, on the basis of the functions performed and risk assumed by the domestic place of business.[304] This represents a major change from the NTA's previous position that all sales income (or marketing income), after apportioning manufacturing income to the home country jurisdiction, was to be regarded as domestic-source income. Domestic-source income arising from the sale of products to Korea and attributable to a deemed domestic place of business or PE in Korea was previously determined in accordance with formulae published by the NTA on March 22, 1990.[305] Pursuant to the "March 22 rule," the total income arising from the sale of manufactured products was to be split into marketing and manufacturing categories. For example, in the case of sales of chemical products manufactured outside Korea by a foreign taxpayer, the split was 40:60: 40% Korean-source marketing income and 60% foreign-source manufacturing income. Effective January 1, 1994, the definition of this fifth category of domestic-source income was expanded to include any income permitted to be taxed by Korea pursuant to a tax treaty.[306] However, the NTA abolished the March 22 rule on July 28, 1994.[307] The formulary apportionment method no longer applies. According to the July 1994 ruling, the tax office must apply a transfer pricing analysis even if the taxpayer does not maintain adequate books and records. Further, the ruling indicates that the tax authorities should use the exchange of information provisions of the relevant tax treaty(ies) to obtain the necessary information. The estimation method of assessment (applying a standard profit rate) is to be used only after such procedures have been exhausted.

Category 6: income arising from the provision of personal services within Korea as prescribed by Presidential Decree. Income from certain technical services provided on or after January 1, 2017, outside Korea, as designated by the Presidential Decree, is deemed to be Korean source if such income is taxable in Korea under a relevant tax treaty.

Category 7: income arising from transfers of property located in Korea as provided under Article 94 of the ITL; Article 94 covers income arising from the transfer of four categories of property:

(i) Land and buildings;

(ii) Rights associated with real property as prescribed by Presidential Decree. Article 157(3) of the Income Tax Law Enforcement Decree (ITL-ED) prescribes two categories of rights associated with real property: (a) superficies and *chonse* rights (*chonse* is a type of lease whereby the lessee deposits a sum of money for the use of the lessor during the term of the lease); and (b) rights to acquire real property;

(iii) Other property as designated by Presidential Decree. Article 158 of the ITL-ED prescribes that such transfers are: certain transfers of goodwill; transfers of corporate stock carrying with it the right to use exclusive membership facilities; and transfers of any equity interest in a corporation where 80% or more of the assets consist of real property assets and where the corporation operates a golf or ski resort or other recreational facility; and

(iv) "Real estate rich company" stock where 50% or more of the company's assets consist of real property or real property related rights as of the beginning date of the fiscal year in which the transfer takes place.

For share transfers taking place on or after January 1, 2016, for purposes of determining whether the 50% "real estate-rich" company threshold is exceeded, the value of shares in any other real estate-rich companies held by the tested company will be treated as real estate in the same ratio as the value of real estate owned by such other real estate-rich companies bears to their total assets.

In May 2001, the then Ministry of Finance and Economy (MOFE) decided to impose Korean tax on gains earned from the transfer by a U.S. shareholder of real estate rich company stock. Pursuant to a competent authority agreement between Korea and the United States, the United States accepted Korea's authority to impose such a tax in the absence of a specific clause in the Korea-United States tax treaty prohibiting such imposition. This decision was based on the reciprocity principle, the United States having applied a similar rule to "foreign real property holding company" stock.[308]

Category 8: forestry income arising from timber located in Korea.

Note: Forestry income has been deleted and merged into business income as of December 30, 2006.

Category 9: royalties, rents, or other payments of a similar nature received as compensation for use within Korea, or compensation paid from Korea, with respect to the following assets, information or rights:

• Copyrights in scholarly or creative works (including films), patent rights, trademark rights, designs, models, drawings, secret formulae or processes, film and tapes for

[302] CTL-ED, Art. 132(1).
[303] CTL-ED, Art. 132(4).
[304] *Kukil* 46501-493.
[305] NTA Ruling, *Kukil* 22630-143 (Mar. 22, 1990).
[306] CTL, Art. 55(1)(5), which became CTL, Art. 93(1)(5) in 1999.
[307] *Kukil* 46510-432.
[308] MOSF ruling, *Kukjo* 46017-89 (May 2001); Lee YS, *International Taxation* in Korean, Jokyungsa Publisher (Oct. 2001), p. 259.

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radio and television broadcasting and any other similar assets or rights; and

• Information concerning industrial, commercial or scientific knowledge, experience and skill or know-how.

For royalties paid on or after January 1, 2020, consideration for any manufacturing know-how, technical information, etc. that is part of a patent that is not registered in Korea and is used for domestic manufacturing, production, etc. is treated as "remuneration for other similar property, rights" under tax treaties, which grant the taxing rights on royalty income based on the place of use (e.g., the Korea-U.S. Tax Treaty)

Comment: It is difficult to draw a distinction between the services described in category 6 and the services associated with the use of rights described in category 9. Professional services regarded as standardized, such as the preparation of simple design drawings or services using knowledge generally held by engineers working in a particular field, are regarded as category 6 services and are subject to a 20% (22% including the local income surtax) withholding tax. Payments for the transfer of undisclosed technical information, which may be described as the provision of "know-how," are regarded as royalties under category 9 and are subject to a 20% (22% including the local income surtax) withholding tax.[309]

In September 1993, the NTA announced a guideline with respect to withholding tax on payments of software fees. Under the guideline, most software fees fall within category 9 domestic-source income, thus obligating Korean payers to withhold tax. A few exceptions to this general classification include: "canned" or "off-the-shelf" software (provided the technical level of the software is not above the level that can be developed in Korea and provided the software can be assigned to a third party without the supplier's permission being obtained); made-to-order software, where comprehensive rights (including copyrights) are transferred to the purchaser; and software bundled with hardware where the price of the software is not separable from the price of the hardware. The withholding obligation applies also to carrier media that were imported after September 27, 1989 and subjected to customs tax. Fees for software were classified as payments for know-how or payments for copyrighted software, which might result in a different withholding rate depending on the relevant treaty. For example, Article 14 of the Korea-United States tax treaty reduces the withholding rate on copyrighted software to 10%, while the rate applicable to know-how is 15%. (A 10% inhabitant surtax is added to these rates to arrive at the effective tax rate.)

In July 1994, the NTA clarified its September 1993 Guideline on software by specifying the types of software that are to be exempt from withholding tax as: operating software (such as DOS, UNIX, WINDOWS, etc.); programming language software (such as Cobol, Basic, etc.); tool software; document management software; PC graphics software; utility software; software for statistics; and multimedia software.

Effective August 1, 1994, the NTA promulgated a Corporation Tax Basic Guideline that includes rules for the taxation of intellectual property.[310] A fee paid to a foreign company for software will be classified as a copyright royalty or a know-how royalty unless it specifically falls within one of the exempt categories. The transfer of know-how is to be distinguished from the provision of personal services based on published criteria. For example, fees for the provision of engineering services that are not available in Korea constitute a know-how royalty, as do fees for plans, drawings, product specifications, formulae, process diagrams, and research reports.

The NTA appears to accept the following definition of know-how provided by the *Association des Bureaux pour la Protection de la Propriete Industrielle*, and set out in the Commentary to the 1992 Organisation for Economic Co-operation and Development (OECD) Model Tax Convention: "all the undivulged technical information, whether capable of being patented or not, that is necessary for the industrial reproduction of a product or process." One significant aspect of this definition on which Korea differs is that Korea regards "undivulged" information from its own perspective, considering that information that may be in the public domain in other countries may nevertheless be "undivulged" in Korea.

Note re Supreme Court decision of November 27, 2014: On November 27, 2014, the Korean Supreme Court rendered a decision that may affect many taxpayers with patents registered abroad. The Supreme Court ruled that fees for the use of patents registered in the United States but not in Korea should not be viewed as domestic-source income subject to Korean withholding tax (in accordance with the Korea/U.S. Tax Treaty), regardless of whether the patents were used in Korea in connection with manufacturing or sales activities.

Article 6, paragraph 3 of the U.S./Korea tax treaty states that royalties (as described in Article 14, paragraph 4) shall be treated as Korean-source income only if paid for the use of, or the right to use, defined property within Korea. As patent rights (e.g., proprietary production, usage, transfer, lending, importation, exhibition, etc.) are only effective in the country in which they are registered, in accordance with the territorial principle of patents, the Supreme Court ruled that fees received by a U.S. taxpayer for the use of patent rights should be treated as domestic-sourced income only to the extent that they are duly registered in Korea. This decision is consistent with Supreme Court decisions rendered in past years and pursuant to Article 28 of the International Tax Coordination Law.

However, the recent Supreme Court decision is significant in that it confirms that the Korea/U.S. tax treaty takes precedence over domestic tax law, even after considering recent (December 26, 2008) revisions to the Corporate Income Tax Law. Based on the 2008 amendments, income or fees derived by a foreign company for the domestic use of patents registered overseas are considered domestic-source income even if they are not registered in Korea. These revisions led to substantial tax assessments by the NTS on U.S. taxpayers.

As a result of this decision, many U.S. taxpayers will have a strong legal basis to claim refunds of withholding tax on patent royalties.

Category 10: income arising from the transfer of securities by a domestic corporation or by the domestic place of business of a foreign corporation, as designated by Presidential Decree. From 2023, capital gains from national bonds and currency stabilization bonds received by a foreign company or non-resident individual without a permanent establishment in Korea is exempt.

[309] CTL Basic Guidelines, Art. 93-132-7.
[310] CTL Basic Guidelines, Art. 93-132-8.

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Comment: Effective January 1, 1991, revisions to the Presidential Decree make it clear that the transfer outside Korea (where such transfer is not effected through a Korean broker) of Korean securities by a foreign corporation having no place of business in Korea to another foreign corporation having no place of business in Korea is not taxable, provided the transferor has not held 10% or more of the securities issued by the Korean company within the past five years. Whether this condition is satisfied is tested taking into account all the securities owned by a party in a special relationship to the transferor.[311]

Effective October 25, 1997, to encourage the transfer of funds (primarily from Japan and Hong Kong), the government promulgated revisions to Article 122(6) of the CTL-ED[312] that expand the tax exemption for gains on transfers of stock. The 10th category of domestic-source income, gains earned (by a foreign person) from the transfer of securities, is now defined to include:

(i) Gains earned from a transfer of stock or investment securities by a foreign corporation that has a domestic place of business;

(ii) Gains earned from the transfer of stock or investment securities by a foreign corporation that has no domestic place of business, provided, however, that gains from the transfer of stock or investment securities traded on the Korea Securities Exchange (including those traded over-the-counter, or in certain other special circumstances) are excluded. In addition, the exclusion applies only when the transferor and its related parties hold stock and investment securities not exceeding 25% of the total number of the issued and outstanding shares or investment securities issued by the issuing company concerned in the year when the transfer takes place and the five years prior to that year. Prior to January 1, 2000, the exclusion applied only to a transferor whose country or territory of residence provided such tax-free treatment or a tax exemption to a Korean corporation as to its holding of stock and investment securities in a manner similar to the foregoing exclusion; effective January 1, 2000, the reciprocity requirement was removed;

(iii) Gains earned from the transfer of securities other than stock and investment securities by a foreign corporation having a domestic place of business; and

(iv) Gains earned from the transfer of securities other than stock and investment securities by a foreign corporation having no domestic place of business to a domestic corporation or a domestic place of business of a foreign corporation or a nonresident.

Category 11: other income as prescribed by Presidential Decree. Article 93(11) of the CTL prescribes 10 categories of other income:

(i) Insurance proceeds, reparations and compensation for damages incurred in connection with the conduct of a business in Korea or in connection with real property or other property located in Korea;

Comment: The characterization of compensation for damages, insurance payments, and "consolation" (similar to "pain and suffering") payments as income fails to deal with the underlying question of the extent to which such payments restore the recipient to the status he was in before the damage or the extent to which payments should be characterized as increases in net wealth. It may be argued that insurance proceeds not exceeding compensation for actual damages are not income and that to that extent the provisions of this decree are *ultra vires.* Nevertheless, there have been no cases in Korea on this point, and the matter remains unresolved.

(ii) Payment or compensation paid in Korea due to breach or termination of a contract concerning property rights that exceeds the payments specified in the contract;[313]

(iii) Income accruing from the receipt of donations of property located in Korea;

(iv) Income accruing from the receipt of money, goods, or other economic benefits received as prizes from contests in Korea;

(v) Income arising from the discovery of property buried in Korea (treasure);

(vi) Income accruing from the transfer of rights created by license, permit or other similar disposition under Korean law, and from the transfer of Korean property other than real property;

(vii) Lottery winnings paid by banking institutions as part of a savings promotion scheme;

(viii) Income resulting from tax office adjustments;

(ix) For payments (e.g., damage compensation, reward, settlement, lost profits) made from Korea on or after January 1, 2020, for damages arising from the infringement of a patent that is registered overseas (but not registered in Korea) and owned by a resident of a country with which Korea has a tax treaty that provides for the taxation of royalties based on the place of use, but only to the extent that manufacturing know-how, technology, information, etc. contained in such patent is used for domestic manufacturing or production.

Comment: A taxpayer may be required to withhold tax at the rate of 20%, plus surcharges (an effective rate of 22% from 2009) on deemed other income arising from adjustments made by the tax office.

The Korean taxpayer is required to withhold tax under Article 93(11) of the CTL, absent a treaty provision preventing this treatment (for example, a provision based on Article 21, Other Income, of the OECD Model Convention treaty, which provides that items of income not dealt with in the treaty are to be taxed by the country of residence of the recipient rather than the country of source).

A taxpayer is thus exposed not only to additional corporation tax resulting from income adjustments, but

[311] CTL-ED, Art. 122(6), which became CTL-ED, Art. 132(7) in 1999.

[312] CTL-ED, Art. 132(7) as revised effective January 1, 1999.

[313] CTL-ER, Art. 67.

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also to the obligation to withhold on deemed income to its foreign related party.[314]

(x) Income earned by a foreign corporation from a disproportionate change in shares resulting from a merger, a corporate division, or an increase or reduction of capital. A foreign company is deemed to earn domestic-source income from transactions in Korea between parties in a special relationship, as set forth in XIII.A., below; and

(xi) Income from a virtual (digital) asset (for income accruing on or after January 1, 2025); and

(xii) Income arising from the receipt of economic benefits in connection with the conduct of business in Korea or the provision of personal services within Korea, or in connection with property located in Korea (including income from compensation for damages in excess of actual damages), except for income described above in (i) through (xi).

The Corporation Tax Basic Guidelines provide that contractual penalties for delay received from a Korean party by a foreign party not having a PE in Korea and damages in excess of actual damages received as compensation for claims arising from the normal course of business, are to be considered Korean-source income.[315]

Comment: These guidelines have the effect of putting what might otherwise be thought of as business profits (taxable at the rate of 2%, as described at C., below, or exempt under a treaty) into the category of "other income" taxable by withholding at the rate of 25% of gross.

C. Withholding Tax Rates

The withholding tax rates for domestic-source income not attributable to the domestic place of business of a foreign taxpayer vary by category of source income as follows.[316]

(i) For categories 4 and 5 (the leasing of vessels and vehicles, certain business income): 2%. However, for payments of income from the leasing of equipment made on or after January 1, 2013, the withholding tax rate is 20% (instead of 2%) if the relevant tax treaty treats the income as a royalty income;

(ii) For category 6 (the provision of certain personal services): 20% (3% for technical services income deemed sourced in Korea). A recipient may choose taxation on a net rather than a gross basis (see further below);

(iii) For categories 1, 2, 9 and 11 (interest, dividends, royalties, and other income): 20% for payments in these categories made on or after January 1, 2009. However, interest on bonds issued by national and local government entities and by any domestic company is subject to 14% and to 15% with respect to item (ix) of "other income";

(iv) For category 7 (real property) and category 10 (securities): 10% of the gross amount, except that, if the acquisition cost can be verified, the rate is 25% of the net gain. To substantiate the appropriateness of that taxation on the net gain, the transferor should present to the transferee, on or before the day of payment, a capital contribution receipt, transfer certificate, payment receipt or other proof of acquisition cost. Payments in these categories made on or after January 1, 2009, are subject to a 10% withholding tax rate on the gross amount, except that, if the acquisition cost can be verified, the rate is 20% of the net gain.[317]

For the rates of source country taxation applying to investment income, services income and capital gains under Korea's domestic law and tax treaties and the context for the application of those rates, see the Withholding Tax Chart.

For income from category 7 (real property), the seller has an obligation to file a tax return in addition to the buyer's obligation to withhold while the seller of category 10 (securities) does not have a filing obligation unless the seller has a PE to which income is attributable.

Comment: Because the duty to withhold lies with the transferee, the transferor may be unable to obtain a refund from the tax authorities after the withholding tax has been paid over by the transferee. The tax authorities take the position that no government action is involved in accepting the payment from the transferee. Therefore, the transferor's only remedy may be against the transferee.

A foreign corporate transferee having no domestic place of business in Korea is required to withhold tax on transfers of securities in non-publicly held Korean companies. Payment is to be made to the district tax office having jurisdiction over the head office of the Korean company the securities of which are being transferred.[318] Further, Korean securities companies are required to withhold tax with respect to transfers of securities of Korean publicly traded corporations, even if the transfers take place between nonresidents of Korea.[319] The moving average cost method applies to the calculation of the acquisition cost of stock sold by a foreign corporation.[320] No provision specifically allows the deduction of a loss on the sale of other stock in the capital gains computation. The transferor or seller is required to file a tax return paying tax in the case of a transfer of Depository Receipts, stock acquired and sold on a foreign listed market or Korean *won*-denominated securities that are traded outside Korea if the buyer did not make the withholding.[321]

No tax is required to be withheld on income arising under categories 3 and 8 (real property and timber-related income) or category 7 if the payor is a nonresident individual. Foreign per-

[314] For fiscal periods beginning on and after January 1, 1996, the Other Income treatment for interest on the deemed loan treatment on transfer pricing adjustments is specified in ITCL-ED, Art. 15(3). The Other Income treatment as such no longer applies as of August 24, 2006, when deemed loan treatment was repealed. Consequently, the adjustment will be treated as either dividend income or an increase in capital contribution. ITCL-ED, Art 23.

[315] CTL Basic Guidelines, Art. 93-132-17.

[316] CTL, Art. 98(1). A 10% local income surtax is separately charged. It should be added to the rates listed to arrive at the effective tax rate. For example, the 25% rate would become an effective rate of 27.5%. (10% × 25% = 2.5%; 25% + 2.5% = 27.5%.) Prior to 1996, the inhabitant surtax (renamed as the local income surtax) was 7.5% and the effective rate was 26.875%. See XVII.B., below.

[317] CTL, Art. 99(1)(3), (3-2) and (4).

[318] CTL, Art. 9(4), proviso; CTL-ED, Art. 7(2).

[319] CTL, Art. 59(1), proviso.

[320] CTL-ED, Art. 138.

[321] CTL, Art. 98-2(3); CTL-ED, Art. 138-2(3).

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sons receiving Korean-source income under these categories are required to file tax returns.[322]

As a separate matter from the withholding tax under Article 98(1) of the CTL referred to above, the Article 98(8) provision requires the payor (project owner) to withhold tax on payments to a foreign contractor. Payments may relate to construction, installation, assembly or other work relating to buildings, machinery or equipment, or may be payments for services rendered in connection with supervision or direction of work (business profits), or payments falling within category 6 domestic-source income (personal service income). The withholding obligation applies even if the income is attributable to the foreign contractor's domestic place of business. The obligation is waived if the foreign contractor has registered, pursuant to law, with the relevant tax office.[323]

Comment: The tax office is able to enlist the help of the Korean payor in persuading the foreign contractor to register because this will enable the Korean party to avoid the burden of having to withhold taxes.

Dividend income or other income arising from tax office income adjustments for earnings and profits purposes is deemed to have been paid to a foreign related party on the date on which the Korean taxpayer receives a notice of such treatment from the tax office.[324] The Korean taxpayer is required to withhold tax even if no cash payment is actually made.

A resident of a country that has a tax treaty with Korea that grants an exemption from withholding tax or withholding tax-free treatment must obtain advance approval from the district tax office having jurisdiction over the Korean resident withholding agent to benefit from such exemption or tax-free treatment. Qualifying payments include royalties, capital gains from the transfer of stock, dividends, and interest, but do not include income from the provision of personal services or business income.[325] A payor of domestic-source income is to issue a disbursement report to the foreign payee. The payor is to file a copy of the report with the relevant tax office by the end of the month immediately following the semiannual period in which the payment was made.[326] Payments required to be reported under Article 98-4 of the CTL, based on a treaty exemption claim, and categories 3, 5, 6, and 7 of domestic-source income are exempt from this requirement.[327] A tax clearance certificate is no longer required.

With regard to category 11 (see category 11, item ix), withholding tax is due, even if no cross-border payment is made, when a merger or corporate division is registered with the court or an increase or reduction of capital has been decided.[328]

A disbursement report must be filed once a year by the end of February of the following year, rather than on a semiannual basis, as previously required.[329]

The MOSF has the authority to implement a special regime for residents of tax treaty countries if the government has reason to believe that the real party in interest is not in fact entitled to the protection of the treaty concerned. To date only one country, Malaysia (Labuan), has been so designated. In such a situation, the Korean payor is required to apply the withholding tax rates specified by Korean law, rather than the relevant tax treaty or a tax-exemption measure under Korean law, when remitting dividends, interest, royalties or the purchase price of a Korean company's stock to a nonresident or foreign company. The recipient of such income (the taxpayer) may later claim a refund of the tax based on the relevant tax treaty provision or provision of Korean law. The refund claim must be filed by the recipient with the director of the district tax office with whom the payor filed its withholding tax return. The claim should be made within five years after the end of the month in which the payor withheld tax. The district tax office must advise the claimant of its decision within six months after receipt of the claim. The claimant may also apply to the commissioner of NTS for an advance waiver of the application of this special regime.[330]

Effective January 2009, the partnership tax regime, which applies to foreign companies and individuals, as well as domestic companies and individuals, that are partners of a Korean partnership, covers gain from transfers of partnership interests and the distribution of earnings to partners. Generally speaking, such transfers give rise to capital gains and withholding tax as would be the case upon the sale of company stock. From distributions to nonresident partners, the partnership is required to withhold tax at the maximum applicable income tax rate (24% for foreign corporate partners and 45% for foreign individual partners) when the partners are considered active partners. The recipient active partners may then elect to file a tax return claiming a refund. The distribution to passive partners is considered dividend income subject to 20% domestic withholding tax or applicable tax treaty rate on dividends.[331] From 2023, the character of the income distributed to passive partners is determined following the character of the underlying income. A partner is a passive partner only if the partner (i) does not allow the use of his name or company name for the partnership, (ii) does not assume unlimited liability, and (iii) does not play a role as a person similar to a director of a company.

Effective for payment of income for personal services rendered on or after January 1, 2009, a foreign service provider may choose to file a tax return claiming deductible expenses, rather than a gross receipt based withholding tax.[332] Such person should file the return within three months after completion of rendering the services and may deduct withholding tax of 20% that the payer has deducted upon payment.

Effective for income paid on or after July 1, 2012, under Article 98-6 of the CTL, to claim a reduced withholding tax rate pursuant to a tax treaty, an appropriate application must be completed by the beneficial owner and submitted to the withholding agent (e.g., Korean company, custodian bank, etc.) prior to the payment of Korean-source income. For applications submitted on or after January 1, 2023, if the withholding tax

[322] CTL, Art. 91(1).
[323] CTL, Art. 98(8).
[324] CTL-ED, Art. 123-2(1), which was changed to CTL-ED, Art. 137(1), effective January 1, 1999; ITL-ED, Art. 192.
[325] CTL, Art. 98-4.
[326] CTL, Art. 120-2; NTS Guideline of June 2002.
[327] CTL-ED, Art. 162-2.
[328] CTL-ED, Art. 137(6).
[329] CTL, Art. 120-2.
[330] CTL, Art. 98-5.
[331] TILL, Art. 100-24.
[332] CTL, Art. 99.

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to be exempt is 1 billion *won* or more, the applicant must also submit information regarding the board members, shareholders and audit reports for the past three years, and information relating to the IP right in case of royalty income. The submitted application must be retained by the withholding agent for five years starting from the day following the withholding tax payment due date and submitted upon request to the Chief of the district tax office having jurisdiction over the withholding agent. In general, the application will be valid for three years from the submission date; however, a new application must be completed and submitted if there are any changes to the information provided in the previously submitted application before the receipt of additional income. If the application is not submitted, the withholding agent will be required to apply the higher domestic statutory withholding tax rates.

If a foreign entity is an overseas investment vehicle ("OIV"), the beneficial owner investors of the OIV are treated as relevant taxpayers. An OIV is broadly defined as any overseas vehicle that raises funds through an investment offering, manages investment assets, derives value from the acquisition and disposition of such assets, and distributes such derived value to its investors. The OIV itself could be a relevant taxpayer as a corporation if the relevant tax treaty provides as such or it is subject to tax in the resident country and is not established for tax avoidance purposes.

Comment: Article 98-4 applies to claims of exemption under a tax treaty while Article 98-6 applies to claims of reduced withholding tax.

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VII. Taxation of Branches

A tax on branch profits is imposed at the rate of 20% on the Korean branches of foreign corporations resident in certain countries, pursuant to the principle of reciprocity, unless lowered by a treaty allowing for the branch profits tax. Residents of the following countries are affected: Australia and Brazil — 15%; Indonesia, Philippines and Thailand — 10%; Canada, France, Kazakhstan, and Morocco — 5%.[333]

[333] CTL, Art. 96, which was introduced as CTL, Art. 57-2, effective Jan. 1, 1996.

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VIII. Taxation of Partnerships

Doing business in the form of a partnership by large companies was rare though small business enterprises, such as small retail shops, small wholesale businesses and certain small workshops, were conducted in the form of a *chohap* (contractual partnership) or as a *kongdong saopja* (literally, "joint enterprise"). These business units are not considered to be taxpayers. Their members are required to report income and pay taxes separately, either under the Income Tax Law (ITL) or the Corporation Tax Law (CTL). However, such business units are required to be registered for VAT purposes and report VAT with respect to each "place of business." See XIV, below, for further discussion on VAT. A *kongdong saopja* is also required to keep records for tax purposes, register with the tax office and report information on allocation of income.[334]

Somewhat comparable to the above-described contractual partnerships or joint enterprises, a formal partnership was introduced in recent years. For a discussion of partnership taxation (*dong-up-gi-up gwase*) as offered by the Tax Incentive Limitation Law, see XV, Q, 4, below.

[334] CTL, Arts. 43 and 87.

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IX. Assets Revaluation Law

The Assets Revaluation Law (ARL), which allowed a company to revalue certain assets provided it paid tax on the increase in value under the ARL,[335] was repealed effective January 1, 2001.

[335] Law No. 1691 of 1965, as amended by Law No. 5584 of 1998.

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X. Taxation of Individuals

A. Residence

Individual taxpayers are classified on the basis of residence rather than nationality.

1. Definition of a Resident

A resident individual is an individual who has a domicile in Korea for any length of time or who has had a "residence" in Korea for 183 days or more (before 2015, one year or more). A nonresident individual is any individual who is not a resident.[336] As soon as an individual has a domicile in Korea, he or she is a resident for tax purposes. A "residence," however, must exist for 183 days or more before an individual, who does not have a Korean domicile, becomes a resident. A "residence" is defined, unhelpfully, as a place where one "resides."[337]

a. Domicile

The Civil Code defines the term "domicile" as the place that constitutes the center or base of a person's life.[338] Under the income tax enforcement orders, the presence of property or the presence of family are factors to be considered in determining whether a person has a domicile within the country [339]and also give rise to a presumption that the person has a domicile within the country.[340] Close family relationships are found at a domicile, but not necessarily at a residence.[341]

A person is presumed to have a domicile in Korea when he or she has an occupation that would ordinarily require him or her to "reside" continuously in the country for 183 days or more (before 2015, one year or more) or when he or she is presumed to reside continuously in Korea for 183 days or more considering the presence of family, occupation and property.[342] Conversely, a person "residing" overseas is deemed not to have a domicile in Korea if he or she is a citizen or resident of a foreign country and no presumption arises that he or she will return to Korea because of family or property located within Korea.[343] In short, something or someone located in Korea and related to the taxpayer is required to create a domicile. Residence, on the other hand, does not necessarily require family or property.

b. Residence

Having a domicile in Korea makes an individual a resident for tax purposes. Having a residence in Korea for 183 days or more (before 2015, one year or more) has the same effect.

The term "residence" is more restricted than the term "domicile." A place where an individual "resides" without his family may be a residence even though it would not qualify as a domicile. For example, a hotel room may be a residence for tax purposes.

Korean government employees and "managers or employees who work for resident individuals or domestic corporations" who are stationed overseas are deemed to be residents of Korea even if they have no domicile in Korea.[344] Temporary absence from Korea does not change residence. Absence is presumed to be temporary if the resident maintains an abode in Korea to which he or she intends to return.[345] Absence is also presumed to be temporary if the resident leaves family or property in Korea, but this provision seems redundant since such family or property would be sufficient to give rise to the presumption that a domicile existed in Korea.

The term "family" as used in the income tax enforcement orders includes those family members who form an economic unit. In most cases this would mean the spouse and dependents of the taxpayer. The term "property" as used in the regulations is usually restricted to household property or items that would indicate an intent to live in Korea, but this term is not defined.

Comment: Since a person will be presumed to have a Korean domicile and, hence, to be a resident from the outset if he is found to have an occupation that would ordinarily require her or him to stay for a year or more, foreign nationals going to work in Korea on a temporary basis should document that their stay will be brief if they wish to be taxed as nonresidents.

The case of a Korean national who leaves Korea for more than one year presents analytical and practical problems. Let us assume that such an individual leaves behind no family or property in Korea, does not work for the Korean government or a Korean company, and clearly plans to be gone for more than one year. Such a person would not have a domicile in Korea. He or she would have a residence in Korea if his absence were to be "temporary."

Although it is not clear whether an individual would be regarded as resident or nonresident in these circumstances, there is at least a negative implication that Korean nationals who cease to have domiciles in Korea are regarded as nonresidents of Korea for tax purposes: a Presidential Decree has been promulgated to the effect that Korean government employees and the employees of domestic businesses stationed abroad are deemed to be residents of Korea even if they have no Korean domicile. Other Korean nationals abroad who do not have Korean domiciles are not considered to be residents of Korea.[346]

B. Taxation of Resident Individuals

1. Taxation of Worldwide Income

a. Worldwide Income

Resident individuals are subject to Korean tax on their worldwide income (to the extent it is "covered by the act"). This interpretation is well settled.[347] Taxation of worldwide income is an inference and not explicitly stated in the statute. Resident individuals are subject to tax on "all income covered by the act." Nonresident individuals are taxable on income

[336] ITL, Art. 1.
[337] ITL-ED, Art. 2(2).
[338] CC, Art. 18.
[339] ITL-ED, Art. 2(1).
[340] ITL-ED, Art. 2(3).
[341] ITL-ED, Art. 2(2).
[342] ITL-ED, Art. 2(3).
[343] ITL-ED, Art. 2(4).
[344] ITL-ED, Arts. 2(5) and 3.
[345] ITL-ED, Art. 4(2).
[346] ITL-ED, Arts. 2(5) and 3.
[347] Seung-Young Yun, "Alien Income Tax in Korea," 1 *Korean J. Comp. L.* 100 (1973).

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from Korean sources only.[348] The inference is therefore that resident individuals are taxable on income from non-Korean sources. The Korean tax authorities have enforced this interpretation sporadically. For example, there have been a few cases where the foreign-source interest or dividend income of a Korean resident was taxed when information was supplied to the Korean tax authorities by Korea's treaty partner under the information exchange provisions of a treaty.

As an exception to the foregoing general rule, with respect to income earned on or after January 1, 2009, a resident with a foreign nationality may be taxed in Korea on foreign-source income that has been remitted into Korea if such person maintained a domicile or residence in Korea for an aggregate period of five years or less out of the 10-year period ending on or before the last day of the relevant tax period.[349]

b. Definition of Income for Resident Individuals

The Korean Income Tax Law (ITL) defines income for a resident individual by listing categories of items that constitute income. The list of categories is complicated and extensive, but it is not all-inclusive. Even the last category, "other income," is defined restrictively. Therefore, any item that does not fall within one of the listed categories is not income and not taxable.

The ITL divides the income of individuals into "global income," "severance income," "capital gains" and, prior to January 1, 2007, "forestry income."[350] Effective January 1, 2007, forestry income was integrated into business income. However, effective for income accruing on or after January 1, 2023, a category for "financial investment income" will be introduced, which will be subject to a separate income calculation and tax rate. Some of the income items that are currently taxed as capital gains or dividend income will be reclassified to come under the financial investment income category.

Global income is further subdivided into interest income, dividend income, business income, wage and salary income, other income[351] and, effective January 1, 2001, pension income.[352] Prior to January 1, 2007, there was also a category of ephemeral asset income, which included income from the transfer of paintings and antiques,[353] and from the transfer of intellectual property rights, industrial information, industrial secrets, trademarks, mining rights, fishing rights, and similar property or rights.[354] Effective January 1, 2007, following the repeal of the ephemeral asset income category, income from intellectual property rights, etc., has been integrated into the "other income" category. In addition, prior to January 1, 2010, there was also a real property income category, which was repealed as of that date and real property income is now integrated into business income. Severance income refers to payments received upon termination of employment.[355] Capital gains are defined restrictively to include only gains from the transfer of land and buildings, and gains specified by Presidential Decree[356] (see further, below). Other transfers escape taxation as capital gains because they are not listed. Before its repeal, the forestry income category was limited to income from the sale of certain standing or felled timber.[357]

The other income classification, a sub-category of global income, is further subdivided into specific categories, the last of which authorizes the addition of classes of temporary income as determined by Presidential Decree.[358] Accretions to wealth not falling within one of these numerous categories are not income. What is sometimes referred to as "unrealized appreciation" and capital gains on certain transfers of stock are two examples of accretions to wealth that are not taxed as income to resident individuals. Such items do not fall within any of the categories listed.

