2019 Tax Revision Proposal

Overview

On July 30, 2018, the proposal of 2019 tax revision was announced by the Ministry of Strategy and Finance. It is understood that this proposal was drafted as part of a continued effort for the government to promote income redistribution and sustainable national growth with job creation. This proposal of tax revision was passed through the Cabinet Council in late August this year, after a 20-day pre-announcement period, the revision bill would be brought to the National Assembly in September 2018. Once enacted by the National Assembly, most of tax revisions in the proposal would become effective from January 1, 2019.

We summarized below the major tax revisions that may materially affect to foreign investors and foreign invested companies.

I. Corporate Income Tax Law

1. Expanded scope of permanent establishment for non-resident
(Corporate Income Tax Law §94 (4), Individual Income Tax Law §120 (4))

Under the current tax law, a permanent establishment ("PE") of a non-resident corporation or individual shall not include the following:

a. Place solely used for the purpose of purchasing goods
b. Place solely used for the purpose of storage or custody of goods held not for sale
c. Place solely used for the purpose of processing the non-resident's goods by others
d. Place solely used for the purpose of preliminary and auxiliary activities, including advertising,

market research, collecting information, etc.

The tax revision proposal reflects the revised OECD's Model Tax Convention on Income and on Capital in November 2017 to expand the rights to impose tax on Korean source income of a non-resident in accordance with the BEPS initiatives. In this respect, the tax revision expands the scope of a PE, by strengthen the criteria for the exemption of special activities constituting a PE. Under the tax revision, PE shall not be established only when the activities carried out at the above stated places of business 'a' ~ 'c' are limited to preliminary and auxiliary activities.

Once the proposed tax revision is enacted, the above changes will be effective from the fiscal year commencing on or after January 1, 2019.

2. Anti-abuse rules for PE exemption for preliminary and auxiliary activities
(Corporate Income Tax Law §94 (5), Enforcement Decree of the Corporate Income Tax Law §133 (3), Individual Income Tax Law §120 (5), Enforcement Decree of the Individual Income Tax Law §180)

To reinforce taxation on domestic sourced income of non-resident corporations and individuals, the proposed tax revision includes anti-abuse rules stipulating that PE is established when preliminary or auxiliary activities carried out at the specific place of business by the non-resident falls into either one of the following.

1. When the preliminary and auxiliary activities meet both of the below conditions:
   a. The non-resident or its related parties have a place of business in Korea at the same place or other place in Korea as the specific place of business where the preliminary or auxiliary activities are carried out.
   b. The preliminary or auxiliary activities carried out at the specific place of business are complementary to the business activities conducted at the non-resident's or the non-resident's related parties' domestic place of business.
2. When the combination of business activities carried out by the non-residents or their related parties are complementary each other and are not preliminary or auxiliary in nature.

Once the proposed tax revision is enacted, the above changes in the criteria on preliminary or auxiliary activities in determining establishment of PE will be effective from the fiscal year commencing on or after January 1, 2019.

3. Expanded definition of dependent agent and clarification of contracts subject to the dependent agent rule
(Corporate Income Tax Law §94 (3), Individual Income Tax Law §120 (3))

The current tax law stipulates that existence of a dependence agent of non-resident corporations or individuals who has the authority to conclude contracts on behalf of the non-resident and habitually exercises such authority shall constitute the PE of the non-resident.

The tax revision proposal provides broader scope of a dependent agent in which a person satisfying all of the below descriptions shall be treated as a dependent agent.

a. A person who has significant role in concluding contracts on behalf of the non-resident while he/she does not have the authority to conclude such contracts.
b. The non-resident does not modify the key terms and conditions of the contracts being concluded

Furthermore, the types of contracts subject to the above dependent agent rules are newly introduced in the tax revision proposal.

a. Contracts being concluded in the name of the non-resident
b. Contracts for the transfer of the non-resident's assets or for the grant of right to use the non-resident's properties
c. Contracts for service to be provided by the non-resident

Once the proposed tax revision is enacted, the above changes related to dependent agent rules in determining establishment of PE will be applicable from the fiscal year commencing on or after January 1, 2019.

