

# Proposed Tax Law Amendments in 2014 – International Taxation

We summarize below the major amendments to Korean tax laws contained in the proposed draft announced by the Ministry of Strategy and Finance of Korea on August 6, 2014, which are relevant to international taxation.

## 1. Tightening of Criteria to Qualify as a Resident

The proposed amendments to the Income Tax Law and the Inheritance Tax and Gift Tax Law tighten the criteria for determining who qualifies as a resident in order to prevent tax evasion by disguising a foreign resident. Listed below are major points of the proposed amendments. (Article 1-2 of the Income Tax Law and Article 1 of the Inheritance Tax and Gift Tax Law)

Current	Proposed Amendments
<p>■ Criteria for determination of resident</p> <ul style="list-style-type: none"> <li>• (Principle)               <ul style="list-style-type: none"> <li>- A person who holds his domicile in Korea</li> <li>- A person who has held his temporary domicile in Korea for 1 year or more</li> </ul> </li> <li>• (Exceptions) A person who falls under any of the following cases shall be deemed to have his address in Korea:</li> </ul>	<ul style="list-style-type: none"> <li>- Same as in the left column</li> <li>- A person who has held his temporary domicile in Korea for 183 days or more</li> </ul>

<ul style="list-style-type: none"> <li>- if such person has an occupation which requires him to dwell in Korea for 1 year or longer; or</li> <li>- if such person is considered to dwell in Korea for 1 year or longer in view of his family, occupation and property status.</li> <li>- In case where a person having a residence in Korea returns to Korea after his departure from Korea, and where the purpose of his departure is deemed to be clearly of a temporary nature, the relevant period of his stay outside of Korea shall be regarded as the period of having a dwelling place in Korea.</li> </ul>	<ul style="list-style-type: none"> <li>- if such person has an occupation which requires him to dwell in Korea for 183 days or longer; or</li> <li>- if such person is considered to dwell in Korea for 183 days or longer in view of his family, occupation and property status.</li> <li>- The proposed amendment lists, as examples, purposes of departure from Korea which are clearly of a temporary nature: tourism, treatment for diseases, business trip, training, etc.</li> </ul> <p>* The 183-day period (6 months) is applied by most of the OECD member countries, such as the United States, the United Kingdom and Germany.</p>
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The proposed amendments will be applicable to income arising on or after January 1, 2015.

## 2. Heightened Enforcement against Tax Evasion of Multinational Companies

The proposed amendments to the International Tax Coordination Law (“ITCL”) tighten the criteria for thin capitalization rules and refine taxation rules on reserved earnings of controlled foreign corporations (CFC) located in countries with low tax rates. Such provisions are designed to prevent multinational companies operating in Korea from deducting excessive interest expenses and ensure more stringent taxation on retained earnings reserved in a foreign subsidiary located in a country with low tax rates. The major points of the proposed amendments are as follows:

Subject	Proposed Amendments
Tightening of criteria for thin capitalization rules (Article 14, <i>et seq.</i> of the ITCL)	<ul style="list-style-type: none"> <li>• Criteria for application of thin capitalization rules               <ul style="list-style-type: none"> <li>- Inclusion of loans from anyone who is a relative of a foreign controlling shareholder of the relevant domestic company.</li> </ul> </li> <li>• Multiple               <ul style="list-style-type: none"> <li>- General type of business: 3 times → 2 times</li> <li>- Financial business: 6 times (unchanged)</li> </ul> </li> <li>• The above amendment will be applicable from the taxable year commencing on or after January 1, 2015.</li> </ul>

Refinement of taxation on reserved income of controlled foreign corporations (CFC) (Article 17 of the ITCL)	<ul style="list-style-type: none"> <li>• Criteria for determination of control relationship               <ul style="list-style-type: none"> <li>- Inclusion of the shares in a foreign corporation which are owned by a 'resident'* who is a relative of the relevant Korean national.</li> <li>* The current provision includes the shares in a foreign corporation which are owned by a 'non-resident', rather than a 'resident'.</li> </ul> </li> <li>• The above amendment will be applicable from the taxable year commencing on or after January 1, 2015.</li> </ul>
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### 3. Extension of Application Period of Tax Benefits for Foreign Workers

The proposed amendments to the Special Tax Treatment Control Law ("STTCL") abolish or extend the application period of certain tax benefits for foreign workers, in order to induce foreign investment generating high added value and thereby invigorating growth potential. Major details of the proposed amendments are as follows (Article 18-2 of the STTCL).