Gains from transfer to a private person (other than a museum or gallery) of paintings of a deceased artist or of an antique, the value of which, per item, exceeds 60 million *won* is included in other income.[359] A deduction is allowed to the extent of 80% of value (or 90% if the holding period is 10 years or longer) pursuant to a Presidential Decree of February 2009.

The definition of income for a nonresident individual is different from the definition of income for a resident individual. Nonresidents are taxed on Korean-source income only. The definition of Korean-source income contains 13 major categories analogous, but not identical, to the list of categories in the definition of the income of a resident individual.[360] A Presidential Decree expands the list of Korean-source income to include items "other than those prescribed above accruing from businesses operated in Korea, personal services provided in Korea or from economic benefits received in connection with assets located in Korea."[361] The term "economic benefits" is not defined. The word "received" could be interpreted to mean "realized," so that unrealized appreciation would be excluded. Because of the Presidential Decree, the Korean-source definition applicable to a nonresident appears to be comprehensive in contrast to the selective definition of income applicable to a resident individual.

Note: Only the income of individuals is defined selectively.

For an individual taxpayer, taxable capital gains are defined as income arising from the transfer of the following assets:

(i) Land and buildings;[362]

(ii) Rights in real property, such as the right to acquire land, superficies, and registered *chonse* leasehold rights;[363]

[348] ITL, Art. 3.
[349] ITL, Art. 3.
[350] ITL, Art. 4.
[351] ITL, Art. 4.
[352] ITL, Art. 20-3.
[353] Effective January 1, 1998, Addendum of Law No. 5031 (Dec. 1995), Art. 1.
[354] ITL, Arts. 4(1) and 20-2.
[355] ITL, Art. 22.
[356] ITL, Art. 94. Effective January 1, 1996, the ITL was revised to provide a chapter for capital gains, separate from the chapter covering global income, severance income, and forestry income. The article numbers were substantially changed at that time.
[357] ITL, Art. 23.
[358] ITL, Art. 21(1).
[359] ITL, Art. 12(5)(vi) and (vii), Art. 14(3)(5-2), and Art. 21(1)(25).
[360] ITL, Art. 119.
[361] ITL-ED, Art. 179(11)(7).
[362] ITL, Art. 94(1).
[363] ITL, Art. 94(2); ITL-ED, Art. 157(3).

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(iii) Stock of listed companies sold inside the Korean security market by a large shareholder holding 1% (2% for KOSDAQ market shares) or more of the total number of outstanding shares of the stock of the subject company, or if the total value of the issued and outstanding stock of the company is valued at 1 billion *won* or more and any stock of listed companies sold outside the Korean security market;[364]

(iv) Stock of unlisted companies;[365]

(v) Stock of a corporation, 50% or more of the assets of which consist of real property assets ((i) and (ii) above), where 50% or more of the outstanding stock is transferred by a single taxpayer (see VI.B., above — Category 7, (iii));[366] For share transfers taking place on or after February 3, 2015, for purposes of determining whether the 50% "real estate-rich" company threshold is exceeded, the value of shares in any other real estate-rich companies held by the tested company will be treated as real estate in the same ratio as the value of real estate owned by such other real estate-rich companies bears to their total assets.

(vi) Goodwill alone or goodwill that is deemed to have been included in the transfer price of a business;[367]

(vii) Stock or membership certificates carrying with them the right to use exclusive membership facilities;[368]

(viii) Stock of a corporation 80% or more of the assets of which consists of real property assets and that operates a golf or ski resort or other recreational facilities; [369]

(ix) Certain derivatives including KOSPI 200 futures, KOSPI 200 options and other "similar derivatives" as may be prescribed by Ministry of Strategy and Finance ("MOSF") Decree with respect to transactions taking place on or after January 1, 2016, and KOSPI 200 ELW (equity linked notes) for transactions taking place on or after April 1, 2017; and

(x) Gains accruing from the transfer of foreign company shares (for transfers on or after January 1, 2020).

(xi) Gains from the sale of a trust beneficiary right other than an (investment) beneficiary right or (investment) beneficiary certificate under the Financial Investment Services and Capital Market Act ("FCMA") (effective for income accruing on or after January 1, 2021).

For income accruing on or after January 1, 2025, items (iii), (iv) and (x) will be reclassified and taxed as a financial investment income.

The financial investment income category will also include the following items that are not treated as interest income, dividend income or capital gains:[370]

(i) Income from the sale of equity securities (e.g., shares which are not real estate rich company shares);

(ii) Income from the sale of debt securities;

(iii) Income from the sale of an investment contract;

(iv) Income from the sale, cancellation or redemption of collective investment securities and distributions from qualified investment securities sourced from financial investment income;

(v) Income from derivative linked securities; and

(vi) Income from transactions or actions of derivative products.

Gains on the sale of land located outside Korea are taxable in the hands of an individual resident if the individual has resided in Korea for five years.[371]

Certain residents who depart Korea on or after January 1, 2018 will be subject to an "exit tax." The shares of domestic stock held by such emigrants are deemed to be sold on the date of emigration and subject to a 20% (25% for income over 300 million *won*) exit tax on the deemed gain on the shares. The exit tax applies only to residents who (i) maintained an address or abode in Korea for five or more years during the 10-year period before the date of emigration; and (ii) is a "large shareholder" of a listed company as defined in section X.B.1.b., above, and a large shareholder holding 4% or more of a unlisted company or whose share value is 2.5 billion *won* (1.5 billion *won* on or after April 1, 2018, and 1 billion *won* on or after April 1, 2020) or more.

2. Gross Income

As described at X.B1.b., above, the income of a resident individual is divided into three main categories: global income, severance income and capital gains.[372] However, a fourth category, covering financial investment income, will be introduced from 2025. Income not falling within one of these main categories is not income of a resident individual and therefore is not taxable. Income within these categories before any adjustments or deductions may be referred to as gross income.

3. Adjusted Gross Income

Adjusted gross income is calculated separately for each of the main categories of gross income listed in X.B.2., above.

The category of global income is subdivided into six subcategories: interest income; dividend income; business income; wage and salary income; pension income (see X.B.1.b., above); and other income. Each of these subcategories is treated separately to arrive at adjusted gross income. Interest paid on bonds that have a term of 10 years or more is subject to a final withholding tax of 30%, and the individual taxpayer need not report such income on his global returnsn. A withholding tax of 14% applies to dividends and interest paid on bonds and bank deposits accruing from other than private loans.[373] These withholding taxes are in the nature of a prepayment of tax for a

[364] ITL, Art. 94(3), effective for trades made on or after April 1, 2016; ITL-ED, Art. 157(4).
[365] ITL, Arts. 94(4) and 94(1)(3)(c); ITL-ED Art. 157(5)(1) and (2).
[366] ITL, Art. 94(5); ITL-ED, Art. 158(1)(1).
[367] ITL, Art. 94(5); ITL-ED, Art. 158(1)(3).
[368] ITL, Art. 94(5); ITL-ED, Art. 158(1)(4).
[369] ITL, Art. 94(5); ITL-ED, Art. 158(1)(5).
[370] ITL, Art. 87-6.
[371] ITL, Arts. 118-2 through 118-7.
[372] ITL, Art. 4(1).
[373] ITL, Art. 129(1); effective January 1, 2005, the rate was lowered to 14% from 15%.

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taxpayer whose interest and dividends of the qualified category exceed 20 million *won* for a year. Interest paid on private loans is subject to a 25% withholding tax, again as a prepayment of tax.

The adjusted gross income figures for the subcategories are then aggregated to give adjusted gross global income.

Comment: In the past, Korean residents were permitted to conduct banking transactions under fictitious names or in the names of other persons. From the early 1990s, Koreans debated adopting a policy that would require individuals to conduct banking transactions on a real name basis. The administration discouraged persons from maintaining bank accounts under a pseudonym, or a disguised or borrowed name. A tax system was to be introduced to include interest and dividends in the global income reporting system. As a first step, President Y.S. Kim promulgated the Emergency Presidential Decree on Real Name Financial Transactions in August 1993. In December 1994, as the second step, the National Assembly enacted a new Income Tax Law, to be effective on January 1, 1996. The new law included a plan to bring more items of income into the global system and to reduce the amount of income subject to final withholding at fixed rates. An exception was to be capital gains from transfers of listed company stock. In December 1997, Korea experienced the "IMF liquidity crisis" or economic meltdown that led the administration of President D.J. Kim to suspend the second step measures from calendar year 1998 forward (Real Name Financial Transaction Law of December 1997). As a result, qualified taxpayers were required to report dividends and interest as part of their global income in tax returns for calendar years 1996 and 1997, but not for calendar years 1998, 1999 and 2000, and to report again for 2001 and thereafter.

No deductions are allowed from gross interest income or gross dividend income in arriving at adjusted gross interest income and adjusted gross dividend income. Necessary expenses are deductible from gross business income in arriving at adjusted gross business income. Certain wage and salary income deductions, including a fixed annual deduction, a medical deduction and an insurance deduction, are taken from gross wage and salary income in arriving at adjusted gross wage and salary income. Necessary expenses are deductible from gross other income in arriving at adjusted gross other income.[374]

The dividend income subcategory includes the par value of shares received as the result of an unlisted company transferring revaluation reserves, earned surplus reserves, retained earnings, and certain other reserves to paid-in capital.

Severance income is composed of lump sum payments received by employees on termination of their employment, either as required by the Labor Standards Act or as stipulated by contract.

Comment: Pension payments or annuities received under the National Pension Law (NPL), Government Employee Pension Law, Teacher's Pension Law and other laws were tax-free salary income. However, effective 2001, such income is included in taxable global income.[375] Payments having the nature of compensation for damages remain tax free, such as compensation for funeral expense.

Prior to January 1, 2016, gross severance income was adjusted by a 40% deduction plus a deduction calculated on the basis of the number of years of employment in arriving at adjusted gross severance income.[376] From January 1, 2016, the 40% deduction was repealed. Instead, the following deductions are applied after annualizing the retirement income (by multiplying income by 12) and dividing by the number of service years ("converted salary"):

– Not more than 8 million *won*: 100% of converted salary;

– Over 8 million *won* up to 70 million *won*: 8 million *won* + 60% of excess over 8 million *won*;

– Over 70 million *won* up to 100 million *won*: 45.2 million *won* + 55% of excess over 70 million *won*;

– Over 100 million *won* up to 300 million *won*: 61.7 million *won* + 45% of excess over 100 million *won*;

– In excess of 300 million *won*: 151.7 million *won* + 35% of excess over 300 million *won*

Capital gains are not taxable in the hands of a resident individual except in cases specifically set forth in the statute. Taxable gains include gains on the transfer of "real property assets." Real property assets include land, buildings and rights related to real property. The list of capital transfers that are taxable in the hands of an individual also includes transfers of the stock of unlisted companies, transfers of the stock of listed companies owned by a large shareholder, and the stock of listed companies that is transferred outside the stock exchange. From 2023, capital gains from transfers of stock that is not "real estate rich company stock" will be taxed as financial investment income.

Adjusted capital gains are calculated by deducting a special deduction for long-term holding. The gain may be reduced if the property is held for specified periods of time: by 10% to 30% depending on the holding period.[377]

4. *Personal Exemptions*

The personal exemptions allowed to a resident individual are deducted from global income.

Personal exemptions are available as follows. First, personal exemptions in the amount of 1,500,000 *won* per exemption for: (i) the taxpayer; (ii) the taxpayer's spouse (provided the spouse's income does not exceed one million *won* or from 2016, 5 million *won* in case only the spouse has salary income); and (iii) dependents of the taxpayer, including children under 20 years of age, father, mother, father-in-law and mother-in-law over the age of 60, and brothers and sisters of the taxpayer under 20 or over 60 (provided the income of such brothers or sisters, does not exceed one million *won* or from 2016, 5 million *won* in case only the dependent has salary income).[378]

[374] Other income of 3 million *won* or less may not be included in global income, ITL, Art. 14(3)(5). Certain categories of other income such as lecture fees, manuscript fees, etc. are subject to a 75% deduction, ITL, Art. 37, ITL-ED, Art. 87.

[375] ITL, Art. 12(4)(d) and (e).

[376] ITL, Art. 48; five years or less in employment, 300,000 *won* times number of years in employment; five to 10 years, 1,500,000 *won* plus 500,000 *won* times number of years in employment in excess of five years, etc.

[377] ITL, Art. 95(2).

[378] ITL, Art. 50.

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Second, additional exemptions for: (i) certain handicapped persons (2 million *won*); (ii) each elderly dependent of at least 70 years of age (1 million *won*);[379] (iii) a female head of household having no spouse but having at least one dependent 0.51 million *won*);[380] and (iv) a person without a spouse who has children eligible for personal exemption (1 million *won*).[381]

5. Taxable Income

Taxable income for the global income category is calculated by deducting the personal exemptions from the adjusted global income according to the procedures described in X.B.4., above. Taxable income for severance income equals the adjusted gross severance income as described in X.B.3., above. Taxable income for capital gains is calculated by deducting 2.5 million *won* per each category of capital gain. Furthermore, from 2025, taxable income for the financial investment income category will be calculated by deducting (i) 50 million *won* for gains from the sale of listed shares, shares of unlisted small and medium-sized companies traded in the OTC market, and certain public collective investment securities; and (ii) 2,500,000 *won* for other items. This process gives the amount of taxable income for each of the main categories of income. Graduated tax rates are applied separately to each of the categories of taxable income. The same table of tax rates is applied to taxable income for the categories of global and severance income, but the rates are applied to each category separately.

A different set of tax rates is applied to taxable income in the capital gains category. These rates vary, depending on how long the asset was held and whether the transfer was registered.

For the category of financial investment income, to be introduced in 2025, the tax rate will be 20% for taxable income up to 300 million *won* and 25% for taxable income in excess thereof.

A full integration system applies with respect to the income of corporations and individual shareholders from tax year 1999. A minimum gross-up is based on the low end of the corporate tax rates. As from year 2006, the low end of the corporate tax rates was 13%, making the gross-up rate 15%, i.e., 13/87.[382] The gross-up rate for 2009 and 2010 was reduced to 12%. From 2011, when the corporate tax rate for the lowest bracket is 10%, the gross-up rate is 11%, i.e., 10/90. The integration system works as follows:

Corporation:		
Taxable income		100
Corporation tax on low bracket		10
Income after tax		90
Individual Shareholder:		
Dividend income	90	
Gross-up per ITL, Art. 17(3), 13 over 87	11	11% of dividend income
Dividend income plus gross-up	100	
Income tax rate (maximum)		42%
Income tax before credit	42	
Credit per ITL Art. 56 (1)	11	
Income tax payable	31	

[379] ITL, Art. 51.
[380] ITL, Art. 51(1)(3).
[381] ITL, Art. 51(1)(6).
[382] ITL, Art. 17(3).

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X. Taxation of Individuals

A. *Residence*

Individual taxpayers are classified on the basis of residence rather than nationality.

1. *Definition of a Resident*

A resident individual is an individual who has a domicile in Korea for any length of time or who has had a "residence" in Korea for 183 days or more (before 2015, one year or more). A nonresident individual is any individual who is not a resident.[336] As soon as an individual has a domicile in Korea, he or she is a resident for tax purposes. A "residence," however, must exist for 183 days or more before an individual, who does not have a Korean domicile, becomes a resident. A "residence" is defined, unhelpfully, as a place where one "resides."[337]

a. *Domicile*

The Civil Code defines the term "domicile" as the place that constitutes the center or base of a person's life.[338] Under the income tax enforcement orders, the presence of property or the presence of family are factors to be considered in determining whether a person has a domicile within the country [339]and also give rise to a presumption that the person has a domicile within the country.[340] Close family relationships are found at a domicile, but not necessarily at a residence.[341]

A person is presumed to have a domicile in Korea when he or she has an occupation that would ordinarily require him or her to "reside" continuously in the country for 183 days or more (before 2015, one year or more) or when he or she is presumed to reside continuously in Korea for 183 days or more considering the presence of family, occupation and property.[342] Conversely, a person "residing" overseas is deemed not to have a domicile in Korea if he or she is a citizen or resident of a foreign country and no presumption arises that he or she will return to Korea because of family or property located within Korea.[343] In short, something or someone located in Korea and related to the taxpayer is required to create a domicile. Residence, on the other hand, does not necessarily require family or property.

b. *Residence*

Having a domicile in Korea makes an individual a resident for tax purposes. Having a residence in Korea for 183 days or more (before 2015, one year or more) has the same effect.

The term "residence" is more restricted than the term "domicile." A place where an individual "resides" without his family may be a residence even though it would not qualify as a domicile. For example, a hotel room may be a residence for tax purposes.

Korean government employees and "managers or employees who work for resident individuals or domestic corporations" who are stationed overseas are deemed to be residents of Korea even if they have no domicile in Korea.[344] Temporary absence from Korea does not change residence. Absence is presumed to be temporary if the resident maintains an abode in Korea to which he or she intends to return.[345] Absence is also presumed to be temporary if the resident leaves family or property in Korea, but this provision seems redundant since such family or property would be sufficient to give rise to the presumption that a domicile existed in Korea.

The term "family" as used in the income tax enforcement orders includes those family members who form an economic unit. In most cases this would mean the spouse and dependents of the taxpayer. The term "property" as used in the regulations is usually restricted to household property or items that would indicate an intent to live in Korea, but this term is not defined.

Comment: Since a person will be presumed to have a Korean domicile and, hence, to be a resident from the outset if he is found to have an occupation that would ordinarily require her or him to stay for a year or more, foreign nationals going to work in Korea on a temporary basis should document that their stay will be brief if they wish to be taxed as nonresidents.

The case of a Korean national who leaves Korea for more than one year presents analytical and practical problems. Let us assume that such an individual leaves behind no family or property in Korea, does not work for the Korean government or a Korean company, and clearly plans to be gone for more than one year. Such a person would not have a domicile in Korea. He or she would have a residence in Korea if his absence were to be "temporary."

Although it is not clear whether an individual would be regarded as resident or nonresident in these circumstances, there is at least a negative implication that Korean nationals who cease to have domiciles in Korea are regarded as nonresidents of Korea for tax purposes: a Presidential Decree has been promulgated to the effect that Korean government employees and the employees of domestic businesses stationed abroad are deemed to be residents of Korea even if they have no Korean domicile. Other Korean nationals abroad who do not have Korean domiciles are not considered to be residents of Korea.[346]

B. *Taxation of Resident Individuals*

1. *Taxation of Worldwide Income*

a. *Worldwide Income*

Resident individuals are subject to Korean tax on their worldwide income (to the extent it is "covered by the act"). This interpretation is well settled.[347] Taxation of worldwide income is an inference and not explicitly stated in the statute. Resident individuals are subject to tax on "all income covered by the act." Nonresident individuals are taxable on income

[336] ITL, Art. 1.
[337] ITL-ED, Art. 2(2).
[338] CC, Art. 18.
[339] ITL-ED, Art. 2(1).
[340] ITL-ED, Art. 2(3).
[341] ITL-ED, Art. 2(2).
[342] ITL-ED, Art. 2(3).
[343] ITL-ED, Art. 2(4).
[344] ITL-ED, Arts. 2(5) and 3.
[345] ITL-ED, Art. 4(2).
[346] ITL-ED, Arts. 2(5) and 3.
[347] Seung-Young Yun, "Alien Income Tax in Korea," 1 *Korean J. Comp. L.* 100 (1973).

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from Korean sources only.[348] The inference is therefore that resident individuals are taxable on income from non-Korean sources. The Korean tax authorities have enforced this interpretation sporadically. For example, there have been a few cases where the foreign-source interest or dividend income of a Korean resident was taxed when information was supplied to the Korean tax authorities by Korea's treaty partner under the information exchange provisions of a treaty.

As an exception to the foregoing general rule, with respect to income earned on or after January 1, 2009, a resident with a foreign nationality may be taxed in Korea on foreign-source income that has been remitted into Korea if such person maintained a domicile or residence in Korea for an aggregate period of five years or less out of the 10-year period ending on or before the last day of the relevant tax period.[349]

b. Definition of Income for Resident Individuals

The Korean Income Tax Law (ITL) defines income for a resident individual by listing categories of items that constitute income. The list of categories is complicated and extensive, but it is not all-inclusive. Even the last category, "other income," is defined restrictively. Therefore, any item that does not fall within one of the listed categories is not income and not taxable.

The ITL divides the income of individuals into "global income," "severance income," "capital gains" and, prior to January 1, 2007, "forestry income."[350] Effective January 1, 2007, forestry income was integrated into business income. However, effective for income accruing on or after January 1, 2023, a category for "financial investment income" will be introduced, which will be subject to a separate income calculation and tax rate. Some of the income items that are currently taxed as capital gains or dividend income will be reclassified to come under the financial investment income category.

Global income is further subdivided into interest income, dividend income, business income, wage and salary income, other income[351] and, effective January 1, 2001, pension income.[352] Prior to January 1, 2007, there was also a category of ephemeral asset income, which included income from the transfer of paintings and antiques,[353] and from the transfer of intellectual property rights, industrial information, industrial secrets, trademarks, mining rights, fishing rights, and similar property or rights.[354] Effective January 1, 2007, following the repeal of the ephemeral asset income category, income from intellectual property rights, etc., has been integrated into the "other income" category. In addition, prior to January 1, 2010, there was also a real property income category, which was repealed as of that date and real property income is now integrated into business income. Severance income refers to payments received upon termination of employment.[355] Capital gains are defined restrictively to include only gains from the transfer of land and buildings, and gains specified by Presidential Decree[356] (see further, below). Other transfers escape taxation as capital gains because they are not listed. Before its repeal, the forestry income category was limited to income from the sale of certain standing or felled timber.[357]

The other income classification, a sub-category of global income, is further subdivided into specific categories, the last of which authorizes the addition of classes of temporary income as determined by Presidential Decree.[358] Accretions to wealth not falling within one of these numerous categories are not income. What is sometimes referred to as "unrealized appreciation" and capital gains on certain transfers of stock are two examples of accretions to wealth that are not taxed as income to resident individuals. Such items do not fall within any of the categories listed.

Gains from transfer to a private person (other than a museum or gallery) of paintings of a deceased artist or of an antique, the value of which, per item, exceeds 60 million *won* is included in other income.[359] A deduction is allowed to the extent of 80% of value (or 90% if the holding period is 10 years or longer) pursuant to a Presidential Decree of February 2009.

The definition of income for a nonresident individual is different from the definition of income for a resident individual. Nonresidents are taxed on Korean-source income only. The definition of Korean-source income contains 13 major categories analogous, but not identical, to the list of categories in the definition of the income of a resident individual.[360] A Presidential Decree expands the list of Korean-source income to include items "other than those prescribed above accruing from businesses operated in Korea, personal services provided in Korea or from economic benefits received in connection with assets located in Korea."[361] The term "economic benefits" is not defined. The word "received" could be interpreted to mean "realized," so that unrealized appreciation would be excluded. Because of the Presidential Decree, the Korean-source definition applicable to a nonresident appears to be comprehensive in contrast to the selective definition of income applicable to a resident individual.

Note: Only the income of individuals is defined selectively.

For an individual taxpayer, taxable capital gains are defined as income arising from the transfer of the following assets:

(i) Land and buildings;[362]

(ii) Rights in real property, such as the right to acquire land, superficies, and registered *chonse* leasehold rights;[363]

[348] ITL, Art. 3.
[349] ITL, Art. 3.
[350] ITL, Art. 4.
[351] ITL, Art. 4.
[352] ITL, Art. 20-3.
[353] Effective January 1, 1998, Addendum of Law No. 5031 (Dec. 1995), Art. 1.
[354] ITL, Arts. 4(1) and 20-2.
[355] ITL, Art. 22.
[356] ITL, Art. 94. Effective January 1, 1996, the ITL was revised to provide a chapter for capital gains, separate from the chapter covering global income, severance income, and forestry income. The article numbers were substantially changed at that time.
[357] ITL, Art. 23.
[358] ITL, Art. 21(1).
[359] ITL, Art. 12(5)(vi) and (vii), Art. 14(3)(5-2), and Art. 21(1)(25).
[360] ITL, Art. 119.
[361] ITL-ED, Art. 179(11)(7).
[362] ITL, Art. 94(1).
[363] ITL, Art. 94(2); ITL-ED, Art. 157(3).

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(iii) Stock of listed companies sold inside the Korean security market by a large shareholder holding 1% (2% for KOSDAQ market shares) or more of the total number of outstanding shares of the stock of the subject company, or if the total value of the issued and outstanding stock of the company is valued at 1 billion *won* or more and any stock of listed companies sold outside the Korean security market;[364]

(iv) Stock of unlisted companies;[365]

(v) Stock of a corporation, 50% or more of the assets of which consist of real property assets ((i) and (ii) above), where 50% or more of the outstanding stock is transferred by a single taxpayer (see VI.B., above — Category 7, (iii));[366] For share transfers taking place on or after February 3, 2015, for purposes of determining whether the 50% "real estate-rich" company threshold is exceeded, the value of shares in any other real estate-rich companies held by the tested company will be treated as real estate in the same ratio as the value of real estate owned by such other real estate-rich companies bears to their total assets.

(vi) Goodwill alone or goodwill that is deemed to have been included in the transfer price of a business;[367]

(vii) Stock or membership certificates carrying with them the right to use exclusive membership facilities;[368]

(viii) Stock of a corporation 80% or more of the assets of which consists of real property assets and that operates a golf or ski resort or other recreational facilities; [369]

(ix) Certain derivatives including KOSPI 200 futures, KOSPI 200 options and other "similar derivatives" as may be prescribed by Ministry of Strategy and Finance ("MOSF") Decree with respect to transactions taking place on or after January 1, 2016, and KOSPI 200 ELW (equity linked notes) for transactions taking place on or after April 1, 2017; and

(x) Gains accruing from the transfer of foreign company shares (for transfers on or after January 1, 2020).

(xi) Gains from the sale of a trust beneficiary right other than an (investment) beneficiary right or (investment) beneficiary certificate under the Financial Investment Services and Capital Market Act ("FCMA") (effective for income accruing on or after January 1, 2021).

For income accruing on or after January 1, 2025, items (iii), (iv) and (x) will be reclassified and taxed as a financial investment income.

The financial investment income category will also include the following items that are not treated as interest income, dividend income or capital gains:[370]

(i) Income from the sale of equity securities (e.g., shares which are not real estate rich company shares);

(ii) Income from the sale of debt securities;

(iii) Income from the sale of an investment contract;

(iv) Income from the sale, cancellation or redemption of collective investment securities and distributions from qualified investment securities sourced from financial investment income;

(v) Income from derivative linked securities; and

(vi) Income from transactions or actions of derivative products.

Gains on the sale of land located outside Korea are taxable in the hands of an individual resident if the individual has resided in Korea for five years.[371]

Certain residents who depart Korea on or after January 1, 2018 will be subject to an "exit tax." The shares of domestic stock held by such emigrants are deemed to be sold on the date of emigration and subject to a 20% (25% for income over 300 million *won*) exit tax on the deemed gain on the shares. The exit tax applies only to residents who (i) maintained an address or abode in Korea for five or more years during the 10-year period before the date of emigration; and (ii) is a "large shareholder" of a listed company as defined in section X.B.1.b., above, and a large shareholder holding 4% or more of a unlisted company or whose share value is 2.5 billion *won* (1.5 billion *won* on or after April 1, 2018, and 1 billion *won* on or after April 1, 2020) or more.

2. Gross Income

As described at X.B1.b., above, the income of a resident individual is divided into three main categories: global income, severance income and capital gains.[372] However, a fourth category, covering financial investment income, will be introduced from 2025. Income not falling within one of these main categories is not income of a resident individual and therefore is not taxable. Income within these categories before any adjustments or deductions may be referred to as gross income.

3. Adjusted Gross Income

Adjusted gross income is calculated separately for each of the main categories of gross income listed in X.B.2., above.

The category of global income is subdivided into six subcategories: interest income; dividend income; business income; wage and salary income; pension income (see X.B.1.b., above); and other income. Each of these subcategories is treated separately to arrive at adjusted gross income. Interest paid on bonds that have a term of 10 years or more is subject to a final withholding tax of 30%, and the individual taxpayer need not report such income on his global returnsn. A withholding tax of 14% applies to dividends and interest paid on bonds and bank deposits accruing from other than private loans.[373] These withholding taxes are in the nature of a prepayment of tax for a

[364] ITL, Art. 94(3), effective for trades made on or after April 1, 2016; ITL-ED, Art. 157(4).
[365] ITL, Arts. 94(4) and 94(1)(3)(c); ITL-ED Art. 157(5)(1) and (2).
[366] ITL, Art. 94(5); ITL-ED, Art. 158(1)(1).
[367] ITL, Art. 94(5); ITL-ED, Art. 158(1)(3).
[368] ITL, Art. 94(5); ITL-ED, Art. 158(1)(4).
[369] ITL, Art. 94(5); ITL-ED, Art. 158(1)(5).
[370] ITL, Art. 87-6.
[371] ITL, Arts. 118-2 through 118-7.
[372] ITL, Art. 4(1).
[373] ITL, Art. 129(1); effective January 1, 2005, the rate was lowered to 14% from 15%.

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taxpayer whose interest and dividends of the qualified category exceed 20 million *won* for a year. Interest paid on private loans is subject to a 25% withholding tax, again as a prepayment of tax.

The adjusted gross income figures for the subcategories are then aggregated to give adjusted gross global income.

Comment: In the past, Korean residents were permitted to conduct banking transactions under fictitious names or in the names of other persons. From the early 1990s, Koreans debated adopting a policy that would require individuals to conduct banking transactions on a real name basis. The administration discouraged persons from maintaining bank accounts under a pseudonym, or a disguised or borrowed name. A tax system was to be introduced to include interest and dividends in the global income reporting system. As a first step, President Y.S. Kim promulgated the Emergency Presidential Decree on Real Name Financial Transactions in August 1993. In December 1994, as the second step, the National Assembly enacted a new Income Tax Law, to be effective on January 1, 1996. The new law included a plan to bring more items of income into the global system and to reduce the amount of income subject to final withholding at fixed rates. An exception was to be capital gains from transfers of listed company stock. In December 1997, Korea experienced the "IMF liquidity crisis" or economic meltdown that led the administration of President D.J. Kim to suspend the second step measures from calendar year 1998 forward (Real Name Financial Transaction Law of December 1997). As a result, qualified taxpayers were required to report dividends and interest as part of their global income in tax returns for calendar years 1996 and 1997, but not for calendar years 1998, 1999 and 2000, and to report again for 2001 and thereafter.

No deductions are allowed from gross interest income or gross dividend income in arriving at adjusted gross interest income and adjusted gross dividend income. Necessary expenses are deductible from gross business income in arriving at adjusted gross business income. Certain wage and salary income deductions, including a fixed annual deduction, a medical deduction and an insurance deduction, are taken from gross wage and salary income in arriving at adjusted gross wage and salary income. Necessary expenses are deductible from gross other income in arriving at adjusted gross other income.[374]

The dividend income subcategory includes the par value of shares received as the result of an unlisted company transferring revaluation reserves, earned surplus reserves, retained earnings, and certain other reserves to paid-in capital.

Severance income is composed of lump sum payments received by employees on termination of their employment, either as required by the Labor Standards Act or as stipulated by contract.

Comment: Pension payments or annuities received under the National Pension Law (NPL), Government Employee Pension Law, Teacher's Pension Law and other laws were tax-free salary income. However, effective 2001, such income is included in taxable global income.[375] Payments having the nature of compensation for damages remain tax free, such as compensation for funeral expense.

Prior to January 1, 2016, gross severance income was adjusted by a 40% deduction plus a deduction calculated on the basis of the number of years of employment in arriving at adjusted gross severance income.[376] From January 1, 2016, the 40% deduction was repealed. Instead, the following deductions are applied after annualizing the retirement income (by multiplying income by 12) and dividing by the number of service years ("converted salary"):

– Not more than 8 million *won*: 100% of converted salary;

– Over 8 million *won* up to 70 million *won*: 8 million *won* + 60% of excess over 8 million *won*;

– Over 70 million *won* up to 100 million *won*: 45.2 million *won* + 55% of excess over 70 million *won*;

– Over 100 million *won* up to 300 million *won*: 61.7 million *won* + 45% of excess over 100 million *won*;

– In excess of 300 million *won*: 151.7 million *won* + 35% of excess over 300 million *won*

Capital gains are not taxable in the hands of a resident individual except in cases specifically set forth in the statute. Taxable gains include gains on the transfer of "real property assets." Real property assets include land, buildings and rights related to real property. The list of capital transfers that are taxable in the hands of an individual also includes transfers of the stock of unlisted companies, transfers of the stock of listed companies owned by a large shareholder, and the stock of listed companies that is transferred outside the stock exchange. From 2023, capital gains from transfers of stock that is not "real estate rich company stock" will be taxed as financial investment income.

Adjusted capital gains are calculated by deducting a special deduction for long-term holding. The gain may be reduced if the property is held for specified periods of time: by 10% to 30% depending on the holding period.[377]

4. *Personal Exemptions*

The personal exemptions allowed to a resident individual are deducted from global income.

Personal exemptions are available as follows. First, personal exemptions in the amount of 1,500,000 *won* per exemption for: (i) the taxpayer; (ii) the taxpayer's spouse (provided the spouse's income does not exceed one million *won* or from 2016, 5 million *won* in case only the spouse has salary income); and (iii) dependents of the taxpayer, including children under 20 years of age, father, mother, father-in-law and mother-in-law over the age of 60, and brothers and sisters of the taxpayer under 20 or over 60 (provided the income of such brothers or sisters, does not exceed one million *won* or from 2016, 5 million *won* in case only the dependent has salary income).[378]

[374] Other income of 3 million *won* or less may not be included in global income, ITL, Art. 14(3)(5). Certain categories of other income such as lecture fees, manuscript fees, etc. are subject to a 75% deduction, ITL, Art. 37, ITL-ED, Art. 87.

[375] ITL, Art. 12(4)(d) and (e).

[376] ITL, Art. 48; five years or less in employment, 300,000 *won* times number of years in employment; five to 10 years, 1,500,000 *won* plus 500,000 *won* times number of years in employment in excess of five years, etc.

