



Tax News Flash

- Transfer Pricing

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Samjong KPMG Transfer Pricing & Customs Service Group provides readers with Transfer Pricing related recent local tax issues and trends.

This newsletter is a monthly publication of Samjong KPMG Transfer Pricing & Customs Service Group. If you need more detailed explanation, please feel free to contact key contacts or Tai-Joon Kim for transfer pricing matters and Tae-Joo Kim for customs matters.



The following is a recent Korea's tax ruling in relation to transfer pricing

A decision on whether the service fee complies to the arm's length principle.
<Tax Tribunal Decision 2021Suh5598, 2023.08.09>

Background

- The taxpayer provides contents related support services including information regarding the local contents market, local contents production support and administration services to its overseas related party (hereinafter, 'AAA'). In accordance with the services provided, the taxpayer receives a service fee of the related costs with a 10% mark-up.

Tax Office's (Defendant) Claims

- The tax office re-characterized the taxpayer as a content distributor to which AAA outsourced content production and the taxpayer outsourced such functions to another content production company. Moreover, the tax office also claimed that the taxpayer performed key functions such as the purchase and sale of contents rather than the simple administration or support functions. Accordingly, the tax office claimed that the cost plus markup scheme without considering AAA's purchase price for the contents from the 3rd party was not appropriate.
- Claiming the taxpayer as a content distributor, the tax office restructured the service transaction in which the service fee remunerated by AAA should comprise the production costs paid by AAA to the domestic content producer as additional sales and COGS related expenses of the taxpayer. (i.e., adding the production costs to sales of the taxpayer and the costs to expenses of the taxpayer at this same time) According to the restructured transaction, the adjusted operating profit recorded by the taxpayer was lower than the arm's length range of the comparables selected by the taxpayer in the TP report.

Taxpayer's (Plaintiff) Claims

- The taxpayer claimed that the service fee paid by AAA was remunerated at a 10% mark-up which is within the arm's length range calculated by the profitability of comparable companies.
- The taxpayer also claimed that the restructure of the service transaction proposed by the tax office does not reflect the substance of the transaction. Moreover, the COGS related expenses were generated due to the provision of services and was not relevant to the production of contents.

Tax Tribunal Decision

- Due to the circumstances in which the tax office could not provide adequate reasonable grounds for the re-characterization of the transaction, did not make any comparability adjustment between the existing transaction structure and the restructured transaction, which may affect factors/transactional terms & conditions considered in calculating the arm's length price, and did not provide any specific reason that the transfer pricing method and the comparable companies selected by the taxpayer were inappropriate, the Tax Tribunal concluded that the tax office was incorrect in the taxation regarding the service transaction.

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