4. Extended carry-forward period for donations
(Corporate Income Tax Law §24 (4), Individual Income Tax Law §34 (3) & §61 (2))

Under the current tax law, excess donation expense over the tax limit can be carried forward for 5 years. To promote charitable contributions, the tax revision proposal includes extension of the carry-forward period to 10 years.

Once the proposed tax revision is enacted, the extended carry-forward period will be applicable on the tax returns being filed on or after January 1, 2019.

5. Revision on dividend received deduction bracket for a Holding Company
(Corporate Income Tax Law §18-2)

When a Holding Company receives the dividend from its subsidiaries, certain portion of dividends are deducted from taxable income of the Holding Company (i.e. the Dividend Received Deduction, "DRD") depending on the shareholding ration. To increase the Holding Company's shareholding in subsidiaries, the tax revision proposal introduces an additional breakdown of the DRD bracket for the Holding Company as below.

<table>
<tr><th colspan="3">Current DRD Rate</th></tr>
<tr><th colspan="2">Ownership % of Holding Company</th><th rowspan="2">DRD %</th></tr>
<tr><th>Listed</th><th>Non-listed</th></tr>
<tr><td>40%~</td><td>80%~</td><td>100%</td></tr>
<tr><td>20~40%</td><td>40~80%</td><td>80%</td></tr>
<tr><td>~20%</td><td>~40%</td><td>30%</td></tr>
</table>

<table>
<tr><th colspan="3">Proposed DRD Rate</th></tr>
<tr><th colspan="2">Ownership % of Holding Company</th><th rowspan="2">DRD %</th></tr>
<tr><th>Listed</th><th>Non-listed</th></tr>
<tr><td>40%~</td><td>80%~</td><td>100%</td></tr>
<tr><td>30~40%</td><td>50~80%</td><td>90%</td></tr>
<tr><td>20~30%</td><td>40~50%</td><td>80%</td></tr>
<tr><td>~20%</td><td>~40%</td><td>30%</td></tr>
</table>

Once the proposed tax revision is enacted, the revised DRD rate for the holding company will be applicable on the dividend received on or after January 1, 2019.

6. Newly introduced penalty on illegitimate cash receipts

(Corporate Income Tax Law §75-5)

Based on tax revision proposal, a 2% penalty shall be levied for receiving fraudulent cash receipts or credit card receipts on goods or services that have not been provided.

Once the proposed tax revision is enacted, the newly introduced penalty will be applicable on the receipts received on or after January 1, 2019.

7. Strengthened limitation on utilization of net operating loss for foreign corporations

(Corporate Income Tax Law §91)

Under the current tax law, foreign corporations can utilize the outstanding Net Operating Loss (“NOL”) up to 80% of the taxable income. For domestic corporations, outstanding NOL in the fiscal year commencing on or after January 1, 2018 can be utilized to offset only up to 70% of the taxable income, and up to 60% of the taxable income in the fiscal year commencing on or after January 1, 2019, as introduced in the prior year’s tax revision.

To provide equal limitation on the utilization of NOL on foreign corporations to that of domestic corporations, the tax revision proposal further limits the utilization of NOL for foreign corporations to 60% of the taxable income.

Once the proposed tax revision is enacted, the 60% limitation will be applicable from fiscal years commencing on or after January 1, 2019.

8. Rationalization of taxation regime for the domestic source income of Overseas Investment Vehicle (hereafter referred to as "OIV") – Rationalize the standard for foreign corporation determination
(Enforcement Decree of Corporate Income Tax Law §1)

Under the current tax law, the corporation that satisfies the one or more of following standards shall be regarded as foreign corporation.