[377] ITL, Art. 95(2).

[378] ITL, Art. 50.

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Second, additional exemptions for: (i) certain handicapped persons (2 million *won*); (ii) each elderly dependent of at least 70 years of age (1 million *won*);[379] (iii) a female head of household having no spouse but having at least one dependent 0.51 million *won*);[380] and (iv) a person without a spouse who has children eligible for personal exemption (1 million *won*).[381]

5. Taxable Income

Taxable income for the global income category is calculated by deducting the personal exemptions from the adjusted global income according to the procedures described in X.B.4., above. Taxable income for severance income equals the adjusted gross severance income as described in X.B.3., above. Taxable income for capital gains is calculated by deducting 2.5 million *won* per each category of capital gain. Furthermore, from 2025, taxable income for the financial investment income category will be calculated by deducting (i) 50 million *won* for gains from the sale of listed shares, shares of unlisted small and medium-sized companies traded in the OTC market, and certain public collective investment securities; and (ii) 2,500,000 *won* for other items. This process gives the amount of taxable income for each of the main categories of income. Graduated tax rates are applied separately to each of the categories of taxable income. The same table of tax rates is applied to taxable income for the categories of global and severance income, but the rates are applied to each category separately.

A different set of tax rates is applied to taxable income in the capital gains category. These rates vary, depending on how long the asset was held and whether the transfer was registered.

For the category of financial investment income, to be introduced in 2025, the tax rate will be 20% for taxable income up to 300 million *won* and 25% for taxable income in excess thereof.

A full integration system applies with respect to the income of corporations and individual shareholders from tax year 1999. A minimum gross-up is based on the low end of the corporate tax rates. As from year 2006, the low end of the corporate tax rates was 13%, making the gross-up rate 15%, i.e., 13/87.[382] The gross-up rate for 2009 and 2010 was reduced to 12%. From 2011, when the corporate tax rate for the lowest bracket is 10%, the gross-up rate is 11%, i.e., 10/90. The integration system works as follows:

Corporation:		
Taxable income		100
Corporation tax on low bracket		10
Income after tax		90
Individual Shareholder:		
Dividend income	90	
Gross-up per ITL, Art. 17(3), 13 over 87	11	11% of dividend income
Dividend income plus gross-up	100	
Income tax rate (maximum)		42%
Income tax before credit	42	
Credit per ITL Art. 56 (1)	11	
Income tax payable	31	

[379] ITL, Art. 51.
[380] ITL, Art. 51(1)(3).
[381] ITL, Art. 51(1)(6).
[382] ITL, Art. 17(3).

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XI. Taxation of Nonresident Individuals

A. Scope of Taxation

Nonresident individuals are taxable only on income arising from sources within Korea. A nonresident individual having a domestic place of business in Korea or real estate income from Korean sources is required to file an annual income tax return and is entitled to certain deductions from gross income in arriving at taxable income. A nonresident individual is entitled to claim the basic exemption for him or herself, but is not entitled to claim the other personal exemptions available to resident individuals.[383]

A nonresident individual who has neither a domestic place of business in Korea nor income from real estate located in Korea is taxable at flat rates by the mechanism of withholding, in most cases (i.e., except in the case of severance income, capital gains), on gross income from Korean sources. The withholding tax is applied to each item of Korean-source income at source and is required to be withheld by the payor.[384] The financial investment income category, to be introduced from 2025, will apply only to resident individuals. Therefore, the Korean-source income classification applicable to nonresident individuals and foreign companies will not be affected by the introduction of this income category.

A nonresident individual is taxed on severance income and capital gains income in the same manner as a resident, i.e., the filing of a return is required.[385]

B. Domestic Source Income

Income from domestic sources is itemized under Article 119 of the Income Tax Law (ITL) as follows:

Category 1: interest as defined in Article 16(1) of the ITL and interest arising from other types of loans, and the profits from trusts, received from the national or a local government, resident individuals, domestic corporations, the domestic place of business of a foreign corporation under Article 94, of the Corporation Tax Law (CTL) or any domestic place of business of a nonresident under Article 120 of the ITL, and interest received from a foreign corporation or nonresident that clearly relates to the payor's domestic place of business in Korea and that was deducted from revenues earned from the domestic place of business, except for interest arising from loans taken out directly by the foreign place of business of a resident person or domestic corporation for use by its foreign place of business;

Category 2: dividends as defined in Article 17(1) of the ITL received from a domestic corporation. Furthermore, income from the sale, cancellation or redemption of collective investment securities (except for income treated as Category 12), income from non-qualified collective investment securities and income from distributions from qualified investment securities, which will be treated as financial investment income (for income accruing on or after January 1, 2023), distributions from a trust treated as a corporation (for income accruing on or after January 1, 2021), and income from derivative linked bonds (for income accruing on or after January 1, 2023);

Category 3: income arising from the transfer, leasing or other disposition of real property or real property rights, mining rights located in Korea, mineral exploration and exploitation rights and quarrying rights acquired in Korea, except for income from transfers under Category 9;

Category 4: income arising from the leasing of vessels, aircraft, registered vehicles, heavy equipment, and industrial, commercial or scientific equipment to a resident individual, a domestic corporation, or the domestic place of business of a foreign corporation under Article 94 of the CTL or the domestic place of business of a nonresident individual under Article 120 of the ITL;

Category 5: income arising from businesses described in Article 19 of the ITL (a general, quite comprehensive, description including many types of business) conducted within Korea, including Korean-source income as defined under the terms of an applicable tax treaty,[386] except for income from personal services under Category 6;

Category 6: income arising from the provision of personal services within Korea, as prescribed by Presidential Decree. For services provided on or after January 1, 2017, income from certain technical services provided outside Korea as designated by Presidential Decree is deemed to be Korean source if such income is taxable in Korea under a relevant tax treaty;

Category 7: wages and salaries received in consideration for work performed in Korea;

Category 8: income, as prescribed by Presidential Decree, in the form of severance pay received in consideration for work performed in Korea;

Category 8-2: pension income as prescribed by Article 20-3 of ITL received in Korea (from January 1, 2013);

Category 9: income arising from transfers of property located in Korea as provided for under Article 94(1), (2) and (3) of the ITL, which includes income arising from the transfer of three categories of property:

(i) Land and buildings;

(ii) Rights associated with real property as prescribed by Presidential Decree — Article 157(3) of the Income Tax Law Enforcement Decree (ITL-ED) prescribes two categories of rights associated with real property: superficies and *chonse* rights (*chonse* is a type of lease whereby the lessee deposits a sum of money for the use of the lessor during the term of the lease) and rights to acquire real property; and

(iii) Transfers of other property as designated by Presidential Decree — Article 158(1) of the ITL-ED prescribes that such transfers must be: transfers of 50% or more interests in certain closely-held corporations, 50% or more of the assets of which consist of real property or real property rights; certain transfers of goodwill; transfers of stock or membership certificates carrying with them the right to use exclusive membership facilities; transfers of stock of a corporation 80% or more of the assets of which

[383] ITL, Arts. 121(2) and 122. Before 1996, nonresidents were not entitled to claim any personal exemptions.

[384] ITL, Arts. 121(3) and 126.

[385] ITL, Art. 121(2).

[386] ITL-ED, Art. 119(5).

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consists of real property assets and that operates a golf or ski resort or other recreational facilities;[387]

Note: Effective January 1, 2001, any transfer (not limited to a transfer of a 50% or more interest) falls in this category if the subject company has real property or real property rights the value of which is 50% or more of the value of its total assets. For share transfers taking place on or after January 1, 2016, for purposes of determining whether the 50% "real estate-rich" company threshold is exceeded, the value of shares in any other real estate-rich companies held by the tested company will be treated as real estate in the same ratio as the value of real estate owned by such other real estate-rich companies bears to their total assets.

Category 10: prior to December 30, 2006, forestry income arising from property located in Korea, as defined in Article 23(1) of the ITL. This category was repealed on December 30, 2006, and forestry income merged into the business income category.

Category 11: royalties, rents, or other payments of a similar nature received as compensation for use within Korea or of compensation paid from Korea[388] with respect to the following assets, information or rights, and income arising from the transfer of such assets, information or rights:[389]

(i) Copyrights on scholarly or creative works (including films), patent rights, trademark rights, designs, models, drawings, secret formulae or processes, film and tapes for radio and television broadcasting and any other similar assets or rights; and

(ii) Information concerning industrial, commercial or scientific knowledge, experience and skill or know-how.

Category 12: income arising from the transfer of securities as prescribed by Presidential Decree (including all stock of Korean companies, whether listed or unlisted); and

Category 13: other income as described in Article 119(13) of the ITL, as follows:

(i) Insurance proceeds, reparations and compensation for damages received in connection with the conduct of a business in Korea, or in connection with real property or other property located in Korea;

(ii) Payments resulting from the breach of a contract or compensation for damages paid from Korea, the value of which exceeds the value of the goods or services at issue;[390]

(iii) Money, goods or other economic benefits received as prizes paid from Korea;

(iv) Income arising from the discovery of property buried in Korea (treasure);

(v) Income accruing from the transfer of rights within Korea created by license, permit or other similar disposition under Korean law, and from the transfer of property other than real property within Korea;

(vi) Lottery winnings from lottery tickets, etc. issued within Korea and proceeds from winning horse race tickets issued in Korea;[391]

(vii) Other income resulting from tax office income adjustments;

(viii) Lottery winnings from slot machines and the like;

(ix) Income earned by a foreign related party from the nonproportionate merger, capital reduction, or corporate division of a domestic company whose stock is owned by a foreign related party; and

(x) For payments made on or after January 1, 2020, payments made from Korea for damages arising from an infringement of a patent (e.g., damage compensation, rewards, settlements, lost profits) that is registered overseas (but not registered in Korea) and owned by a resident of a country with which Korea has a tax treaty that provides for the taxation of a royalty based on the place of use, but only to the extent that manufacturing know-how, technology, information, etc. contained in such patent are used for domestic manufacturing or production;

(xi) Income from virtual assets (for income accruing on or after January 1, 2025); and

(xii) Income arising from the receipt of economic benefits in connection with the conduct of business in Korea or the provision of personal services within Korea, or connected with property located in Korea except for income described above in (i) through (xi).

C. Withholding of Tax on Payments to Nonresident Individuals

Nonresident individuals having domestic places of business in or real estate income from Korea are required to file annual returns and to pay tax at graduated rates in the same way as resident individuals. A nonresident individual is entitled to a basic exemption.

Nonresident individuals without a domestic place of business in Korea or real estate income from Korea are taxable on their Korean domestic-source income as itemized at B, above. Except for Categories 8 and 9 (severance income and capital gains), each category of domestic source income is taxed at a flat rate on the gross amount of the payment. The tax is withheld at source by the payor.

Except in relation to Categories 8 and 9, the rates for taxes to be withheld by the payor are the same as for the corresponding categories of domestic-source income for corporations having no domestic place of business or real estate income within Korea. See VI, B, above.

Nonresident individuals without domestic places of business in, or real property income from, Korea, that have their domestic-source income falling in Categories 8 and 9 (severance income and capital gains), and who are thus required to file returns are entitled to the basic personal exemption (but not to other personal exemptions) and may otherwise make adjust-

[387] ITL, Art. 94(5); ITL-ED, Art. 158(1)(5).

[388] If an applicable tax treaty provides that Korean-source income is determined by where the use took place, the payment from Korea itself would not lead to a finding of Korean source-income (ITL, Art. 119(11), proviso).

[389] ITL, Art. 119(11).

[390] ITL-ED, Art. 179(11)(1.2); ITL-ER, Art. 86-2.

[391] ITL-ED, Art. 179(11)(5).

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ments to gross income as if they were resident individual taxpayers.

Effective January 1, 2009, a payor in Korea is required to withhold tax at the rate of 22% (that consists of a 20% income tax and a 10% local income surtax) from payment to a foreign company for the services of an entertainer or athlete not effectively connected to a domestic place of business, irrespective of a provision of a relevant tax treaty.[392] In turn, the foreign company is required to withhold tax at the rate of 22% from its payment to the entertainer or athlete. The foreign company may apply for a refund if the former tax exceeds the latter tax.

Comment: This provision begs the question of whether a treaty override is intended. In addition, there appears to be an incentive for a foreign company, having received a large payment, to withhold payment from or make a small payment to the professional, and to claim a refund based on the discrepancy.

D. Tax Benefits for Individual Taxpayers

1. Tax Credits for Employees Paid in Foreign Currency

Any individual receiving wages or salaries from outside Korea,[393] which are not charged to a domestic place of business of the employer,[394] may join a taxpayers' association to which his wages and salaries will be reported and through which income tax will be paid. Tax association members are entitled to a 5% tax credit (10% before 2019).[395] From 2022, the tax credit is subject to a limitation of 1 million *won*. The tax credit is offered as an incentive for those receiving their wages or salaries from abroad in foreign currency to report their income and to pay Korean taxes.

2. Income Tax Exemptions

A foreign technician who works under an engineering service contract, or works for a Korean company that engages in certain technology intensive business, is exempt from tax. See XV.C.7. below.

3. Nontaxable Overseas Allowances

A foreign national receiving wages or salaries for work performed in Korea is entitled to elect taxation at a flat 19% (17% for income arising prior to January 1, 2017) of gross salary with no deduction or tax credits.[396] See also XV.C.7., below.

4. Nontaxable Housing Benefits

Employers in Korea may provide housing in kind to their foreign national employees without giving rise to income in the hands of such employees. The housing must be supplied in kind. Cash payments made directly to the employee do not qualify for tax-exempt treatment. The housing provided to the foreign national employee may be either owned or leased by the employer.[397]

5. Salary Income Tax Credit

A salary income tax credit is allowed to the extent of 55% of tax of 1,300,000 *won* or less (plus 30% of the tax in excess of 1,300,000) arising from global taxable income, subject to an annual maximum of 740,000 *won*.[398]

6. Other Tax Credits

Special tax credits for certain expenditure are provided, as follows:

(i) 12% of life or casualty insurance premiums with a cap of 1 million won;

(ii) 15% of medical expenses for the taxpayer and any senior or handicapped dependents with no limit (however, medical expenses for other family members are limited to 3% of the taxpayer's wage and salary income, capped at 7 million won per year;

(iii) 15% of admission fees, tuition and other amounts paid to schools, up through college for children, and brothers or sisters of the taxpayer;

(iv) 15% of donations to institutional charities of up to 30% of the taxpayer's annual income; and

(v) 15% of contributions to private and public pensions capped at 6 million won for private pensions and 9 million won for public pensions.[399]

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[392] ITL, Art. 156-5; ITL-ED, Art. 207-7.

[393] These wages and salaries were previously categorized as "Class B" wages and salaries. Effective from Jan. 1, 2010, the terms "Class A" and "Class B" are no longer used to distinguish salary income according to the status of the payer.

[394] ITL, Art. 20(1)(2).

[395] ITL, Arts. 150(3) and 151.

[396] TILL, Art. 18-2, as applied for year 2004 and thereafter, as extended.

[397] ITL-ED, Art. 38(1)(6).

[398] ITL, Art. 59.

[399] ITL, Arts. 59-3, 59-4.

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XII. Inheritance and Gift Tax

A. *Introduction*

1. *Tax Borne by Transferee*

The Korean inheritance tax and gift tax are covered by a single act, the Inheritance and Gift Tax Law (IGTL),[400] which provides for a coordinated, if not an entirely unified, system. The salient feature of the system is that the tax is borne by the transferee, not by the transferor or the transferor's estate. Each heir is jointly liable for the inheritance tax imposed on the other heirs of the deceased.[401] Liability is limited in most cases to the value of property received. The donor is also liable to pay the gift tax if the donee is outside the jurisdiction of the tax authorities or is insolvent, or if the donee is holding the property in trust.[402]

2. *Residence*

Jurisdiction to tax is based on residence. The definition of residence and resident appears in Article 18 of the Civil Code. A resident is a person who has a domicile in Korea for any period of time or who maintains a "residence" in Korea for 183 days or more (before 2016, one year or more).[403] The effect of residence upon the imposition of each of the two taxes is discussed below.

B. *Inheritance Tax*

All property, wherever located, of a decedent resident in Korea at the time of his death is taxable to the heirs of the decedent, regardless of whether the heirs are resident in Korea.[404] Only the property located in Korea of a decedent who is not a resident of Korea at the time of his death is taxable to the heirs of the decedent, again regardless of whether the heirs are resident in Korea.[405]

To restate the principles set forth in the statute relating to inheritance:

(i) The residence of the decedent determines jurisdiction to levy the tax.

(ii) The residence of the heir is not relevant in determining jurisdiction to tax, although the tax is borne by the heir.

(iii) Location of the property is relevant only if the decedent is not a resident of Korea at the time of his death.

Inheritance tax does not apply in the case of a decedent residing outside Korea owning property located outside Korea, even if his or her heirs are residents of Korea. For example, if a Korean citizen resident in the United States at the time of his death holds property only outside Korea, bequests to his Korean resident heirs are not taxable by Korea. On the other hand, in the case of a United States citizen residing in Korea at the time of his death holding property only outside Korea, bequests to all of his heirs, whether residing in Korea, the United States or some third country, are subject to the Korean inheritance tax. For inheritance tax purposes, the residence of the decedent is controlling. It is irrelevant whether a particular heir is a resident or nonresident of Korea.

C. *Gift Tax*

All property, regardless of its location, received as a gift by a Korean resident donee is taxable to the resident donee. For a deemed gift that applies to property registered under the nominee's name, the donor (i.e., the actual owner) will be the taxpayer for deemed gifts arising from 2019. Only property located in Korea at the time of the gift is taxable to a nonresident donee. As an exception, if a resident donor donates to a nonresident donee such property in the form of shares of a foreign company the Korean assets of which consist 50% or more of the total assets of the company and funds in foreign financial accounts, the nonresident donee is subject to gift tax in Korea.[406] The rules related to excepted property under IGTL, however, have been repealed for gifts made on or after January 1, 2017, and the gift tax consequences for the excepted property governed by the International Tax Coordination Law, as further discussed under D. below.

To restate the principles set forth in the statute relating to gifts:

(i) The residence of the donor is not relevant in determining jurisdiction to levy the tax.

(ii) The residence of the donee is relevant in determining the scope of the tax.

(iii) The location of the property is relevant only if the donee is not a resident of Korea at the time of the gift.

D. *Effect of the International Tax Coordination Law*

As is evident from C, above, the receipt of a gift by a nonresident donee of property located outside Korea is not taxable under the IGTL. This gap in the statutory scheme has been closed to some extent by the International Tax Coordination Law (ITCL).[407] Article 35 of the ITCL provides, in pertinent part:

> Where a resident donates any property located abroad to a nonresident (excepting a donation effectuated by the death of the donor), the donor shall be obligated to pay the gift tax pursuant to this Act, notwithstanding Article 4(2) of the Inheritance Tax and Gift Tax Act.

An exception to the above is where the foreign country imposes a gift tax or tax of a similar nature, or provides an exemption from such tax. If the donation is made to a related party, then a foreign tax credit applies in lieu of the exception.

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[400] Inheritance Tax and Gift Tax Act, Law No. 5193 of Dec. 30, 1996, as last amended by Law No. 15224 on Dec. 19, 2017 (IGTL).

[401] For convenience, the authors use the term "heir" to refer to both legatees under a will and heirs under the statutory provisions for intestate succession.

[402] IGTL, Art. 4.

[403] Civil Code, Law No. 471 of Feb. 22, 1958, as amended, Art. 18. IGTL, Art. 2.

[404] The term "heir" is used here to include heirs and legatees, for convenience's sake.

[405] IGTL, Art. 3.

[406] IGTL, Art. 2(1), 4(1), (2).

[407] ITCL, Art. 35.

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E. Administration of Estates

1. General

Under Korean law, the property of a decedent passes directly to his or her statutory heirs, without a period of probate.[408] The estate is not a separate taxpayer. In most cases, the estate is not administered under the supervision of any court. The duty of administration falls on the heirs themselves, who must pay the creditors of the decedent from the estate property. Failure to settle with the creditors may make the heirs liable for the debts of the decedent. This liability may exceed the value of the property inherited. Although most estates are settled without the intervention of any court, any interested person may petition the court to appoint an administrator, and the court is required to act in such a case. A holographic will, recorded will, or secret will must be presented to the court for confirmation under the court seal.[409]

The debts of the decedent are assumed by each statutory heir in the same proportion as the value of property each inherits, but the amount of the debt assumed is not limited to the value of the property inherited. Therefore, an heir can suffer a net loss on an inheritance.[410] However, an heir's liability may be limited to the value of the property inherited if the heir petitions the local court with proper notice to creditors and certain heirs within three months after the death of the decedent for permission to make a limited acceptance.[411]

2. Intestate Succession

Wills are not common in Korea, and most property passes in accordance with the law of intestate succession. Property of the decedent passes by intestate succession as follows: first to children in equal shares, or issue of deceased children by representation, with a share to a surviving spouse as described below ("category 1"); next to parents in equal shares, with a share for a surviving spouse ("category 2"); next to siblings in equal shares, or to issue of deceased siblings by representation ("category 3"); next to lineal ascendants up to the fourth degree, collateral ascendants, aunts and cousins ("category 4"). A surviving spouse shares with other heirs in categories 1 and 2 as follows: each heir in the category is assigned one unit, and the surviving spouse 1.5 units. Thus, the estate of a decedent leaving two children and a spouse would be assigned 3.5 units, one for each child and 1.5 for the spouse, and would be divided proportionally. If the decedent is survived by a spouse and there are no heirs in either category 1 or category 2, the spouse inherits the entire estate.[412] To inherit, a spouse must be registered in a Korean family record (*ho jok*). A person may have only one spouse.[413] A child from an unregistered spouse may be recognized as a child outside of marriage, entitled to inherit in category 1 and receiving a share equal to that of a legitimate child. Children conceived but unborn at the time of the decedent's death are regarded as children for these purposes.[414]

3. Testamentary Dispositions

The Civil Code provides for holographic wills, recorded wills, notarial wills, wills by secret documentation and dictated wills.[415] A notarial will is prepared by a testator declaring or writing his will in the presence of two witnesses and a notary public. The notary may transcribe the will and must read it to the testator and the witnesses to confirm its correctness. The testator and the witnesses then each sign before the notary. A will by secret documentation consists of a holographic will that is placed in a sealed envelope upon which two witnesses record confirmation that the holographic will is enclosed. The sealed envelope must then be presented to a notary public or court clerk for verification within five days after confirmation by the witnesses. In an emergency, as in the case of a grave illness, a testator may dictate his will in the presence of two or more witnesses, one of whom must transcribe the will at the testator's request. The will is then read aloud to the testator and the witnesses, each of whom signs after confirming its correctness. Despite the existence of all of these provisions for testamentary transfers, as noted in 2, above, wills are seldom used in Korea.

A testator may designate in a will that either of the following is to govern: (i) the law of the country in which the habitual residence of the decedent is located at the time of the designation (the designation will be effective only if the decedent had maintained his habitual residence in the country until the time of his death); or (ii) the law of the situs of the real property with respect to the inheritance of real property. Absent such a designation, the will is to be governed by the law of the country of which the testator is a national at the time the will is executed. The amendment or revocation of a will is governed by the law of the country of which the testator is a national at the time of the amendment or revocation of the will.[416]

Trusts are solely creatures of statute and are neither suitable nor used for estate planning in Korea.[417]

4. Forced Heirship

Despite testamentary disposition to the contrary, the spouse and children of a decedent are entitled to claim one-half of the decedent's net estate, which they share in the same ratio as is prescribed for intestate succession. If no child or spouse survives the decedent, the lineal ascendants or, in their absence, the siblings of the decedent are entitled to claim one-third of the net estate. Gifts made within one year before death and gifts made to others with intent to cause harm to any statutory heir, regardless of when made, are included in the net estate and are subject to the forced heirship rules.[418]

5. Ancillary Administration

The Korean statutes do not provide for the ancillary administration of the Korean situs property of a nonresident decedent in a court of law. A nonresident heir or donee must instead designate a tax administration agent (who may be a lawyer or

[408] Civil Code, Art. 1005.
[409] Civil Code, Arts. 1093–1107.
[410] Civil Code, Art. 1007.
[411] Civil Code, Arts. 1019 and 1028.
[412] Civil Code, Art. 1003.
[413] Civil Code, Art. 810.
[414] Civil Code, Art. 855.
[415] Civil Code, Art. 1065.
[416] International Private Act (formerly known as the Law concerning Conflict of Law), Law No. 6465 (2001), Art. 49.
[417] Trust Law, Law No. 900 (1961) as amended.
[418] Civil Code, Art. 1112.

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a tax attorney) and must report the transaction to the relevant tax office. Where the nonresident decedent is of Korean origin, transfer of title to the estate assets can be recorded in the family register (*ho jok*). No procedures exist for transferring title to property of a decedent who is not of Korean origin (and hence not recorded in any family register). Under normal circumstances, an attorney-in-fact for an heir can carry out the procedures, based on proof such as family records, that the heir is legitimate.

6. Expatriation of Property

The expatriation of property from Korea in the form of a gift or inheritance is regulated by Korean law. The nonresident heir or donee must designate a tax administration agent, as in the case of an ancillary administration.[419] The tax administration agent handles all reporting, the payment of tax and other procedures on behalf of the nonresident heir. Bank deposits must be transferred by an appropriate attorney-in-fact from the decedent to the heirs. In this regard, the tax administration agent may act as an attorney-in-fact and must obtain a confirmation notice as to his status from the relevant tax office and present it to the financial institution.

After title to the assets is confirmed in the heir's name, the tax administration agent would prepare the documents necessary for expatriation. In general, a power of attorney may be prepared by heirs. A nonresident of non-Korean origin must use his or her notarized signature for a power of attorney. A nonresident heir of Korean origin may use a registered seal. A confirmation notice should be secured from the district tax office as to the balance of bank deposits to be expatriated. Upon receipt of the confirmation notice, a designated foreign exchange bank may convert Korean *won* into foreign currency and transfer funds out of Korea.[420]

It is far more convenient to use a registered personal seal if possible. A nonresident heir of Korean origin may first register a personal seal with the local county (*dong)* office.[421] A nonresident who does not wish to visit Korea may obtain a certificate of seal impression through a Korean consulate.[422] Local registration of the seal may then be completed through the tax administration agent. Once the seal is registered, the nonresident may act through the agent to effect tax reporting and transfer of the property.

F. General Principles of Inheritance and Gift Tax

1. Property Subject to Tax

In general, gratuitous transfers of all property of whatever kind (whether real or personal, tangible or intangible) and all interests in such property are subject to inheritance and gift tax. If the decedent is resident in Korea at the time of his death, the situs of the property is immaterial. If the decedent is a nonresident of Korea, then only the decedent's Korean situs property is subject to tax. In addition, the value of gifts subject to the gift tax that were made to heirs within 10 years of death are included in the gross estate of the decedent for inheritance tax purposes. Gifts made within five years of death to persons who are not heirs are also included in the gross estate.[423]

2. Presumed Inherited Property

Special rules cover payments or transfers made before death that are unsupported by any evidence of purpose ("unsupported payments"). In certain circumstances, such payments may be presumed to be part of the estate of a decedent. Unsupported payments in the amount of 200 million *won* or more by category (the categories are real property, financial assets and other assets) made within one year before death and unsupported payments in the amount of 500 million *won* or more by category made within two years before death are to be included in the estate. For example, if a decedent made two payments of 150 million *won* each to a third party for no apparent reason within one year before his death, 300 million *won* would be added to taxable inherited properties. These unsupported payments may be referred to as "presumed inherited property."[424]

The provision dealing with unsupported payments was confirmed by the Constitutional Court as constitutional.[425] It was held that the heirs have the burden of proof of showing that payments were made for specific purposes.

Unsupported obligations of a decedent, where the purpose of the obligation is not clear, are not allowed as deductions in accordance with the same parameters as apply to unsupported payments (i.e., 200 million *won* or more by category within one year of death and 500 million *won* or more by category within two years of death).[426] For example, if the deceased borrowed money from a third party in the amount of 200 million *won* twice within one year before death, and it was not clear where he used the borrowed money, the debt is not accepted and thus not deductible from the taxable inherited properties. Such unsupported obligations are also considered to be presumed inherited property.

Taxable property includes, in addition, the corpus of a testamentary trust (taxed to the beneficiary on the death of the testator), the corpus of an *inter vivos* trust (taxed to the beneficiary at the time of the funding of the trust), the right to receive annuity or similar payments, life insurance proceeds to the extent that the premiums were paid by the decedent, and retirement benefits paid to a beneficiary on the death of the decedent.

3. Property Excluded from Taxable Property Subject to Inheritance and Gift Tax

a. Foreign Property

Property of a nonresident decedent that has its situs outside Korea is not subject to inheritance tax. Gifts of property located outside of Korea are taxable under the IGTL if the donee is a resident of Korea or under the ITCL if the donor makes a gift to a nonresident donee. .

b. Property Passing to Charities

A bequest or gift made to a qualified person engaged in religious, charitable, educational, or other activities for the public

[419] NTBL, Art. 82.
[420] FEMR, Art. 4-7.
[421] Registered Seal Law, Law No. 724 (1961), Art. 3(2).
[422] Registered Seal Law Enforcement Decree, Art. 14.
[423] IGTL, Art. 13.
[424] IGTL, Art. 15.
[425] 94 Hun Ba 23 (1995).
[426] IGTL, Art. 15.

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good may be excluded from the taxable property of the decedent or donor. Qualified persons include the Korean national government, local governments, and qualified public interest corporations (i.e., corporations formed for religious, charitable, scientific, artistic, educational, cultural or similar objectives).[427] However, the recipient is subject to tax if the recipient does not in fact use the bequest or gift for the charitable purposes stated within two years. Property may also be excluded from taxable property subject to inheritance tax by an heir who himself or herself makes a gift of the inherited property within six months of the decedent's death to a qualified person.

c. Casualty Losses

Property that is damaged by *force majeure* before the due date for payment of the tax may be excluded from taxable property subject to inheritance and gift tax to the extent of the amount of the damage.[428] The loss is to be valued at market price, but not at a value exceeding the value used for inheritance tax purposes.

d. Life Insurance Proceeds

Insurance proceeds are included in taxable inherited property if the decedent was the purchaser of the insurance contract. Even if the decedent was not named as the purchaser, or contractor, the decedent may be deemed to be a party to the contract if he paid the insurance premiums.[429]

e. Retirement Benefits

Benefits received on a decedent's death under national pension and other government-sponsored pension schemes are exempt from inheritance and gift taxation.

4. Property Valuation

All property of the decedent is to be valued at its fair market value at the date of the decedent's death. Gifts are to be valued as of the date of delivery. The methods for valuing specific assets, such as various types of land, inventory, ships, intangibles, telephone rights, goodwill, stocks in closely held corporations, bonds, annuities, trusts, etc., are laid down in regulations.[430] The valuation of unlisted company stock is based on the higher of asset value or earning power value. Control premium applies in the case of shares that comprise more than 50% of the total outstanding stock of a company. The premium may not apply if the company is completely liquidated before the tax return becomes due.

Land is appraised for tax purposes annually by the local government.[431]

5. Property Situs

Korea has no estate, inheritance or gift tax treaty with any country; the situs of property is determined solely by domestic law.

a. Immovables and Movables

Real property and tangible personal property, and rights associated with such property, have their situs where the property is physically situated or where the rights are exercised.

b. Obligations

Obligations generally have their situs at the residence of the obligor. Bearer instruments are situated at the head office of the issuing corporation. Korean government bonds and local government bonds are deemed situated in Korea, whether in registered or bearer form.

c. Stock

The place of the head office or principal place of business of the issuing company is the situs of shares of stock.[432] The stock of a Korean corporation that has its head office in Seoul and its principal place of business offshore is arguably still a domestic asset.

d. Ships and Aircraft

The situs of ships and aircraft is the place of their registration.

e. Intellectual Property

The situs of patents, trademarks and other intellectual property rights is the place of their registration.

f. Business Property

The situs of other property related to a business is the location of the place of business associated with the property.

6. Tax Basis

As a general rule, heirs and donees receive a stepped-up tax basis in inherited and gifted property. Upon resale or other transfer, the assessed market value of the property at the time of death or gift is used as its tax cost. An exception to this general rule applies when a donee sells real property within five years of the gift. In such a case, and if the donation is deemed to have been intended to reduce capital gains tax unreasonably, a carryover basis is used to compute the tax.[433]

7. Computation of Tax

a. Inheritance Tax

(1) Gross Inherited Property

Inherited property consists of all property actually distributed to the heirs. The term is important in determining whether shares or real property can be transferred to the tax office in lieu of payment of tax in cash (payment-in-kind). Gross inherited property consists of inherited property plus presumed inherited property (discussed at 2, above).

Gross inherited property is reduced by tax-free gifts — qualified gifts made by the heir after the death of the decedent but before an inheritance tax return becomes due (see 3, b,

[427] IGTL, Art. 16.
[428] IGTL, Art. 23.
[429] IGTL, Art. 8.
[430] IGTL, Arts. 60–66.
[431] Law Concerning Public Notice of Values and Appraisal of Lands and Other Property, Law No. 4120 (1989), as amended, Art. 10(2).
[432] IGTL, Art. 5(1)(6).
[433] ITL, Art. 101(2).

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above) — and is increased by pre-death gifts. Pre-death gifts include any gifts that the decedent made to the heirs within 10 years before his death or to persons other than heirs within five years before his death. The value of such gifts is to be added to gross inherited property. Allowable deductions are subtracted from gross inherited property, to arrive at taxable inherited property.

(2) Allowable Deductions

(a) Resident Decedents

Allowable deductions for heirs of resident decedents include the following:

(i) All obligations of the decedent that are certain at the time of death and not barred by any statute of limitations. Obligations must be supported by adequate documentation; and

(ii) Funeral expenses, which may not exceed 10 million *won*, plus up to 5 million *won* for an enshrinement facility or natural burial site.[434]

No deduction is allowed for administration expenses, executor fees, or attorney or accounting fees.

(b) Nonresident Decedents

The heir of a nonresident decedent may deduct only obligations that relate specifically to the property that he inherits, such as taxes against the property, obligations secured by a lien or mortgage, and expenses of transferring the property.

