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South Korea – New Tax Reform Bill Contains Measures Affecting Individuals

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On 8 August 2012, the Ministry of Strategy and Finance for South Korea released the 2012 tax law revision bill, providing for various changes to the country's tax system.[1] The Bill will undergo review in the National Assembly, during which time it may be subject to further changes. Once the Bill is passed into law by the National Assembly at the end of this year, the amendments will be enforceable starting from 1 January 2013.

In this *Flash International Executive Alert*, we will focus on those measures impacting individuals and their employers.

Extension of Sunset Clause and Adjustment of Tax Rate

There is a sunset clause that was scheduled to automatically abolish from South Korea tax law the provision on the flat tax rate (16.5-percent including resident surtax) as of 1 January 2013. The provision is to be extended for another two years (i.e., applicable to income earned on or before 31 December 2014). This extension should further encourage talented foreign workers to come to work in Korea and support foreign investment in the country. However, the flat tax rate is raised from 16.5 percent to 18.7 percent (including the resident surtax).

Introduction of Deduction for a Single Parent

An income deduction of KRW 1,000,000 per year is available for a single parent supporting children (the child/children must be no more than 20 years old). However, an individual cannot claim both the single parent deduction and the "female income earner deduction."[2]

Expansion of Education Expenses Eligible for Income Tax Deduction

The type of education expenses eligible for a tax deduction will be expanded to include:

- after-school class textbooks for elementary, middle, and high school children;
- meal costs;
- after-school class fees; and
- textbook costs for pre-school children.

However, the total deduction allowed remains the same (KRW 3,000,000 per child per year).

Adjustment of Foreign Financial Accounts Reporting Rules

Under the existing rule, tax residents in South Korea are required to file a foreign financial accounts report form with the National Tax Service ("NTS") by 30 June of the following year if the aggregate value of cash and listed stocks held in foreign financial accounts exceeds KRW 1 billion on any day during the tax year. Under the new rule, the reportable criterion will be extended to include all financial assets including bonds, derivatives, etc. In addition, the KRW 1 billion value-measurement date has changed from "on any day during the year" to "end of the quarter" for the convenience of taxpayers in determining the reportable financial accounts value.

KPMG Note

Tax residents in South Korea are required to file the foreign financial accounts report form; however, the following tax residents are exempt from the filing requirement:

- Foreigners who have stayed in South Korea not more than five years out of the previous 10-year period as of the end of the reporting year.
- South Korean nationals residing overseas who have stayed in South Korea not more than one year out of the previous two-year period as of the end of the reporting year.

Reduction of Tax Base for Consolidated Taxation of Financial Income

The threshold tax base for consolidated taxation[3] of interest and dividend income is reduced from KRW 40,000,000 to KRW 30,000,000. If the taxpayer's total interest and dividend income is less than KRW 30,000,000, that income will continue to be taxed separately at a flat rate of 15.4 percent (including resident surtax).

Reduction of Short-term Capital Gains on Sale of Residential Housing

To normalize the depressed housing market by easing the tax burden on gains arising from short-term transactions, the applicable tax rates will be reduced from 50 percent to 40 percent if the house is transferred within one year of acquisition, and from 40 percent to normal progressive tax rates (i.e., between 6 percent and 38 percent) if transferred within two years of acquisition.

Footnotes:

1 Source: "2012 Tax Law Revision Bill", the Ministry of Strategy and Finance, 9 August 2012.

2 Where the resident is a woman who has no spouse and is the head of a household with dependents, a deduction of KRW 500,000 per year can be claimed. The same deduction can be claimed by a woman who has a spouse (in other words, a married woman) who is not a head of household regardless of whether she has dependents – since there is no joint filing allowed for married couples in South Korea, as such, this is a relief measure for the female spouse of dual income couples.

3 According to South Korean tax law, interest income paid by financial institutions and dividend income paid by public companies generally are subject to the "separate taxation" rule unless the aggregate income amount exceeds the threshold amount – i.e., the withholding taxes (at 15.4 percent) are the final tax and these incomes do not need to be reported on the annual tax return.

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KRW 1 = USD 0.00088
KRW 1 = EUR 0.000705
KRW 1= GBP 0.0005585
KRW 1 = AUD 0.000856

The information contained in this newsletter was submitted by the KPMG International member firm in South Korea. The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser.

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