- An entity endowed with legal personality having corporate status pursuant to the law of the jurisdiction in which it was incorporated
- The entity solely consists of members (or partners) with limited liability.
- The entity possesses separate rights and obligations, such as ownership of property, or being able to sue or be sued in a lawsuit (party to a lawsuit), independently from its members (i.e. the standard for rights and obligation).
- The entity is either considered the same type of, or bears high similarity with, a Korean entity that is classified as corporation under the relevant Korean law.

In accordance with the proposed tax revision, the standard for rights and obligation is eliminated from the foreign corporation determinations in order to rationally reform the current standards.

Under the current tax law, even though the overseas investment vehicle ("OIV") is not treated as a corporation in the country where it is incorporated (hereafter referred to as 'resident country'), such OIVs are classified as the foreign corporation for the Korean tax purposes in many cases according to the standard for separate rights and obligation, in which case, OIV is subject to corporate income tax, not the individual investor. The proposed tax revision will rectify such discrepancy.

Once the proposed tax revision is enacted, this new regulation for rationalizing the standard for foreign corporation determinations will take place on or after January 1, 2020.

9. New special provision on substantive owner of domestic source income for OIV
(Individual Income Tax Law §121, Corporate Income Tax Law §93-2 (Newly Enacted))

In accordance with the proposed tax revision, the special provision is granted on substantive owner for OIV in order for domestic tax law and tax treaty to be applied on the basis of substantive investor. The new special provision is established to address situation where an OIV would be deemed as a substantive owner of domestic source income, provided that any of the following three conditions are met. Please note that, if OIV is not treated as a corporation, only the last two conditions, ② and ③, shall apply.

① If the OIV satisfies all of the following criteria
  - The OIV shall be liable to pay tax in its resident country; and
  - The OIV is not established for the purpose of avoiding tax on the Korean source income; or

② If the OIV cannot identify the investors (if the investors are partially identified, this provision will apply to the portion which is not identified)

- Even though the OIV is deemed as the substantive owner, it will be subject to the tax pursuant to the domestic tax law (i.e. not being entitled to the tax treaty benefits under the applicable tax treaty between Korea and the resident country of OIV); or

③ If the OIV is deemed as the substantive owner under the applicable tax treaty

Once the proposed tax revision is enacted, this new regulation for the OIV regarded as a substantive owner of domestic source income will be effective from fiscal year commencing on or after January 1, 2020.

10. Reduction of fines for failure to issue cash receipt
(Punishment of Tax Evaders Law §15, Individual Income Tax Law §81-2, Corporate Income Tax Law §75-6)

The fines imposed for failure to issue cash receipt are stipulated in the current Punishment of Tax Evaders Law. Currently, the failure to issue the cash receipt is subject to fine at 50% of the transaction amount. The domestic corporation which operates the business required to issue the cash receipt is obliged to issue the cash receipts for the goods at price of KRW 100,000 won or more, even without the request from the recipient.

In accordance with the proposed tax revision, the fines are converted into the penalty under the Individual income Tax Law or Corporate Income Tax Law, which is reduced to 20% of the transaction amount.

Once the proposed tax revision is enacted, this new regulation will apply to the case of failure to issue the cash receipt on or after January 1, 2019.

II. <u>Tax Incentive Limitation Law</u>

1. New 10% tax credit for profit sharing for a Small or Medium Sized Enterprises (hereafter referred to "SMEs")
(Tax Incentive Limitation Law §19)

Under the proposed tax revision, the 10% new tax credit for SMEs is introduced to support the SMEs which share their profits with their employees. The SMEs which adopt or agree to adopt the profit sharing with their employees will receive tax credit corresponding to 10% of the amount that the SMEs share with their employees (except for executive officers and employees earning KRW 70million or more of annual salary). However, the new tax credit will not be available if the number of full-time employees is decreased or if the SMEs already receive the exiting tax credits for enterprises increasing earned income (Tax Incentive Limitation Law §29-4).

