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GMS Flash Alert

2017-133 | September 6, 2017

South Korea - Proposed Tax Revisions Aim to Better Tap Expatriates' Wealth

The 2017 Tax Law Amendment Bill ("the Bill") announced by South Korea's government on 2 August 2017, is currently under review in the National Assembly and is expected to be finally approved toward the end of year.

In this GMS *Flash Alert*, we provide a summary of the key features of the Bill that could impact international executives and their multinational employers.

WHY THIS MATTERS

Notwithstanding the loosening of the criteria for tax residency, tax costs and budgeting for assignments to and from South Korea could be affected by the modification in income tax rates, which we discuss further below.

Additionally, employers may need to make the necessary payroll adjustments and update hypothetical taxes for tax equalized assignees.

In order to mitigate surprises and risks, the changes we describe in this newsletter with respect to tax rate changes, withholding tax rates, and foreign account financial reporting should be taken into account when evaluating international assignments both into and out of South Korea.

Loosened Tax Residency Condition

Currently, one of the criteria for tax residency is having a domicile in South Korea for 183 days or more starting from two years before the end of the relevant year. However, effective from 1 January 2018, this rule is to be loosened to 183 days or more in one tax year with a view that this will induce more investment in the country from South Korean nationals residing abroad.

New Top Marginal Income Tax Rates

Effective from 1 January 2018, the new top marginal income tax rate of 42 percent (46.2 percent including local income tax) will be applied to taxpayers with an income tax base in excess of KRW 500 million and the second top income tax rate of 40 percent (44 percent including local income tax) will be applied to tax bases in excess of KRW 300 million up to KRW 500 million. This step is intended to improve income redistribution in the country by asking those with higher incomes to pay a greater share of taxation.

Currently, the highest marginal income tax rate is 40 percent (44 percent including local income tax) which is applicable to tax bases in excess of KRW 500 million and the second highest marginal income tax rate is 38 percent (41.8 percent including local income tax) which is applicable to tax bases in excess of KRW 150 million up to KRW 500 million. (For prior coverage of changes to the rates, see GMS *Flash Alert* 2017-006, 12 January 2017.)

KPMG NOTE

- Of interest to high-income earning international assignees, a foreign worker who starts to work in South Korea before 31 December 2018, can elect to have the flat tax rate of 20.9 percent (inclusive of local income tax) applied for five consecutive tax years, including the first year he/she starts to work in the country.

- Foreign workers who had been "continuously" working as of 1 January 2014, will be able to apply a flat tax rate until 31 December 2018. The tax costs for those who are not eligible for the flat tax rate will be affected by the changes in the top marginal income tax rate.

Increased Withholding Tax Rate for Employees Dispatched from a Foreign Entity and Extended Mandatory Withholding Agent

Under certain conditions, a South Korean company is required to file a payroll withholding tax return at a flat rate of 17 percent (18.7 percent including local income tax) on the service fee payable to a foreign entity dispatching its employees. (For prior coverage, see GMS *Flash Alert* 2016-057, 6 May 2016.) However, according to the Bill, the withholding tax rate is to be increased to 19 percent (20.9 percent including local income tax) effective from 1 July 2018. In addition, the conditions that apply to South Korean companies are being extended since the government wishes to exercise greater fiscal control over expatriates subject to tax in the country. The conditions are:

1) The annual service fee payable to the foreign entity exceeds KRW 2 billion (currently, KRW 3 billion).

2) The business of the South Korean entity falls under one of the following "mandatory" industries: aviation transportation, construction, professional, scientific or engineering services and the following newly-added industries, ship-building and financial services.

3) Prior year's gross sales of the South Korean entity are KRW 150 billion or more, or the prior year's total assets are KRW 500 billion or more.

KPMG NOTE

- The assignee-related withholding obligation is applicable to domestic corporations. A South Korean branch of a foreign headquarters is therefore exempt from this rule.

- The assignee-related withholding tax rate is increased in conformity with previous amendment to the flat tax rate effective from 1 January 2017. Ship-building and financial services are newly added to the categories of businesses falling under this regulation.

Toughened Requirement for Reporting Foreign Bank and Financial Accounts (FBAR)

Tax residents in South Korea that have financial accounts opened with foreign financial institutions are required to file a Report of Foreign Bank and Financial Accounts (FBAR) by 30 June if the aggregate balance in those foreign financial accounts (securities, derivatives, or other financial instruments) exceeds KRW 1 billion on the last day of the month during the year. However, effective from 1 January 2018, the balance that triggers the reporting obligation is being reduced to KRW 500 million. Penalties can be imposed for non-compliance.

KPMG NOTE

A foreign resident who has or had his/her domicile or place of residence in the Republic of Korea for not more than five years in total starting from 10 years prior to the end of the relevant year is exempt from South Korean FBAR reporting.

KRW 1 = EUR 0.00074
KRW 1 = USD 0.00088
KRW 1 = GBP 0.00676
KRW 1 = AUD 0.0011
KRW 1 = JPY 0.096

Contact us

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