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Korean Tax Brief

Update on Current Issues and Trends

Contents

1. The foreign tax included in the gross income when calculating a corporate tax base by selecting the tax credit method under the Corporate Income Tax Act cannot be deducted from the tax base of the corporate local income tax (Josim 2017Ji 0333, 2017 6. 8.)

A company included the foreign tax in the gross income by treating such tax amount as a deemed income when filing a tax base of corporate income tax. Since there is no provision under the local tax related acts to deduct such foreign tax from the tax base of local income tax or the tax amount, the foreign tax payment cannot be excluded from the tax base of the corporate local income tax.

Article 103-19 of the Local Tax Act ("LTA") stipulates that the tax base of the corporate local income tax on the income of a Korean corporation in each business year shall be the amount calculated pursuant to Article 13 of the Corporate Income Tax Act ("CITA"), and Article 103-21(1) of the LTA stipulates that the amount of corporate local income tax on the income of a Korean corporation for each business year shall be calculated by applying a tax rate under Article 103-20 to the tax base calculated under Article 103-19 of the LTA. Based on the fact that i) in case the tax base of the corporate income tax is calculated under the tax credit method for the foreign tax amount, there is no provision under the LTA or the Restriction of Special Local Taxation Act to exclude the foreign tax amount from the tax base of corporate local income tax calculated according to Article 13 of the CITA, and ii) the company included such tax amount in the gross income at its own discretion for the corporate income tax filing, considering that the tax credit method is more advantageous than the deduction method (i.e., including the foreign tax in the deductible expenses), the tax amount at issue should not be excluded from the tax base of the corporate local income tax unless the corporation has filed an amended tax return or a tax refund claim for the corporate tax base for the considered year.

2. National Tax Service will be managing withholding taxes on overseas subsidiaries and non-residents through NTIS

The National Tax Service ("NTS") made a partial revision of the administrative rules of international taxation, according to the changing international tax landscape and the organizational change associated with the implementation of automatic exchange of financial information, and the revisions of relevant laws and ordinances, and published an advance notice.

The purpose of the revision is to improve efficiency of the international tax administrations by standardizing the administrative procedures governing the tax payment of non-residents and foreign companies with domestic source income, tax exemption of foreign invested companies, enforcement of transfer pricing taxation, operation of the advance pricing agreement (APA) program, information exchange between countries, reporting of overseas financial accounts, and taxation of foreign business income of domestic companies, etc.

As one of the major revisions, the rationale for the identification number system of overseas subsidiaries is provided. The head of the NTS (International Tax Resources Management Office) will compile the incorporation data and the annual business performance report of overseas affiliates every month and build such information on the NTIS (Neo Tax Integrated System) annually. The NTS prescribed detailed methods and procedures concerning the assignment of new identification number, management of changes, liquidating process and duties to report the overseas company data, etc. under the revision.

In addition, the NTS stipulated the commissioner of a regional tax office having jurisdiction over the place of tax payment of withholding agent (Chief of Corporate Tax Payment Division) to take charge of the procedures for withholding taxes on non-residents. In addition, it was set forth that the head of the competent tax office receiving the pre-approval notice for the special exemption or reduction of withholding tax should utilize it for the tax resource management, etc. and the head of the competent tax office (Chief of the Withholding Tax Resource Management Division) should take charge of the civil services such as issuance of payment certificate of income tax or corporate tax on the domestic source income.

3. Whether the defined contribution pension premium falls under the personnel expenses qualified for research/human resource development tax credits (Daebub 2016 du 63200, 2017.5.30)

Defined contribution pension paid to researchers working at the research center of a company can be recognized as expenses for the relevant business year, and the premiums definitely belong to the individual researchers, therefore, such premiums are regarded as personnel expenses qualified for research and human resource development tax credit under the Restriction of Special Taxation Act ("RSTA").

The plaintiff argued that "the pension premium qualifies for tax credits because it is actually expended in each business year and recognized as deductible expense". On the other hand, the tax authorities refuted that "such premium paid by the plaintiff to the researchers does not qualify for tax credits under the RSTA". With respect to the dispute, the Supreme Court stated that "the actual premium paid by the plaintiff based on the continued service of the researchers in the research center for each taxable year according to the defined contribution pension plan can be recognized as expenses for the relevant business year and it is viewed that the amount equivalent to the insurance premium is definitely attributable to each researcher." The Supreme Court also stated that "since the premium paid by the plaintiff to the researchers is actually expended for each researcher, it is different from the provision of retirement allowance which is reasonably estimated for the purpose of proper periodical accounting". Based on these facts, the Supreme Court concluded that "the premium of the pension plan at issue paid by the plaintiff falls under the personnel expenses qualified for the research/human resources development tax credit specified by the RSTA".

4. If a trustee supplies goods while managing or disposing of the trust assets transferred from the trustor, whether the trustee transferring the rights to use or consume the goods through the transaction of supplying goods to the counterparty is a VAT taxpayer (Daebup 2017. 5. 18. 2012Du22485)

The Supreme Court concluded that "if a trustee supplies goods while managing or disposing of trust assets transferred from a trustor, the trustee himself or herself has become a contracting party as a party to the rights and obligations of trust assets and accordingly, the VAT taxpayer must be the trustee transferring the right to use and consume the goods to the counterparty through the transaction of supplying goods, and the fact that the profit and expenses arising from the management and disposition of the trust assets are ultimately attributable to the trustor or beneficiary who does not have a direct legal relationship with the counterparty will not change the decision."

In addition, considering the characteristics of VAT, which is a multi-level transaction tax that entails the issuance of tax invoices, it is necessary to regard the trustee as the subject of supply and the taxpayer from disposition of trust assets in order to easily recognize the contracting party relating to trust under the Value-added Tax Act and to prevent a confusion in recognizing the tax basis and the supply price.

5. The Government signs anti-BEPS multilateral agreement to prevent tax avoidance of multinational corporations

The Korean government has decided to participate in the international coordination system to prevent tax avoidance (offshore tax evasion) across borders. The Ministry of Strategy and Finance announced that the Ambassador of Korean delegation to the OECD, Yun Jong-won, signed the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting ("Multilateral Instrument" or "MLI") at the OECD headquarters in Paris on June 7, on behalf of the Korean government. 68 countries, including 33 OECD member countries, participated in this agreement. BEPS, which stands for Base Erosion and Profit Shifting, refers to tax avoidance of multinational corporations exploiting the differences and loopholes in the bilateral tax treaties by transferring the profits from countries with high tax rates to the countries with low tax rates. The tax treaties between countries that signed the MLI will be automatically revised through the MLI even without bilateral treaty negotiations.

Among the 91 tax treaties signed by the Korean government, there are 45 treaties in which the contents are changed in accordance with the MLI. First, regulations to prevent tax avoidance of multinational corporations are introduced. In other words, when the purpose of trading of a multinational corporation is to receive benefits such as non-taxation and low taxation in a tax treaty concluded between the specific countries, a basis for denying the treaty benefits is provided. Institutions where a taxpayer can file an objection to an unfair taxation of a country is extended from the tax authority of the taxpayer's country of residence to the tax authority of both countries. The government plans to carry out domestic related procedures such as the ratification of the National Assembly.

The United States ("US") is excluded from the signing countries, however, declared that there is a rare chance of offshore tax evasion in the US since it is already taking strong regulatory actions. On the other hand, the Korean Government signed an agreement with the US on June 22, 2017 to exchange the country-by-country report, which is prepared by a head office of a multinational corporation on business activities (sales, income, assets, tax payment status, etc.). Under this agreement, Korea will exchange the country-by-country reports annually with the US starting from 2018.

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