Last month, we looked at two of the six major points in the government’s tax law amendments (the “Amendment”), which was submitted to the National Assembly by Korea’s Ministry of Strategy and Finance on September 30. Below is an overview of the four remaining major Amendment items that may affect foreign-invested companies or foreign corporations conducting business in Korea.

1. Stricter application procedures for claiming a withholding tax exemption treatment under the Korean tax treaties

According to the withholding tax procedures in effect since July 1, 2012 (Article 98-6 of the Corporate Income Tax Law (the “CITL”)), which stipulate the procedures necessary for foreign corporations to claim reduced withholding tax rates under the tax treaties, the foreign corporation that substantively owns the Korean source income (the “Substantive Owner”) must submit an “Application for Reduced Treaty Rate on Korean Sourced Income” to the withholding agent in order to claim the reduced withholding tax rates. In addition, where Korean source income is paid through an investment vehicle established overseas (“Overseas Investment Vehicle” or “OIV”), the OIV must collect the Application for Reduced Treaty Rate on Korean Sourced Income from the Substantive Owners and, in turn, submit the “Report of Overseas Investment Vehicle” and “Details of the Substantive Owners” to the withholding agent for the withholding agent to apply the reduced withholding tax rate.

Similar to the withholding tax procedures discussed above, the Amendment includes a new provision that requires the Substantive Owner to submit a tax exemption application to the tax office that has jurisdiction over the payor in order to claim a tax exemption on the tax exempt Korean source income under the tax treaties (such as capital gains from stocks). Furthermore, where the income is paid through an OIV, the Amendment also introduces a new provision that requires the OIV to collect the Application for Reduced Treaty Rate on Korean Sourced Income from the Substantive Owners and, in turn, submit the “Report of Overseas Investment Vehicle” and “Details of the Substantive Owners” to the tax office that has jurisdiction over the payor. The amendment is effective with income paid after January 1, 2014.

2. Amendment of special income tax regime for expatriate workers

Before the amendment of the law, expatriate workers could receive the benefit of a special income tax that has a flat tax rate of 17 percent (18.7 percent including 10 percent local income surtax). However, according to the Amendment, the above special income tax regime will only apply for five years from the date of employment in Korea, and expatriate workers related to the employer (e.g., a family member of that employer) will be excluded from the benefits of the above regime. The Amendment is effective with income arising on or after January 1, 2014.

3. Expanded scope of exchange of financial information under tax treaties

Until recently, only taxpayers’ financial information specifically identified by the local tax authority in Korea was subject to the exchange of information and exchanged with the foreign tax authority with which Korea had a tax treaty. However, according to the Amendment, a group of taxpayers’ financial information not specifically identified by the local tax authority may be exchanged with foreign tax authorities under the tax treaties. For example, local financial institutions in Korea must provide relevant information on all holders of a particular financial product to Korean tax authorities, which would then be exchanged with relevant foreign tax authorities upon their request, pursuant to the information exchange clause of a tax treaty. In the event of a non-compliance with the request for information, a non-compliant financial institution will be subject to a penalty of up to KRW 30 million.

4. Extension of period to offset losses for funds investing in foreign assets

Under the previous regulation, losses related to share transactions or securities valuation incurred by funds having invested in foreign assets during the tax-exemption period (June 1, 2007 through December 31, 2009) could be offset only against the profits derived between 2010 and 2013. However, the Amendment extends the period by one year to 2014.

By Kyung Geun Lee
Tax Partner, Yulchon LLC / Ph.D. (Economics)
Non-standing Professor, University of Seoul
kygelee@yulchon.com