

# Korean Tax Brief

## Update on Current Issues and Trends

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### 1. New rule on the arm's length interest rate for loan transactions with foreign related parties

On 6 February 2017, the Tax & Customs Office of the Ministry of Strategy and Finance ("MOSF") made a pre-announcement of legislation for the revisions to the enforcement rules of 15 tax laws. Major revisions to the Enforcement Rule of the Law for the Coordination of International Tax Affairs are as follows.

(1) The MOSF introduced the new forms for the country-by-country reporting ("CbCR") and the advance notification of reporting entity. It is delegated to the Minister of Strategy and Finance to announce the specific scope of foreign related parties subject to the CbCR requirements.

(2) The MOSF updated the rules on the arm's length interest rate applicable for the loan transactions between a resident and a foreign related party. Under the new rule, the interest rate for overdrafts prescribed by Article 43 (2) of the Enforcement Rule of the Corporate Tax Act ("CTA") shall be deemed as arm's length interest rate for the resident's lending to the foreign related party and the 12-Month LIBOR plus 1.5% shall be deemed as the arm's length interest rate for the resident's borrowings from the foreign related party.

For fiscal years beginning on or after 1 January 2016, all domestic corporations and foreign corporations with Korea-source income whose sales revenue exceeds KRW 100 billion and the volume of cross-border related-party transactions exceeds KRW 50 billion are required to submit both Master file and Local file to the head of the tax office having jurisdiction over the place of tax payment within 12 months from the fiscal year-end. The country-by-country ("CbC") report is also required to be submitted by domestic corporations (ultimate parent company) with the prior year's consolidated sales revenue exceeding KRW 1 trillion.

## **2. A payment statement should be submitted even if there is no tax withheld from a foreign corporation's domestic source income due to a loss from transfer of stocks (Joshim 2016, 3808, 2017. 2. 14)**

The withholding agent who pays a domestic income to a foreign corporation is exempted from the obligation to submit a payment statement if the amount of withholding tax is less than KRW 1,000, under Article 162-2 (1) (7) of the Enforcement Decree of the CTA. As an exception to the waiver, however, in case of transfer of securities including stocks, the withholding agent should submit a payment statement regardless of the amount of withholding tax. In light of the above, it is reasonable to conclude that the withholding agent should submit a payment statement even if a loss has incurred from the transfer of stocks.

## **3. A foreign engineer who is a Korean national shall not be entitled to the tax holiday of 50% reduction of income tax on the employment income under Article 18 of the Restriction of Special Taxation Act (Joshim2017jeon419, 2017.03.02)**

Article 16 (1) of the Enforcement Decree of the Restriction of Special Taxation Act ("RSTA") restricts those who have Korean nationality from the scope of foreign engineers eligible for the tax holiday under Article 18 of the RSTA and it is stipulated by the addendum that the restriction applies to the income earned from 2010. Therefore, it is reasonable to conclude that the foreign engineer with Korean nationality should not be entitled to the tax reduction for foreign engineers for the employment income earned during the period from 2011 to 2013.

## **4. Guidelines and clarification on the deduction of company car expenses (Article 27-2 of the CTA) (Jaebeobin-320, 2017.03.06)**

(1) The rule does not apply to the cars owned and used by the foreign business place of domestic companies.

(2) Only for the first fiscal year starting on or after 1 January 2016, the amount calculated by the following formula shall be used for corporate tax purposes as the amount of company car expenses incurred for business purpose in case that the company car was insured by a business-only car insurance for a partial period of the year (lease period in case of leased cars);

Company car expenses × Ratio of usage for business purposes × (Number of days of the actual coverage period of the business-only car insurance on or after 1 April 2016 ÷ Number of days of the mandatory coverage period of the business-only car insurance on or after 1 April 2016)

(3) The rule applies to the cars that are rented to customers by a domestic corporation engaging in auto repair services while the customers' cars are being repaired.

## **5. The MOSF introduced draft revisions to the Corporate Tax Act and the Income Tax Act**

The MOSF has undertaken a project of tax law revision since 2011 in order to improve the clarity and accessibility of tax laws and announced on 23 February 2017 the draft revisions to the Corporate Tax Act and the Income Tax Act. In the proposed revisions, the structure of the laws is reorganized by defining tax liability by income type and arranging the articles in the order of tax filing process so that taxpayers can more quickly find applicable laws. Also, new articles of overview are added in order to allow taxpayers to easily understand the flow and logic of calculating tax base and tax liability by income type.

The structure of law is revised by categorizing taxpayers into two parts, domestic and foreign corporations, and further subdividing the part of domestic corporations into the chapters pertaining to the scope of taxable income and the taxation method. Separate chapters are created for the topics such as capital gains on transfer of land, etc., excess retained earnings taxation, and withholding tax, which used to be dealt together with the taxable income for the fiscal year. The period of the administrative pre-announcement of legislation lasts until 16 March 2017, so anyone who holds opinion on the revision bill may put forth his or her opinion to the Tax Reform team of the MOSF.

## **6. Korea-Hong Kong Agreement on Automatic Exchange of Financial Account Information**

The MOSF signed on 23 January 2017 the Korea-Hong Kong Agreement on the Automatic Exchange of Financial Account Information. According to the agreement, the two countries will annually exchange information with respect to reportable accounts held by the citizens of the other country including the identifying information (name, address, TIN, etc.), the account information (account number and the name of reporting financial institution, etc.), and the financial information (account balance, type of income such as interest and dividend), etc. on an automatic basis starting in 2019.

Although the two countries have provided the other with tax information upon request in accordance with the Korea-Hong Kong double tax treaty entered into force since 2016, the agreement on regular and automatic exchange of information will enable the two countries to more effectively tackle international tax evasion.

In addition, the government has continued to expand its efforts to improve international tax compliance by signing the multilateral agreement on automatic exchange of financial account information with other countries in October 2014. The MOSF released its plan to work on bilateral exchange agreements with 45 countries in 2017, including the Netherlands, Belgium, and Ireland, and add 31 countries in 2018 to the list of automatic exchange agreements in force.

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