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Landmark Supreme Court Decision on Royalties for Patents Unregistered in Korea

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1. Overview

On September 18, 2025, the Supreme Court issued an en banc decision holding that royalties paid to foreign corporations for patents registered abroad but not in Korea may nonetheless constitute Korean-source income (Supreme Court Decision 2021Du59908, en banc, Sept. 18, 2025). The core issue in this judgment concerned the definition of "use" of a patent under the Korea–U.S. Tax Treaty ("Treaty"), which is the decisive criterion for determining the source of royalty income. For more than 30 years, the Supreme Court interpreted the "use" of a patent narrowly, adhering to the territoriality principle that patents may be executed only within the country of registration. Under this interpretation, "use" of patents was limited to the legal execution of patents themselves within the jurisdiction of registration, and the Court declined to recognize the concept of "use" for patents that are unregistered in Korea. As a result, the Supreme Court has consistently maintained the position that royalties for patents that are not registered in Korea do not constitute Korean source income.

However, the Supreme Court, through this en banc decision, ruled that **the 'use' of a patent must be interpreted to mean the use of the manufacturing method, technology or information which is the subject of the patent (hereinafter 'patented technology'). Furthermore, if the patent is not registered in Korea but the technology which is the subject of the patent of is used within Korea, the royalty income received as compensation for such use constitutes Korean source income.** This decision completely reverses a long-standing position that had been maintained by the Supreme Court.

This Supreme Court decision is expected to have a significant impact on international taxation and patent practice going forward. Below, we will analyze its key points and implications in detail.

2. Summary of the Supreme Court's En Banc Decision

A. Background

Plaintiff, a Korean company engaged in the manufacture and sale of semiconductor devices, was sued for patent infringement in the United States around June 2011 by a U.S. non-practicing patent entity ("USCo").

In December 2013, Plaintiff entered into a patent license agreement with USCo, thereby settling the pending litigation on the condition that Plaintiff pay royalties for 40 patents registered in the United States. The agreement granted Plaintiff a license with a worldwide territorial scope. Pursuant to this agreement, Plaintiff remitted USCo royalties in the amount of USD 1.6 million in 2014 and paid the withholding tax on the royalty payment to Korean tax authorities.

Subsequently, Plaintiff filed a claim for a refund of the withholding tax, contending that the royalty payment represented compensation for patents that are not registered in Korea and therefore did not constitute Korean-source income subject to withholding. When the tax authority denied the claim, Plaintiff brought suit seeking revocation of the decision.

B. The Supreme Court's Previous Position

Historically, the Supreme Court held that based on the territoriality principle of patents, the 'use' of a patent could only occur within the country where the patent was registered. On this basis, the Court deemed it inconceivable that a patent that is not registered in Korea could be "used" in Korea or that royalties could be paid for such use. Accordingly, prior case law uniformly concluded that royalties for patents not registered in Korea did not constitute Korean-source income subject to withholding tax.

C. Summary of the Supreme Court En Banc Decision

Article 14(4)(a) of the Treaty[1] defines as royalties all payments of any kind received as consideration for the use of a patent or for the right to use it,[2] while Article 6(3) provides that royalties for the use of a patent should be treated as income arising in a Contracting State only when they are paid in that Contracting State as consideration for the use of the patent or for the right to use it.[3] Furthermore, Article 2(2) provides that "any other term used in this Convention and not defined in this Convention shall, unless the context otherwise requires, have the meaning which it has under the laws of the Contracting State whose tax is being determined."[4]

Meanwhile, Article 93(8) of the former Corporate Income Tax Act ("CITA")(as amended prior to December 15, 2015, Act No. 13555; the same applies hereinafter) defines Korean-source royalty income and states in its proviso that "**where a convention for avoiding double taxation on income stipulates that whether such income constitutes domestic -source income shall be determined based on the place of use, remuneration for rights that are used abroad should not be deemed as Korean-source income, regardless of whether it is paid for in Korea.** In such cases, rights requiring registration for their exercise, such as patent rights, utility model rights, trademark rights, and design rights, shall be deemed to be used in Korea if such **rights are registered abroad but used in Korea for manufacturing, sales, etc. regardless of whether they are registered in Korea.**"[5]

The Supreme Court first held that the Treaty constitutes a "convention for avoiding double taxation on income" as defined in Article 93(8) of the former CITA, which determines the source country of royalty income based on the place of use. Since the Treaty does not separately define the meaning of "use," the Court presupposed that the meaning of 'use' must be interpreted in accordance with the "law of the Contracting State in which the tax is determined" pursuant to Article 2(2) of the Treaty, namely the CITA of Korea. It then held that the latter part of the proviso to Article 93(8) of the

former CITA stipulating that “where a patent that is not registered in Korea but used in Korea for the manufacture and sales,” shall be interpreted such that it does not mean the use of the patent itself but shall mean **the use of the technology that is the subject of that patent,** regardless of whether it is registered in Korea .”Therefore, if the patented technology of an unregistered patent was used in Korea, the royalty income received as compensation for such use constitutes Korean source income. Furthermore, the Court held that its prior decisions—which held that “under the territoriality principle of patent rights, the domestic use of an unregistered patent or the payment of compensation for such use cannot be conceptualized, and thus the latter part of the proviso to Article 93(8) of the former CITA contradicts the context of the Treaty”— was erroneous.