(3) Exemptions

From taxable inherited property, certain exemptions may be deducted: (i) the basic exemption of 200 million *won*; (ii) the spousal exemption, which is the spouse's statutory share of inherited property, up to a limit of 5 billion *won*, including any gift added to gross inherited property; (iii) the children's exemption of 30 million *won* per child; (iv) the minor child's exemption of 5 million *won* times the number of years of age up to age 20; (v) the senior citizen heir's exemption of 30 million *won*; and (vi) the disabled heir exemption of 5 million *won* times the number of years of age up to age 75. As an alternative to the basic and other exemptions, but not the spousal exemption, a taxpayer may claim an overall deduction of 500 million *won*. A casualty loss exemption may apply if the inherited property was destroyed or damaged by *force majeure*. An exemption of 20%, up to a limit of 200 million *won*, may be taken from the value of financial assets (bank deposits, stocks, bonds, insurance proceeds, etc.).

After deduction of these exemptions, the result is the inheritance tax base, to which the tax rates apply.

(4) The Basic Tax

The basic tax is calculated on the inheritance tax base, irrespective of the number of heirs. Each heir is liable for tax in proportion to the value of the property each inherits. Taxable inherited property of all of the heirs is computed. Then the tax base of each heir is calculated to arrive at each heir's portion of inheritance tax.[435] A single tax return is filed by all of the heirs in the form of a single document signed by each heir or his representative.

The basic inheritance tax is determined by applying the following rates to the inheritance tax base.

Inheritance Tax Base	Inheritance Tax
Not over 100 million *won*	10% of such amount
Over 100 million *won* but not over 500 million *won*	10 million *won*, plus 20% of the excess of such amount over 100 million *won*
Over 500 million *won* but not over 1,000 million *won*	90 million *won*, plus 30% of the excess of such amount over 500 million *won*
Over 1,000 million *won* but not over 3,000 million *won*	240 million *won*, plus 40% of the excess over 1,000 million *won*
Over 3,000 million *won*	1,040 million *won*, plus 50% of the excess over 3,000 million *won*

For example, if the total inheritance tax base of an estate is 5 billion *won*, the total inheritance tax liability is 2.04 billion *won*. If four heirs are to receive equal shares of the property of the estate, each heir is liable for tax of 510 million *won*.

Note: As noted above, the basic tax is computed on total inherited property as a single item. Then, each heir is liable for his or her respective portion of the tax. The liability for payment of the inheritance tax falls upon the heirs individually in the proportion that the value of the property that each heir receives bears to the inheritance value of the total net estate of the deceased. In addition, each heir is jointly liable for the tax imposed on the other heirs up to the value of the property received by such heir.[436] Executors and administrators have no personal responsibility to file tax returns or pay the tax. A set of progressive tax rates is applied to the total value of the net estate. This method of applying tax rates differs from that of, for example, Japan. Under Japanese rules, the inheritance tax is calculated separately for each heir.[437]

b. Gift Tax

Gift tax is imposed at the same progressive tax rates as inheritance tax. The spousal deduction is 600 million *won* and the child's deduction is 50 million *won* (for a minor child, 20 million *won*). A deduction for a gift from an unrelated person is available in the amount of 5 million *won*.

[434] Inheritance and Gift Tax Law Enforcement Decree (IGTL-ED), Art. 9.

[435] IGTL, Art. 25.

[436] IGTL, Art. 3(4).

[437] See 7200 T.M., *Business Operations in Japan*.

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c. Credits

(1) Credit for Gift Tax

If the taxable property includes gifts to heirs made by the decedent within 10 years of death, or to other persons within five years of death, and gift tax was paid on the gifts, the amount of the gift tax paid is creditable against the inheritance tax.[438]

(2) Credit for Timely Payment of Tax

Heirs are entitled to a deduction of 3% from 2019 (5% for inheritance or gift made in 2018 and 7% before 2018) of the tax liability if they file the tax return on or before the due date. An heir whose residence is in Korea is required to file a return within six months after the decedent's death if the decedent resided in Korea. The filing period is extended to nine months if either the decedent or the heir has his address outside Korea.[439]

(3) Credit for Tax on Prior Transfers

When there are successive inheritances within 10 years of each other, a portion of the tax on the first inheritance is creditable against the tax on the second inheritance. The credit decreases ratably over the 10-year period.[440]

(4) Foreign Tax Credit

Foreign estate and inheritance taxes may be credited against the Korean inheritance tax. The limit on the credit for the foreign tax is equal to the lesser of actual foreign tax paid or the following:

$$\text{(Total inheritance tax)} \times \frac{\text{(Value of net taxable assets situated abroad)}}{\text{(Value of total net taxable assets)}}$$

d. Payment of Tax in Kind

Heirs and donees may pay tax by transferring real estate or company stock when more than 50% of their share of inherited property consists of real estate or company stock and tax due exceeds 10 million *won*. The director of a district tax office will approve an application for payment-in-kind if the subject property is adequate for "maintenance and disposition."[441] Payment-in-kind would relieve heirs and donees from losses realized on bargain sales of assets to raise cash to pay taxes. Properties that are not adequate for maintenance and disposition include: encumbered land; land upon which a building was built and owned by a third party (superficies); land upon which a grave or an unapproved building exists; land owned jointly with third parties; and other items of a similar nature as determined by the commissioner of the National Tax Service (NTS).[442] Cases where a decision was made in favor of the taxpayer found that: land that faces redesignation for public use is not disqualified from being used for a payment-in-kind;[443] the fact that the property consists of unlisted company stock does not prevent it from qualifying for payment-in-kind; and a significant decline in stock price after the death of the decedent should not disqualify it for payment-in-kind.[444] Nevertheless, whether to approve a payment-in-kind is within a tax office's director's prerogative.

e. Fixing of Tax Liability

Liability to inheritance and gift tax is established by the government's review and approval, unlike the corporation tax and other taxes, where tax liability is established by the filing of the taxpayer's return. After receipt of an inheritance or gift tax return, the tax office is required, in normal circumstances, to review, examine, and determine the tax within six months after receipt.[445]

f. Generation-Skipping Surtax

A surtax of 30% is added to the basic tax of any heir who is not a spouse, a child, or a parent of the decedent.[446] For donation or inheritance received on or after January 1, 2016, a 40% surtax applies if the value of the property exceeds 2 billion Korean *won*.

g. Additional Tax (Penalties)

Penalties in the form of "additional tax" (*kasanse*) are imposed as follows:

(i) Failure to file: a penalty of 20% (40% if failure to file is caused by a fraudulent method) of the tax due is imposed in the case of failure to file an inheritance or gift tax return at the time prescribed by statute.

(ii) Underreporting: a penalty of 10% (40% if underreporting is caused by a fraudulent method) is imposed on any value unreported or underreported.

(iii) Late payment: in the event that one or more heirs fail(s) to pay the tax at the time prescribed, a penalty of 0.025% (0.03% before February 11, 2019) per day is imposed.

[438] IGTL, Art. 28.
[439] IGTL, Art. 67.
[440] IGTL, Art. 30.
[441] IGTL, Art. 73.
[442] IGTL-ED, Art. 71, and Inheritance and Gift Tax Law Enforcement Regulation (IGTL-ER), Art. 19-4.
[443] National Tax Tribunal, Kuksim 2001 seo 1307 (2001).
[444] National Tax Service (NTS) Appeal Decision, SimSaJeungYeo 99-525 (2001).
[445] IGTL, Art. 76, and IGTL-ED, Art. 78. A tax office's director should inform heirs of the reasons for the delay if the tax liability cannot be established within the given period for unavoidable reasons.
[446] IGTL, Art. 27.

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XIII. Inter-Company Pricing

A. Transactions in Korea Between Parties in a Special Relationship

The tax authorities may recompute the income for the fiscal year of a corporation if the following factors are present:

(i) The transaction from which the income subject to tax arises is between the taxpayer and a person in a special relationship with the taxpayer or between the taxpayer and a person that is deemed to exercise *de facto* influence over the taxpayer corporation's management (for example, because that person has the power to appoint officers or manage the policy of the corporation, or has other kinds of influence) and the family members of such a person;

(ii) The transaction results in an unreasonable reduction of tax liabilities; and

(iii) The transaction lacks commercial reasonableness.[447]

Persons deemed to be "in a special relationship" to the taxpayer are:

(i) Any person that is deemed to influence the operations of a company by exercise of the authority to designate officers or operational policy (including any such person that is a director under Article 401-2(1) of the Commercial Code (CC) and his family members);

(ii) Any investor in the taxpayer (except for a shareholder holding less than 1% of the issued shares of a taxpayer[448] and the relatives of such an investor — the term "relative" is defined quite broadly under Article 767 of the Civil Code);

(iii) Any employee of the taxpayer or of an investor in the taxpayer and any person that depends on the taxpayer or its investors for his livelihood, and any relative living together with such persons;

(iv) Any corporation in which the investors of the taxpayer or the persons referred to above in (i) through (iii) has management control;

(v) Any corporation in which a corporation within (iv) has management control;

(vi) Any individual or corporation holding 30% or more of the equity of a corporation that holds 30% or more of the equity of the taxpayer; and

(vii) Any company in the taxpayer's Large Business Group (as defined in the Fair Trade Law (FTL)).

Effective from January 1, 2012, Article 2 of the National Tax Basic Law adopted a common definition of a related party, to be applied in lieu of terms used to define a related person in various tax laws. The definition, however, does not apply to a cross-border transaction, to which a separate definition of related person applies under the International Tax Coordination Law. A person is deemed to have management control in a corporation if it, along with persons falling within (i) to (v), above, either: (1) owns 30% or more of the interest in a corporation; or (2) is deemed to exercise *de facto* influence over the taxpayer corporation's management (for example, because that person has the power to appoint officers or manage the policies of the corporation). A person is deemed to have management control in a nonprofit corporation if the person, along with persons falling within (i) to (v), above, either: (1) has a majority seat in the board; or (2) contributed 30% or more to the fund for the establishment of the nonprofit corporation and any one of whom is an incorporator of the nonprofit corporation.

Article 52(2) of the Corporation Tax Law (CTL) indicates that market price as determined in consideration of sound social customs and business practices should be used as the basis for determining whether a transaction reduced tax liabilities unreasonably. Situations in which the tax burden is deemed to be unreasonably reduced are specified in the enforcement decrees. Nine categories of transactions in the nature of disguised distributions are listed.[449]

Comment: Article 52(2) of the CTL serves as the basis for the nine categories of unreasonable transactions. Article 20 of the old CTL did not specifically authorize Presidential Decrees prescribing such transactions. Thus, it might be argued that Article 88(1) of the Corporation Tax Law Enforcement Decree (CTL-ED) is *ultra vires.* However, the provisions of Article 88(1) of the CTL-ED are accepted in practice. The decrees provide that current market value is the standard for determining reasonableness. Current market value is determined by considering normal transactions between unrelated parties, sound social practices and business customs.[450]

In the case of a loan made by a company to a related party, the company is deemed to have received interest from the related party at the rate at which the corporation borrows money or alternatively, on an election basis, a bank overdraft rate which is announced by the government (currently 6.9%).[451]

If a special relationship is found to exist and if a transaction unreasonably reduces the tax burden of the taxpayer, the tax authorities may restructure the transaction. It should be noted, however, that the rules setting forth the procedures for restructuring such transactions were ruled unconstitutional in a 1995 case.[452]In line with the holding in the case, the relevant provisions were revised, but Article 67 of the CTL still leaves some room for argument. A taxpayer could assert that secondary effects and any income classification arising therefrom should be based on facts and circumstances. A tax inspector would try, as a general matter, to deem such income to be within the enumerated income classifications under Article 106 of the CTL-ED.

The relevant rules are discussed below.

First, the tax authorities disallow unreasonable expenses and include deemed revenue. Second, the tax liability of the taxpayer is recomputed accordingly. Third, a determination is

[447] CTL, Art. 52.

[448] CTL-ED, Art. 87(2), (3) and (4). Namely, an investor that held less than 1% of the total number of issued and outstanding shares of stock but excluding a "controlling shareholder." Effective January 1, 2003, the 1% limit applies to unlisted stock as well as to listed stock. CTL-ED, Art. 87(2).

[449] CTL, Art. 88(1).

[450] CTL Basic Guidelines, Art. 2-14-1(20).

[451] CTL-ED, Art. 89(3).

[452] *Taejin Tour Co. v. Pusanjin District Tax Office*, Constitutional Court case no. 93 Hun-ba 32 en bloc (Nov. 1995).

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made as to whether the recomputation of the tax affects the earnings and profits of the corporation. In the event that the disallowance of an expense or the imputation of revenue does not increase or decrease the earnings and profits of the corporation, the tax authorities look to the person that received the benefit of the transaction. If the person receiving the benefit is a shareholder of the corporation, the expenditure is considered to be in the nature of a dividend. If the person receiving the benefit is an employee, the benefit is characterized as salary income. If the transaction accrues benefit only to the corporation itself, there are no further tax consequences.[453]

Taxpayers may rely on business customs and practices in arguing that their transactions do not lack commercial reasonableness.[454]

There is no statutory mechanism for a corresponding adjustment. Thus, the transaction partner is not allowed to reduce its tax liability as a result of an increase in the subject taxpayer's transaction value. For example, assume Party A sold products to Party B at a price lower than market price. The tax authorities added income to Party A. Party B, however, is not allowed to increase its purchase price resulting from the adjustment to Party A's income.

Comment: The computation of earnings and profits for tax purposes is important under Korean law because of tax exemptions granted under Article 121-2 of the TILL for a foreign investment and other special laws. Tax benefits generally run for a period of years, for example, 10 years under Article 121-2 of the TILL. Benefits associated with dividends paid out of earnings and profits must be matched with earnings and profits of a specific year. Therefore, the calculation of the level of earnings and profits for tax purposes for a particular year affects the tax benefits associated with the dividends. For example, where the tax authorities disallow the deduction of expenses for the payment of insurance premiums not actually paid out by the company in the fiscal period concerned, the disallowance would have the effect of increasing the earnings and profits of the corporation because the benefit is retained by the corporation. On the other hand, penalty tax paid by the corporation during the fiscal period would reduce the earnings and profits for tax purposes and reduce the earnings and profits from which dividends could be declared to shareholders. A loan to an employee at a preferential rate of interest is deemed to create income for the corporation for tax purposes as described above. Because the corporation does not actually receive payment of the interest, however, imputing such income to the corporation does not increase the earnings and profits for the fiscal period concerned. The benefit is deemed to accrue only to the employee. Thus, the employee is deemed to have received salary income to the extent that the employee did not pay the market interest rate because of the employee's special relationship.

The commissions of offer agents and other trade brokers have been subject to scrutiny under the rules pertaining to parties in a special relationship. The tax authorities used to compare actual rates to "standard" published rates to determine whether the parties were dealing with others on an arm's-length basis. The published rates could thus function as safe harbors for commissions for related parties. Import commissions are treated differently from export commissions. Safe harbor import commissions are calculated by multiplying the first US$100,000 of the transaction value by the published rate, and any amount exceeding US$100,000 by 50% of the published rate.[455] Export commissions are 70% of import commissions. The standard published rates are listed by product category and are reproduced in part in the Worksheets.[456]

The standard commission rate approach was called into question by the Supreme Court decision of *Mitsubishi Corp. v. Sokong Tax Office*.[457] The Supreme Court affirmed a High Court decision striking down the use of a standard commission rate where the taxpayer was able to show that the actual commission rate applied between related parties, although lower than the standard commission rate, was not lower than a comparable, uncontrolled rate between unrelated parties. Based on this decision, the tax authorities have reconsidered their approach to related-party transactions and have abandoned the standard commission system.[458]

A domestic corporation or resident individual may adjust taxable income to correspond to a settlement reached between two competent authorities pursuant to the mutual agreement article of one of Korea's tax treaties.[459] The taxpayer has to file an amended return or a refund claim within three months after being advised of the settlement.[460]

B. Cross-Border Transactions Between Parties in a Special Relationship

1. Transfer Pricing Regime

a. Scope

The International Tax Coordination Law, Law No. 4981, of 1995 (ITCL), which came into effect on January 1, 1996, introduced a new transfer pricing regime for cross-border transactions, separate from the domestic transaction regime. Even without a finding of "unreasonable reduction of tax," under the ITCL, the tax authorities may impose an income adjustment to the extent the transaction price is lower or higher than a "normal" arm's-length price. In determining an arm's-length price for transactions between parties in a special relationship, the taxpayer is to choose the "best method" from the following: the comparable uncontrolled price method; the resale price method; the cost-plus method; the profit split method; or the transactional net margin method. If none of these methods is applicable, another reasonable method may be used.

Effective from January 1, 2003, the arm's-length principle and other provisions in the ITCL have priority over domestic

[453] CTL, Art. 67; CTL-ED, Art. 106.

[454] Corporation Tax Basic Guidelines, Art. 2-14-1(20); *Taegu Veterans Welfare Carpenters Ass'n v. Tong Taegu Dist. Tax Office*, 90 Nu 1014, Supreme Court (1990); *Taeduck Indus. Co., Ltd. v. Kwangmyung District Tax Office*, 88 Nu 10640, Supreme Court (1989); Ahn Kyung Bong, "A Study on Tax Avoidance," p. 84, Unpublished Ph.D. Thesis, Seoul National University (1993).

[455] NTA Notice No. 1108, Dec. 18, 1991.

[456] NTA Directive No. 943.

[457] 94 Nu 2541, June 28, 1994.

[458] *Kukil* 46507-530, Sept. 23, 1994.

[459] CTL, Art. 53; ITL, Art. 99.

[460] CTL-ED, Art. 91; ITCL, Art. 12; International Tax Coordination Law Enforcement Decree (ITCL-ED), Art. 21.

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transfer pricing rules for international transactions, except in the case of certain capital transactions and cross-border gifts.[461]

Two parties are deemed to have a "special relationship" for transfer pricing adjustment purposes when one party owns, directly or indirectly, 50% or more of the equity of another party, or when a party has the capacity to affect the business decisions of another party. This new regime is known as the "effective control" approach, and the overall effect is to broaden the definition of "special relationship" for Korean transfer pricing purposes. Special relationships may include: interlocking boards of directors; significant borrowing; business dependency; and reliance on the other party's intangible property.

An advance approval procedure is available to taxpayers seeking assurance that their transfer pricing method will be accepted by the tax authorities and that they will not be challenged for under-reporting income.

For instance, transfer pricing adjustments may create deemed dividends for a foreign company holding, directly or indirectly, the shares of a Korean subsidiary.

Effective for tax assessed on or after December 26, 2008, taxpayers may be relieved of the 40% or 10% additional tax in case of underreporting income (see V.B.10. and 11(ii)), if they have appropriate documentation for the chosen transfer pricing methodology and its application to their tax return.[462]

From taxable years commencing on or after January 1, 2019, a new rule is introduced to reflect international standards and clarify the principles for transfer pricing methods with respect to arm's length remuneration for the development, improvement, maintenance, protection, and utilization of intangible assets.

The CUP, PSM or DCF Valuation Methods take precedence over other methods. Use of the DCF Valuation Method requires objective and reasonable collection and computation of all elements such as cash flow projections, growth and discount rates, useful and residual value, tax burden, etc. Intangibles include patents, design rights, trademarks, copyrights, service mark rights, company names, brands, know-how, trade secrets, client information, rights under a contract, business rights granted by the government such as mining rights, road tolling rights, etc., and goodwill or ongoing concern value.

For hard-to value intangibles (HTVI), an ex-post valuation of HTVI is allowed as described below.

Intangibles are HTVI: (i) if there is no reliable comparable and (ii) at the time the transaction is entered into, projection of future cash flows or income expected to be derived from the transferred intangible, or the assumptions used in valuing the intangible, are highly uncertain.

Where the ex-post value differs significantly (e.g., more than 20%) from the ex-ante price, the latter will be deemed not to be based on reasonable assumptions. An adjustment of the arm's length price will then be made on an ex-post basis in consideration of transaction conditions and economic circumstances. However, the following exemptions apply:

- If the taxpayer sufficiently proves the appropriateness of the pricing in the subject transfer/use of intangibles;
- If the difference between the transaction price (based on financial projections at the time of the transfer) and the ex-post pricing (actual outcome) is not greater than 20%;
- If the transfer of the HTVI is covered by a bilateral advance pricing arrangement in effect for the period in question between the countries of the transferee and the transferor.

From taxable years commencing on or after January 1, 2020, for low value-added intra-group services, 5% cost plus mark-up can be applied as a safe harbor if certain conditions are satisfied. However, if the cost-plus 5% exceeds the lesser of 5% of revenues or 15% of operating expenses, the safe harbor does not apply. Qualified low value-adding services include accounting, auditing, legal services, human resource activities, etc., but exclude R&D, manufacturing, sales, procurement of raw materials, marketing, finance, insurance and reinsurance, extraction, exploration and processing of natural resources.

b. Reporting Requirements and Administrative Fines Under the Transfer Pricing Regime

Taxpayers are required to prepare and submit, within six months of the end of the fiscal year, a transfer pricing methodology report (for transactions of goods worth more than 5 billion *won* or services of more than 1 billion *won*); a summary transaction report; and a summary income statement of related parties (for transactions of goods worth more than 1 billion *won* or services more than 200 million *won*). However, there are some taxpayers who are exempt from the reporting obligation, as it will be explained below.

The summary income statement report form requires information on sales; cost of sales; general and administrative expenses; operating income and income before tax of all the foreign related parties with which a taxpayer has entered into transactions. Non-reporting or false reporting of the summary transaction report is subject to an administrative fine of up to 100 million *won*.

In line with the current OECD BEPS recommendations, a new comprehensive report on international transactions ("Comprehensive Report") must be submitted together with corporate tax returns. This new report, applicable from fiscal years commencing on or after January 1, 2016, is in addition to the summary of international transactions already required, covers controlled transactions and provides key information on the business operations of Multi National Enterprises ("MNE"). The detailed requirements relating to the filing of this Comprehensive Report are as follows:

(i) Content of Comprehensive Report:

– Local file: description of the local entity (organizational structure, business, etc.), financial information, and transfer pricing information on local entity's primary controlled transactions.

– Master file: MNE's group structure, business, intangibles, financial activities and tax positions.

(ii) Affected Taxpayers: all Korean companies and permanent establishments ("PEs") of foreign companies with annual revenue of more than 100 billion *won* and

[461] ITCL, Art. 4.
[462] ITCL, Art. 17.

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annual international related party transactions of more than 50 billion *won*

(iii) Filing responsibility:

– Local file: local taxpayer

– Master file: ultimate parent company of business group to which the local taxpayer belongs. If such ultimate parent company is not in Korea, the master file is to be filed via the local taxpayer.

(iv) Forms and procedures:

– The Comprehensive Report should be filed with the district tax office having jurisdiction over the local taxpayer and it may be filed electronically.

• Language:

• Local file: Korean

• Master file: Korean or English (on the condition that a Korean translation is provided within one month)

– Update of Comprehensive Report is required annually (though certain recurring items to be designated by Ministerial Decree may be updated every three years)

(v) Due date: within 12 months of the end of the fiscal year (may be extended up to one year upon approval due to unavoidable circumstances)

Effective from fiscal year ending on December 31, 2016, taxpayers must file a Country-by-Country (CbC) report for 2016 by December 31, 2017. CbC reporting has been added to the Comprehensive Report. Based on the amendment, taxpayers with international related party transactions and revenue meeting the criteria under the Presidential Decree are required to submit the CbC report within 12 months of the fiscal year end. Non-reporting or false reporting is subject to an administrative fine of up to 100 million *won*. The requirements under the revised ITCL-PD are as follows:

• The Comprehensive Report now includes the CbC report (in addition to the local file and master file).

• The following taxpayers are required to submit a CbC report:

(i) Ultimate (Korean) parent company of MNE whose prior year consolidated revenue exceeds 1 trillion *won*,

(ii) Korean subsidiary or branch of the MNE, where the parent company of a foreign MNE (1) is not required to file the CbC report under the law of its residence country or (2) is a resident of a country which does not have an agreement for the exchange of CbC reports with Korea,

(iii) Taxpayers belonging to an MNE group with consolidated revenue exceeding 1 trillion *won* that are required to file the master file and local file. It should be noted that a taxpayer belonging to an MNE group must notify the local tax office within six months of the fiscal year end to declare the entity that will file the CbC report on behalf of the MNE group. Failure to submit this information within the time limit will result in each of the above taxpayers being required to file the CbC report.

• Contents of the CbC report: Information set out in the ministerial decree, including breakdown of primary businesses by country in which the MNE operates, allocation of income, profit or loss before tax, tax payments, and capital.

• Due date: Within 12 months of the fiscal year end of the parent company. (The due date for filing the local file and master file has been extended from the current corporate tax return filing due date to within 12 months of the fiscal year end.)

• Form of CbC report: Both Korean and English language reports should be filed manually or electronically with the local tax office.

• Exchange of CbC reports: CbC reports received through the end of 2017 are expected to be exchanged with other tax authorities during 2018 pursuant to the CbC Multi-Competent Authority Agreement ("MCAA"). As of December 7, 2016, 50 countries (including Korea) are signatories to the MCAA.

2. Special Foreign Corporation

The anti-tax-haven provisions came into effect on January 1, 1997, and they apply in cases that meet the following circumstances:

(i) The Korean resident owns at least 10% of a foreign corporation;

(ii) They are deemed to have a special relationship (see V.B.1.a); and

(iii) The main or head office is located in a country with an effective tax rate of nil or less than 70% of the highest corporate income tax rate (currently 24%, 25% before 2023).

If these conditions are met, the Korean resident is then required to treat the foreign corporation's distributable earnings as dividends, except where the foreign corporation is in fact engaging in a trade or business through an office, shop, factory or other fixed form of business presence. Effective for fiscal years beginning on or after December 26, 2008, the anti-tax-haven provisions do not apply to an overseas subsidiary that receives income from sales of products to unrelated customers located in a tax haven jurisdiction.[463]

3. Thin Capitalization and Other Interest Expense Limitation Rules

The thin capitalization rules affect the Korean subsidiaries and branches of foreign corporations. Such subsidiaries and branches are required to treat as nondeductible a portion of the interest paid on loans from a foreign controlling shareholder (FCS) (or the head office in the case of a branch) or from third parties under a guarantee from an FCS. The debt-to-equity threshold rate is 3:1 (6:1 for certain financial institutions prior to this threshold rate's repeal as of January 1, 2008). However, effective from 2015, the threshold rate for non-financial institutions is reduced to 2:1. Even if the ratio exceeds the threshold

[463] ITCL, Art. 27-34.

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rate, a taxpayer may still be able to avoid non-deductibility by showing that the conditions and amount of borrowing from an FCS are comparable to those applying in the case of loans from an independent third party (i.e., an arm's-length principle applies) or that the debt-to-equity ratio prevailing in the relevant industry is higher than the threshold rate. In applying the thin capitalization rule, a taxpayer may take into account the greater of its net worth or paid-in capital, which is to be an average through-the-year balance rather than a year-end balance.

Comment: The thin capitalization rules are not applicable to a Korean company borrowing from a Korean controlling shareholder. Interest on excessive debt is not deductible to a Korean company for fiscal years beginning on or after January 1, 2000. It could, therefore, be argued that the rules violate the nondiscrimination provisions of some of Korea's tax treaties in the sense that they are designed to regulate a Korean company's borrowing from its foreign controlling shareholders only.

To implement Action 4 of the OECD BEPS Action Plan on limiting the deduction of excess interest expense paid to foreign related parties, a new interest denial rule based on EBITDA has been introduced which will apply from the fiscal years beginning on or after January 1, 2019.[464] The new limitation rule does not apply to financial and insurance businesses.

Under the new rules, non-deductible interest is the greater of (1) the amount of interest deduction denied under the thin capitalization rules and (2) net interest expense that exceeds 30% of the adjusted taxable income.

Adjusted taxable income is taxable income for the year plus depreciation on fixed assets and net interest expense. Net interest expense is total interest paid to foreign related parties less total interest received from related parties.

To implement the recommendation of Action 2 of the OECD BEPS Action Plan, interest paid by a Korean company (including a permanent establishment of a foreign company) to its offshore related party will not be tax deductible if such interest is not subject to tax in the jurisdiction of the offshore related party within a certain period of time.[465] This rule applies to fiscal years commencing on or after 1 January 1, 2018.

4. *Substance Over Form Principle in Cross-border Transactions*

Effective for fiscal years beginning on or after May 24, 2006, the tax authorities have specific authority to assess tax against the real party in interest, that is, the party who actually earned the income or was involved in the transaction, regardless of the party that appears on the transaction documents. Where a series of transactions is used unjustly to take advantage of a tax treaty, the tax authorities employ a step-transaction doctrine to collapse the steps into a single transaction in order to tax the real party in interest. In addition, transfer pricing rules regarding cost contribution and the use of intangibles have been introduced. In connection with a primary adjustment to the income of a Korean company, the tax authorities may make an upward adjustment to a price paid to such company by a person in a special relationship, and may deem dividends to be paid out, even though such party is not a shareholder of the Korean company.[466]

To enhance the effectiveness of taxation by clarifying which party bears the burden of proof involving an international transaction under suspicion of tax avoidance, a new rule on such burden was introduced with respect to taxable years on or after January 1, 2020.

Where domestic tax liabilities[467] are reduced by 50%[468] or more through a circumventive transaction, the burden of proof will shift from the tax authorities to the taxpayer, i.e., it will be the taxpayer's obligation to prove that there is no intent of tax avoidance; otherwise, such transaction will be deemed to have been entered into for the purpose of exploiting the relevant tax treaty and, consequently, the substance-over-form principle will apply. This provision does not apply if (i) the amount of reduced domestic tax liabilities is 100 *won* million or less and (ii) the amount of the circumventive transaction is 1 billion *won* or less.

Note: With regard to withholding tax on dividends, the Tax Tribunal has reached a meaningful decision as applied to a domestic Leveraged Buyout (LBO) investment structure of an offshore private equity fund.

The case concerned an offshore private equity fund (the "Offshore Fund") that established a Korean holding company ("KHoldCo") through a capital injection. KHoldCo then purchased shares of a domestic target company ("OpCo") with a combination of capital and LBO borrowings (the "Borrowings") from local and foreign financial institutions. OpCo then paid dividends to its domestic shareholder, KHoldCo, that subsequently used the dividend income to repay the principal and interest of the Borrowings. Although the dividends received by KHoldCo were not flowed through to the shareholder of KHoldCo (i.e., the Offshore Fund), the Korean tax authority made a withholding tax assessment (at 22% under the domestic tax rules) plus penalties on OpCo (i.e., withholding obligor) based on the assertion that the dividend income should be deemed to be paid to the Offshore Fund. The reasons behind this assessment arose from the Korea tax authority's allegation that KHoldCo was a mere conduit established for tax avoidance purpose; and the borrowings were in fact arranged by the Offshore Fund, and thus the beneficial owner of the dividend income is the Offshore Fund.

The Tax Tribunal acknowledged not only that the LBO investment structure adopted by the Offshore Fund was ordinary, but also that KHoldCo was established aimed at investing its capital and borrowings into OpCo and repaying the principal and interest of the borrowings using any dividends received. As a result, this structure was not put in place for an abusive purpose. The Tax Tribunal also found it difficult to believe that the Offshore Fund exercised substantial and practical influence over the dividend income. Furthermore, there is no provision under the Corporate Income Tax Law that the undis-

[464] ITCL, Art. 24.
[465] ITCL, Art. 25.
[466] ITCL-ED, Art. 23.
[467] Domestic tax items in this context include personal income tax, corporate income tax and other taxes covered by a relevant tax treaty.
[468] Percentage of reduction in domestic tax liabilities is calculated in comparison with the amount of domestic taxes that would have been payable if the transaction was re-characterized in accordance with the substance-over-form principle.

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tributed dividend income which the offshore shareholder does not receive is subject to withholding taxes. In conclusion, the Tax Tribunal ruled in favor of the withholding obligor, OpCo, and ordered the tax authority to cancel the withholding tax assessment and penalties.

The Tax Tribunal's decision bears meaningful implications, as it substantially eliminates the significant uncertainty surrounding a potential withholding tax exposure on dividends received by a domestic LBO vehicle, under a domestic LBO investment structure of an offshore private equity fund. As such, this case can be used as a point of reference for similar domestic LBO investment structures contemplated by offshore private equity funds in future.[469]

5. *Reporting Requirements for Offshore Financial Accounts*

A provision requires Korean residents and Korean companies, with the exception of financial institutions and residents subject to remittance-based taxation, to report offshore accounts. If the aggregate value of the balance of offshore financial institution accounts held by a Korean resident or Korean company as of the end of any month during a calendar year exceeds 0.5 billion won (before 2018, 1 billion *won*), the Korean resident or Korean company is required to file offshore financial institution account information with the tax office between June 1 and June 30 of the year following the subject calendar year. A maximum penalty of 10% (4.5% for accounts held during the 2010 calendar year) of the underreported account balance can be imposed. The rules are effective for accounts held during the calendar years beginning on January 1, 2010, and thereafter. Accordingly, the first report containing 2010 account information had to be filed between June 1, 2011, and June 30, 2011.

6. *Global Minimum Tax (Pillar Two)*

The global minimum tax rule was introduced into the ITCL in December 2022. It has 27 articles — from Article 60 to Article 86 — and it follows closely the Pillar Two Model rule issued by the OECD on December 20, 2021. However, the global minimum tax rule enacted by Korea does not include the Qualified Domestic Minimum Top-up Tax (QDMTT) and the domestic Income Inclusion Rule (IIR).

MNEs in scope will be subject to top-up taxes if the effective tax rate of constituent entities in a jurisdiction is less than 15%. Both the Pillar Two IIR and the Under Taxed Profit Rule (UTPR) were introduced, and they will apply to fiscal years beginning on or after January 1, 2024.

Korea is, so far, the only country that will introduce the UTPR in 2024. The detailed rules will be implemented through the ITCL enforcement decree, which is expected to be promulgated in late 2023 or early 2024. The first filing due date would be June 30, 2026, namely, 18 months after the fiscal year ending on December 31, 2024.

