

## International Tax Korea Highlights 2017



### Investment basics:

**Currency** – South Korean Won (KRW)

**Foreign exchange control** – Controls exist, but gradually have been liberalized. Foreign loans in excess of a specified amount must be reported in advance to the Ministry of Strategy and Finance. Loans granted to foreign borrowers also must be reported.

**Accounting principles/financial statements** – Korean GAAP and IFRS. IFRS is mandatory for listed companies and financial institutions and optional for unlisted companies.

**Principal business entities** – These are the stock corporation, limited liability company and branch of a foreign corporation.

### Corporate taxation:

**Residence** – A corporation is resident in Korea if its headquarters or place of effective management is located in Korea.

**Basis** – Residents are taxed on worldwide income; nonresidents are taxed only on Korean-source income.

**Taxable income** – Corporate income tax is imposed on a company's taxable income, which is its book net income after adjustments for differences between the accounting and tax rules. Subject to some exceptions, normal business expenses are deductible expenses for tax purposes.

**Taxation of dividends** – The dividends received deduction (DRD) is available for dividend income received by a Korean resident company from another Korean company. The DRD ratio ranges from 30% to 100% and varies depending on whether the parent company is a qualified holding company under Korean law and the ownership percentage of the parent company. Dividends

received from a foreign company are, in principle, subject to corporate income tax in Korea, but the recipient company may be eligible for an indirect foreign tax credit for foreign income taxes paid by the foreign company in its country of residence.

**Capital gains** – Capital gains or losses usually are reflected in normal taxable income subject to corporate income tax. Korean-source capital gains derived by a nonresident are taxed at the lesser of 11% (including the local surtax) of the sales proceeds received or 22% (including the local surtax) of the gains realized.

**Losses** – Losses may be carried forward for up to 10 years. Effective from 1 January 2016, companies other than small and medium-sized enterprises (SMEs) may utilize their tax loss carryforwards to set off only 80% of the taxable income for a fiscal year.

SMEs may be allowed to carry losses back for one year.

**Rate** – The tax rate is 10% on the first KRW 200 million of taxable income, 20% on taxable income above KRW 200 million up to KRW 20 billion and 22% of taxable income above KRW 20 billion.

**Surtax** – The local income tax rate is 1% on the first KRW 200 million of taxable income, 2% on taxable income above KRW 200 million up to KRW 20 billion and 2.2% of taxable income above KRW 20 billion. A local income tax return should be separately filed.

**Alternative minimum tax** – Corporate taxpayers are subject to a minimum tax that is imposed at a rate of 10% on taxable income up to KRW 10 billion, 12% on taxable income above KRW 10 billion up to KRW 100 billion and 17% on taxable income over KRW 100 billion (7% for SMEs).

**Foreign tax credit** – A Korean resident subject to tax in Korea and overseas in respect of income earned overseas

is entitled to a foreign tax credit for foreign tax paid. The credit is limited to the amount of tax payable in Korea on the foreign-source income.

**Participation exemption** – No

**Holding company regime** – Holding companies are regulated under the Monopoly Regulation and Fair Trade Act and qualifying holding companies under the law may be granted a higher DRD. See under "Taxation of dividends."

**Incentives** – Various types of tax credits and exemptions are available, such as an investment tax credit, R&D tax credit, tax exemption for high-tech foreign-invested companies, etc., provided the requirements of the Tax Incentive Limitation Law are met.

#### Withholding tax:

**Dividends** – No withholding tax is levied on dividends paid to a domestic company.

Dividends paid to a nonresident company or individual are subject to a 22% withholding tax (including the local surtax). The rate may be reduced under a tax treaty, although withholding at the domestic, rather than treaty, rate may be required for certain payments to jurisdictions regarded as tax havens.

**Interest** – Interest on a regular loan paid to a nonresident company or an individual is subject to a 22% withholding tax (including the local surtax). Interest on bonds is subject to a 15.4% withholding tax (including the local surtax). The rate may be reduced under a tax treaty, although withholding at the domestic, rather than treaty, rate may be required for certain payments to jurisdictions regarded as tax havens.

**Royalties** – Royalties paid to a nonresident company or an individual are subject to a 22% withholding tax (including the local surtax). The rate may be reduced under a treaty, although withholding at the domestic, rather than treaty, rate may be required for certain payments to jurisdictions regarded as tax havens.