The Supreme Court, applying the above legal principle, overturned the lower court's judgment, which had concluded that royalties paid by Plaintiff to USCo did not constitute Korean-source income solely because they related to a patent that is unregistered in Korea, without examining whether the patented technology was actually used in Korea for manufacturing, sales, etc. The Supreme Court remanded the case to the lower court.

3. Implications and Considerations

As a result of this decision, the payment of royalties for the use of patents that are unregistered in Korea will be subject to withholding tax if the technologies which are the subject of the patents are used in Korea as such payments constitute Korean-source income. Consequently, Korean companies making royalty payments to foreign companies will be obligated to pay withholding taxes on such royalty payments to Korean tax authorities.

Going forward, the careful drafting of license agreements will take on heightened importance. The scope of the licensed subject matter, the territorial reach of the license, and the method of calculating royalties will serve as critical factors in determining the applicability and extent of Korean corporate income tax liability. Accordingly, when entering into future license arrangements, thorough legal review of relevant provisions is highly recommended as a means for mitigating prospective tax risks.

In particular, where a single contract covers both domestic and international use of patented technology, a key challenge will be to reasonably allocate the portion of total royalties attributable to Korean-source income and to substantiate that allocation. As highlighted in both the dissenting opinion and the majority’s supplementary opinion in this ruling, such allocation poses considerable practical difficulties. Accordingly, it is advisable to seek expert guidance to clearly identify and address these issues.

The Supreme Court’s ruling should be understood as reflecting policy considerations that extend beyond its explicit legal reasoning. It may prompt a comprehensive reassessment of pending cases involving similar issues and could also reinforce the tax authorities’ position in international tax matters more broadly. Accordingly, companies affected by this development should proactively formulate response strategies in consultation with experts.

Finally, relying on the previous Supreme Court rulings, a foreign licensor might have received a full amount of royalty without the Korean withholding tax. In this event, the licensor might have to brace for a litigation or arbitration from the licensee seeking the return of the tax portion. The issue of course depends upon the language of the license contract,

and licensors in this situation must carefully review the contract.

[1] The Convention between the United States of America and the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and the Encouragement of International Trade and Investment

[2] **Article 14 (Royalties)**

(4) The term "royalties" as used in this Article means

(a) Payment of any kind made as consideration for the use of, or the right to use, copyrights of literary, artistic, or scientific works, copyrights of motion picture films or films or tapes used for radio or television broadcasting, patents, designs, models, plans, secret processes or formulate, trademarks, or other like property or rights, or knowledge, experience, or skill (know-how), or ships or aircraft (but only if the lessor is a person not engaged in the operation in international traffic of ships or aircraft)

[3] **Article 6 (Source of Income)**

(3) Royalties described in paragraph (4) of Article 14 (Royalties) for the use of, or the right to use, property (other than as provided in paragraph (5) with respect to ships or aircraft) described in such paragraph shall be treated as income from sources within one of the Contracting States only if paid for the use of, or the right to use, such property within that Contracting State.

[4] **Article 2 (General Definitions)**

(2) Any other term used in this Convention and not defined in this Convention shall, unless the context otherwise requires, have the meaning which it has under the laws of the Contracting State whose tax is being determined. Notwithstanding the preceding sentence, if the meaning of such a term under the laws of one Contracting State is different from the meaning of the term under the laws of one Contracting State is different from the meaning of the term under the laws of the other Contracting State, or if the meaning of such a term is not readily determinable under the laws of one of the Contracting States, the competent authorities of the Contracting States may, in order to prevent double taxation or to further any other purpose of this Convention, establish a common meaning of the term for the purposes of this Convention.

[5] **Former CITA** (as amended prior to 15 December 2015 by Act No. 13555)

Article 93 (Domestic Source Income) The domestic source income of a foreign corporation shall be classified as follows: 8. Income arising from the use within Korea of any of the rights, assets or information (hereinafter referred to in this subparagraph as "rights, etc.") falling under any of the following subparagraphs, or from the payment within Korea of consideration for such use, and from the transfer of such rights, etc. However, where a double taxation convention on income determines whether such income constitutes domestic-source income based on the place of use, remuneration for rights, etc., used abroad shall not be deemed domestic-source income, regardless of whether it is paid domestically. In such cases, rights requiring registration for their exercise, such as patent rights, utility model rights, trademark rights, and design rights (hereinafter referred to as "patent rights etc." in this subparagraph), shall be deemed to have been used domestically, irrespective of whether they are registered domestically, if the relevant patent rights etc. are registered abroad and used for manufacturing, sales, etc., domestically.

a. Copyrights in academic or artistic works (including motion picture films), patent rights, trademark rights, designs, models, drawings, secret formulas or processes, films and tapes for radio or television broadcasting, and other similar assets or rights. I. Information or know-how relating to industrial, commercial or scientific knowledge or experience

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