Furthermore, this new provision allows 50% exemption on the individual income tax on the amounts made by the qualifying SMES under such profit share regime.

Once the proposed tax revision is enacted, this new regulation will apply on or after January 1, 2019.

2. New tax credit for employees returning from childcare leave
(Tax Incentive Limitation Law §29-3)

Under the proposed tax revision, the new tax credit for the SMEs and middle sized enterprises which maintain the employees returning from the childcare leave for more than 6 month. The tax credit amount will be 5% for middle sized enterprises (10% for SMEs) of the salary expenses of such employees.

However, this new regulation is not available if the total number of full-time employees is decreased. In addition, the tax credit amount provided will be cancelled in case those employees do not work for more than 1 year after reinstatement.

Once the proposed tax revision is enacted, this new tax credit regulation will apply on or after January 1, 2019.

3. Expansion of tax credit to support the youth employment growth
(Tax Incentive Limitation Law §29-7)

Under the current tax law, the company which increases its employees can claim the tax credit for certain amount per employee.

In order to enhance the support for youth job creation companies, this new regulation provides an additional tax credit in the amount of KRW 5 million per full time youth employee newly hired.

If this additional tax credit is introduced, the tax credit amount per person provided for increase in employment is as follows.

(Unit : KRW in millions)

<table>
<tr><th colspan="2" rowspan="2">Types</th><th colspan="2">SME</th><th rowspan="2">Middle-Sized Enterprise</th><th rowspan="2">Large Enterprise</th></tr>
<tr><th>Metropolitan</th><th>Rural</th></tr>
<tr><td colspan="2">Full-time employees</td><td>7</td><td>7.7</td><td>4.5</td><td>n/a</td></tr>
<tr><td rowspan="2">Full-time youth employee</td><td>General</td><td>10</td><td>11</td><td>7</td><td>3</td></tr>
<tr><td>Youth-friendly</td><td>15</td><td>16</td><td>12</td><td>8</td></tr>
</table>

	company				

* Standard for youth friendly company will be announced later.

Once the proposed tax revision is enacted, this new regulation will be effective from the tax filing reported on or after January 1, 2019.

4. Accelerated depreciation for innovative growth investment asset
(Tax Incentive Limitation Law §28-3)

This new regulation is established to allow the accelerate depreciation for innovative growth investment asset in order to promote the investment activities. In accordance with the proposed tax revision, the companies are eligible to apply the accelerated useful life within 50% range of statutory useful life specified in the tax law for R&D facilities and the new growth technology commercialization facilities acquired from July 1, 2018 to December 31, 2019.

Once the proposed tax revision is enacted, this new tax provision will apply to the investment assets acquired on or after July 1, 2018.

5. Abolishment of income tax exemption for foreign direct investment
(Tax Incentives and Limitations Law §121-2, 121-5)

Under the current Tax Incentives and Limitations Law, foreign investors making qualifying investments in Korea such as investment on new growth engine industry or investment on business operating in Foreign Investment Zone(FIZ) or Free Economic Zone(FEZ), can claim the tax exemptions.

In order to provide equal and fair tax treatment between domestic and foreign capital, the tax exemption benefits applicable to qualifying foreign direct investments will be abolished.

Once the proposed tax revision is enacted, this revised provision will be effective from the tax exemption applications made on or after January 1, 2019.

6. Extension of preferential tax rates for foreigner employees
(Tax Incentive Limitation Law §18-2)

Under current tax laws, foreign employees are able to elect to apply flat income tax rate of 19%, instead of regular progressive income tax rates, for the first 5-year period starting from the year in which they begin working in Korea. This flat rate is applicable for foreign employee who start to work in Korea before December 31, 2018.

According to the proposed tax revision, the sunset date of December 31, 2018 is extended to December 31, 2021. But this extension of preferential tax rate will not apply to foreign employees for whom 5 years of period is expired before December 31, 2018.