**Technical service fees** – Services rendered by a nonresident company or an individual in Korea generally are classified as personal services income and subject to a 22% withholding tax (including the local surtax). An exemption may apply under a treaty. Technical service fees for any transfer of technical information or know-how may be classified as a royalty.

**Branch remittance tax** – In general, there is no branch remittance tax. However, a branch tax, ranging from 5% to 15% of after-tax profits less deemed reinvested capital, may be levied if a tax treaty between Korea and the country in which the branch's head office is resident allows Korea to impose the branch tax.

#### Other taxes on corporations:

**Capital duty** – A capital registration tax of 0.48%, including the local surtax, is levied when a company registers its incorporation or capital increase with the court registry. The capital registration tax rate for a company incorporated in the Seoul Metropolitan Area triples to 1.44%.

**Payroll tax** – A company must withhold taxes on salary paid to its employees.

**Real property tax** – A company that owns land, buildings, ships and aircraft as at a certain assessment date is subject to property tax on such assets. The tax rates range from 0.24% to 0.6% (including the education surtax), depending on the type of property. A company that owns real estate, such as land or residential buildings, is subject to the comprehensive real estate tax in addition to the local property tax.

**Social security** – An employer must make social security contributions (i.e. national pension, medical insurance, unemployment insurance and industrial injury compensation insurance) to the relevant social security authorities. The social security contribution rates vary depending upon number of employees and the industry.

**Stamp duty** – Stamp tax is levied on agreements relating to the creation, transfer or alteration of rights.

**Transfer tax** – Securities transaction tax is levied on the transferor of shares at 0.5% of the share transfer price. The rate is reduced to 0.3% if listed shares are transferred.

**Other** – A company acquiring real estate, motor vehicles, heavy equipment and certain other items must pay acquisition tax, generally at 4.6%, including the local surtax.

#### Anti-avoidance rules:

**Transfer pricing** – Transactions with overseas related parties must be made on arm's length terms. The following transfer pricing-related information must be disclosed when filing a corporate income tax return: a report on the selected transfer pricing method and the reason for its selection; a schedule of the taxpayer's international transactions with foreign related parties; and a summary income statement for foreign related parties.

Effective from 1 January 2016, domestic companies and permanent establishments of a foreign company that have annual sales of more than KRW 100 billion and a transaction volume with foreign related parties of more than KRW 50 billion per year are required to submit additional transfer pricing documentation (i.e. a

comprehensive report on cross-border transactions, including a "master file" and a "local file"), which provides organization/management information, cross-border transaction information, various business/intangible asset/financial/tax information, etc.

Both unilateral and bilateral advance pricing agreements are available.

**Thin capitalization** – If a foreign-invested company borrows from a foreign controlling shareholder (FCS) or third party with a guarantee from the FCS, and the borrowing exceeds 200% (or 600% for financial companies) of equity (or contributed capital if greater than equity), the interest expense on the debt exceeding 200% (or 600%) of the FCS's share of the borrower's equity is not deductible.

**Controlled foreign companies** – When 10% or more of the issued shares in a foreign company are owned by a Korean resident and the average effective income tax rate of the foreign company for the most recent three consecutive years is 15% or less, the Korean resident is deemed to have received a dividend of an amount equal to "deemed distributable retained earnings" multiplied by the shareholding ratio, even though there has been no actual distribution of such retained earnings to the Korean resident.

**Disclosure requirements** – See under "Transfer pricing," above.

**Other** – The substance-over-form principle applies to transactions between Korean and foreign entities. The principle is applied in the case of treaty shopping.

#### Compliance for corporations:

**Tax year** – A company's tax year is its accounting period as specified in the articles of incorporation. This normally is a 12-month period. The tax year cannot exceed 12 months.

**Consolidated returns** – A consolidated return system is available for a parent company and its 100% directly or indirectly owned domestic subsidiaries.

**Filing requirements** – Korea operates a self-assessment system. If the business year is longer than six months, advance tax must be paid for the first six-month period of the business year, based on 50% of the previous year's tax liability or the actual financial performance for the six-month period. Filing and payment of advance tax must be made within two months after the first six-month period. Companies must file a year-end income tax return within three months (four months for companies filing a consolidated tax return) after the end of a fiscal year and attach the balance sheet, income statement, statement of appropriation of retained earnings (or statement of

disposition of deficit) and other relevant documents. A branch of a foreign corporation may be granted an extension of time to file its tax return in certain cases. Domestic companies subject to mandatory external audit also may have a one-month extension for filing in certain cases.