The Korean government released a 2023 Tax Law Amendment Bill, which includes a one year delay of Korea's UTPR. If enacted, the UPPR will be effective on January 1, 2025. This bill also includes proposed changes to reflect the Administrative Guidance issued in February and July 2023 by the OECD. The bill does not have any provisions on the QDMTT.

7. *Others*

The ITCL also contains provisions concerning cross-border gift/inheritance tax, and an extensive set of rules on competent authority assistance procedures, exchange of information and other administrative matters.[557]

[469] Kim & Chang Tax Alert, "Recent Tax Tribunal's Decision on Withholding Tax Assessment on Dividend Income Under a Domestic LBO Investment Structure," Jan. 16, 2015.

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XIV. Value Added Tax Law

A. *In General*

A value added tax (VAT) was created in 1976 to replace the various taxes that were previously levied on the supply of goods and services.[470] Each business person in the chain of supply pays a tax on the difference between the value of goods and services he sells and the goods and services he purchases. This difference is the value added. Each domestic supplier of goods and services acts as a government collection agent, collecting VAT from its purchaser. The customs office (not the supplier) collects VAT on imports. It is thus the supplier (or the customs agent) who is required to collect and pay the tax to the government, while the purchaser bears the tax burden. If no VAT is collected, it is the supplier, not the purchaser, who is liable to pay the government for the shortfall.

From the purchaser's perspective, the tax paid on goods and services purchased is an "input tax." From the supplier's perspective, the tax collected on goods and services sold is an "output tax." Each business person is entitled to credit input tax paid against output tax collected.

For all goods and services that are VAT leviable, the supplier must issue VAT receipts to the purchaser. (The only exception is where the supplier does not have a place of business in Korea, in which case the purchaser is required to issue the receipts.) Unless the transaction is exempt from VAT or the tax rate is zero, the supplier must collect the output tax from the purchaser. The supplier is required to file a quarterly tax return and to pay output tax, less a credit for input tax, to the tax office. If input tax exceeds output tax, the supplier is entitled to a refund. Ultimate consumers are not entitled to input tax credits. In this way, the VAT burden is passed on to the ultimate consumer, who pays a tax measured by the VAT rate times the price of the goods or services consumed. As a theoretical matter, the government does not levy a higher tax under a VAT system than under a simple retail sales tax system, but compliance may be more accurately monitored under a VAT system and, as a particular matter, tax revenues are higher.[471]

For further research on Korea's VAT system, see the VAT Navigator.

B. *Registration of Taxpayers*

1. *Taxpayers*

Every person engaged in the business of supplying goods or services, whether or not for profit (a "business person"), is required to collect VAT on all VAT-leviable transactions, unless the tax rate is zero.[472] Business persons include individuals, corporations, the national and local governments and unincorporated organizations and associations.

2. *Places of Business*

VAT is to be collected at each place of business.[473] A place of business is defined as a place where a business person or a business person's employees are located and a portion of a transaction is conducted.[474] The place of business of a foreign corporation or nonresident individual is that person's domestic place of business as defined in the Corporation Tax Law (CTL) or the Income Tax Law (ITL) (see V.A.2., above).[475] Every business person, at every place of business, is required to collect VAT from customers (a separate place of business of a business person is also treated as a customer), pay VAT to vendors and pay net VAT, if any, to the tax office. A business person having more than one place of business may pay VAT on a consolidated basis to the tax office having jurisdiction over its main place of business.[476] Each place of business of such a business person is, however, still required to file a VAT return with the tax office in its district.

If a foreign corporation contracts out to an independent, third-party logistics service provider for maintenance/delivery of goods in a bonded warehouse and does not undertake any other activities in Korea, while the foreign corporation undertakes conclusion of contracts and receipt/execution of orders from customers outside Korea, the bonded warehouse will not be considered to be a place of business of the foreign corporation under the VAT Law, provided that the bonded warehouse is not considered a place of business under Article 94 of the Corporate Income Tax Law.[477]

3. *Registration*

A business person is required to apply for a business entity registration certificate for each place of business within 20 days from the date of commencement of business.[478] The application may be made before the commencement of business.

Comment: The government computerizes VAT transactions using the registration numbers of the business places, so that input tax and output tax can be matched for each transaction.

Instead of registering each place of business separately, effective January 1, 2010, any business person may choose to register as a single business unit.[479]

C. *Tax Periods*

Each calendar year is divided into two six-month basic tax periods.[480] At the end of the first quarter within each basic tax period (the "preliminary period"), a preliminary VAT return must be filed. A final return must be filed at the end of each six-month basic tax period. There is no necessary connection between the taxpayer's fiscal year and the VAT periods, which follow the calendar year.

[470] Value Added Tax Law (VATL), Law No. 2543 of 1976, as amended.

[471] *See* T.R. Lee, "The Value Added Tax Act of 1976," 3 *Korean J. Comp. L.* 27 (1977).

[472] VATL, Art. 2.

[473] VATL, Art. 4.

[474] Value Added Tax Law Enforcement Decree (VATL-ED), Art. 4(1).

[475] VATL-ED, Art. 4(5).

[476] VATL, Art. 4(2).

[477] Ruling by the Ministry of Strategy and Finance, Nov. 10, 2010.

[478] VATL, Art. 5.

[479] VATL, Art. 4(3).

[480] VATL, Art. 3.

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D. Taxable Transactions

1. In General

Except where a specific exemption is provided, VAT is levied on the supply within Korea of all goods and services and the importation into Korea of all goods. The supply of goods and services necessary and incidental to a main transaction for the supply of goods or services is deemed to be included in the main transaction.[481]

2. Supply of Goods

Goods include all tangible and intangible property that has value.[482] Tangible property includes commodities, products, raw materials, machinery, buildings and other property having tangible form. Intangible property includes power, heat, and other property (including "rights") that does not have tangible form.[483] The supply of goods includes all deliveries or transfers of goods pursuant to law or contract.[484]

Comment: Effective December 31, 1992, the definition of intangible property was amended to include "rights."[485] The intent of this change was evidently to make clear that the supply of know-how is VAT leviable.

The self-supply of goods by a business person is included in the concept of supply and is thus taxable. Where a business person acquires or produces goods in the course of business and consumes such goods, but not for a purpose related to the business, output tax is deemed to be imposed on such consumption.

The personal use of goods acquired or produced in the course of business and donations of such goods are also included in the concept of the supply of goods and are thus taxable.[486] The giving of samples to customers and to the "unidentified public" is not considered to involve the supply of goods.[487]

Inventory held at the time of the closing of a place of business is considered to be supplied to the business person concerned.[488]

The consignor is the supplier of goods sold on consignment unless the consignor is unknown, in which case the consignee is deemed to be the supplier.

The putting up of goods as security is not taxable, nor is the transfer of a business as a whole.[489]

Effective for transactions entered into on or after January 1, 1999, the seller of a business as a whole (which specifically includes a person selling a business to which the purchaser adds a new business line or changes the business line purchased) could elect to have VAT apply at a 10% rate.[490] This election was repealed effective for transactions from January 1, 2007. Due to the repeal of the election, the sale of business as a whole is not a VAT-taxable transaction and no 10% election is granted.

3. Supply of Services

For VAT purposes, the term "supply of services" refers to the provision of services for consideration pursuant to law or contract, except for services provided by an employee to his employer.[491] The donation of services is not considered to be the supply of services for VAT purposes. Effective from July 1, 2012, the donation of a real property lease to a related party is a taxable transaction.

4. Importation of Goods

The importation of goods from outside Korea or from a bonded area is taxable under the Value Added Tax Law (VATL).

5. Timing of Supply of Goods

The statute provides general rules for determining when the taxable supply of goods takes place. Goods that are to be moved are deemed to be supplied upon delivery. Goods that are not required to be moved are deemed to be supplied when they are ready for the customer. If neither of these rules can be applied, the goods are deemed to be supplied at the time when the obligation to supply is fixed by law or contract.[492]

The enforcement decrees provide rules for determining the time of supply of goods, based on the type of transaction:

(i) Goods sold for cash or financed by a third party are deemed to be supplied when delivered.

(ii) Goods sold under installment and deferred payment contracts are deemed to be supplied in segments when each payment is to be received pursuant to the contract.

(iii) Goods sold under conditional sales agreements are deemed to be supplied when the conditions are fulfilled.

(iv) Goods, such as electrical power, that are supplied on a continuous basis, are deemed to be supplied when each payment is to be received. Long-term contracts calling for percentage of completion payments are also treated in this way.[493]

6. Timing of Supply of Services

The statute provides that services are deemed to be supplied when the work is completed or when the rights are exercised.[494]

Comment: The licensing of technology is considered to be the supply of services. The services are deemed to be supplied when the technology is used by the licensee. If the license is long term, supply will be deemed to occur as each payment falls due under the license agreement.

The enforcement decrees provide that service contracts providing for percentage of completion payments, deferred payment terms, and installment terms result in recognition of

[481] VATL, Art. 1(4).
[482] VATL, Art. 1(2) and VATL-ED, Art. 1.
[483] VATL, Art. 1(3) and VATL-ED, Art. 2.
[484] VATL, Art. 6(1).
[485] VATL-ED, Art. 1(2).
[486] VATL, Art. 6(3).
[487] VATL-ED, Art. 16(2).
[488] VATL, Art. 6(4).
[489] VATL-ED, Art. 6(6).
[490] VATL, Art. 6(6).
[491] VATL, Art. 7.
[492] VATL, Art. 9.
[493] VATL-ED, Art. 21.
[494] VATL, Art. 9(2).

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the supply of services at the time each payment is to be received under the terms of the contract.[495]

7. Place of Supply

Goods are generally deemed to be supplied at the place of business where the movement of the goods starts. If the goods do not need to be moved, the location of the goods is the place where the goods are deemed to be supplied.

Services are generally deemed to be supplied at the place of business where the work is performed. The international carriage of cargoes and passengers is deemed to be a service supplied at the place where the cargoes or passengers are loaded. As a result, all the compensation attributable to outbound international transport is subject to VAT, although the rate applied is zero, as discussed at F., below. For supplies made on or after January 1, 2021, certain electronic services including digital content are deemed to be supplied where the service recipient has a place of business, address or abode.

E. Tax Rate

The statutory VAT rate is 10%.[496]

If the price quoted does not include VAT, the VAT rate is applied to the price. If the price quoted includes VAT, however, VAT is calculated on the sum of 100% of the price plus the VAT rate times the price (i.e., 10/110 of the price quoted). If the supplier fails to collect the VAT, he must nevertheless pay to the tax office VAT calculated as if it were included in the price.

F. Zero-Rate VAT

Certain transactions are subject to zero-rate VAT. This means that the supplier is sometimes required to issue a VAT receipt and to file VAT returns with respect to such transactions, but that the purchaser does not pay any tax. Furthermore, the supplier is able to credit input tax against zero-rate output tax, and may thus be entitled to a refund. In this way, reporting zero rate VAT provides a more complete exemption than do the VAT-exempt transactions discussed at G., below. The following categories of transactions are zero rated: (i) the export of goods; (ii) the supply of services outside Korea; (iii) the supply of international transportation services by vessel or aircraft; and (iv) the supply of certain goods or services the compensation for which is received in foreign exchange, as designated by Presidential Decree.[497] (See also XV.M.1., below.)

A nonresident individual or foreign corporation is entitled to claim zero-rate VAT treatment only if the country of which that individual or corporation is a tax resident does not have a tax similar to the Korean VAT, or, if it has such a tax, gives Korean persons treatment equivalent to or similar to zero-rate treatment on a reciprocal basis.[498]

Goods and services, the supply of which generates foreign exchange and is therefore taxed at the zero rate, include:

(i) Certain qualified goods or services supplied within Korea to a nonresident individual or foreign corporation without a domestic place of business in Korea, the compensation for which is received through a foreign exchange bank and converted into *won*. For specialty services, business facility management services and business support services supplied on or after July 1, 2016, zero-rate VAT will only apply if the service recipient country allows similar zero-rate VAT treatment or does not have a similar tax to the Korean VAT.

Comment: The receipt of foreign exchange must be substantiated in writing by a foreign exchange bank. When the compensation is converted into Korean *won*, the foreign exchange bank issues a certificate of foreign exchange purchased. Under the Korean Foreign Exchange Transaction Law, the Ministry of Finance and Economy (MOSF) may require residents to bring into Korea foreign exchange earned when this is deemed necessary to achieve stability in the foreign exchange market.[499]

(ii) Certain qualified services supplied pursuant to a contract entered into directly with a nonresident individual or foreign corporation having a domestic place of business in Korea where the compensation for the services is received in Korean currency through a foreign exchange bank from the nonresident individual or foreign corporation. For specialty services, business facility management services and business support services supplied on or after July 1, 2016, zero-rate VAT will only apply if the service recipient country allows similar zero-rate VAT treatment or does not have a similar tax to the Korean VAT.

Comment: This provision was introduced by an amendment to the Presidential Decree in 1983 to give Korean agents a legal basis for applying the zero VAT rate to commissions received from foreign principals having domestic places of business in Korea, as well as from foreign principals not having domestic places of business in Korea. The rule applies provided the contract is entered into with, and the services are supplied to, the head office of the foreign principal and not its Korean domestic place of business.[500]

(iii) The processing of goods to be exported;

(iv) The supply of goods or services to vessels and aircraft in international service;

(v) The supply of goods or services to foreign governments and international organizations, and to the United Nations or U.S. armed forces stationed in Korea; and

(vi) The supply of goods or services in connection with a project financed by foreign or international monetary organizations.[501]

[495] VATL-ED, Art. 22.

[496] VATL, Art. 14.

[497] VATL, Art. 11.

[498] There are 33 such countries, including Japan and the United States, and most of the European countries, including France, Germany and the United Kingdom.

[499] FETL, Art. 7, effective Apr. 1, 1999.

[500] See Supreme Court case No. 84 Nu 571, Feb. 26, 1985, confirming the same approach.

[501] VATL-ED, Art. 26.

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G. Tax Exemption

The supply of certain designated goods and services is exempt from VAT. VAT is not collected by the supplier of these designated goods or services, so the supplier is in a position to charge less to the purchaser. The supplier is not, however, able to deduct input tax associated with such goods and services. The input tax is thus borne by the supplier as if he were the ultimate consumer. The term "VAT exempt" is misleading in the sense that the supplier must bear a tax that it would otherwise be able to pass on to the purchaser.

The supply of the following goods and services is treated as VAT exempt:

(i) Unprocessed basic foodstuffs;

(ii) Tap water;

(iii) Briquettes and anthracite coal;

(iv) Medical and health services (including the services of veterinarians, nurses, midwives, and pharmacists) and the supply of human blood;

(v) Educational services;

(vi) Passenger transportation services excluding transportation by aircraft, express bus, chartered bus, taxi, and certain other types of transportation;

(vii) Books, newspapers, magazines, official gazettes, and broadcasting, excluding advertising, but including electronic publications;

(viii) Postage stamps (excluding postage stamps for collections), revenue stamps, certificate stamps, notary certificates, and the use of public telephones;

(ix) Goods subject to the control of the Office of Monopoly (particularly tobacco, processed tobacco of less than 200 *won*, and ginseng);

(x) Banking and insurance services, such as the services rendered by commercial banks, securities companies, trust companies, securities investment trust companies, pawn shops, leasing companies, insurance companies, and other money lending businesses;

(xi) Leases of residential housing and land associated with such housing, not exceeding 10 times the area of the land upon which the housing is situated;

Comment: The lease of office space is treated as VAT leviable, while the lease of residential housing is VAT exempt. The imputed interest on key money (*chonse*) paid for the lease of office space is subject to VAT to be borne by the lessor unless otherwise stipulated in the lease agreement. Monthly lease payments for office space are subject to VAT, to be borne by the lessee unless otherwise stipulated in the lease agreement.

(xii) Land;

(xiii) The personal services of writers, composers and other persons specified by Presidential Decree. The Presidential Decree specifies dancers, actors, professional sportspersons and entertainers.[502] (The services of lawyers, tax attorneys, certified public accountants and engineers became VAT leviable with respect to services rendered on or after January 1, 1999);[503]

(xiv) Artistic works, artistic events, cultural events and nonprofessional sports events;

(xv) Admission to libraries, science exhibitions, museums, art galleries, zoos and botanical gardens;

(xvi) Goods and services supplied by religious, charitable, scientific or other organizations that are devoted to the public interest;

(xvii) Goods and services supplied by the government, local autonomous organizations, local autonomous group cooperatives or entities that carry out certain projects on behalf of the government, as specified by Presidential Decree, such as postal services and services provided by the Farmland Improvement Cooperatives; and

(xviii) Goods and services supplied free of charge to the government, local autonomous organizations, local autonomous group cooperatives or public interest groups, as specified by Presidential Decree.[504]

The above categories apply to the supply of goods and services within Korea. The supply of goods by importation into Korea is VAT leviable unless specifically exempted. Goods, the importation of which is VAT exempt, include certain goods exempt from customs duties and other designated goods.[505] (See XV.M.3., below.)

A business person may elect to treat otherwise VAT-exempt goods or services as VAT-leviable goods or services to take advantage of a zero-rate tax. This election is also available with respect to the supply of goods or services in categories 11, 13, or 16 of VATL Article 12(1) (leases, personal services, and goods and services supplied by public interest organizations).

H. Tax Base

The sum to which the VAT is applied (the "tax base") is defined as the total compensation to be received in money. If the consideration is not money, the tax base is the market value of the goods or services supplied. Market value is also used as the tax base where no compensation or unreasonably low compensation is received and for inventory held at the time of closure of a business.[506]

The tax base is the actual price as discounted, if a discount is given, and does not include the value of goods returned, the value of goods destroyed, damaged or lost before they reach the customer, or government subsidies.[507] In calculating the tax base, discounts provided after the supply of goods or services, bad debt losses, and promotional payments are disregarded.[508] Money deposits to assure the return of containers or packages are not included in the tax base.[509]

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[502] VATL-ED, Art. 35(1).
[503] VATL-ED, Art. 12(1)(3); Addendum to Law No. 5585 (Dec. 28, 1998), Art. 5.
[504] VATL, Art. 12(1).
[505] VATL, Art. 12(2).
[506] VATL, Art. 13.
[507] VATL, Art. 13(2).
[508] VATL, Art. 13(3).
[509] VATL Basic Guideline, Art. 13-48-5, ¶1.

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The tax base for imported goods is the value subject to customs tax, special consumption tax or liquor tax.[510]

The Korean *won* amount, as actually converted, is the tax base for transactions denominated in foreign exchange where conversion is made prior to the date on which the goods or services are deemed to be supplied. In other situations, the tax base is computed by applying the basic rate or arbitrage rate as announced on the date on which the goods or services are deemed to be supplied. Foreign exchange gains or losses arising from later conversion into Korean *won* are not taken into consideration in determining the tax base.[511]

The tax base for goods self-supplied to a business person (see D.2., above) is the market value at the time of consumption, except in the case of depreciable goods, to which special rules apply.[512]

I. VAT Receipts

A supplier is required to prepare two copies of each VAT receipt (VATL-ER Form No. 11), one for the supplier and the other for the buyer.[513]

VAT receipts must include the supplier's name and registration number, the registration number of the buyer, the tax base, the amount of VAT, the date of preparation and other information. If any of the required information is erroneous or is missing, the tax office may consider that no VAT receipt has been issued and may impose additional tax as described at L.2., below. The customs authorities issue VAT receipts to importers of goods.[514]

The "date of preparation" of the receipt is generally the date on which the goods or services are deemed to be supplied in accordance with the rules described at D.5. and 6., above. Business persons may also elect to issue VAT receipts for all transactions in a month, indicating the end of the month as the "date of preparation." Such receipts should be issued within 10 days after the end of the month. As an alternative, a business person may elect to issue VAT receipts on a semi-monthly basis.[515]

An amended VAT receipt may be issued in black ink (the initial VAT receipt is in red ink), before the tax office has imposed tax on the supplier. This may be necessary to rectify an error or to reflect an event that occurred after the initial VAT receipt was issued.[516] The VAT return may be amended within three years after the filing date if the supplier is entitled to a tax refund; the VAT return may be amended before the tax office imposes tax in the situation where the amended return results in the payment of additional tax.[517]

Comment: When an amended VAT receipt is issued by a supplier, the purchaser should be able to include it in his amended return, claiming a tax refund, while the supplier needs to make additional payment through the amended return. Having both parties claim is the only way to pass the VAT burden from one to the other. The purchaser, however, is subject to the three-year rule for claiming a tax refund, so that such an amendment is only effective if made within three years after filing.

In the case of the following specified transactions, VAT receipts need not be issued: (i) the hiring of taxis and transactions with peddlers; (ii) self-supply; (iii) the supply of services to specially related parties; (iv) the supply of goods for export, the supply of services outside Korea and the supply of international transportation services; (v) the supply of services to a foreign corporation that does not have a domestic place of business in Korea, the compensation for which is received in Korean *won* through a foreign exchange bank; (vi) the supply of goods or services to a nonresident or a foreign corporation that does not have a domestic place of business in Korea; and (vii) the receipt of imputed interest on key money in connection with the supply of VAT-leviable rental services.[518]

A simplified form of receipt (*yongsujeung*) that does not show the amount of VAT separate from the tax base may be used by certain kinds of businesses (e.g., retail sales, restaurants, hotels and the carriage of passengers).[519]

Another simplified form of VAT receipt (*keisanso* — ITL-ER Form No. 28) that does not show the amount of VAT separate from the tax base may be used in certain transactions — the rendering of VAT exempt services, for example.[520] The customer may present his business entity registration certificate request that the supplier issue a VAT receipt showing the amount of VAT in most such cases (except for the carriage of passengers).[521]

Both supplier and purchaser are required to submit a list of output VAT and input VAT transactions to the tax office, listing the names, amounts, etc. The list may be submitted in the form of a diskette.[522]

A supplier may issue an electronic VAT receipt. An electronic VAT receipt should have 30 fields as specified by the NTS notice and must be transmitted in an encoded form through a certification organization.[523]A business person may file tax returns through the National Tax Service (NTS) (website: http://www.hometax.go.kr/home/eaeehpe1.jsp (Korean language); http://www.nts.go.kr/eng/ (English language)).

Effective January 1, 2011, all corporate business persons must issue electronic receipts to customers with a tax credit of 100 *won* per receipt with a maximum of 1 million *won* per year. The tax credit reduces net VAT payable or increases net VAT refundable as shown in quarterly VAT returns. Such persons shall transmit data electronically to the tax office within 10 days after the end of each quarterly reporting period. Effective January 1, 2012, individual business persons with gross revenue of over 1 billion *won* must also issue electronic receipts.

[510] VATL-ED, Art. 13(4).

[511] VATL-ED, Art. 51, effective Jan. 1, 1999; VATL Basic Guideline, Art. 13-51-1.

[512] VATL-ED, Art. 49.

[513] VATL Enforcement Regulation (VATL-ER), Ministry of Finance and Economy Decree No. 1246 of 1977, as amended, Art. 16.

[514] VATL-ED, Art. 56.

[515] VATL-ED, Art. 54.

[516] VATL-ED, Art. 59; VATL Basic Guideline, Art. 16-59-1.

[517] NTBL, Arts. 45 and 45-2.

[518] VATL-ED, Art. 57.

[519] VATL, Art. 32; VATL-ED, Art. 79-2; VAT-ER, Art. 25; the form of receipt is determined by the commissioner of the NTA.

[520] ITL, Art. 163(1); CTL, Art. 121(1).

[521] VATL-ED, Art. 57(1.2).

[522] VATL, Art. 20; VATL-ED, Art. 66.

[523] VATL-ED, Art. 53(6); NTS Notice No. 2001-4, Jan. 16, 2001.

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With approval from the relevant tax office, a purchaser may issue a tax receipt if the supplier does not.[524] Effective January 2010, the procedure of purchasers issuing a VAT receipt must be applied for within three months where the value per instance is no less than 100,000 *won*.[525]

J. Bookkeeping

Every business person is required to maintain, at every place of business, ledgers in which VAT transactions are recorded.[526] The ledgers must show the names of buyers, the kinds of goods and services supplied, the tax base, the tax, the date of supply and other information. Separate ledgers are to be maintained for input tax and output tax. The ledgers are required to be kept for five years from the filing date for the VAT return with respect to the transactions recorded.[527]

Incentives, such as a tax credit of up to 2% of the value of all VAT transactions (a maximum annual credit of 5 million *won*), are offered to individual business persons accepting credit cards.[528]

K. Filing Returns

1. In General

Every business person engaged in the supply of VAT-leviable goods or services is required to file VAT returns on a quarterly basis. The returns show input tax as a credit against output tax, and net VAT payable or refundable. Payment must be made at the time the return is filed.

2. Net VAT Payable or Refundable

Input tax is creditable against output tax except for input tax in connection with:

(i) Transactions with respect to which the VAT receipts are incomplete, erroneous or not available.

(ii) Transactions not directly related to business.

(iii) Transactions in connection with the acquisition and maintenance of a small passenger car.

Comment: Input tax paid on the purchase of passenger cars and gasoline, and for the repair of passenger cars is not creditable against output tax, except by a business person whose main business is the operation of passenger vehicles.

(iv) The purchase of entertainment as defined in Article 35 of the ITL and Article 25 of the CTL, and the payment of expenses that are not directly related to business.

(v) Purchases made by a business person supplying VAT-exempt goods or services (a business person supplying both VAT-leviable and VAT-exempt goods or services is required to segregate the input tax associated with the VAT-leviable supplies).[529]

(vi) The purchase of goods or services deemed to have been supplied before registration with the tax office.

Comment: The date on which the application for business entity registration is filed is deemed to be the date of registration with the tax office.[530] The application should be filed as early as possible to ensure that input tax paid will be creditable against output tax.

A business person purchasing certain VAT-exempt agricultural, forest, or marine raw materials may credit deemed input tax calculated on the price paid for such raw materials.[531]

3. VAT Returns

VAT returns of business persons showing the tax base and net VAT payable or refundable are due 25 days after the end of the preliminary and basic tax periods.[532] A list, rather than copies, of input and output VAT receipts must be submitted with every return.[533]

An individual business person may prepare and file a preliminary VAT return on the basis of one-half of the VAT paid in the preceding basic tax period, if the total supply transaction value in the preceding basic tax period was less than 150 million *won*. Notwithstanding this, a return may be prepared on the basis of actual transactions, rather than on the basis of one half of the VAT paid in the previous period, when the total supply transaction value in the current preliminary tax period is less than 1/4 of the total supply transaction value in the preceding basic tax period due to a temporary business closure or business setback, or when the business person is eligible for, and wishes to receive, an early refund.[534]

VAT returns must be filed with the tax offices that have jurisdiction over each place of business. Application may now be made, however, to have the net VAT paid on a consolidated basis to the tax office that has jurisdiction over the business person's main place of business (see further below).[535]

The VAT liability of a business person is fixed when the return is filed. This means that a business person has no claim through administrative channels for a refund of VAT that was voluntarily paid without filing a legitimate amended return. Mistakes in the return for the preliminary or basic tax period may be amended by filing an amended VAT return, within three years after the date for filing the initial return, if a refund is requested on the amended return. However, the return must be filed before the tax office imposes tax, if the amended return is accompanied by an additional payment.[536]

A company may file a single VAT return with the tax office that has jurisdiction over its head or main office, rather than multiple returns by business place.[537]

[524] TILL, Art. 126-4.
[525] TILL-ED, Art. 121-4, as amended Feb. 2010.
[526] VATL, Art. 31.
[527] VATL, Art. 31(3).
[528] VATL, Art. 32-2.
[529] VATL-ED, Art. 61(1).
[530] VATL-ED, Art. 60(6).
[531] VATL, Art. 17(3).
[532] VATL, Arts. 18(1) and 19(1).
[533] VATL, Art. 20.
[534] VATL, Art. 18(2); VATL-ED, Art. 64(5).
[535] VATL, Art. 4.
[536] NTBL, Arts. 45(1)(1) and 45-2.
[537] VATL, Art. 4(3).

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L. Assessment

1. Determination of Tax

Each business person fixes his own VAT liability by filing a VAT return. The government may determine the tax base and the net VAT payable or refundable only if the business person fails to file a return, if the return contains errors or omissions, or if the business person is found to be evading taxes.[538]

If the VAT receipts, accounting books and records or any other evidence necessary for computing the tax base are either missing or substantially incomplete or false, the tax office may calculate the tax due using an estimation method.[539] The tax office has the authority to determine the total turnover of a business person based on information collected from similar businesses that maintain adequate books and records, from the production yield and efficiency rates promulgated by the National Tax Administration, and from other relevant standard rates such as inventory turnover rates.[540]

2. Additional (Penalty) Tax

Additional tax[541] (*kasanse*), in the nature of a penalty, is imposed for:

(i) Failure to register: 1% of the total value of goods and services supplied from the date of omission until the date of compliance;

(ii) Failure to issue VAT receipts or issuing erroneous VAT receipts: 2% of the value of the transactions concerned;

(iii) Failure to file returns: 20% (40% in case of a fraudulent method) of the tax due;

(iv) Underreporting: 10% (40% in case of a fraudulent method) of the tax due;

(v) Failure to pay VAT: 8.03% (9.125% before February 15, 2022, 10.95% before February 11, 2019) of the tax due per annum; and

(vi) Failure to report the tax base subject to zero-rate VAT: 0.5% of the value of the transactions concerned.

3. Refunds

Where input VAT paid exceeds output VAT collected, the government is required to make a refund within 30 days after the due date for filing the basic tax period VAT returns.[542] Refunds are thus paid semi-annually. A refund may be made within 15 days after a tax return was filed if a zero rate applies or if the goods or services are supplied in connection with the expansion of facilities. In such a case, the business person may choose to file monthly or bimonthly returns.[543]

M. Special Rules for Small Businesses

In 1996, the small business VAT system was amended to include a new simplified compliance regime (*kan-i*). Under the *kan-i* system, business persons whose annual revenue is less than 48 million *won* are taxed at the normal 10% VAT rate with respect to the value added, which is computed by means of a deemed value-added rate ranging from 20% to 40% of revenue, depending on which of 13 types of businesses is involved. For example, a retail business and a commission agent business are deemed to have 20% and 30% value added rates, respectively. Wholesale business is not one of the 13 types of businesses.

N. Collection of VAT on Payments to Foreign Businesses

A business person that engages in the supply of VAT-exempt goods or services in Korea (such as a hospital), and that receives services rendered in Korea by a nonresident individual or foreign corporation not maintaining a domestic place of business in Korea is required to collect VAT on payments for such services.[544] This is an exception to the usual requirement that VAT is to be collected by the supplier. The obligation to collect VAT on behalf of foreign persons does not apply to a business person that is engaged in the supply of VAT-leviable goods or services.[545]

O. Supply of Digital Content Services

Effective July 1, 2015, VAT applies to digital content, including game, software, music and movie files, provided in Korea by a foreign company or a non-resident without a Korean permanent establishment. When a foreign digital content provider directly sells digital content to a Korean user, it will be obligated to file VAT returns and pay VAT. If a foreign intermediary, such as an online open marketplace, is instead used to provide the digital content, the foreign intermediary is obligated to file VAT returns and pay VAT instead of the foreign digital content provider. The rule does not apply for services provided to a business taxpayer.

From July 1, 2019, in addition to the previously covered games, voice or video files, electronic documents, software, etc., cloud computing services, advertisement publication services, and brokerage services for goods or services are also included as VAT-able electronic services provided by foreign businesses.

Effective from July 1, 2022, a foreign business providing digital content services must maintain information on the type of digital content services provided, amount of supply and VAT, date of supply, and name and status of the customer.

[538] VATL, Art. 21.
[539] VATL, Art. 21(2).
[540] VATL-ED, Art. 69(1).
[541] NTBL, Arts. 42-2, 42-3 and 42-4, VATL, Art. 22.
[542] VATL-ED, Art. 72.
[543] VATL-ED, Art. 72.
[544] VATL, Art. 34.
[545] VATL, Art. 34.

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XV. Tax Incentive Limitation Law

A. *In General*

The Tax Incentive Limitation Law (TILL)[546] superseded the Tax Exemption and Reduction Control Law (TERCL).[547] TILL covers the same subject matter as TERCL.

TILL, like TERCL, provides its own tax incentives and regulates the administration of tax incentives specified in 23 other statutes, such as the Income Tax Law (ITL), the Corporation Tax Law (CTL), the Value Added Tax Law (VATL) and the Local Tax Law (LTL).

TILL provides tax incentives primarily to Korean residents, as defined in Article 1 of the ITL, and domestic corporations incorporated under Korean laws. In addition, since May 24, 1999, TILL has also covered all tax exemption and reduction provisions applicable to foreign investment and technology transfers under the Foreign Investment Promotion Law (FIPL). The major features of TILL are described in sections B. to T., below.

In the wake of the financial crisis that developed in the last quarter of 1997, the government liberalized the rules for the issuance by domestic Korean corporations and government entities of bonds denominated in foreign currencies. Since December 16, 1997, the government has relaxed restrictions on commercial loans and the issuance of foreign currency denominated securities for companies engaged in services, trading and manufacturing. Along with these liberalization measures, interest on foreign currency denominated bonds issued by domestic corporations and by agencies of the central government and local governments, is exempted from Korean corporation tax.[548] Effective for foreign currency denominated bonds issued on or after January 1, 2012, the exemption applies only if the bonds are issued outside Korea and the interest income is not attributable to a permanent establishment. In addition, the government expanded the exemption from taxation of gains realized from the transfer of stock of a Korean corporation by introducing an exclusion clause to the 10th category of domestic source income. See VI, B, above.

B. *Incentives for Small Enterprises*

1. *Definition of Small Enterprise*

The definition of a small enterprise (in Korean, literally "medium-small" enterprise) varies by industry category. Prior to January 1, 2015, a small enterprise could be defined as anything from an enterprise having no more than 50 employees up to a company having no more than 300 employees; the upper capital limits varied from no more than 2 billion *won* to no more than 80 billion *won*; the upper sales limits varied from no more than 30 billion *won* to no more than 50 billion *won*.[549] No "Large Group Company," as defined in the Fair Trade Law, could be included in the definition of a small enterprise. The definition also includes computer facility consulting businesses, software consulting, development and supply businesses, data processing businesses, database businesses, value added telecommunication businesses, and architectural, engineering and technical inspection service businesses.