7. Extension of tax exemption period for foreign engineers
(Tax Incentive Limitation Law §18)

Under current tax laws, foreign engineers who first begin working in Korea before December 31, 2018 are able to claim 50% tax exemption on their Korean sourced employment income for the first 2 year period starting from the year when they begin working in Korea.

According to the proposed tax revision, the sunset date of December 31, 2018 is extended to December 31, 2021 and the 2 year exemption period is extended to 5 years.

Once the tax revision is enacted, the new tax exemption will apply for foreign engineers who begin working in Korea on or after January 1, 2019.

III. International Tax Coordination Law

1. Abolishment of priority for application of the tax treaty on income classification over the domestic tax law
(International Tax Coordination Law §28)

Under the current tax law, income classification of Korean source income for non-resident under treaty has priority over the classification under the domestic tax law.

In order to prevent the case where the Korea's right to impose tax on Korean source income may be weakened where there is a conflict in the income classification between the tax treaty and the domestic tax law, the proposed tax revision abolishes the regulation under which the income classification under the tax treaty takes the priority over the domestic tax law.

2. Enhancement of effectiveness of transfer pricing
(International Tax Coordination Law §5)

Under the current International Tax Coordination Law, the transactions with related parties must be conducted at arm's length price. The arm's length price is defined as the price which would be applicable to the transaction between unrelated parties and transaction conditions, such as the nature of goods or services traded, economic circumstances, and other related matters should be taken into consideration in determining the arm's length price.

The proposed tax revision adds the following requirements in order to enhance the effectiveness of the arm’s length principle;

- ✓ Tax authorities shall have clear understanding of the transaction by considering the commercial/financial relationship, contract conditions, and other related matters between domestic taxpayer and its overseas related parties, etc., and determine whether such transaction is reasonable.

- ✓ If the related party transactions lacks reasonable commercial grounds compared to transactions with non-related third parties, such transaction should either be excluded or substituted with another transaction in determining the arms’ length price.

It is expected that the tax authority will apply strict standards in determining the arm’s length price under the revised tax provision. No announcement was made with regards to the effective date.

3. New disclosure requirement for the result of Mutual Agreement Procedure (“MAP”)
(International Tax Coordination Law §27)

Under the current International Tax Coordination Law, the Minister of Strategy and Finance may announce the result of MAP at closing to the public.

In order to enhance the transparency of the MAP process, the proposed tax revision introduces a new provision which requires the result of MAPs related to the adoption/interpretation of tax treaty to be announced to the public.

Once the proposed tax revision is enacted, this provision will be effective from MAP results concluded on or after January 1, 2019.

4. Extended range for substantive owners of foreign financial accounts owned by foreign corporations
(International Tax Coordination Law §50-4)

Under the current International Tax Coordination Law, the scope of substantive owner who is subject to reporting requirement on foreign financial accounts includes a domestic corporation which directly or indirectly owns 100% of voting shares of another foreign corporation having a foreign financial account if it is located in jurisdiction which does not have tax treaty with Korea.

The proposed tax revision has extended the range of substantive owner to include individual resident, who directly or indirectly, with its related parties, owns 100% of shares in a foreign corporation located in jurisdiction with no tax treaty with Korea.

Once the proposed tax revision is enacted, this new regulation will apply to the reporting of foreign financial account owned in 2019.

5. Minimum fine for non-reporting/under-reporting of foreign financial accounts
(International Tax Coordination Law §34-2)

Under the current International Tax Coordination Law, non-reporting or under-reporting of foreign financial account would be subject to fine at 10% ~ 20% of the amount of non-reported or under-reported account. However, if criminal punishment is made, the entire amount of fine is canceled.

In order to enhance the effectiveness in penalty for the non-compliance of reporting requirement for the foreign financial accounts, the proposed revision introduces the minimum monetary fine amount at 13% of non-reported/under-reported amount, regardless of whether or not criminal penalty is imposed.

