Taxation, especially the income tax rate, is an issue of concern for CEOs of foreign-invested companies in Korea. Foreign companies have always emphasized the importance of a predictable tax system. To provide foreigners working in Korea with incentives, the Restriction of Special Taxation Act (“the Act”) has offered various tax benefits since 2003. Still, Korea’s inbound foreign direct investment (FDI) has been less than a third of the outbound FDI of Korean companies over the past seven years.

In the beginning of the year, Korean President Park Geun-hye invited the CEOs of foreign businesses and representatives from foreign chambers of commerce to a luncheon at the Blue House. The president shared the government’s proactive FDI promotion policies, including those aiming to attract large-scale FDI from multinational businesses as well as the research and development (R&D) centers and Asian headquarters of global companies to create jobs and boost the economy.

The income tax act has been revised numerous times. Under the latest amendment, which took effect January 1, 2013, the flat income tax rate applied to foreign workers has increased from the previous 15 percent to 17 percent, and the sunset period was extended for another two years, until December 31, 2014. On August 9, 2013, however, the Ministry of Strategy and Finance (MOSF) announced new legislation to narrow the scope of foreign workers who may be taxed under the flat rate, which would be effective a year ahead of the previously scheduled sunset date. The proposal included new provisions that would waive the application of the flat tax rate for any foreigner who works for a “specially related person” and set the time limit of the applicable period at five years from the date a foreigner started working in Korea. According to the proposal, foreigners who have worked in Korea for longer than five years will not be subject to the flat rate from January 1, 2014, instead of from January 1, 2015.

Representatives of foreign chambers of commerce in Korea, foreign financial firms, foreign investors, executives and employees spoke with Foreign Investment Ombudsman Dr. Ahn Choong Yong about the lack of consistency in law enforcement in light of the fact that the Act was revised twice in one year without the consideration of foreign workers’ opinions and will go into effect a year faster than scheduled. Inconsistent amendments would not only deteriorate the business environment for foreign-invested firms but also undermine foreign investors’ confidence in the stability and predictability of Korea’s legal system. So Dr. Ahn set out to resolve the issue.

Before the government proposal went to the National Assembly in September of 2013, Dr. Ahn formally raised the issue with the MOSF through an official document that stressed the need for predictability of law, and the Ombudsman’s experts, called Home Doctors, held meetings with public officials in charge of the matter. The Ombudsman also posed the problem of the revision bill to the Chairman of the Strategy and Finance Committee, the Chairman of the Taxation Subcommittee and their members through official emails and documents prior to deliberation by the National Assembly. Dr. Ahn even contacted the lawmakers of relevant subcommittees individually.

As a result, a newly revised bill that can improve the predictability of law enforcement was passed in an Assembly plenary session and promulgated on January 1, 2014. The main provisions of the amendment are to apply the previous taxation rules to foreigners who started working in Korea before January 1, 2014 and to exclude the foreign-invested companies prescribed by Presidential Decree from the scope of “specially related person.”

The situation highlighted once again the need to improve the taxation system and the time and effort that go into persuading the legislative body. The amendment of the act has provided such new momentum that the Ministry of Trade, Industry & Energy is pushing to apply the flat tax rate benefit to executives and employees of any foreign company that has built a global headquarters or R&D center in Korea. A transparent and predictable tax regime is key to attracting foreign investors. That is why the Foreign Investment Ombudsman has kept in contact with and convinced National Assembly members, not just public officials, about the need to further improve Korea’s investment climate.

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