**Penalties** – Penalties may be imposed for late filing or failure to file a return and for an understatement of taxable income. Interest penalties also may apply.

**Rulings** – The tax authorities may issue a private tax ruling in response to a taxpayer's inquiry as to the interpretation/application of the tax law. An advance ruling system also is in place.

#### Personal taxation:

**Basis** – Residents generally are subject to tax on worldwide income. However, with respect to foreign-source income, short-term resident foreigners whose total period in Korea does not exceed five out of the past 10 years are taxed only on foreign-source income paid in or remitted to Korea. Other nonresidents are taxed only on Korean-source income.

**Residence** – An individual who has a domicile or place of residence in Korea for at least 183 days generally is deemed to be resident in Korea. An individual normally is considered resident upon arrival in Korea if his/her occupation generally would require him/her to reside in Korea for 183 days or more or if the individual's family accompanies him/her to Korea and the individual has substantial assets (e.g. household property) in Korea.

**Filing status** – No provisions exist for married couples to file a joint personal tax return.

**Taxable income** – Taxable income comprises wages and salaries, dividends, interest income, rental income, business income, pension income, severance income and other income.

**Capital gains** – Capital gains are taxed separately, with the rate depending on the type of asset, holding period, etc.

**Deductions and allowances** – Various deductions, allowances and credits are permitted, including an earned income deduction, credits for qualifying medical expenses, certain educational expenses, certain charitable donations, etc.

**Rates** – Progressive rates of up to 44% apply, including the local surtax.

#### Other taxes on individuals:

**Capital duty** – No

**Stamp duty** – Stamp tax is levied on agreements

relating to the creation, transfer or alteration of rights, but the tax is not significant.

**Capital acquisitions tax** – An individual acquiring real estate, motor vehicles, heavy equipment and certain other items is required to pay acquisition tax, generally at 4.6%, including the local surtax (a lower acquisition tax rate applies to acquisition of residential property).

**Real property tax** – An individual who owns land, buildings, ships and aircraft as at a certain assessment date is subject to a property tax on the assets. The tax rates range from 0.24% to 0.6% (including the education surtax), depending on the type of property. An individual who owns real estate, such as land or residential buildings, is subject to the comprehensive real estate tax in addition to the local property tax.

**Inheritance/estate tax** – Inheritance tax is levied on the beneficiary at progressive rates up to 50%.

**Net wealth/net worth tax** – No

**Social security** – Individuals are required to pay national pension, medical insurance and unemployment insurance premiums.

#### Compliance for individuals:

**Tax year** – Calendar year

**Filing and payment** – A resident generally is required to file an individual income tax return and pay the tax due on such income before 31 May of the following year or before his/her permanent departure from Korea. A taxpayer who receives only salary or severance income may not be required to file a return, since employers are required to withhold income tax at source on such income on a monthly basis and finalize the employee's tax liability in February of the following calendar year.

**Penalties** – Penalties may be imposed for late filing or failure to file a return and the understatement of taxable

income. Interest penalties may also apply.

#### Value added tax:

**Taxable transactions** – VAT is levied on the supply of goods and provision of services. As from 1 July 2015, VAT applies to foreign suppliers that provide electronic services (e.g. games, audio or video files, software, etc. activated through mobile communication devices or computers) to persons (other than tax-registered businesses) in Korea using information communication networks.

**Rates** – The standard VAT rate is 10%. A zero rate applies to exports, services rendered outside Korea, etc.

**Registration** – All domestic businesses supplying taxable goods or services must register with the tax authorities for VAT purposes. Foreign suppliers that provide electronic services via information communication networks should access the National Tax Service (NTS) website and apply for simplified registration of the business with the NTS.

**Filing and payment** – Filing and payment generally are made on a quarterly basis, but monthly filing is permitted for early VAT refund if the goods or services provided by the business are zero-rated for VAT purposes.

**Source of tax law:** Corporate Income Tax Act, Personal Income Tax Act, Value Added Tax Act, International Tax Coordination Law, Local Tax Act, etc.

**Tax treaties:** Korea has tax treaties with more than 80 countries.

**Tax authorities:** National Tax Service

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