Effective for taxable years commencing on or after January 1, 2015, the limits on the number of employees and capital are abolished and a different sales limit of up to 150 billion *won* applies depending on the type of business. Also, no company with an asset size of over 500 billion *won* can qualify as a small enterprise.[550]

2. *Tax Incentives*

Small enterprises are eligible for the tax incentives described in a to c, below.

a. *Tax Credit for Investment*

The following investment tax credit was allowed prior to 2021: 3% of the price of machinery and equipment acquired and used for business purposes.[551] Used machinery and equipment did not qualify. From 2022, this provision has been repealed and incorporated into a unified investment tax credit under Article 24 of the TILL (see E.4.).

b. *Tax Exemption for Establishing a Small Enterprise*

Small enterprises established before 2024 in rural areas, are eligible for a 50% reduction in their corporate tax for the fiscal year in which the profits are first generated, and for the following three years (100% reduction applies to small enterprises established by certain qualified young business persons outside the Seoul Metropolitan area).[552] Newly established small enterprises with less than 80 million *won* annual revenue are granted a 100% exemption (50% if they are established inside the Seoul Metropolitan area).

The same tax treatment applies to venture enterprises recognized as such within three years after formation pursuant to the Special Measure Law Concerning Fostering Venture Enterprises.[553]

The definition of businesses eligible for the tax benefits described above also includes manufacturing, mining, value added communications, research and development (R&D) business, cable broadcasting, program production, data processing, computer operations, engineering, and certain cargo moving.[554]

c. *Special Tax Exemption for Small Enterprises*

Corporation tax may be reduced for small enterprises engaged in certain manufacturing activities, value added communications, R&D, broadcasting business, engineering business, information processing, computer operating business, and cargo moving business.[555] The tax reduction rate ranges from 5% to 30%, depending on the location and size of the company

[546] Law No. 5584. effective Dec. 28, 1998.
[547] Law No. 1723 (1965), as amended.
[548] TILL, Art. 21.
[549] Small Enterprises Basic Law's Enforcement Decree, Presidential Decree No. 17026 (as entirely revised on Dec. 27, 2000), as amended, Art. 2, Tables 1 and 2.
[550] TILL-PD, Art. 2.
[551] TILL, Art. 5.
[552] TILL, Art. 6(1)(1).
[553] TILL, Art. 6(1)(2).
[554] TILL, Art. 6(2).
[555] TILL, Art. 7.

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concerned, and is effective for fiscal years ending on or before December 31, 2025. Effective from fiscal years commencing in 2018, the tax reduction is subject to a limitation. The maximum exempt amount is limited to 100 million *won* and is reduced in case of a decrease in the total number of employees as compared to the prior year. In such cases, the decrease is of 5 million *won* per employee.

C. *Incentives for Research and Development of Manpower*

The categories of tax incentives set out below (known as Incentives for Development of Technology and Manpower prior to January 1, 2003) are available to resident individuals and domestic corporations engaged in certain kinds of business to encourage them to develop technology and manpower.

1. *Research and Manpower Development Reserves*

Persons engaged in manufacturing, mining, construction or engineering service businesses could establish tax-deductible reserves to the extent of 3% of revenue (5% in the case of parts, materials, a technology intensive industry and a capital intensive industry) up to the fiscal year ending on or before December 31, 2006. These reserves must be used first when eligible expenditure is incurred for purposes of improving or creating technology, or developing manpower. The reserves must be used in this way within three years after they are established. Any reserve remaining at the end of the three-year period will be subject to an interest penalty. Such reserves are treated in the same way as the small enterprise reserves described at B, 2, a, above.[556]

The foregoing reserve sunset on December 31, 2006, but was again extended effective for fiscal years beginning on or after January 1, 2009. Thus, 3% of revenue could be set up as a tax-free reserve with the same feature of reversing over three years. The reserve is no longer available after the extended sunset ended on December 31, 2013.

2. *Tax Credits for Research and Development of Manpower*

Persons are granted a tax credit for research and development (R&D) costs for technology and manpower.[557]

For R&D expenditure spent for New Growth Industries and Original Technology Areas, a special credit of 20% (30% for small companies) of current expenditure plus the ratio of expenditure over three times the revenue (capped at 10%) is available. Effective from January 1, 2022, through December 31, 2024, R&D expenditure in National Strategic Technology Areas is eligible for a tax credit of 30% (40% for small companies) plus the ratio of expenditures over three times the revenue (capped at 10%).

For other R&D expenditure, taxpayers may select the credits based on:

(i) Their current expenditure; or

(ii) The excess of expenditure from the previous year.

In applying method (i), the credit rate for the increase over the previous year is 25% and 50% for small companies, whereas in applying method (ii), the credit rate for the current R&D expenditure is the ratio of a taxpayer's R&D expenses over the total sales capped at 2% (for small companies, the rate is fixed at 25%).

3. *Tax Credit for Facility Investment for Research and Manpower Development*

Credits are allowed for different types of investments such as research and manpower development facility, energy saving facility, safety facility, productivity improvement facility, etc. Credit rates ranges from 1% to 10% depending on the type of facility and size of the company. From 2019, various investment tax credits granted under different articles were moved to Article 25 (tax credits for certain facility investments) of TILL to combine and simplify the provisions.

4. *Tax Credit for Income from Technology Transfers*

Any person purchasing patents and utility models from a domestic person that developed such technology on or before December 31, 2018, is entitled to 5% (10% for small enterprises) of the purchase price as a tax credit.[558] The credit is not to exceed 10% of tax liability for the year concerned.

5. *Tax Exemption for Income from Transfers of Shares for Venture Capital Investment*

Gains earned by a Small Enterprise Investment Company under the Small Enterprise Creation Support Law, a limited liability company under the Special Law Concerning Fostering Venture Enterprises, or a New Technology Investment Company under the Specialized Credit Financing Business Law from the transfer of stock of qualified venture capital corporations may be excluded from taxable income.[559] Dividends earned by such qualified investment companies through 2022 are exempt from corporation tax.

Gains earned by any person from the transfer of stock of a credit extending short-term investment company that makes investments only in New Technology Investment Companies, gains earned by a Venture Capital Investment Partnership (*chohap*) from the transfer of venture capital, stock gains earned by a New Technology Investment Partnership from the transfer of venture capital stock and gains earned from the transfer of venture investment stock that has been held for five years or more are exempt from tax. The tax exemption applies to transfers of stock that was obtained from an initial stock offering, not to transfers of stock purchased from existing shareholders.[560]

A Small Enterprise Investment Partnership or a New Technology Investment Partnership must withhold tax when the partnership pays dividends to its partners.[561]

In addition, a partnership is to withhold tax on payments to its partners after deduction of partnership expenses.[562]

[556] TILL, Art. 9.
[557] TILL, Art. 10.
[558] TILL, Art. 12.
[559] TILL, Art. 13.
[560] TILL, Art. 14(1).
[561] TILL, Art. 14(4)–(7).
[562] TILL, Art. 14(6).

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6. Income Deduction for Venture Capital Investment

A resident individual may claim a 10% income (up to 50% of global income) deduction from global income in a single calendar year as selected from the period consisting of the investment year and the two years after the investment year, before 2017.[563]

7. Tax Exemption for Foreign Technicians

A foreign technician is eligible for a 50% income tax exemption for a period of 10 years (70% for the first three years and 50% for the following two years if employed by a leading company specialized in material, part and equipment business). This tax exemption is applied to the remuneration received by the foreign technician as compensation for labor provided to a Korean resident or a domestic corporation. The term "foreign technician" includes the following:

(i) Any person providing technical services under a technical service agreement as defined by the Ministry of Science and Technology pursuant to the Engineering Technology Promotion Law and whose contract price is no less than US$ 300,000; or

(ii) Any person having at least five years of experience (two years if the person holds a doctorate degree) at certain qualified foreign research institutes and working at certain qualified Korean research institutes including research centers of Korean enterprises with which he or she has no special relationship.[564]

The exemption is granted to employment contracts commencing before December 31, 2023.

8. Flat Rate Election for Foreign Nationals

Any foreign national, irrespective of his area of expertise, may elect to claim either a 19% flat tax rate on their gross salary with no deductions, or claim tax credits for the first 20 years after the commencement of work.[565] This treatment applies to employment contracts commencing before December 31, 2023. For foreign nationals working at a qualified regional headquarter company of a multinational group, the flat tax rate applies even if the work starts after 2023. However, the flat rate election does not apply if the foreign national is engaged by a company with a special relationship.

D. Cross-Border Capital Transactions

1. Public Loans

The lender of a public loan, as defined in Article 2(6) of the Law Concerning Inducement and Management of Public Loans (LIMPL),[566] is exempt from Korean tax.[567] To qualify, the public loan must contain a tax clause that indicates the tax exemption and the public loans must be ratified by the National Assembly.

A service or technology provider that is paid from a public loan may be exempt from Korean tax pursuant to the terms and conditions of the loan.[568]

Comment: Despite the tax exemption clause under the LIMPL, the government has not included a tax exemption clause in a public loan package since 1978/79, when Korea Nuclear Power Units 5 and 6 were financed by the Export-Import Bank of the United States.

2. International Banking Transactions

The following income derived by a person other than a resident, domestic company and foreign company with a domestic place of business, is exempt from income tax and corporation tax:

(i) Interest and commissions on foreign currency bonds issued by the central government, a municipal government or a Korean company. Effective with bonds issued on or after January 1, 2012, income is exempt only if such bonds are issued offshore;

(ii) Interest and commissions on foreign currency indebtedness if the borrowing is made, in accordance with the Foreign Exchange Transactions Regulations (FETR), by a foreign exchange institution from a foreign financial institution and is repayable in foreign currency;

(iii) Interest and commissions earned starting with foreign currency-denominated certificates of deposit or notes which are issued by financial institutions and issued or sold outside Korea; and

(iv) Income earned from the transfer of securities issued outside Korea by the central government, a local government or a domestic corporation.[569]

3. Tax Exemption for Dividends Received from Overseas Natural Resources Investment

Income received from investments in certain overseas resource development projects is exempt from corporation tax and income tax for fiscal years ending on or before December 31, 2015, to the extent the income was not subject to tax in the host country.[570]

E. Encouragement of Investment

1. Tax Credit or Additional Depreciation for Productivity Improvement Facilities

A resident who invests in productivity improvement facilities is entitled to a tax credit of 1% or 7% in the case of a small company.[571] Productivity improvement facilities include: (i) production process improvement or automation systems; (ii) state-of-the-art facilities; and (iii) enterprise resource planning systems, e-commerce facilities, logistic network management facilities, and customer relation management facilities. Used equipment is not eligible for this credit. As from 2022, the cred-

[563] TILL, Art. 16.
[564] TILL, Art. 18(1); TILL-ED, Art. 16.
[565] TILL, Art. 18-2.
[566] Law No. 5551 (1998).
[567] TILL, Art. 20(1).
[568] TILL, Art. 20(2).
[569] TILL, Art. 21.
[570] TILL, Art. 22.
[571] TILL, item 6, Art. 25(1).

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it has been repealed and incorporated into a unified investment tax credit under Article 24 of the TILL (see 4., below).

2. Investment Credits for Facilities in Environmental Protection or Security Facilities

A resident that invested in a special facility is entitled to a tax credit of 3% (10% in the case of a small company).[572] Special facilities are defined as: (i) fire prevention facilities; (ii) logistic business facilities; (iii) facilities installed in a consignee company by a consignor company; (iv) industrial disaster prevention facilities; (v) mining safety facilities; and (vi) facilities extended under the Emergency Protection Resources Management Law. No used equipment is eligible for the credit. Effective January 1, 2010, a resident who invests in energy saving facilities may claim a 1% credit (7% in the case of a small company) for investments made before 2021.[573]

Effective on and after January 1, 2010, a taxpayer may claim an investment credit of 3% (or 10% for a small company) of investment in environmental protective facilities made before 2021.[574]

As from 2022, these credits have been repealed and incorporated into a unified investment tax credit under Article 24 of the TILL (see 4., below).

3. Tax Credits for Job Creation

The credit for job creation applied to investments made until December 31, 2017. The temporary investment tax credit was available to Korean domestic corporations and resident individuals engaged in manufacturing, mining, engineering, retail, wholesale and most other businesses. A credit of 7% was available for fiscal year 2010 (reduced from 10% in 2009).[575] Effective for investments made on or after January 1, 2011, through 2014, the rate was reduced to 3% (4% for small and medium enterprise) and the credit granted on the condition that the number of jobs is not decreased. An additional credit based on the number of jobs created and a fixed amount (10 million *won* to 20 million *won* per job) was granted subject to a limit of 2% (3% for a small and medium enterprise) of the investment. Effective for investments made on or after January 1, 2015, through 2017, the basic rate of 3% applied only to small companies with a reduction of credit of 10 million *won* per each job lost. An additional fixed credit of 3% or 4% (6% or 7% in the case of small companies) was available but was subject to a ceiling per job added of 10 million *won* to 20 million *won*.

4. Unified Investment Tax Credit

As from 2021, in place of certain investment tax credits, such as those for small enterprises or small and medium-sized enterprises (SMEs) (article 5, TILL) and for productivity enhancement and special purposes (article 25, TILL), resident individuals and domestic companies are eligible for unified investment tax credits (excluding investments in land or vehicles) for investments in certain facilities, as follows:[576]

- Basic tax credit for general facilities: investment amount of the current year x 1% (10% for SMEs) plus incremental tax credit (current investment amount – three-year average investment amount) x 3% (10% for SMEs). For investments made in 2013, a basic rate of 3% (12% for SMEs) and an incremental rate of 10% applies;
- Basic tax credit for new growth business facilities: investment amount of the current year x 3% (12% for SMEs) plus incremental tax credit (current investment amount – three-year average investment amount) x 3%. For investments made in 2013, a basic rate of 6% (18% for SMEs) and an incremental rate of 10% applies; or
- Basic tax credit for national strategic business facilities: investment amount of the current year x 15% (25% for SMEs) plus incremental tax credit (current investment amount – three-year average investment amount) x 4%. For investments made in 2013, an incremental rate of 10% applies.

5. Special Withholding Tax Rate on Interest on Social Overhead Capital Bonds

A 14% final withholding tax applies to interest on bonds with a maturity term of seven years or longer issued on or before December 31, 2014, pursuant to the Law Concerning Fund Raising for Social Overhead Projects.[577] Such interest is not added to global income.

6. Tax Credit for Investment in Pharmaceutical Manufacturing Facilities

A taxpayer could claim 1% (6% in the case of small companies) of investment in pharmaceutical manufacturing facilities that met good manufacturing practice standards, as defined. Qualifying investments were to be made on or before December 31, 2019.[578] This credit was repealed and incorporated into the unified investment tax credit under Article 24 of the TILL from 2021, discussed above.

F. Industrial Structure Adjustment Measures

1. Capital Gains Tax Exemption on Consolidation of Small Enterprises

A small enterprise may defer the capital gains tax (*iwol kwase*) with respect to capital gains earned from the transfer of business property to an enterprise as part of a consolidation of small enterprises that engage in qualified lines of business.[579] The transferee enterprise takes the transferor's acquisition cost of the assets concerned as its own acquisition cost in the event of resale by the transferee. These tax benefits are recaptured, with interest, if the transferee closes the business or resells the assets concerned within five years after the consolidation.

A small enterprise that claims a tax exemption under Article 6 of the TILL, as a result of incorporation in a rural area, may continue to claim the tax exemption under the small enterprise consolidation regime.

[572] TILL, item 3, Art. 25(1).
[573] TILL, item 2, Art. 25(1).
[574] TILL, item 3, Art. 25(1).
[575] TILL, Art. 26; TILL-ED, Art. 23.
[576] TILL, Art. 24.
[577] TILL, Art. 29.
[578] TILL, Art. 25-4.
[579] TILL, Art. 31.

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2. Capital Gains Tax Exemption on Conversion from Sole Proprietorship to Corporation

An individual incorporating an existing business, other than the business of hotel and lodging, restaurants with a liquor license, etc., is subject to the same tax treatment as described in 1, above.[580]

Comment: Incorporation of a business not designated as exempt gives rise to capital gains tax for the individual proprietor that transfers business property to the corporation. By applying for a deferral of tax (*iwol kwase*), an incorporator or transferee will be relieved from capital gains tax, and the new company takes a carryover basis in the assets.

Effective January 1, 2008, the exemption applies to any Trade Adjustment Company, as defined, that requires restructuring as stipulated in a Foreign Trade Agreement.[581]

3. Restructuring by In-Kind Contribution

A domestic company could contribute assets or stock to a new company before 2010 with the following tax effects.[582] This provision was repealed effective December 26, 2008. Prior to this date, for ordinary corporation tax purposes, a transferor company could defer taxation from such an in-kind contribution until the transferee company's stock was sold; the transferee company used current market value, rather than the transferor's book value, for the assets or stock. A similar provision has been incorporated in Article 47-2 of the Corporation Tax Law as of December 26, 2008.

Different from the foregoing regime, a domestic company's contribution of its overseas subsidiary's stock in kind before 2016 continues to be subject to partially tax-neutral treatment. This is because, although the initial provision has been repealed, the basic concept still applies to the restructuring of an investment portfolio in foreign subsidiaries. When it transfers an overseas subsidiary's stock, a domestic company may defer income arising from the contribution of the stock to a new or existing subsidiary in a foreign country in return for stock. The income should be recognized in equal installments over three years after a three-year grace period. The benefit applied to contributions made before December 31, 2021, and it ended without any extension.[583]

4. Contribution In-Kind of Company Stock

Tax deferral applies when company stock is contributed in kind to establish a holding company before 2024.[584]

5. Assumption of Guaranteed Debt

A shareholder that guaranteed a debt for the company in which it is a shareholder could claim a deduction to the extent that it took over or repaid the company's bank if the company was liquidated by the end of year 2000 or the shareholder transferred all the stock to a purchaser designated by the creditor banking institution no later than December 31, 1999.[585]

The above provision had expired and was reactivated effective from May 21, 2009. The provision stated that a shareholder that assumed and repaid the debt owed by a company in which it is a shareholder could claim a deduction for the amount of the debt assumed and repaid provided that the shareholder disposed of its interest in the company to a third party by December 31, 2023, according to the financial structure improvement, and the company was liquidated no later than December 31, 2024, in accordance with a company liquidation plan submitted to a relevant tax office.[586]

6. Sale of Assets

An individual or a company could sell real property on or before December 31, 2012, and enjoy full exemption from, or a reduction of, capital gains tax if the sales proceeds were donated by the seller to a company the stock of which the shareholder owned, pursuant to a financial structure improvement plan.[587] This provision has now expired.

Effective from May 21, 2009, a company that sells assets no later than December 31, 2023, to repay bank loans is entitled to a tax deferral and any gain from sale of assets is deferred for three years and is taxed in equal installments over three years after the fourth fiscal year from the year in which the company sold the assets.[588]

A shareholder who sold assets and donated such cash to a company in which it is a shareholder by December 31, 2023, is exempt from tax on gains derived on such sale of assets. Alternatively, if a shareholder donated the assets to a company by December 31, 2021, so that the company uses the assets in repaying the bank debt, the donating shareholder can claim a deduction for the assets donated. In either case, the company that receives cash or assets is entitled to a deferral of tax on income upon receipt of cash or assets for three years and is taxed in equal installments over the next three years starting from the fourth fiscal year.[589]

7. Cancellation of Bank Debt in Connection with Corporate Reorganization or Composition Plan

Banking institutions may forgive debts to a borrower that is undergoing a corporate debtor recovery proceeding under terms approved by the court before 2022. The bank may claim the forgiven amount as a deductible write-off. The borrower need not immediately recognize income from the debt cancellation, but may recognize such income in equal installments over three years after the fourth fiscal year from the year in which the cancellation took place.[590] Pursuant to May 21, 2009, amendments, the tax deferral applies to a company whose debt is forgiven on or before December 31, 2012, pursuant to: (i) the Debtor Recovery and Bankruptcy Law; (ii) the Promotion of Corporate Reorganization Law; (iii) a special arrangement with a financial institution to whom the debt is owed; or (iv) an adequacy corrective measure under the Financial Industry Restructuring Law.[591]

[580] TILL, Art. 32.
[581] TILL, Art. 33-2.
[582] TILL, Art. 38.
[583] TILL, Art. 38-3.
[584] TILL, Art. 38-2.
[585] TILL, Art. 39.
[586] TILL, Art. 39; TILL-ED, Art. 36.
[587] TILL, Art. 40.
[588] TILL, Art. 34.
[589] TILL, Art. 40.
[590] TILL, Art. 44.
[591] TILL, Art. 44.

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A company under a Corporate Debtor Recovery Proceeding may create a new company in accordance with a plan of reorganization free of registration and acquisition tax.

8. Transfer of Company Ownership

Two separate business groups could exchange stock of each other's companies on or before December 31, 1999, and benefit from a tax deferral effect.[592] A transferring business group ("transferor") could transfer all of its interest in a target company ("target") to a receiving business group ("transferee") and could receive the tax benefits of deferral if the proceeds were used by the transferor to repay or take over the target's bank debt under an enterprise structure adjustment plan. Any gains from the transfer could be deferred until the transferor sold the stock. The target was allowed to deduct the deemed donation income that arose due to the transferor's debt payment. Also, the transferor was allowed to avoid the secondary effect that would otherwise have arisen due to the writing off of the asset deficiency. The transferor was allowed to deduct the repayment or to take over target's debt, and the loans taken over were not taken into account when applying the thin capitalization rules. The transferee was exempt from acquisition tax that might otherwise have arisen from the deeming of the transferee to have acquired the transferor's real property.[593]

The above provision had expired but, effective from May 21, 2009, it was reactivated with the modification that the transfer should take place no later than December 31, 2017, pursuant to a Financial Structure Improvement Plan.[594] Income from the transfer of shares may be deferred until the transferor disposes of the stock received in return.

9. Comprehensive Exchange of Stock

Effective as of January 1, 2010, capital gains from a comprehensive transfer of all the shares in a domestic company for shares in a new company or an existing company can be deferred if (i) the domestic company has been engaged in the business for one year or more, (ii) 80% or more of the consideration for the transferred shares is for shares in the new company or the existing company, and (iii) the new shares are distributed in proportion to the previous ownership ratio in the domestic company.[595]

G. Financial Institution Structure Adjustment Measures

1. Sound Bank Taking Over Net Liabilities of Distressed Bank

A sound bank taking over a distressed bank before 2019, pursuant to a "Corrective Measure" of a "Contract Transfer Decision" issued by the Financial Supervisory Commission (FSC), may claim as a deduction that part of the assumed liabilities that exceeds its total assets, including its loan portfolio ("Net Liabilities"). Deductible Net Liabilities include liabilities arising from customer deposits or bank borrowing. Net Liabilities must be either guaranteed by the Korea Deposit Insurance Corporation (KDIC) or affirmed by the FSC.[596]

2. Securities Market Stabilization Fund

A corporate partner of a partnership (*chohap*) may recognize dividend income in the year in which it is received, rather than when the partnership earns the income, with respect to a securities market stabilization fund in which an investment is made on or before December 31, 2004.[597]

3. Real Estate Investment Company

A real estate investment company (REIC), as defined in the Real Estate Investment Company Law,[598] is granted a 50% exemption on income from leasing of certain qualified housing for the first five years.[599]

H. Benefits Granted for Balancing Growth Between Geographic Areas

There are tax incentives for businesses in certain areas, for example, for the relocation of businesses from cities to rural areas.

1. Deferral of Income from Factory Relocation

A taxpayer that has income arising from the sale of an old factory in a metropolitan area before January 1, 2026, may defer such income after offsetting accumulated deficits. The deferred income may be recognized as income equally in the sixth through the tenth fiscal years after the sale.[600].

2. Deferral of Income from Corporate Head Office Relocation

A taxpayer may defer income from the transfer of real property on which its head or main office is located if the sale occurs before January 1, 2025, and the head or main office is moved to an area other than a population-intensive area within a metropolitan district.[601] The deferred income, after offset against accumulated deficit, may be recognized as income equally in the sixth through the tenth years after the sale.

3. Tax Exemption for Enterprise Relocating Factory

A small enterprise with operations in a population-intensive area within a metropolitan district for two years or more that sells an old factory, relocates outside the area, and starts operations in a new location by December 31, 2025, may be exempt from corporation tax or income tax on profits from operations completely in the fiscal year in which the plant is relocated and for the subsequent six years. In addition, tax may be reduced by 50% for the three years following the six-year period.[602]

A company engaging in business other than real estate business, "consumptive" business (for example, the business of a hotel, bar, or dance hall) or construction business may ap-

[592] TILL, Art. 46.
[593] TILL, Arts. 119(1)(9) and 120(1)(8).
[594] TILL, Art. 46; TILL-ED, Art. 43.
[595] TILL, Art. 38.
[596] TILL, Art. 52.
[597] TILL, Art. 57. This provision is no longer applicable but is still in the law.
[598] Law No. 06471 of 2001, as amended.
[599] TILL, Art. 55-2.
[600] TILL, Art. 60.
[601] TILL, Art. 61.
[602] TILL, Art. 63.

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ply the above tax exemption upon the relocation of a factory or head office by December 31, 2025.[603]

4. Tax Exemption for Enterprises Entering Agri-Industrial Complex

A domestic person entering an "Agri-Industrial Complex" on or before December 31, 2023, and starting a business that develops sources of agricultural and fisheries income or a small enterprise that engages in business within an industrial complex exclusively for small enterprises, is eligible for a 50% reduction of corporation tax for three years, as described in the first paragraph of XV.B.2.c. , above.[604]

I. Reduced Tax for Public Activities

1. Designated Cooperative Chohap Juridical Persons

Seven designated cooperative juridical persons (*chohap pobin*) (Credit Cooperatives, Agriculture Cooperatives, Regional Units of Fishing Cooperatives, Cooperatives of Small Enterprises, Cooperatives for Forestry, Tobacco Cooperatives and Cooperatives for Consumer Life) are subject to a 9% (12% for book profits in excess of 2 billion *won*) tax rate on book profits earned in fiscal years ending on or before December 31, 2025. These cooperatives do not have to maintain double-entry bookkeeping systems.[605]

2. Deductions for Income Generating Activities of Nonprofit Organizations

Schools, social welfare corporations, national university hospitals, art exhibition corporations and culture-related corporations may claim a tax-deductible nonprofit activity reserve for fiscal years ending on or before December 31, 2025, to the extent of the profits generated from income-generating activities.[606]

3. Deduction of Contributions to Political Parties

A taxpayer may claim a tax credit or deduction for contributions to a political party pursuant to the Law Concerning Political Funds.[607]

4. Reduction of Capital Gains for Public Projects

Income arising from the transfer of land for certain public projects on or before December 31, 2023, is eligible for a reduction of 20% of capital gains tax under the ITL.[608]

J. Benefits for Savings

1. Income Deductions for Personal Pension Savings

An individual could deduct from taxable income the lesser of 720,000 *won* or 40% of the principal on deposit at the time when the individual began to receive a pension after the term of a pension savings account matured.[609] This provision was repealed as of January 1, 2013.

2. Tax-Free Interest on Long-Term Savings

Interest income earned from long-term savings is tax free if it is used by an individual taxpayer to purchase a house and the following conditions are met:

(i) The account holder is at least 18 years old and has no house;

(ii) The quarterly deposit amount is less than three million *won*;

(iii) The term of the savings agreement is more than seven years; and

(iv) The taxpayer has only one such account, opened on or before December 31, 2012.[610]

3. Special Withholding Tax on Workers' Deposits

Financial institutions are to withhold 9% (instead of 14% on interest or dividends under Article 129 of the ITL) as a final tax, on income from accounts that:[611]

(i) Are installment-type or one-time-payment-type accounts offered by financial institutions;

(ii) Have a term exceeding one year; and

(iii) Have a total deposit per person not exceeding 10 million *won* (or 30 million *won* for a senior whose age is 60 or older or a handicapped person).

4. Korean Nationals Residing Overseas

Effective from May 21, 2009, a Korean national residing overseas could be exempt from tax on the income earned from a qualified investment fund if he/she joined the qualified fund between March 16, 2009, and December 31, 2010. No tax was imposed on dividends received on or before December 31, 2012, in regard to an investment of up to 100 million *won* per fund. For an investment exceeding 100 million *won*, a lower tax rate of 5% applied to the income earned from the funds.[612]

K. Citizen Security Benefits

1. Investment Credit for Employee Welfare Facilities

A domestic person may claim a tax credit to the extent of 7% of the acquisition or construction cost of employee housing facilities of a standard national economic size, dormitories, children's day care centers, and facilities for the disabled, the aged and pregnant women. Qualified investments are limited to those made on or before December 31, 2018.[613] Effective for acquisition of housing facilities outside the Seoul metropolitan area on or after January 1, 2011, the credit rate is increased to 10%.

[603] TILL, Art. 63-2.
[604] TILL, Art. 64.
[605] TILL, Art. 72.
[606] TILL, Art. 74(1); CTL, Art. 29; CTL-ED, Art. 56(4).
[607] TILL, Art. 76.
[608] TILL, Art. 77.
[609] TILL, Art. 86.
[610] TILL, Art. 87; TILL-ED, Art. 81(1).
[611] TILL, Art. 89.
[612] TILL, Art. 91-12.
[613] TILL, Art. 94; TILL-ED, Art. 94; TILL-ER, Art. 43.

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2. Capital Gains from Transfer of Houses Under Long-Term Lease Arrangements

A domestic person that leases five or more housing units of a standard national economic size may reduce its capital gains tax by 50% when transferring the units after leasing them for five years or more. A 100% tax exemption applies in the case of leases of 10 years or more, or in the case of houses constructed for leasing purposes, under the Leased Housing Law, for five years or more.[614]

3. Capital Gains from Transfer of Qualified Housing Units Purchased from Builder Holding Such Units as Inventory and Unable to Locate Tenant

An individual may apply either a flat 20% capital gains tax or tax at graduated rates (8–35%) on global income with respect to gains earned from the transfer of standard qualified housing units. Qualified units are units of a specified size purchased from a housing construction contractor between November 1, 1995, and December 31, 1997, and located outside the Seoul area, held for five years or longer, and on which the seller has obtained confirmation from the head of a local government unit to the effect that the contractor held such housing units as inventory and was unable to locate a tenant when he purchased the units.[615]

The same tax treatment applies to housing units purchased between January 1, 1998, and December 31, 1998, with identical qualifications.[616]

4. Capital Gains Tax Exemption for Transfer of New Housing Units

An individual may be exempt from capital gains tax on gains arising from the transfer of a new housing unit that he himself built and obtained a use permit or a construction completion confirmation for between May 22, 1998, and June 30, 1999, or that he acquired from a housing construction contractor. The transfer must take place within five years after acquisition or the capital gains tax qualifying for exemption is limited to the capital gains tax that the individual would have paid if the unit had been sold on the fifth anniversary of acquisition.[617]

L. Other Tax Benefits

1. Tax Exemption for Forest Development

Income arising from the sale made before 2019 of cut timber or standing timber that is not less than 10 years old qualifies for a credit of 50% of the income tax or corporation tax attributable to such income.[618]

2. Tax Credit for Taxpayer Filing Returns Electronically

Effective for tax returns filed on or after January 1, 2004, a taxpayer filing electronically may claim a tax credit of 10,000 *won*.[619]

3. Tax Credit for Developer of Overseas Resources

Effective on or after December 31, 2007, a developer may claim an investment credit of 3% of total investment necessary to secure a mining or exploration right or to make investment in a foreign company that has access to natural resources as defined by the Law Concerning Development of Natural Resources in Foreign Countries.[620] The credit is available on or before December 31, 2013.

M. Value-Added Tax Benefits

1. Zero-Rate Transactions

Zero-rate VAT is applied to the following transactions:

(i) The provision of military supplies by an enterprise licensed under the Defense Business Law;

(ii) The supply of petroleum products to a unit or agency of the Armed Forces under the Armed Forces Organization Law; and

(iii) The provision of subway construction services directly to the government or a subway corporation established pursuant to the Urban Railroad Law.[621]

2. Exemption from VAT on Goods and Services

The following transactions are exempt from VAT:

(i) The supply of petroleum products on or before December 31, 2015, to the National Fishery Cooperative Federation for electricity generation on islands to which electricity is not supplied;

(ii) The supply of food on or before December 31, 2015, by schools or companies commissioned to operate school cafeterias;

(iii) Fishing and farming services on or before December 31, 2015, provided by farming service corporations or fishing cooperatives;

(iv) The supply of "standard national housing" units and construction services related thereto (without time limit); and

(v) The supply of petroleum products directly to the central federation of fisheries corporations for use by vessels engaged in coastal and offshore fisheries or to a farmer or fisherman for the farming or fishery activities (full exemption until December 31, 2015).[622]

3. Exemption from VAT on Imported Goods

The following items are exempt from VAT when imported: (i) anthracite coal; and (ii) vessels to be used for taxable business.[623]

[614] TILL, Art. 97; TILL-ED, Art. 97.
[615] TILL, Art. 98(1); TILL-ED, Art. 98(1).
[616] TILL, Art. 98(3).
[617] TILL, Art. 99.
[618] TILL, Art. 102.
[619] TILL, Art. 104-8.
[620] TILL, Art. 104-15.
[621] TILL, Art. 105.
[622] TILL, Arts. 106(1) and 106-2.
[623] TILL, Art. 106(2).

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4. Tourists

Goods purchased by a tourist may either be subject to a zero rate of VAT or attract a VAT refund. They may also be exempt from individual excise tax. A foreign corporation that does not have a domestic place of business may receive a VAT refund with respect to food and lodging, advertisement services, or those goods or services purchased through its own liaison office.[624]

N. Individual Excise Tax, Liquor Tax, Stamp Tax and Other Taxes

Diplomats are exempt from individual excise tax on vehicles,[625] as are disabled individuals.[626]

In-kind contributions of stock under a qualified transfer or transfer of shares pursuant to a qualified merger or spin-off are exempt from the 0.5% securities transaction tax.[627]

O. Local Tax Exemptions

1. Registration and License Tax

The registration tax applicable on registration of acquired assets has been combined into the acquisition tax as of January 1, 2011. Registration tax not associated with the registration of acquired assets and license tax have been combined into the registration and license tax.

