The following tax information is translated from the Korean for foreign-invested companies and is not legally binding.

Q. What is an APA?

A. An Advance Pricing Arrangement or Advance Pricing Agreement (APA) is an arrangement agreed upon between a taxpayer and the NTS on the application of transfer pricing methodology (TPM) in determining an arm’s length price in advance of future international transactions with foreign-related parties.

A transfer pricing regime refers to a taxation system where tax authorities recalculate taxable income based on an arm’s length price and impose taxes on a company in the event the taxable income is reduced because the company applied a price higher or lower than the arm’s length price to transactions with foreign-related parties.

Multinational enterprises undertaking transactions with foreign-related parties may be exposed to the risk of double taxation through the transfer pricing regime. Against this backdrop, the APA program was introduced to help eliminate the risk of double taxation prior to actual international transactions. (Article 6 of the LCITA)

APAs are initiated by taxpayers and are finalized by the approval of the Commissioner of the NTS. Once an APA is concluded, the taxpayer can use the APA approved by the Commissioner as the most appropriate method during the covered APA term as long as the taxpayer complies with the critical assumptions.

APAs can be concluded either bilaterally or unilaterally. In bi-APAs, both the NTS and the foreign tax authorities are involved, whereas uni-APAs are only concluded between the taxpayer and the Korean tax authority. Bi-APAs are more useful in addressing the issue of double taxation related to transfer pricing. However, bi-APAs usually take more time for conclusion compared to uni-APAs, as the former involves a negotiation process with foreign tax authorities.

Even though the APA is an arrangement on the future application of the TPM between the taxpayer and the tax authorities, the taxpayer may also request a rollback of the proposed TPM to tax years prior to the proposed APA term.

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Q. Are there any benefits of an APA?

A. First, taxpayers can reduce the potential tax uncertainty arising from the future application of the transfer price regime related to their transactions with foreign-related parties. If a taxpayer files tax returns and pays taxes according to the agreed upon APA, the taxpayer can concentrate on business without worrying about a possible transfer pricing audit. Depending on the situation, taxpayers may request the extension of the covered APA term so that they may reduce the risk of transfer pricing audits for a prolonged period of time.

Second, taxpayers can allocate the company’s assets or human resources more efficiently. If an APA is concluded, the taxpayer may place the human resources and money in more productive areas, which, otherwise, would have been used to respond to a transfer pricing audit. Moreover, an APA helps taxpayers address the transfer pricing issue at a more affordable cost when compared to the considerable time and money spent on hiring tax advisors and filing a lawsuit in the event of a tax audit.

Third, an APA eliminates the possibility of double taxation. In bi-APAs, where both sides reach an agreement, there is no possibility of double taxation, as corresponding and compensating adjustments are made according to the APA agreed upon between the two tax authorities. Since a uni-APA does not involve an agreement between the two relevant tax authorities, the taxpayer should request a Mutual Agreement Procedure (MAP) for the resolution of a double taxation issue.
Lastly, an APA helps taxpayers make reasonable decisions on transfer pricing. In an APA process, professional tax advisors and the TP experts of the NTS are involved, making it possible to strictly apply internationally accepted tax standards. Moreover, the taxpayer and the Korean tax authority can make more reasonable decisions in APAs since the competent Korean authority negotiates on equal terms with the other tax authorities to reach an agreement. Since taxpayers are allowed to present their opinion anytime throughout the APA process, and exchange their positions with the tax authorities, both the taxpayer and the NTS can reach a mutually satisfactory agreement.

Q. Are there any procedures for the protection of Applicant’s Rights?

A. Where an APA application is rejected because it was deemed to be inappropriate, the NTS shall return all the documents the applicant submitted. Also, all the information the taxpayer presents for an APA request shall not be used for purposes other than APA evaluation and post-APA management. (Article 9, Sections 4 and 5 of the Presidential Enforcement Decree on the LCITA)

For more information, please contact the International Tax Resource Management Office of the National Tax Service (82-44-204-2888~90).