Current	Proposed Amendments
<ul style="list-style-type: none"> <li>■ Tax Benefits for Foreign Workers</li> <li>• Details of tax benefits               <ul style="list-style-type: none"> <li>- Application of a flat tax rate of 17% for five (5) years after the commencement date of work in Korea.</li> </ul> </li> <li>• Applicable until December 31, 2014</li> </ul>	<ul style="list-style-type: none"> <li>• Same as in the left column</li> <li>• Abolition and extension of application period               <ul style="list-style-type: none"> <li>- For companies with certification for headquarters*: Abolition of application period</li> <li>- For other companies: December 31, 2016 (extension of two years).</li> </ul> </li> <li>* To be regulated in the Enforcement Decree of the STTCL: Performing activities of support for and coordination of core functions (business strategy, personnel management, R&amp;D, etc.) of global companies</li> </ul>

The proposed amendments above will apply to foreign workers who will first provide services on or after January 1, 2015; provided, however, that the proposed amendments will also apply to those who provide services for companies which receive certification for headquarters on or after January 1, 2015 or after.

## 4. Reduction of Scope of Foreign Engineers Eligible for Exemption of Income Tax and Extension of Application Period

In order to support foreign investments generating high added value, the proposed amendments to the STTCL extend the exemption period for income tax on foreign engineers, while reducing the scope of eligible foreign engineers. Major details are set forth in the table below (Article 18 of the STTCL)

Current	Proposed Amendments
<ul style="list-style-type: none"> <li>■ Exemption of income tax for foreign engineers</li> <li>• Eligible persons: Foreign engineers who provide services in Korea (researchers, professional technicians, etc.)</li> <li>• Exemption benefit: Reduction of income tax by 50% for 2 years</li> <li>• Application period: Until December 31, 2014</li> </ul>	<ul style="list-style-type: none"> <li>■ Reduction of the scope of eligible persons and extension of application period</li> <li>• Eligible persons: Reduced to foreign engineers, etc. working at R&amp;D centers of foreign invested companies</li> <li>• Exemption benefit: Same as in the left column</li> <li>• Application period: Until December 31, 2018</li> </ul>

The proposed amendments will apply to services provided on or after January 1, 2015; provided, however, that those who are entitled to exemption of income tax under the provisions of the current STTCL will remain covered by such provisions.

## 5. Introduction of Advance Coordination System between Taxable Prices for National Taxes and Customs Duties

Scheduled to be newly introduced are Article 6-3 (Application for Advance Coordination of the Calculation Method of Arms-Length Price for National Taxes and Determination Method of Dutiable Value for Customs Duties) of the International Tax Coordination Law and Article 37-2 (Advance Coordination of International Transaction Value) of the Customs Law. Major details are set forth in the table below:

Subject	Proposed Amendments
Introduction of advance coordination between taxable values	<ul style="list-style-type: none"><li>• Timing for application: An application for advance coordination can be made at the same time as an application for unilateral Advance Pricing Agreement (APA) in respect of arms-length prices for domestic taxes or an application for Advance Customs Valuation Arrangement (ACVA) for customs duties.</li><li>• Case subject to application: In cases where the calculation methods of taxable values for national taxes and customs duties are similar</li><li>• Method of coordination: The method for evaluation of taxable prices and an appropriate scope shall be decided in consultation between the Commissioner of the National Tax Service and the Commissioner of the Korea Customs Service.</li></ul>

The proposed amendment will apply to advance coordination applied for on or after January 1, 2015.

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

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