The following are exempt (50% exemption for item (i)) from the registration and license tax:

(i) The registration of mortgage assignment, provisional attachments or provisional enforcements on or before December 31, 2014, under the Asset Backed Securitization Law;

(ii) The registration of incorporation of a qualified small and medium enterprise until December 31, 2020; and

(iii) The tripled registration and license tax under Article 28 of the Local Tax Law does not apply to the registration of incorporation until December 31, 2021, of an investment company, private equity investment company or investment purpose company under the Financial Investment Services and Capital Markets Act, real estate investment company under the Real Estate Investment Company Act, and project financing company under CTL.[628]

2. Acquisition Tax

Acquisition tax is payable for the acquisition of such assets as real property, vehicles, memberships, etc The tax rate differs depending on the type of assets but, in general, is 4% of the acquisition price. The following are exempt from the acquisition tax until December 31, 2024:[629]

(i) 50% for the acquisition of assets in a merger between companies engaged in non-consumptive business for more than one year (60% in case of merger between small companies);

(ii) 75% exemption for the acquisition of real property by the resulting company after in-kind contribution under Article 47-2 of CTL;

(iii) 75% exemption for the acquisition of real property by the resulting company after a corporate division under Article 46 of CTL, a drop-down under Article 47 of CTL; and

(iv) 75% exemption for four years for real property acquired by a SME established before December 31, 2023, outside the Seoul Metropolitan area.

P. Tax Incentives for Foreign Investment

All tax-related provisions of the FIPL were moved to the TILL effective May 24, 1999.

1. Corporation Tax on Profits Earned by Foreign-Invested Enterprises

Note: For a foreign investment for which an exemption application is filed on or after January 1, 2019, the income tax exemption as discussed below no longer applies.

Foreign investments in certain high technology and industry support service areas, certain qualified investments in industrial complex type or individual type Foreign Investment Zones (FIZ) and investments in Free Economic Zones (FEZ), and other investments for which an exemption is deemed necessary to attract foreign capital are eligible for tax exemption under Chapter 5 of the TILL.[630] If the tax exemption is granted, the foreign-invested enterprise (FIE) is exempt from corporation tax in proportion to the foreign equity investment for the year in which profits are first generated (or the fifth year after the beginning of commercial operations if no profit has been generated by then) and for the following five years (three years for investment in industrial complex type FIZ and FEZ). Thereafter, the tax is reduced by 50% for the following two years.

Under the current rules, however, the cumulative tax incentive is limited to an aggregate amount of (i) 50% or 40% (for industrial complex type FIZ and FEZ) of the investment amount and (ii) 10 million to 20 million *won* per each new employee, but only up to 50% or 40% (for industrial complex type FIZ and FEZ) of the investment amount. The current rules took effect starting with tax exemption applications filed on or after January 1, 2016.

A tax exemption application must be submitted to the MOSF no later than the end of the fiscal year in which the FIE commences commercial operations.[631] Also, a foreign investor may apply for a pre-confirmation before the investment is made to confirm whether the investment qualifies for high technology or industry support service.

[624] TILL, Art. 107.
[625] TILL, Art. 110.
[626] TILL, Art. 112.
[627] TILL, Art. 117(1)(14).
[628] LTILL, Art. 58-3, 180-2. Prior to January 1, 2015, all of the registration and license tax exemptions were provided under Art. 119 of TILL, now repealed and moved to the Local Tax Incentive Limitation Law or LTILL. Some of the previous benefits are repealed.
[629] LTILL, Art. 57-2, 58-3. Prior to January 1, 2015, the acquisition tax exemptions were provided under Art. 120 of TILL, now repealed and moved to LTILL.
[630] TILL, Arts. 120 and 121-2(1).
[631] TILL, Art. 121-2(6).

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The term "high technology" includes only technology introduced into Korea no earlier than three years before the investment concerned; if the technology was introduced earlier, the applicant must show that its version of the technology is more efficient in terms of production or cost. The list of high technology areas specifies eligible product and service types.[632] Effective for applications made on or after February 7, 2017, high technology has been redefined for tax incentive purposes to ensure alignment with technologies entitled to R&D tax incentives for new growth engines/original technologies. If income from a business that is specifically eligible for the tax incentive constitutes 80% or more of the combined income from all related businesses, the tax incentive will apply with respect to all such combined income (assuming that all related businesses are effectively connected with the business specifically eligible for the tax incentive). In addition to the existing requirements, minimum monetary thresholds of USD 2 million have been added.

Dividends paid out of earnings in fiscal years for which a full tax exemption had been granted were also exempt from taxation by withholding. The withholding tax was reduced by 50% on dividends paid out of the earnings during the year for which the 50% exemption was granted. Effective for exemption applications filed on or after January 1, 2014, the exemption on the dividend withholding tax no longer applies.

Effective for applications for tax exemption filed on or after January 1, 2005, a foreign investment in the FEZ, a foreign project contractor in the FEZ, and a project contractor in the Cheju Investment Promotion Area are eligible for tax exemption. Tax exemption for these categories, and in the case of an investment for which an exemption is deemed necessary to attract foreign capital, consists of a full exemption for three years and a 50% reduction for the ensuing two years.

Effective January 1, 2005, special tax treatment is granted with respect to foreign investment in a foreigner-exclusive industrial district, a district for developing an enterprise-centered city, and contractors for developing such a city.[633]

2. Acquisition Tax, Registration and License Tax, Property Tax and Aggregate Real Estate Tax

An FIE may be granted an exemption from certain property related taxes (i.e., acquisition tax, registration and license tax, property tax and aggregate real estate tax) in proportion to the foreign investments for the first year in which the FIE has profits and the following five years (three years for industrial complex type FIZ, FEZ related investments, etc.). Those taxes may be reduced by 50% for the following two years. A local government may introduce a tax holiday for a maximum period of 15 years.[634]

3. Customs Tax on Foreign Goods

Foreign-source (imported) equipment that falls within the high technology investment classification and investments relating to FIZ and FES are eligible for a 100% exemption from customs tax (and also VAT and individual excise tax for high technology investment and individual type FIZ investment). To qualify, the equipment must be either contributed by the foreign investor or purchased by the FIE out of foreign currency contributed by the foreign investor and must be imported within five years from the report of the foreign investment.[635]

4. Income Tax on Foreign Nationals

See XV.C.7 for further detail.

Q. Other Special Tax Treatment

1. Business Promotion Expenses

Prior to January 1, 2006, a taxpayer that engaged in real property rental business, or restaurant or lodging business was only entitled to 20% of the revenue ceiling used for computing allowable business promotion expenses, resulting in a much smaller amount of deductible entertainment expenses.[636] Effective January 1, 2006, the 20% ceiling has been removed from the real property rental, restaurant and lodging businesses. Government-invested enterprises are now subject to a 70% ceiling, that is, they are subject to a 30% reduction on allowable entertainment expenses.

For qualifying cultural payments made until December 31, 2024, taxpayers may claim up to 20% of the normal limit for deductible business promotion expenses.[637] Qualifying cultural payments are defined as payments for cultural events, museum entrance fees and sporting events.

2. Imputed Income from Rental Deposits

A taxpayer that engages in real property rental business and that has a debt-to-equity ratio of 2-to-1 or higher is required to include a certain amount of deemed income from lease deposits received.[638]

3. Tonnage Tax

For fiscal years beginning on or after January 1, 2005, and ending December 31, 2024, a company that engages in international marine transportation business may choose to pay tonnage tax, rather than tax on its profits. Taxable income is calculated in proportion to the number of days spent in international voyages of each vessel times a fixed fee per ton times the total tonnage of the vessel. The fixed fee is 14 *won* (1,000 tons or less), 11 *won* (between 1,000 and 10,000 tons), 7 *won* (10,000 to 25,000 tons), and 4 *won* for tonnage in excess of 25,000 tons. Also, a special usage rate is to be applied. Once a taxpayer elects to apply this tonnage tax, the election is irrevocable for five years.[639] A taxpayer who is disqualified from applying the tonnage tax in any of two fiscal years is prohibited from applying it for the remaining years of the current election, plus five years, effective January 1, 2006.

[632] Regulation on Tax Exemption concerning Foreign Investment, MOSF Notice No. 2004-16 (Sept. 7, 2004).

[633] TILL, Art. 121-2(1).

[634] LTILL, Art. 78-3.

[635] TILL, Art. 121-3.

[636] TILL, Art. 136.

[637] TILL, Art. 136(3).

[638] TILL, Art. 138.

[639] TILL, Art. 104-10. The regime was to expire in 2009, but was extended for five years.

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4. Tax Regime for Look-through Entities

Effective January 1, 2009, certain entities may elect tax look-through treatment. Such entities are the *chohap* (partnership) as defined in the Civil Code, and the *ikmyong chohap*, the *hapmyong hoesa* and *habja hoesa*, as defined in the Commercial Code. (See III, D and E concerning Forms of Doing Business in Korea.) The *ikmyong chohap* (IC) is a partnership that has silent partners and an active partner, as defined by the Commercial Code, Articles 78 through 86. The IC regime is modeled on the German *stille Gesellschaft.* If an election is filed, no tax is paid by such an entity, but a proportionate share of profit or loss is to be reported, and any tax paid by each member, regardless of whether a member is a resident or a nonresident and regardless of whether a nonresident partner has a domestic place of business in Korea or not. An election is irrevocable for four tax years. Dealings between or among members may be reflected in the proportionate share of taxable income. Distributions to nonresident members which are considered to be passive investors, are considered as dividend income and are subject to withholding tax at 20% (22% including local income surtax) or applicable tax treaty rate.[640]

Comment: Contribution of land or shares by an individual or a corporation to the partnership is a taxable event to the contributing individual or corporation. The Foreign Investment Promotion Law should be amended in order to enable foreign direct investors to form a partnership with a Korean partner. Under the present law, the foreign direct investors are allowed to acquire shares of a *chusik hoesa* or *yuhan hoesa.*

5. Tax Exemption of Income Earned from Transfer of Products in a Logistics Facility or Bonded Area

A nonresident individual or foreign company without a domestic place of business may claim exemption from the 2% withholding tax that a Korean payer might withhold upon payment of business income arising from the first mentioned party's transfer of products that had been manufactured or purchased outside Korea, and held at a logistics facility. The nonresident individual or foreign company should file an application for tax exemption pursuant to the enforcement decree.[641]

R. Limitations on Tax Incentives

Various restrictions are placed on the tax incentives described in A to Q, above.

1. Disallowance of Overlapping Incentives

Only one investment credit can be claimed in the event one asset qualifies for more than one investment credit in the following areas:

(i) Small enterprises (see B, 2, a, above);

(ii) Technology and manpower improvement (see C, 3, above);

(iii) Productivity improvement facilities (E, 1, above);

(iv) Special facilities (see E, 2, above);

(v) Creation of jobs (see E, 3, above); or

(vi) Employee welfare facilities (see K, above).

An FIE is to limit each of the foregoing investment credits in proportion to the domestic investor's interest. In other words, when it is eligible for a tax credit under the FIPL or Chapter 5 of the TILL, the joint venture company is to claim the credit in the proportion that the capital invested by domestic investors bears to the total capital of the joint venture company.[642]

In addition, the investment tax benefits set out above in (i) to (vi) are not available when a taxpayer takes advantage of the following tax benefits:[643]

(i) Creation of a small enterprise in the agricultural and fisheries area and small manufacturing enterprise (see B, 2, b, and c, above);

(ii) Consolidation of small enterprises (see F, 1, above);

(iii) Conversion from a sole proprietorship to a corporation (see F, 2, above);

(iv) Enterprise relocating factory (see H, 3, above);

(v) Entering into an Agri-Industrial Complex (see H, 4, above); or

(vi) Restructuring small enterprises under the former TERCL.

Only one tax exemption can be claimed in the event a taxpayer qualifies for more than one of the following tax exemptions:[644]

(i) Creation of a small enterprise in the agricultural and fisheries area (see B, 2, b, above);

(ii) Small manufacturing enterprises (see B, 2, c, above);

(iii) Consolidation of small enterprises (see F, 1, above);

(iv) Conversion from a sole proprietorship to a corporation (see F, 2, above);

(v) Enterprise relocating factory (see H, 3, above);

(vi) Entering into an Agri-Industrial Complex (see H, 4, above);

(vii) Restructuring small enterprises under the former TERCL; or

(viii) Foreign investments under the FIPL in certain areas (for example, Jeju Island and Industry City Development Area) (see P, 1, above).

2. Establishment of Enterprise Rationalization Reserves

Effective from any fiscal year that included December 11, 2002, a taxpayer may no longer set up the reserve for tax credits or income deductions granted. A taxpayer could convert a past year's reserve to a voluntary reserve that could be paid out as dividends.[645]

[640] TILL, Arts. 100-14 through 100-26.
[641] TILL, Art. 141-2.
[642] TILL, Art. 127(3).
[643] TILL, Art. 127(4).
[644] TILL, Art. 127(5).
[645] Law No. 6762 (2002), Addenda, Art. 25; NTS Ruling Seo I 46012-10646 (2003).

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S. Minimum Tax

A domestic corporation and a foreign corporation with a domestic place of business in Korea that claim an income deduction, a tax credit or a tax exemption are required to pay a minimum tax of (at least) 10% of taxable income of up to 10 billion *won*, 12% of taxable income exceeding 10 billion *won* but up to 100 billion *won*, and 17% of taxable income exceeding 100 billion *won* (for fiscal years that begin on or after January 1, 2014). The rate for small companies is 7%.

A resident individual and a nonresident individual with a domestic place of business are subject to a 35% minimum tax. The minimum tax applies to business income only and is computed in the same manner as the corporate minimum tax.[646]

(i) Expense deductions:

- Development of technology and manpower (see C, 1, above); and
- Certain special depreciation and expense deductions under the former TERCL and the pre-94 TERCL.

(ii) Income deductions:

- Transfers of shares for venture capital investment (see C, 5, above);
- Factory or corporate head office relocation (see H, 1, and 2, above); and
- Income deductions under the former TERCL and the pre-94 TERCL.

(iii) Tax credits:

- Small enterprises (see B, 2, a, above);
- Development of technology and manpower (see C, 2 and 3, above);
- Encouragement of investment (see E, 1–3, above);
- Industrial structure adjustment measures (see F, 1 and 2, above);
- Citizen security benefits (see K, 1, above); and
- Tax credits under the former TERCL and the pre-94 TERCL.

(iv) Tax exemptions:

- Small enterprises (see B, 2, b and c, above);
- Cross-border capital transactions (see D, 2, above);
- Industrial structure adjustment measures (see F, 1, and 2, above);
- Enterprise relocating factory (see H, 3, above);
- Citizen security benefits (see K, 2, above);
- Other tax benefits (see L, 2, above); and
- International banking transactions (see D, 2, above).

Minimum tax is computed as the greater of:

(i) 14% (11% on income ranging from 10 billion *won* to 100 billion *won* and 10% for income up to 10 billion *won*; or 7% on the income of small enterprises for all income levels) of taxable income computed without taking into account the expense deductions and income deductions listed above in (i) and (ii); or

(ii) The corporation tax liability after deduction of the tax credits and tax exemptions listed above in (ii) and (iv) (see Worksheet 1).

The minimum tax may not be less than the corporation tax liability on taxable income (computed without a deduction for loss carryovers or tax-free income) before any foreign tax credit or disaster loss tax credit is taken. Corporation tax liability for this purpose does not include the special additional tax on capital gains (see V, B, 7, above), other additional taxes (see V, B, 11, above) or penalty charges due to recapture.

T. Recapture

1. Disposal of Assets

A taxpayer must recapture any investment tax credit if he disposes of the asset concerned within five years after claiming any of the following tax credits:[647]

(i) Small enterprises (see B, 2, a, above);

(ii) Development of technology and manpower (see C, 3, above);

(iii) Encouragement of investment (see E, 1–3, above); or

(iv) Citizen security benefits (see K, 1, above).

No recapture is required in the case of an in-kind contribution, merger, corporate division or asset exchange set forth in Article 50 of the CTL, the sale of an asset the useful life of which has expired, or a donation to a small enterprise.[648]

2. Employee Benefit Facilities

Recapture applies when a taxpayer uses employee facilities under Article 94 of the TILL for a purpose other than the intended purpose[649] within five years after acquisition or the completion of construction.

[646] TILL, Art. 132(2).

[647] *Id.*, Art. 146(3).

[648] TILL-ED, Art. 137(7).

[649] TILL, Art. 94(4).

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XVI. National Tax Basic Law

The National Tax Basic Law (NTBL)[650] sets forth general principles and rules for the administration of the various national tax statutes.

The NTBL states the general policies for administration of the tax system, including the rule of substance over form, the principle that tax assessment should be based on the books and records of the taxpayer, the principle that taxes may be levied only pursuant to law and the principle that neither law nor administrative collection practices may be changed retroactively to the detriment of the taxpayer.[651]

A. Shareholders' Secondary Tax Liability

One provision of the NTBL that may surprise foreign investors is the rule of secondary liability of certain shareholders of an unlisted corporation for national taxes levied on the corporation. If more than 50% of a corporation is owned, for example, by natural persons that are close relatives, as defined in the statute, such controlling shareholders have secondary liability for payment of the national taxes assessed on the corporation.[652] For tax liabilities that accrue on or after January 1, 2015, the secondary tax liability will also apply to the majority shareholder of a listed corporation. In addition, a company, more than 50% of which is controlled by a single corporate investor, has proportionate secondary liability for the taxes of its majority shareholder. Such liability is limited to the percentage held by the majority shareholder times the total value of the subsidiaries' net assets. Secondary liability arises only if the tax authorities are unable to collect the primary tax liability.[653]

These two principles of secondary tax liability may cause trouble for a foreign person investing in a Korean joint venture company. For example, where a Korean corporation holds more than 50% of the joint venture company, the tax office may hold the joint venture company liable for the unpaid taxes of the Korean investor. Likewise, where a Korean family has holdings in a joint venture company and also holds more than 50% of a Korean domestic company that has tax problems, the tax authorities may attempt to satisfy the tax liability by attaching the shares the family members hold in the joint venture company. If the family members hold more than 50% of the joint venture company, the tax authorities may also look to the assets of the joint venture company to satisfy the tax liability.

B. Priority of the Right to Collect Taxes

Before 1991, the NTBL gave government claims for the collection of taxes priority over the claims of secured creditors perfected less than one year before the assessment of tax. On September 3, 1990, however, the Constitutional Court ruled that the priority provisions of the NTBL were unconstitutional.[654] The offensive provisions have been repealed and, effective January 1, 1991, the government's right to collect taxes does not have priority over security interests registered before the taxpayer's return is filed or the tax liabilities are otherwise fixed (the "statutory period").[655]

Under the statute, the tax office has the right to petition the court to invalidate any fraudulently registered security interest. Security interests registered in favor of a party in a special relationship within one year before the statutory period begins to run are deemed to be fraudulent.[656]

C. Statute of Limitations

The limitation on actions with respect to national and local taxes (other than customs duty) is five years.[657] The statutory period begins to run from the time when the government's right to assess arises (from the deadline for filing, for example). There had long been a question as to whether this limit applied only to the government's right to collect taxes and not to the government's right to impose taxes, or whether it applied to both. The Supreme Court has ruled that the five-year statute of limitations applies both to the government's right to collect and to its right to impose taxes.[658] With respect to the inheritance tax, the government has 10 years to bring an enforcement action.[659]

An exception to the running of the statute of limitations may be made for: a tax office adjustment in accordance with the terms of a settlement reached between competent authorities under a tax treaty.[660]

Exceptions to the five-year rule are provided for: (i) tax evasion due to a fraudulent or other unjust act (10 years or 15 years for offshore transactions); and (ii) non-filing (seven years or 10 years for offshore transactions). Notwithstanding the foregoing rules, the 10-year rule on inheritance and gift taxes continues to apply, but with a 15-year rule for fraud and nonfiling.[661] These rules apply to tax with respect to which the government's right to levy arises on or after January 1, 1995.

Effective from January 1, 2009, the statute of limitations for a loss year that would otherwise expire under an ordinary five-year limit runs for one year after the statutory deadline for filing a tax return for the fiscal year to which the loss was carried forward and is applied to reduce the fiscal year's otherwise positive taxable income. A taxpayer has the obligation to maintain records until the statute of limitations has run.[662]

D. Taxpayers' Bill of Rights

The National Tax Commissioner is required to publish a taxpayer's bill of rights, and each taxpayer undergoing a criminal tax investigation, tax audit or other specified investigation is to be informed of such rights. No second audits are permitted unless tax evasion is alleged or there are other good causes. A taxpayer has the right to consult with a tax adviser during an audit.

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[650] Law No. 2679 of Dec. 21, 1974, as amended.
[651] NTBL, Chapter 2.
[652] NTBL, Art. 39.
[653] NTBL, Art. 40.
[654] Decision No. 89 Hunga 95.
[655] NTBL, Art. 35(1)(3).
[656] NTBL, Art. 35(4).
[657] NTBL, Art. 27(1).
[658] Decision No. 84 Nu 572, Dec. 26, 1984.
[659] NTBL, Art. 26-2(1)(4).
[660] NTBL, Art. 26-2(2)(2).
[661] NTBL, Art. 26-2.
[662] NTBL, Arts. 26-2(1)(5), 85-3(2) proviso.

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Ten days' notice of a tax audit is to be given to each taxpayer unless the tax authorities have reason to believe that the taxpayer is about to destroy evidence. The tax authorities must notify a taxpayer of the results of each audit or investigation. The confidentiality of taxpayer information is to be respected.[663]

E. Refund Claim

A taxpayer (including a nonresident and a foreign company) may file a refund claim with the tax office that has jurisdiction over the withholding agent.[664] The claim should be made within five years (three years prior to 2015) after the withholding agent has filed a withholding tax report. Within two months after it receives such a claim, the tax office must decide whether or not to pay the refund. In the case of a decision rejecting the claim or if there is no response from the tax office, the taxpayer may file an appeal procedure with the National Tax Service (NTS) or the Tax Tribunal (TT) and then to the courts.

Effective for refund claims made on or after January 1, 2009, the ability of a nonresident individual or foreign company to claim a refund is specifically expanded to include all domestic-source income categories that are subject to withholding by a Korean payer, not including the categories of income for which the taxpayer is required to file a return, namely, income relating to operation or sales of real property located in Korea and capital gains from transfer of real estate rich company shares.[665] Effective for refund claims filed on or after January 1, 2020, the ability of a nonresident individual or foreign company to claim a refund of a withholding tax is limited to cases where the withholding agent is being closed or refuses to claim a refund on his or her behalf. Nonresident individuals or foreign companies may claim a refund under the ITL or CTL provisions.

F. Electronic Documentation

A taxpayer may process all or part of its books and records by computer and may maintain them in electronic media such as tapes, disks or electronic storage in accordance with the regulations. Taxpayers will be deemed to have satisfied the documentation requirements if they convert the documents to electronic media and maintain them in a generally recognized electronic document storage format as specified by Article 31-2 of the Electronic Transactions Basic Law, as introduced in 2005, and expanded in 2009.[666]

[663] NTBL, Arts. 81-2 through 81-9.
[664] NTBL, Art. 45-2.
[665] NTBL, Art. 45-2 (4).
[666] NTBL, Art. 85-3.

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XVII. Surcharges

There are three sets of surcharges levied on the income tax and corporation tax of most taxpayers. These are the education tax, the local income surtax, and the agricultural and fishery communities special tax (AFCST).

A. Education Tax

The education tax is imposed on revenue earned by banks and insurance companies, as a surtax on the liquor tax; transportation, energy and environment tax; and the individual consumption tax, and as a surtax on certain local taxes such as the fixed levy inhabitant tax, the registration and license tax, the acquisition tax, the property tax, and the vehicle tax.[667] (See the Worksheets for rates.)

B. Inhabitant Tax

Inhabitant tax is levied on individual income taxpayers at their domiciles or residences within Korea and on domestic and foreign corporations at their places of business as a flat tax amount.[668]

The fixed tax amounts levied on the domiciles, residences and places of business of taxpayers vary by location, ranging up to 10,000 *won* per year, and for corporations, from 50,000 to 500,000 *won* per year.[669] Effective from 2011, the previous workshop tax that was levied on the size of the business place was combined into the inhabitant tax, levied at the rate of 250 *won* per square meter annually.

C. Local Income Tax

Effective from 2011, the previous inhabitant tax levied as a surcharge on the income tax and the corporation tax was renamed as the local income tax. The surcharge is 10%, applied to the amount of the tax due.[670] Effective from 2014, independent from the rules regarding the tax base, the tax rate for the local income tax was introduced into the LTL so that the tax can be assessed independently from the income and corporation taxes (as opposed to a surtax). However, since the local tax base is the same as that of the income and corporation taxes and since the local income tax rate is set at 10% of the income and corporation tax rates for the respective tax brackets, the local income tax in effect (for now) is 10% of the income and corporation taxes.

The 10% tax is also applied to withholding tax on payments to resident individuals, nonresident individuals and foreign corporations without domestic places of business in Korea, so that the tax is not applied only to inhabitants of Korea. Effective from 2015, the 10% surcharge is also applicable to withholding tax on payments made to a domestic corporation.

D. Agricultural and Fishery Communities Special Tax

Effective from July 1, 1994, all taxpayers are subject to the Agricultural and Fishery Communities Special Tax Law (the "AFCST Law").[671] The purpose of this law is to raise funds to strengthen the competitiveness of the Korean agricultural and fishery industries and to develop agricultural and fishery communities in Korea. The tax is scheduled to apply through June 30, 2014.[672]

AFCST is levied in the form of additional taxes on individual and corporate income, additional customs duties, and additional securities transaction tax, and local tax (the "principal taxes"), and is to be reported and paid at the time of the reporting and payment of the principal taxes. See the Worksheets for rates.

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[667] The expanded education tax has adopted some of the features of the defense tax (Education Tax Law, Law No. 4279 of 1990). The defense tax was repealed, effective Dec. 31, 1990. The registration tax was combined into the acquisition tax effective from Jan. 1, 2011. The education surtax applies to the previous registration tax portion of the combined acquisition tax.

[668] LTL, Art. 74.

[669] LTL, Art. 78.

[670] LTL, Art. 92, 103-20.

[671] Law No. 4743, Mar. 24, 1994.

[672] Law No. 7026, Dec. 31, 2003.

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XVIII. Land-Related Tax

Effective January 1, 2005, a new national tax on real estate was introduced.[673] While the property tax (on buildings) and the land tax (on land) were combined under the Local Tax Law (LTL), which lowers the rates somewhat, a national tax was also introduced. Certain property with high value is subject to this tax. The local tax is to be deducted and the current year's tax is not to exceed 150% of the previous year's property tax burden. Land subject to the general tax rate and the separate rate (see below) the aggregate value of which exceeds 500 million *won* and 8 billion *won*, respectively, is subject to this new tax. Residential property, the aggregate value of which exceeds 900 million *won* (1.2 billion *won* for a household with only one residential property, zero *won* for a corporate owner), is also subject to this tax. Valuation is based on the government-assessed value on June 1. Taxpayers must file tax returns in the period from December 1 to December 15 each year. See Worksheet 2 for the rates.

Note: On November 13, 2008, the Constitutional Court ruled that the tax on combined property per household under the Aggregate Real Estate Tax Law (a national tax) is unconstitutional. The court ruled that the taxation of residential property and land that exceed 600 million *won* and 300 million *won* in value, respectively, remains in effect until replaced by a new law, no later than December 31, 2009.[674] As a result, as of December 26, 2008, the government has revised the law and no longer combines the value per household.

Property tax is imposed by local government on land and buildings on an annual basis pursuant to the LTL.[675]

Property tax on land under the LTL applies to all privately held land in the country. Depending on how it is used and its area, land is subject to one of three sets of progressive rates: the general tax rates;[676] the special tax rates;[677] or the separate tax rates.[678] (See Worksheet 2 for details.) Building and residential property is subject to the property tax. The former aggregate land tax was combined into the current property tax.

In 1989, sweeping revisions to the Korean land tax system were designed to cool land speculation fever by taxing "excess" land at progressively higher rates and by taxing above-average increases in the value of land. Whether these taxes cooled the fever or simply added to the value of the land is another matter for speculation.

The Land Excess Profits Tax Law was declared unconstitutional in 1994, was revised later in the year and was finally repealed on December 28, 1998, by Law No. 5586.[679] In 1994, the court held that the law delegated unconstitutionally broad powers to the bureaucracy for determining matters such as land value, which was then used to compute a high tax rate on unrealized gains, and that the tax constituted a double tax on such gains.

A corporation carrying out a development project in a designated area may be required to pay an assessment equal to 25% of the land value increase attributable to government development of infrastructure on adjoining land under the Recovery of Benefits from Development Law.[680]

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[673] Aggregate Real Estate Tax Law, Law No. 7328 (2005).
[674] 2006 Hunba 112, en bloc.
[675] Law No. 827 of Dec. 8, 1961, as amended.
[676] LTL, Art. 111(1)(1)a.
[677] LTL, Art. 111(1)(1)c.
[678] LTL, Art. 111(1)(1)b.
[679] Constitution Court, 92 Hyen-Ba 49 and 92 Hyen-Ba 52, July 29, 1994.
[680] Law No. 4175 (1989).

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XIX. Avoidance of Double Taxation

A. *Treaty Interpretation and Application*

1. *Creating Income Tax Treaty Relationships*

The process of tax treaty negotiation is handled by the Department of International Tax System of the Ministry of Economy and Finance. Once the tax treaty has been signed, it must be approved by the National Assembly, after which the exchange of ratification instruments takes place. In general, tax treaties are deemed to take precedence over domestic legislation.

2. *Administrative Measures Dealing with Tax Treaty Provisions*

The ITCL provides for a mutual agreement procedure dealing with issues related to tax treaty provisions, but in the cases where it is necessary to involve the other Contracting State on the application and interpretation of the relevant tax treaty, the parties can formally apply for a mutual agreement procedure with the Ministry of Economy and Finance.[681]

3. *Treaty Interpretation*

With respect to the interpretation of tax treaty provisions, the authoritative interpretation of the National Tax Service of the Ministry of Economy and Finance may be used. The interpretation is generally based on the Commentaries to the Organisation for Economic Co-operation and Development (OECD) Model and the United Nations (UN) Model.

However, tax rulings issued by the NTS or the Ministry of Economy and Finance are not necessarily consistent with the Commentaries to the OECD and UN Models. In fact, it is actually rare for them to refer to the Model Commentaries. A court's decision may also serve as an important source for tax treaty interpretation. Korean courts have ruled in numerous precedents on the interpretation of tax treaties, such as the meaning of the concept of beneficial owner, permanent establishment, transfer pricing, royalty vs. personal service, among others.

B. *Tax Presence*

1. *Domestic Place of Business Under Korean Domestic Law*

a. *In General*

Both the method and rate of taxation of nonresident individuals and foreign corporations depend on whether such foreign persons have a "domestic place of business" in Korea. Foreign persons without domestic places of business are generally taxed at flat rates on gross receipts from Korean sources. Foreign persons with domestic places of business are taxed at graduated rates on net income from Korean sources. The term "place of business" is analogous to the treaty term, "permanent establishment," and might be translated as "domestic establishment" with linguistic consistency.

[681] ITCL, Art.42(1).

The National Tax Service (NTS) has promulgated Corporation Tax Basic Guidelines containing several provisions on the subject of domestic places of business.[682] (These provisions are also relevant in determining the existence of a permanent establishment (PE) under a bilateral tax treaty.) For example, the guidelines: (i) confirm that activities of a preparatory or auxiliary nature for the entity itself, such as the mere purchase of goods, liaison, advertising, and collection of market information, do not, of themselves, create a domestic place of business; (ii) set forth rules for computing the duration of a construction project in determining whether a PE exists under the provisions of a tax treaty; (iii) set criteria for determining whether a deemed place of business exists; and (iv) set criteria for determining whether an agent of independent status exists under the provisions of a tax treaty.

b. *Definition of Domestic Place of Business*

The statutory definition of domestic place of business is essentially the same for a nonresident individual as for a foreign corporation; i.e., "a fixed place of business in which the business of the enterprise is wholly or partly carried on." This language is based on the language of Article 5 of the OECD 1963 Draft Double Taxation Convention (which language is repeated in the 1977 and OECD Model Conventions thereafter). For purposes of analysis, the definition may be broken down into three categories: (i) fixed place of business; (ii) construction or assembly site; and (iii) agency. The main difference between a construction or assembly site and other fixed places of business is that a construction or assembly site must exist for a specific period of time before it attains the status of a PE (12 months under the OECD Convention, six months under the Korean statute).[683]

(1) *Fixed Place*

Under the Korean statutes, a "fixed place" constitutes a domestic place of business. The term "fixed place" includes, but is not limited to:

(i) A branch, office or place of business;

(ii) A store or other fixed sales place;

(iii) A workshop, factory or warehouse;

(iv) A building site, a place for construction or assembly, or an installation project, and a place where supervisory activities are carried on in connection therewith, lasting for more than six months;

(v) A place where services are rendered by employees for periods exceeding six months in the aggregate in any 12-month period and including, after January 1, 2002, a place where employees, although not present for more than six months out of a 12-month period, nevertheless render such services continuously and repetitively over a two-year period;[684] or

[682] Effective Aug. 1, 1994, entirely revised on Nov. 1, 2001, after the entire CTL was revised in 1999.

[683] CTL, Art. 94(2)(4).

[684] CTL, Art. 94(2)(5).

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(vi) A mine, quarry or place for the exploration and exploitation of natural resources (including the seabed and subsoil areas adjacent to the coast extending beyond the territorial sea to the extent regulated by domestic law).[685]

The "fixed place," so defined, differs from the OECD Convention "fixed place of business" in that it omits the term "place of management," but includes a warehouse.