Once the proposed tax revision is enacted, this new regulation will apply to the reporting of foreign financial account owned in 2019.

IV. Value Added Tax

1. Expanded scope of deemed supply of goods for VAT
(Value Added Tax Law §10 ①)

Under current VAT laws, certain deemed supply of goods (e.g. consumption of goods in VAT exempt business, etc.) is subject to VAT consequence, if input VAT deduction had been claimed for the supplied goods.

According to the revised VAT laws, in addition to the existing conditions, if the goods are purchased at zero-rate VAT in order to export but are used in VAT exempt business, such supply of goods would also be considered as deemed supply of goods which is subject to 10% VAT consequence. .

Once the tax revision is enacted, the new rule will be effective for use or consumption of goods on or after January 1, 2019.

2. Expanded scope of electronic services of foreign service providers being subject to VAT
(Value Added Tax Law §53-2 ①, Enforcement Decree of the Value Added Tax Law §96-2 ①)

Under current VAT laws, provision of certain electronic services by foreign service providers to individuals, including games, music, video, electronic documents, software, and other intellectual property are subject to VAT consequences.

According to the proposed revision, the scope of VAT leviable electronic services provided by foreign service providers will be expanded to include cloud computing (including cloud storage) services to promote equal tax treatment with domestic service providers.

Once the tax revision is enacted, the new rule will apply for services rendered on or after July 1, 2019.

3. Extended payment due dates for proxy VAT payments in case of business transfer
(Value Added Tax Law §52 ④)

Under current VAT laws, even though the comprehensive business transfer is exempt from VAT consequences in principle, if the transferee makes proxy VAT payment by the 10th day of the following month after the business transfer, such comprehensive business transfer is treated as being subject to VAT.

According to the revised VAT laws, the proxy VAT payment due date has been extended to the 25th day of the following month after settlement.

Once the tax revision is enacted, the extended due date will apply for comprehensive business transfers conducted on or after January 1, 2019.

4. Reduction of penalties for VAT
(Value Added Tax Law §60 ②, ⑤)

Under current VAT laws, taxpayers have an obligation to report all tax invoices electronically to the tax authorities by the next business day for which delayed filing penalties are imposed at 0.5% of the sales value if the filing is made within the 11th day of the following month or non-filing penalties at 1% of the sales value if the filing is not made within the 11th day of the following month.

Furthermore, under current VAT laws, in case a taxpayer files amended VAT returns to claim additional input VAT deduction pertaining to purchases made using credit cards, if the credit card purchase receipt had not been filed within the original filing due date, penalties for late submission of credit card purchase receipts at 1% of the purchase price is imposed.

To provide some relief on the penalties, the proposed tax revision reduces penalties for delayed filing of electric tax invoice from 0.5% to 0.3% and penalty for non-filing of electric tax invoices from 1% to 0.5%, respectively, and also extends the cut-off date for delayed filing from the 11th day of the following month after the end of taxable period (i.e. each quarter) to the statutory due date of final VAT returns (25th of the following month after the end of every second quarter). For non-filing of credit card purchase receipts by the original due date, the revised VAT laws reduces penalty rates down from 1% to 0.5%.

Once the tax revision is enacted, the reduced penalty rates and extended cut-off date will apply for sales and purchases made on or after January 1, 2019.

V. Other tax laws

1. Extended statute of limitation for offshore transactions
(National Basic Tax Law §26-2)

In order to enhance the effectiveness of tax to prevent the offshore tax evasion, the proposed tax revision introduces the definition of offshore tax evasion into the National Basic Tax Law and extended the statute of limitation for such offshore transaction.

According to tax revision, the term “offshore transaction” includes transactions, such as domestic and international transactions between Korean resident and non-resident, transactions for offshore assets or offshore services between Korean residents. The statute of limitation applicable to the “offshore transaction” will be 15 years for fraudulent or other illegal acts and 10 years for both non-reporting and under-reporting.

