

2014 Tax Law Amendments

Amendments to Korean tax laws were promulgated on January 1, 2014. Summarized below are the key amendments relevant to international taxation.

1. Reduction in Special Income Tax Rate for Foreign Employees

The Special Tax Treatment Control Act was amended on January 1, 2014 by Act No. 12173 (the “Amended STTCA”) and limits the sunset period of the special tax rate for foreign employees for whom the flat rate of 17% is applicable, to “five (5) years from the date of the commencement of work in Korea”. However, for foreign employees who began working in Korea prior to 2013, the special tax rate will continue to be applicable until the end of 2014, even if five years have lapsed from the date of their commencement of work in Korea. The Amended STTCA excludes from the benefit of the special tax rate “employees who are in a special relationship (e.g., a relationship of management control or family/relatives) with companies employing them”. However, the special tax rate is applicable to a person in a special relationship with a foreign-invested company entitled to tax reduction or exemption (Article 18-2 of the Amended STTCA). The purpose of the amended provision is to prevent unreasonably excessive tax incentives for foreign employees.

The amended provision is applicable to income arising on or after January 1, 2014.

2. Abolition of Tax Reduction or Exemption on Dividends Received by Foreign Investors from Foreign-Invested Companies

The Amended STTCA abolishes the reduction or exemption of corporate tax or income tax on dividends received by foreign investors from foreign-invested companies entitled to tax reduction or exemption. Prior to abolishment, the relevant provisions permitted reduction or exemption of 100% or 50% of corporate tax or income tax on dividends, while the foreign-invested companies concerned were entitled to reduction or exemption of 100% or 50% of the corporate tax. The provision was abolished to prevent unreasonably excessive tax incentives for foreign investment (Article 121-2(3) of the Amended STTCA).

The amended provision is applicable to tax reduction or exemption for which an application is filed on or after January 1, 2014.

3. Tightening of Provisions on Information Collection on Overseas Income/Property

The International Tax Coordination Act was amended on January 1, 2014 by Act No. 12164 (the “Amended ITCA”) and refines and tightens up provisions on the collection of information on overseas income/property, in order to improve the efficiency of information collection on overseas taxation to prevent offshore tax evasion. For details, please refer to the following:

(1) Tightening of Regulations on Failure to Report Overseas Financial Accounts

The Amended ICTA inserts “a failure to meet the demand of taxation authorities for explanation about the source of non-reported or under-reported amounts” as a reason for the imposition of 10% fines for negligence or nonperformance of the obligation to report overseas financial accounts by Korean residents and domestic corporations (Articles 34-3 and 35 of the Amended ICTA).

The amended provisions are applicable to overseas financial accounts held by Korean residents as of 2014 which are to be reported in 2015.

(2) Expanded Scope of Exchange of Taxation-related Financial Information between Tax Treaty Countries

The Amended ICTA (i) adds “a group of not less than two (2) persons whose personal information cannot be specified” to the list of entities to which a request may be made for the exchange of information, (ii) adds “Korean residents and domestic corporations” to those subject to regular exchange of information, and (iii) provides that a fine not exceeding 30 million won shall be imposed for “negligence” on any financial institution which fails to respond to a request for the supply of information (Articles 31 and 31-3 of the Amended ICTA).

The amended provisions are applicable to financial information exchanged with a treaty-contracting country on or after January 1, 2014.

(3) Exclusion of Tax Reduction or Exemption on Investments of Foreigners from Non-Tax Treaty Countries

The Amended STTCA adds “investment of foreigners from a country which has not entered into a tax treaty with Korea” as a subject for which the reduction or exemption of income tax and

corporate tax on foreign investment is excluded in order to prevent the abuse of the tax reduction/exemption system for foreign-invested companies by a Korean national (Article 121-2(11) of the Amended STTCA). Moreover, the enforcement rules of the Amended STTCA will be amended to add “a detailed statement of actual stockholders of the foreign corporation (foreign investor)” as a document required to be submitted when an application for tax reduction or exemption is filed.

The amended provisions are applicable to tax reduction or exemption for which an application is filed on or after January 1, 2015 (provided, however, that the provision on the obligation to submit a detailed statement of actual stockholders of the foreign corporation is applicable to tax reduction or exemption for which an application is filed on or after January 1, 2014).

(4) Tightening of Provisions on Submission of Materials on Overseas Subsidiaries

The Corporate Tax Act and the Income Tax Act were each amended on January 1, 2014 by Act No. 12166 (the “Amended CTA”) and Act No. 12169, respectively (the “Amended ITA”, and collectively, the “Amended CTA/ITA”). The Amended CTA/ITA (i) add “materials on loss-incurring transactions between domestic corporations and overseas subsidiaries,” to those required to be submitted when domestic corporations make an overseas direct investment, (ii) expand the scope of domestic corporations obligated to submit materials on their overseas subsidiaries from those holding at least 50% of the shares in their overseas subsidiaries to those holding at least 10%, with fines to be imposed for negligence or failure to submit such materials, and (iii) tighten the provision on the imposition of such fines for negligence by changing the reason for the imposition of fines from a failure to meet the demand of tax authorities for the submission of materials to “a failure to submit materials”. The Amended CTA/ITA further provide that ‘individuals’ on whom such fines for negligence (as described above) had not been imposed shall now be included in those subject to the imposition of fines for negligence (Articles 121-2 and 121-3 of the Amended CTA, and Articles 165-2 and 165-3 of the Amended ITA).

The amended provisions are applicable from the fiscal year beginning on or after January 1, 2014 (corporations) or to income arising in a fiscal year including January 1, 2014 (individuals).

4. Tightening of Provisions on Obligation to Submit Relevant Materials for Calculation of Reserved Income of Specified Foreign Corporations

The Amended CTA/ITA provide that if domestic corporations fail to submit relevant materials for the calculation of reserved income of a specified foreign corporation, an additional tax equivalent to 0.5% of such reserved income up to KRW 100 million (for small-and mid-sized domestic corporations, KRW 50 million) shall be imposed on the domestic corporations concerned (Article 76(13) of the Amended CTA and Article 81(14) of the Amended ITA).

The amended provisions are applicable to income arising in a fiscal year beginning on or after January 1, 2014.

If you have any questions regarding the above, please contact the authors below.

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