Excluded from the Korean statutory definition of fixed place are the following:

(i) A fixed place used only for the purchase of property;

(ii) A fixed place used only for the storage or custody of property not to be sold;

(iii) A fixed place for advertising, publicity, the collecting and furnishing of information, market research, and other activities that have a character preparatory or auxiliary to the conduct of the business; and

(iv) A fixed place used only for the processing of property by another person.

Comment: A portion of Korea's exports are generated by the "processing trade" in which a foreign entity provides parts or raw materials, title to which remains with the foreign party, to a Korean processor that assembles or processes the parts or raw materials exclusively or primarily for sale abroad. Item (iv) is intended to protect a foreign entity engaged solely in the "processing trade" from having a domestic place of business in Korea.

The significant departure from the language of the OECD Conventions is that maintenance of a stock of goods or merchandise for delivery is not an exception and is therefore arguably included as a fixed place. This is consistent with including "warehouse" as an example of a fixed place. The regulations make clear that a fixed place for storing goods belonging to a foreign person for delivery constitutes a domestic place of business.[686]

(2) Agency

Even though a foreign person does not maintain a fixed place within Korea, that person may nevertheless be deemed to have a domestic place of business if conducting business through a person in Korea who has, and regularly exercises, the authority to conclude contracts on its behalf or through "any person determined to be a similar person by Presidential Decree."[687]

The enforcement decree promulgated under the authority of Article 94(3) of the Corporation Tax Law (CTL) provides that an agent who customarily makes deliveries from a stock of goods maintained in Korea will create a domestic place of business for its foreign principal, as will an agent who is a broker, general consignment sales agent or other agent "of independent status" performing "acts that are an important part of the business" of a specific foreign principal, and also "a person" who collects premiums or insures risks situated in Korea on behalf of a foreign corporation engaging in the insurance business (excluding reinsurance business).[688]

Comment: The last two categories of agents created by the amendments appear to exceed the limits set by the language of the OECD Convention. The regulations appear to have taken the definition of an independent agent (an exception to the dependent agent category) and to have included it as part of the category of agent-type domestic place of business. The insurance agent language apparently comes from the UN Model Treaty.

The Korean statutory provisions concerning agents as domestic places of business differ from the OECD Convention provisions in three important ways. First, they make no exceptions for brokers or other agents of independent status (although this issue is dealt with in the Corporation Tax Basic Guideline, as discussed below); second, they omit the usual exception for activities limited to the purchase of goods or merchandise for the enterprise; and, third, they contain no statement that the presence of a controlled or controlling company is not, of itself, significant.

In contrast to the OECD Convention, under Korean law, a foreign corporation has a domestic place of business if the agent acts on behalf of a controlling shareholder of the foreign corporation, or on behalf of a corporation in which the foreign corporation concerned is a controlling shareholder, or even on behalf of other persons having a "special relationship" to the foreign corporation concerned. A controlling shareholder is defined in Article 39 of the National Tax Basic Law (NTBL) as any member of a group of related shareholders that together holds more than 50% of the shares of a corporation. For a discussion of persons having a special relationship, see XIII, A and B, above. The special relationship test is not included in the orders and regulations concerning nonresident individuals and constitutes the only significant difference between domestic place of business for corporations and individuals.

Under the enforcement decrees for both foreign corporations and nonresident individuals, the presence of an agent who fills orders from a stock of goods, who regularly receives orders, who negotiates or who performs other acts important to the business, is sufficient to create a domestic place of business.

From taxable years commencing on or after January 1, 2019, amendments were made to reflect the amended OECD Model Treaty (November 2017) in accordance with BEPS Action 7. Specifically, the above excepted activities are limited to cases where the activities carried on are of a preparatory or auxiliary character.

The definition of "dependent agent" was expanded and the types of contracts subject to the dependent agent rule are clarified. An agent meeting both of the following conditions will also be deemed to be a dependent agent:

(i) A person who does not have the authority to conclude contracts but habitually plays the principal role leading to the conclusion of contracts; and

(ii) Such contracts are concluded by the nonresident individual or foreign corporation without a material modification.

[685] CTL, Art. 94(2)(6).
[686] CTL-ED, Art. 133(1)(1).
[687] CTL, Art. 94(3).
[688] CTL-ED, Art. 133(1).

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The types of contracts subject to the dependent agent rule include the following:

(i) Contracts in the name of a nonresident individual or foreign corporation;

(ii) Contracts for the transfer of the ownership of property owned by a nonresident individual or foreign corporation or for the granting of the right to use property which the nonresident individual or foreign corporation owns or has the right to use; and

(iii) Contracts for the provision of services by a nonresident individual or foreign corporation.

An anti-fragmentation rule was also introduced to prevent the artificial avoidance of having a domestic place of business (DPOB) in one of the following circumstances:

(a) Where both of the following conditions are met:

• There exists a DPOB of a nonresident individual or foreign corporation or its specially related party in the same place as the place of specific excepted activities or other place in Korea; and

• Activities carried on at the place of specific excepted activities constitute complementary functions to the activities carried on at the DPOB of the nonresident individual or foreign corporation or its specially related parties.

*"Specially related parties" are those set forth under Article 183-2(2) of the ITL-PD and Article 131(2) of the CTL-PD, namely:

Special relationship with a foreign corporation exists:

• Where one party owns directly or indirectly 50% or more of the voting shares of the other party; or

• Where a third party owns directly or indirectly 50% or more of the voting shares of either transactional party.

Special relationship with a nonresident exists:

• Spouse, linear blood relatives and brother/sisters of a nonresident; or

• Where a nonresident owns directly or indirectly 50% or more of the voting shares of a foreign corporation.

(b) Activities carried on by a nonresident individual or foreign corporation or its specially related party at the place of specific excepted activities constitute complementary functions and the overall activity resulting from the combination of activities is not of a preparatory or auxiliary character.

The distinction is clearly drawn between the OECD Convention language, which excludes from the definition of a PE the maintenance of a stock of goods solely for delivery, and the Korean statutes and enforcement decrees, which include the maintenance of a stock by an agent for delivery as an activity that creates a DPOB for the nonresident individual or foreign corporation.

2. Permanent Establishment Under Korea's Tax Treaties

a. General

Each of the tax treaties to which the Republic of Korea is a party defines a PE using the framework of the definition of a PE contained in the 1992 OECD Model Convention or its predecessors (the 1963 Draft Convention and the 1977 Model Convention). Within this framework, a nonresident individual or corporation is considered to have a PE in Korea if the nonresident has in Korea a fixed place of business, a construction or installation site that exists for a specified period of time, or a dependent agent.

In the wake of talks between the Korean and U.S. governments concerning improving the business environment for foreign investment in Korea, representatives of the two governments have initialed a Memorandum of Understanding (MOU) concerning, among other matters, tax policy. The Korean government has stated its intention to interpret and apply tax treaty provisions concerning PEs in accordance with the 1992 Commentaries to the OECD Model Tax Convention. In December 1996, Korea joined the OECD, only the second Asian nation to do so.

As a member of the OECD, Korea intends to renegotiate many of its tax treaties to reflect the provisions of the 1992 Model Convention, subject to certain observations and reservations made upon joining the OECD. A new treaty with the United Kingdom was concluded and went into effect for Korean tax purposes on January 1, 1997, the first of such renegotiated treaties.

Comment: The Korean government has made the following reservations to and observations on the OECD Model Convention and the Commentaries thereto:

(i) Article 2 (Taxes Covered)

Korea, along with Japan, reserves its position on that part of paragraph 1 that states that the Convention is to apply to taxes on capital.

(ii) Article 4 (Resident)

Instead of the term "place of effective management," Korea, along with Japan, wishes to use the term "head or main office."

(iii) Article 5 (Permanent Establishment)

Korea, along with Greece, New Zealand, Portugal and Turkey, reserves its position on paragraph 3, and considers that any building site or construction or installation project that lasts more than six months should be regarded as a PE.

(iv) Article 5 (Permanent Establishment)

Korea reserves its position so as to be able to tax an enterprise that carries on supervisory activities for more than six months in connection with a building site for a construction or installation project lasting more than six months.

(v) Article 7 (Business Profits)

Korea, along with Portugal and Spain, reserves the right to tax persons performing professional services or other

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activities of an independent character if they are present for a period or periods exceeding in the aggregate 183 days in any 12-month period, even if they do not have a PE (or a fixed base) available to them for the purpose of performing such services or activities.

(vi) Article 12, Paragraph 1 (Royalties)

Korea, along with Australia, Japan, Mexico, New Zealand, Poland, Portugal, the Slovak Republic, Spain and Turkey, reserves the right to tax royalties at source.

(vii) Article 12, Paragraph 2 (Royalties)

Korea, along with Canada, the Czech Republic, Hungary, Poland and the Slovak Republic, reserves the right to add the words "for the use of, or the right to use, industrial, commercial or scientific equipment" in paragraph 2.

(viii) Article 12 (Royalties)

With respect to paragraph 14, Korea maintains the opinion that the paragraph may neglect the fact that know-how can be transferred in the form of computer software. Therefore, Korea considers know-how imparted by nonresidents through software or computer programs to be covered by Article 12.

(ix) Article 13 (Capital Gains)

Korea, along with Spain, reserves the right to tax gains from the alienation of shares or other rights forming part of a substantial participation in a company that is a resident.

Comment: The authors understand that the Korean government considers that, in addition to the points listed above, it reserves the right to include in the definition of royalties, income derived from the lease of industrial, commercial, or scientific equipment and income derived from the lease of containers.

The analysis in 2, below, covers treaties now in force, emphasizing those provisions that depart from the language of the OECD Convention in significant respects.

b. Definition of Permanent Establishment

(1) Fixed Place

In the language of the OECD Conventions, "the term 'permanent establishment' means a fixed place of business through which the business of an enterprise is wholly or partly carried on." Seven examples of what is meant by a PE are listed (a place of management, branch, office, factory, workshop, mine or quarry, and a building site). It is clear from the commentary to this article that the list is not intended to be exhaustive. Therefore, variations from the list may be of limited significance unless clearly departing from the generally held idea of a fixed place of business.

The treaties that the Republic of Korea has concluded follow the OECD Conventions in listing a branch, office, workshop, mine, quarry, or other place for the extraction of natural resources. The Korea-Denmark[689] and Korea-Netherlands[690] tax treaties add oil and gas wells.

Note the provision of the Korea-United States treaty that assigns PE status to a resident of one contracting state that has a fixed place of business in the other contracting state,

and goods or merchandise are either:

(a) Subjected to processing in that other Contracting State by another person (whether or not purchased in that other Contracting State); or

(b) Purchased in that other Contracting State (and such goods or merchandise are not subjected to processing outside that other Contracting State) and

all or part of such goods or merchandise is sold by or on behalf of such resident for use, consumption, or disposition in that other Contracting State.

This provision is an incentive for free trade zone foreign investors to keep their wares off the Korean market and to encourage the export of goods processed in Korea. The provision is an exception to an exception because, in conformity with the OECD Convention, the Korea-United States treaty excepts the maintenance of a stock of goods or merchandise for the purpose of processing by another person from the definition of a PE.

(2) Construction and Installation Projects

The language of OECD Model Conventions includes as a PE "a building site or construction or assembly project" that exists for more than 12 months. Korea's treaties depart from this language in several ways:

(i) Most of Korea's treaties require that the site or project exist for more than six months rather than for more than 12 months, as specified in the OECD Model Convention.

(ii) The Korea-Denmark tax treaty includes "an installation used for exploration of natural resources which exists for more than six months."

(iii) Under the Korea-Belgium,[691] Canada,[692] Denmark, France,[693] Japan,[694] Netherlands, Singapore,[695] and

[689] Convention Between the Government of the Kingdom of Denmark and the Government of the Republic of Korea for the Avoidance of Double Taxation with Respect to Taxes on Income, signed on Oct. 11, 1977 (the "Korea-Denmark tax treaty").

[690] Convention Between the Kingdom of The Netherlands and the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on Oct. 25, 1978 (the "Korea-Netherlands tax treaty").

[691] Convention Between the Kingdom of Belgium and the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on Aug. 29, 1977 (the "Korea-Belgium tax treaty").

[692] Convention Between the Government of Canada and the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on Sept. 5, 2006 (the "Korea-Canada tax treaty").

[693] Convention Between the Government of the Republic of Korea and the Government of the French Republic for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on June 19, 1979 (the "Korea-France tax treaty").

[694] Convention Between Japan and the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on Oct. 8, 1998 (the "Korea-Japan tax treaty").

[695] Convention Between the Republic of Singapore and the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal

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Switzerland[696] tax treaties, dependent personal services connected with a project constitute a PE. The services are defined as personal services such as supervisory, technical or any other professional services. It is the site or project that must exist for more than six months. The services need only be provided "in connection" therewith. In addition, under the Korea-United Kingdom tax treaty, the first treaty Korea has renegotiated since becoming an OECD member, a building site, a construction, assembly or installation project, or supervisory activities in connection therewith constitute a PE only if the site, project or activities continue for a period of more than 12 months. This is consistent with the language of the OECD Model Convention.

Personal services rendered in connection with a project obviously represent a special concern on the part of the Korean government. Domestic law includes in the definition of a domestic place of business any place where supervisory activities are conducted in connection with a building site, a construction, assembly or installation project that lasts for more than six months and any place in which services are rendered through an employee for an aggregate of six months out of a 12-month period.[697] See 1, b, above. Personal services do not constitute a PE under the OECD Model Convention, although income from personal services may be taxed by the other contracting state if attributable to a fixed base, in the case of independent personal services, or if the employee is present in the other contracting state for more than 183 days, in the case of dependent personal services.

(3) Agency

Under the OECD Model Convention, an enterprise resident in one state may create a PE for itself in the other state even if it maintains no fixed place of business in the other state, if it acts through an agent of dependent status.

As an exception to the agency rule, the language of the OECD Model Convention further provides that "[a]n enterprise shall not be deemed to have a permanent establishment in a Contracting State merely because it carries on business in that State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business."

Comment: There are analytical problems in distinguishing dependent from independent agents. It is not clear, for example, whether the distinction is primarily quantitative or qualitative. A broker who acts on behalf of many foreign sellers in the ordinary course of his business would most clearly be an agent of independent status. Can a broker acting solely on behalf of one foreign seller maintain independent status?

At least one commentator has concluded that such a broker lacks "the quality of independence required" under U.S. law.[698] Commentary to the OECD Model Convention, however, suggests that a person who has the quality of independence would remain an agent of independent status without reference to the number of foreign clients. This ambiguity is not clarified in Korea's treaties. Each of Korea's treaties follows the outline of the OECD Model Convention language with respect to agents. Departures from the OECD Model Convention may be categorized as described in (a) to (d), below.

(a) Agents Who Fill Orders from a Stock of Goods

Under the OECD Model Convention, "maintenance of a stock of goods, or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery," would not create a PE. Canada reserved its position with regard to this language when the OECD Draft Convention was published in 1963. The Canadian position was that an agent who maintains a stock of merchandise from which he regularly fills orders constitutes a PE for the enterprise that he represents. The Korea-Singapore, -Thailand,[699] -United Kingdom, and -United States tax treaties contain language to this effect. The language varies somewhat from treaty to treaty. The agent "regularly delivers goods or merchandise" (United Kingdom), "regularly fills orders" (United Kingdom), "makes deliveries" (Thailand), "fills orders or makes deliveries" (United States). In each case such an agent constitutes a PE for the nonresident enterprise even if the agent does not have authority to contract on behalf of the enterprise.

(b) Agents Who Secure Orders

The existence of a dependent agent having no authority to conclude contracts does not, of itself, create a PE under the OECD Model Convention language. The Korea-Thailand tax treaty makes exception to this rule in that dependent agents who regularly "secure orders" constitute PEs. Under this treaty, the agent need only regularly secure orders.

(c) Brokers Who Are Not Independent Agents

Korea's treaties have adopted from the OECD Model Convention the idea that an enterprise does not have a PE if it carries on business only through a broker, general commission agent, or other agent of independent status.

Comment: Neither the Corporation Tax Law (CTL) nor the Income Tax Law (ITL) provides an exception for agents of independent status, but one of the Basic Guidelines does provide for such an exception.[700] Until the end of 1996, the Foreign Trade Law required a foreign person to engage a licensed Korean offer agent to handle all import transactions. This requirement was repealed, effective January 1, 1997.[701] Nevertheless, foreign importers will still find occasions when it is convenient to use the services of such an agent. It is still possible that a foreign person having tax residency in a country with which Korea does not have a tax treaty could be deemed to have a

Evasion with Respect to Taxes on Income, signed on Nov. 6, 1979 (the "Korea-Singapore tax treaty").

[696] Convention Between the Republic of Korea and Switzerland for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on Feb. 12, 1980 (the "Korea-Switzerland tax treaty").

[697] CTL, Art. 94(2)(5).

[698] Williams, "Permanent Establishments in the United States," *Income Tax Treaties* 297 (Bischel, Ed. 1978).

[699] Convention Between the Republic of Korea and the Kingdom of Thailand for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on Aug. 26, 1974 (the "Korea-Thailand tax treaty").

[700] Corporation Tax Basic Guideline, Art. 94-133-3, introduced in 1994.

[701] Foreign Trade Law, Law No. 5211 (1996), Arts. 13 and 14.

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domestic place of business in Korea by reason of the activities of a broker or offer agent acting on its behalf. The Korean tax authorities have in practice been considering that certain offer agents (for example, offer agents acting on behalf of affiliated companies) constitute such an agency-type tax presence. It is therefore still prudent to limit the scope of authority of a Korean offer agent by contract to reduce this risk.

(d) Insurance Agents

Because an insurance company that is a resident of one contracting state may do business through a broker or other agent of independent status without creating a PE in the other contracting state, it is possible, under normal treaty rules, for such a company to avoid taxation in the other contracting state on sizable business profits. The OECD Model Convention does not address this problem, but the Commentary to the Model Convention suggests that contracting states may wish to include a special provision on insurance profits. In practice, few contracting states do so.

(4) Employers of Public Entertainers

Under the Korea-Thailand tax treaty, a resident of one contracting state had a PE in the other contracting state if that resident provided the services of certain public entertainers in the other contracting state. PEs arising under this provision represented the least permanent and least established of the PEs to be found in Korea's treaties.[702] The provision was repealed when the Korea-Thailand tax treaty was amended effective June 29, 2007.

(5) Specific Exclusions from Permanent Establishment

The OECD Model Convention specifically excludes certain activities from the definition of a PE, even if conducted through a fixed place. The term "permanent establishment" is deemed not to include:

(i) The use of facilities solely for the purpose of storage, display, or delivery of goods or merchandise belonging to the enterprise;

(ii) The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display, or delivery;

(iii) The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;

(iv) The maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise, or for collecting information, for the enterprise;

(v) The maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character; or

(vi) The maintenance of a fixed place of business solely for any combination of activities mentioned in (i) to (v), provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.[703]

Each of Korea's treaties follows the general pattern of this article, but some variations should be noted.

The fifth category used to be "maintenance of a fixed place of business solely for the purpose of advertising, for the supply of information, for scientific research, or for similar activities which have a preparatory or auxiliary character for the enterprise." In the 1992 Model Convention, the category was modified to include activities of a preparatory or auxiliary character, while including a new category that described a combination of activities. The treaties that Korea has entered into since 1992 have adopted this language, i.e., the Korea-Belarus,[704] -Canada, -China (PRC),[705] -Fiji,[706] -Germany, -Japan, and -United Kingdom tax treaties. The older treaties (for example the Korea-France, -Netherlands, -Thailand, and -United States tax treaties) do not have such language. The Korea-Thailand tax treaty contains an anomaly in that it excludes a fixed place of business for "the storage and/or delivery of goods" while including an agent who maintains a stock of goods "from which he regularly makes deliveries." Thus, activities that would not create a PE if carried out directly through a "fixed place of business" would arguably result in a PE if carried out through an agent of dependent status.

(6) Disregard of Corporate Relationships

Each of the tax treaties into which Korea has entered contains a provision analogous to Article 5(7) of the OECD Model Convention to the effect that corporate control is to be disregarded in determining whether one company constitutes a PE of another. For example, Article 9(7) of the Korea-United States tax treaty provides that: "The fact that a resident of one of the Contracting States is a related person … shall not be taken into account in determining whether that resident … has a permanent establishment… . ."

Until the early 1990s, despite the presence of these provisions in the tax treaties, the trend of enforcement by the National Tax Service (NTS) was to disregard corporate boundaries where the activities of a subsidiary company appeared to exceed the scope of activities "usually conducted" by a subsidiary, and where the subsidiary did not have "substance." For example, corporate boundaries were disregarded in making a finding that a PE existed in cases where a subsidiary conducted activities that its parent would be "expected" to conduct, where a subsidiary did not maintain an office in the jurisdiction where it was incorporated, did not have administrative personnel supervising branch activities, and did not have its own head office communicating with a branch in Korea concerning day-to-day operations. The tax authorities justified this procedure as

[702] Korea-Thailand tax treaty, Art. 8(7).

[703] This language comes from the 1977 OECD Model Convention; the language of the 1992 Model Convention is slightly different.

[704] Convention Between the Government of the Republic of Belarus and the Government of the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on May 20, 2002 (the "Korea-Belarus tax treaty").

[705] Convention Between the Government of the Republic of Korea and the Government of the People's Republic of China for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on Mar. 28, 1994 (the "Korea-China (PRC) tax treaty").

[706] Convention Between the Republic of Fiji and the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on Sept. 19, 1994 (the "Korea-Fiji tax treaty").

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an application of the doctrine of substance over form. Thus, a subsidiary created solely for the purpose of preventing a parent corporation from having a PE in Korea might have had the opposite effect.

The NTS has drawn up an internal guideline on the issue of deemed PEs that suggests that the tax authorities will use transfer pricing rules to correct a misallocation of income, instead of deeming an agency to exist between a parent and subsidiary.[707] As background, the guideline states that, in practice, it is difficult to prove conclusively that an agent of a related party satisfies the dependent agent requirements, so that a finding that the agent is dependent is likely to bring about international confrontation. It also states that "among OECD member countries, it is common to impose tax on related party transactions, not by deemed PE taxation, but by transfer pricing."

In the same internal guideline, the NTS states that the OECD standards for the allocation of income from sales between the PE of a foreign corporation and its head office are to be applied to companies from tax treaty countries, but that current practice, that is, attributing total sales income to the domestic place of business of a foreign corporation, will continue to be applied to companies from nontax treaty countries. Because of acceptance of these OECD standards for the allocation of sales income, the tax authorities may have less interest in making a case that a foreign corporation from a tax treaty country has a deemed PE by virtue of the activities of its subsidiary in Korea.

C. Unilateral Measures to Avoid Double Taxation: Foreign Tax Credit

A foreign tax credit is available to a Korean domestic corporation for taxes levied by foreign governments, including local governments, in the following categories: (i) taxes levied on excess corporate profits and corporate profits; (ii) surcharges on corporate profit taxes; and (iii) taxes levied on gross corporate revenues, if such taxes are in lieu of a corporate profit tax in the taxing jurisdiction concerned. Any foreign tax imposed by a foreign government on any adjustment caused by adjustments made by a domestic corporation is, however, excluded.[708]

Foreign tax credits are claimed by a taxpayer at the time the annual tax return is filed.[709] A taxpayer may elect to take a deduction instead of a credit.[710] A taxpayer may choose either a per-country limit or an overall limit.[711] Losses from one country can be allocated to revenues from another country only up to the ratio that the revenues from the first country bear to total worldwide revenues.[712] Effective from January 1, 2015, only the per-country limit is allowed. Excess foreign tax credits may be carried forward for 10 years.[713]

The CTL does not permit excess foreign tax credits to be carried back. Unilateral tax sparing is given with respect to income exempt from a treaty partner's tax up to the tax rate specified by the applicable treaty.[714]

An indirect foreign tax credit is allowed for foreign income tax paid by a first-tier foreign subsidiary in which a Korean parent company owns 10% (25% prior to fiscal years commencing before January 1, 2023) or more of the total investment and has held the investment for six months or more. [715] Prior to 2015, a 50% indirect tax credit for tax paid by a second-tier subsidiary could be available for a qualified second-tier subsidiary. The indirect foreign tax credit for dividends received through a second-tier subsidiary is no longer available.

D. Bilateral Measures to Avoid Double Taxation: Double Tax Treaties

All the tax treaties that Korea has entered into include provisions for the elimination of double taxation by the credit method.[716] Certain tax treaties provide Korean residents with tax sparing (for example, the Korea-Bangladesh,[717] -China, and -India[718] tax treaties). On the other hand, certain other tax treaties provide residents of the treaty partner country with tax sparing (for example, the Korea-United Kingdom[719] and -Germany[720] tax treaties).

Foreign income earners who claim the reduced withholding rate or exemption under a tax treaty must submit an application to do so to the withholding agent together with residency certificates. If the application is not submitted, the withholding agent can withhold taxes based on the domestic withholding rate. The income earner may file a refund claim within five years after the end of the month in which the withholding is made.[721]

E. MLI

On May 13, 2020, Korea deposited the instrument of ratification for the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI). The MLI took effect for Korea on September 1, 2020. Among 93 tax treaties, 73 tax treaties were notified as covered tax treaties under the MLI. Korea made reservations on most of the MLI articles except for the preamble language under Article 6 (Purpose of a covered tax agreement), the primary purpose test under Article 7 (Prevention of treaty abuse),

[707] *Kukil* 46501-493 (Aug. 11, 1995).
[708] CTL-ED, Art. 94(1) proviso.
[709] CTL, Art. 57.
[710] CTL, Art. 57(1)(2).
[711] CTL-ED, Art. 94(7).
[712] CTL Basic Guidelines, Art. 3-2-7(24-3).
[713] CTL, Art. 57(2).
[714] CTL, Art. 57(3).
[715] CTL, Art. 57(4).
[716] For a complete list of Korea's tax treaties and other tax-related agreements, including the texts and information on signature, entry into force and effective dates, see *International Tax Treaties*.
[717] Convention Between the People's Republic of Bangladesh and the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on May 10, 1983 (the "Korea-Bangladesh tax treaty").
[718] Convention Between the Government of the Republic of India and the Government of the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on July 19, 1985 (the "Korea-India tax treaty").
[719] Convention Between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital Gains, signed on Oct. 25, 1996 (the "Korea-United Kingdom tax treaty").
[720] Agreement Between the Federal Republic of Germany and the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and on Capital, signed on Mar. 10, 2000 (the "Korea-Germany tax treaty").
[721] CTL, Arts. 98-5 and 98-6.

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Article 16 (Mutual agreement procedure) and Article 17 (Corresponding adjustments). MLI integration documents are available from May 2022, which include those for Japan, Ireland, Luxembourg and Canada.

F. South Korea-U.S. FATCA Model 1 IGA

The Intergovernmental Agreement (IGA) signed by Korea and the United States on June 10, 2015, is a reciprocal Model 1 IGA, under which Korean financial institutions agree to report to the Korean tax authority information on financial accounts owned by U.S. persons and, in turn, the Korean tax authority annually transfers the collected account information to the United States. The U.S. government is also required to obtain and annually exchange with South Korea information on accounts in U.S. financial institutions held by residents of Korea. Because the South Korean IGA is based on the reciprocal Model 1 IGA, the provisions of the Korean IGA do not differ much from those of other IGAs based on this model. As with all other reciprocal Model 1 IGAs, the South Korean IGA has three parts: 1) the main body, 2) Annex I, which provides the due diligence obligations and procedures of Korean financial institutions, and 3) Annex II, which provides the categories of institutions and accounts that are in substance not subject to the IGA. Under the Korean-U.S. IGA, Korean financial institutions in general would be relieved of FATCA withholding obligations and would not be subject to FATCA withholding. A Korean financial institution is required to obtain a Global Intermediary Identification Number by registering with the U.S. Internal Revenue Service. On June 24, 2015, the Korean Financial Services Commission issued the IGA enabling regulations, which contain detailed rules to implement and execute the terms of the IGA.

Korea is a party to the Convention on Mutual Administrative Assistance in Tax Matters entered into force on July 1, 2012. Korea also has Exchange of Information Agreements with the Marshall Islands, Bahamas, Bermuda and the Cook Islands.

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TAX FORMS

Worksheet 1	Form VAT3, Return of Annual Trading.
Worksheet 2	Sample Form CT1 (2022), Pay and File Corporation Tax Return (Companies). N.B. This return is now completed via an interactive form on the Revenue On-Line Service (ROS)
Worksheet 3	Irish Revenue guidance in relation to Form CT1.

Working Papers for this Portfolio can be found online at https://bloomberglaw.com.

Additional Resources

Company and Companies Registration Office Related Material

- Form of Constitution of Private Company Limited by Shares
  available at http://www.irishstatutebook.ie/eli/2014/act/38/schedule/1/enacted/en/html#sched1
- Form of Constitution of Public Limited Company
  available at http://www.irishstatutebook.ie/eli/2014/act/38/schedule/9/enacted/en/html#sched9
- Form of Constitution of a Designated Activity Company Limited by Shares
  available at http://www.irishstatutebook.ie/eli/2014/act/38/schedule/7/enacted/en/html#sched7
- Form of Constitution of Private Unlimited Company Having a Share Capital
  available at http://www.irishstatutebook.ie/eli/2014/act/38/schedule/11/enacted/en/html#sched11
- Companies Registration Office, Annual Return, Form B1 (It is only possible to complete the Form B1 online)

Tax Registration Forms

- Form TR1, Tax Registration (Resident Individual, Trust, Partnership or Unincorporated Body Registration for Income Tax, PAYE/PRSI as an Employer, and/or VAT)
  available at https://www.revenue.ie/en/self-assessment-and-self-employment/documents/form-tr1.pdf
- Form TR2, Tax Registration (Resident Limited Company Registration for Corporation Tax, Employer's PAYE/PRSI, RCT and/or VAT)
  available at https://www.revenue.ie/en/self-assessment-and-self-employment/documents/form-tr2.pdf
- Form TR1 (FT), Tax Registration (Non-Resident Individuals, Partnerships, Trusts or Unincorporated Bodies Registering for Tax in Ireland)
  available at https://www.revenue.ie/en/self-assessment-and-self-employment/documents/form-tr1-non-resident.pdf
- Form TR2 (FT), Tax Registration (Non-Resident companies registration for Corporation Tax, Employer's PAYE/PRSI, RCT and/or VAT)
  available at https://www.revenue.ie/en/self-assessment-and-self-employment/documents/form-tr2-non-resident.pdf

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Tax Return Forms

- Form 11, Pay and File Income Tax Return (Individuals Chargeable under Self-Assessment)
  available at https://www.revenue.ie/en/self-assessment-and-self-employment/documents/form11.pdf

- Form 12, Tax Return for the Year (Employees, Pensioners & Non-Proprietary Directors)
  available at https://www.revenue.ie/en/self-assessment-and-self-employment/documents/form12.pdf

- Form 1 (Firms), Partnership Tax Return
  available at https://www.revenue.ie/en/self-assessment-and-self-employment/documents/form1-firms.pdf

Other Tax Forms and Related Material

- Form 11F CRO, Statement of Particulars (TCA 1997, Sec. 882)
  available at https://www.revenue.ie/en/starting-a-business/documents/form-11f-cro.pdf

- Form CG50, Application for Certificate for Tax Not to Be Deducted from Proceeds of Certain Capital Sales
(required if selling an asset on or after 25 March 25, 2002 for over €500,000 or a house or apartment on or after January 1, 2016 for over €1 million),
available at https://www.revenue.ie/en/gains-gifts-and-inheritance/documents/form-cg50.pdf

- Relief for Investment in Corporate Trades
(required to be completed by companies that issue shares from the Employment Investment Incentive scheme (EII), Start-up Capital Incentive scheme (SCI) or Start-Up Refunds for Entrepreneurs scheme (SURE)),
available at https://www.revenue.ie/en/starting-a-business/initiatives-for-startup-businesses-and-smes/relief-for-investment-in-corporate-trades/filing-requirements.aspx

- Form 46G, Return of Third Party Information
(required by traders, businesses and companies who are required to file returns to Revenue containing details of payments made by them to third parties for services provided).
This return is now completed via the Revenue On-Line Service (ROS).

Dividend Withholding Tax Forms and Materials

- Dividend Withholding Tax Declaration, Payslip and Distribution Details
This return is now completed via the Revenue On-Line Service (ROS).

- Dividend Withholding Tax — Claim for or on Behalf of Certain Non-Resident Persons for Refund
available at https://www.revenue.ie/en/companies-and-charities/documents/dwt/dwt-reit-claim-form.pdf

- Dividend Withholding Tax — Exemption from DWT for a Qualifying Non-Resident Company (together with form of wording in lieu of a U.S. auditor's stamp on the non-resident form for management assertion as to XYZ Company being a "Qualifying Non-Resident Person," and independent accountant's report to the board of directors of XYZ Company)
  available at https://www.revenue.ie/en/companies-and-charities/documents/dwt/dwt-non-res-v2b.pdf

- Dividend Withholding Tax — Exemption from DWT for a Qualifying Non-Resident Individual
  available at https://www.revenue.ie/en/companies-and-charities/documents/dwt/dwt-non-res-v2a.pdf

- Dividend Withholding Tax — Exemption from DWT for a Qualifying Non-Resident Person
  (not being an individual or a company)
  available at https://www.revenue.ie/en/companies-and-charities/documents/dwt/dwt-non-res-v2c.pdf

- Dividend Withholding Tax — Exemption for Certain Irish Residents
  available at https://www.revenue.ie/en/companies-and-charities/documents/dwt/dwt-res-v3.pdf

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Revenue Guidance

- Guidance on Revenue Opinions on What constitutes a Trade
  available at https://www.revenue.ie/en/tax-professionals/tdm/income-tax-capital-gains-tax-corporation-tax/part-02/02-02-06.pdf

- Revenue Guidelines for Research and Development Tax Credit
  available at https://www.revenue.ie/en/companies-and-charities/reliefs-and-exemptions/research-and-development-rd-tax-credit/index.aspx

Tax Treaties and Related Material

- Income Tax Treaty and Protocol of July 28, 1997 Between Ireland and the United States
  available at https://www.revenue.ie/en/tax-professionals/documents/double-taxation-treaties/u/usa-1997.pdf

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