Once the proposed tax revision is enacted, this new regulation will apply to the tax obligation arising on or after January 1, 2019.

2. Extension of statute of limitation in the case of change of substantive owner
(National Basic Tax Law §26-2)

Under the current National Basic Tax Law, even after the expiration of general statute of limitation, the tax can be imposed within 1 year from the date when the court decision in relation to the tax imposition is made.

In order to prevent the possible loss of authority to tax upon change of substantive owner, the proposed tax revision introduces new provision which allows the tax authorities to impose tax within 1 year from the date when the substantive owner of the Korean source income is confirmed after the court decision as to the tax imposition is made.

Once the proposed tax revision is enacted, this new regulation will apply to the case where the court decision is made on or after January 1, 2019. However, as an interim measure, the cases where the general statute of limitation is expired before December 31, 2018, the previous regulation will apply.

3. Reduction of interest on penalty applicable to non-compliances with the tax law
(National Basic Tax Law §27-4)

Interest on penalty applicable to non-compliances with tax law will be reduced as follow;

- ✓ Failure to pay tax/Failure to return over-refunded tax: 0.025% per each day delayed (currently

0.03%)

- ✓ Failure to pay withholding tax: 0.025% per each day delayed (currently 3% of underpaid tax + 0.03% per each day delayed)

This new regulation will apply to tax imposition/reporting made on or after the effective date of relevant Presidential Decree.

4. Limit on joint and several tax liability as a result of split-off/split- off merger
(National Basic Tax Law §25)

In the case of split-offs and split-off mergers, the current National Basic Tax Law places joint and several tax liability for the taxes assessed before the split-off to the split-off company, the newly established company after split-off, and the surviving company after spilt-off merger.

In order to reasonably limit the joint tax liability arising from the spilt-offs and split-off mergers, the proposed tax revision places limit on joint and several tax liability of each party resulting from split-off and split-off merger up to the value of asset received from the split-offs.

Once the proposed tax revision is enacted, this new limit will apply to the split-offs and split-off mergers occurring on or after January 1, 2019.

5. Limit on secondary tax liability of the business transferees
(Enforcement Decree of the National Basic Tax Law §22)

Under current law, in case of a comprehensive business transfer, the transferee is subject to secondary tax liability for the taxes fixed prior to the business transfer date to the extent of the value of business transferred.

The proposed tax revision narrows the scope of business transferees that are subject to secondary tax liabilities from ‘all business transferees’ to the business transferee who is related party of the transferor, or the transferee of business transfer conducted for tax avoidance purposes.

Once the tax revision is enacted, the new rule will apply to business transfer conducted on or after January 1, 2019.

6. Right to record discussions during tax audit
(National Basic Tax Law §91-4 ⑤)

To ensure due legal procedures are followed by tax officers, to prevent abuse of tax officers’ rights, and to protect taxpayers’ rights during tax audit, the tax revision introduces the right of taxpayers and tax officers to record discussions during tax audits.

Under the proposed tax revision, taxpayers and tax officers have the right to record all discussions during a tax audit, and for tax officers, prior notification to the taxpayer is required before recording. The tax officer also has an obligation to share any recordings with the taxpayer upon request.

Once the tax revision is enacted, the new rule will apply from tax audits to be conducted on or after January 1, 2019.

7. Expanded scope of limited tax audits
(National Basic Tax Law §81-11)

Under current law, in principle, tax audits are to be conducted on a comprehensive basis to account for all types of tax for which the taxpayer is obligated to pay, but under certain circumstances as prescribed by law, a partial tax audit can be performed whereby the scope of audit is limited to confirming related details.

Under the proposed tax revision, the scope of partial tax audit is extended to include amended returns filed by non-resident individuals or non-resident companies to request refund of taxes paid on income that are non-taxable, exempt or subject to reduced tax rates as prescribed under the tax treaty between Korea and the jurisdiction of the non-resident.
Once the tax revision is enacted, the new rule will be in effect immediately.

8. Expanded scope and rate of exit tax
(Individual Income Tax Law §118-9, §118-11, §118-15)

Under current tax laws, when a Korea resident who is a majority shareholders of listed companies or unlisted companies expatriate from Korea in certain cases, the exit tax is imposed at 20% on any unrealized capital gains from the shares held as of the exit date as calculated based on the difference between the market value of the shares as of the exit date and acquisition price.

According to the proposed tax revision, the scope of expatriate tax is expanded to include majority shareholders in real property rich companies of which 50% (80% for golf courses and ski resorts) or more of its assets is composed of real estates, and the exit tax rate is increased to be progressive in nature where the first KRW 300 million is taxed at 20%, and the remainder at 25%. Furthermore, to encourage voluntary filing by taxpayers, the tax revision introduces new penalty for failure to report shareholding to tax office by the date before the expatriation up to 2% of the face value of shares.

Once the tax revision is enacted, the expanded scope, tax rate, and penalties will be applicable for tax residents exiting Korea on or after January 1, 2019.

VI. Local Tax

1. Reduction of acquisition tax exemption for mergers and split-offs
(Local Tax Incentive Limitation Law §57-2)

Under current tax laws, 85% of acquisition tax is exempted on assets acquired through qualified mergers, split-offs, spin-offs, contributions in kind, exchange of assets, and comprehensive business transfers before December 31, 2018.

According to the proposed tax revision, although the sunset date is extended to December 31, 2021, the exemption ratio is reduced to 50% (60% for mergers between small and medium enterprises, and mergers with technological innovations companies).

Once the tax revision is enacted, the extended sunset date and reduced exemption ratio will apply to qualified asset acquisitions made on or after January 1, 2019.

2. Increased clarity and sunset extension on deemed acquisition tax exemption for holding companies
(Local Tax Incentive Limitation Law §57-2 ⑤)

Under current tax laws, if a company becomes a holding company, or if a holding company acquires shares in a subsidiary, 85% of deemed acquisition tax imposed on the holding company as the controlling shareholder is exempt if the shares are acquired before December 31, 2018.

The proposed tax revision extends the sunset date to December 31 2021, and also provides clarity on non-applicability of the 85% exemption in the case where a company becomes the holding company by way of acquiring shares in unrelated company.

Once the tax revision is enacted, the extended sunset date and limitations on acquisition tax exemption will apply to transactions conducted on or after January 1, 2019.

3. Refund procedures for withheld local income tax
(Local Basic Tax Law §50 ④)

Current local tax laws do not stipulate refund request procedure of the withheld local tax for tax withholding agent nor income recipients.

The proposed tax revision introduces the refund request procedures for over-withheld local income taxes for both tax withholding agents and income recipients.

Once the tax revision is enacted, this new provision will be effective from January 1, 2019.

KPMG contacts

For more information about how KPMG Tax can help your business with tax matters, please contact one of the following professionals.

Head of Tax

Yoon, Hak Sup
T. 82(2)2112-0436
E. haksupyoon@kr.kpmg.com

Head of Global Tax

Oh, Sang Bum
T. 82(2)2112-0721
E. sangbumoh@kr.kpmg.com

Partner of Global Tax

Ihn, Byung Choon
T. 82(2)2112-0983
E. bihn@kr.kpmg.com

Partner of Global Tax

Lee, Sung Wook
T. 82(2)2112-0946
E. sungwooklee@kr.kpmg.com

Partner of Global Tax

Kim, Dong Hoon
T. 82(2)2112-0938
E. dkim@kr.kpmg.com

Partner of Global Tax

Cho, Sang Hyun
T. 82(2)2112-7687
E. sanghyuncho@kr.kpmg.com

kpmg.com/kr