

Newsletter

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This newsletter is prepared and issued by Hanul LLC in Seoul, Korea on a bi-monthly basis and intended to provide foreign investors with an update on tax law changes in South Korea and other related subjects of special interests to foreign investors. The information provided herein should not form a basis of any decision as to a particular course of action, nor should it be relied upon as a substitute for a detailed advice in individual cases.

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■ Proposed South Korean Tax Law Changes in 2021

On July 22, 2020, the Ministry of Economy and Finance (MOEF) of Korea announced the government tax reform proposals to be implemented from 2021. The proposed tax law changes will be finalized after the National Assembly passes the bill. We summarized the major proposed tax law changes in 2021 to keep you updated as follows.

<International Taxation>

● Expansion of the scope of Overseas Specially Related Party (“OSRP”)

Under the proposal, when determining whether a third party is in an overseas special relationship by directly or indirectly owning at least 50% of the voting shares of both transaction parties, the calculation of the shareholding ratio of the third party also includes shares directly or indirectly owned by a relative under the International Tax Coordination Law of Korea (“ITCL”).

As the shares directly or indirectly owned by the relatives shall be included in the overseas special relationship, the transactions subject to the transfer pricing taxation may also be expanded, so care must be taken to ensure that the transactions are not omitted from the list of the OSRP transactions when preparing the Master File and Local File to meet the BEPS requirements. It shall be effective from the tax year beginning on or after January 1, 2021.

● Extension of retrospective application period of Advance Pricing Agreement (“APA”)

Currently, it shall not be possible to apply APA for some of the tax years within the limitation period for tax assessment even if an application for APA is intended to be applied retrospectively.

Under the proposal, the period of retrospective application of bilateral APA through a mutual agreement shall be extended from five years to seven years in accordance with the limitation period for tax assessment on offshore transactions, and the period of retrospective application of unilateral APA shall be extended from three years to five years in accordance with the period of claim.

It shall be applied to the APA applied for the first time on or after January 1, 2021. This amendment is expected to increase the protection of the rights of taxpayers applying for retrospective APA application.

● Extension of deadline for submitting the Schedule of International Transactions (“SIT”)

Under the proposal, the deadline for submitting the SIT and the Summarized Profit and Loss Statement of OSRP (“SPLS”) is extended from the reporting due date of the tax base under the Corporate Income Tax Law (i.e., three months after the end of the tax year) to six months after the end of the tax year.

It shall be applied to the SIT and SPLS submitted on or after January 1, 2021.

● Extension of foreign tax credit carryforward and deduction for unused foreign tax credit

Currently, a company can claim a foreign tax credit for foreign taxes paid or to be paid in relation to its foreign source income for five years if the claimed foreign tax credit is in excess of tax limit.

To strengthen a relief for double taxation of foreign source income, under the proposal, the five-year carryforward period would be extended to ten years.

In addition, for foreign tax credits which are not used during the carryforward period, taxpayers would be allowed to deduct the unused tax credit amount from taxable income for the year immediately following the year in which the carryforward period ends. The proposed change would apply to the unused foreign tax credit whose existing carryforward period (i.e., five years) would not lapse upon income tax return filing on or after January 1, 2021.

<Other Items of Interest>

- **Increased threshold for deductible small entertainment expenses without qualified supporting document**

Currently, all entertainment expenses over KRW 10,000 threshold should be substantiated by valid supporting documents to be tax deductible for corporate tax purposes within tax limit allowed (an exception applies for cash gifts for congratulation/condolence to business partners/customers, which do not need to be supported by valid supporting receipts if the amount is KRW 200,000 or less).

Under the proposal, the threshold of KRW 10,000 shall be raised to KRW 30,000, which would apply for payment from January 1, 2021.

- **Clarification of place of supply for electronic services**

Currently, the place of supply of service is generally the place where the service is performed or where the rights, facilities or other goods, etc. are used. For the international transportation services supplied by a Korean nonresident or foreign (non-Korean) corporation, the place where passengers are on board or freights are loaded would constitute the place of supply.

However, there is no specific provision concerning the place of supply of electronic services. To clarify the place of supply for electronic services, the proposal stipulates that the place of supply of electronic services would be the premise or business place, the address or the place of residence of a person who is supplied with electronic services. It would apply to electronic services supplied on or after January 1, 2021.

- **Increased individual income tax rate**

Under the proposal, the highest individual income tax rate bracket shall be established and the highest tax rate shall be 49.5% (including 10% local surtax). The proposed change would be effective for income earned from January 1, 2021 (in millions or billions of Korean Won).

Current		Proposed Changes	
Taxable income	Tax rate	Taxable income	Tax rate
KRW 12 mil or less	6.6%	Same as left	Same as left
KRW 12 mil ~ KRW 46 mil	16.5%	Same as left	Same as left
KRW 46 mil ~ KRW 88 mil	26.4%	Same as left	Same as left
KRW 88 mil ~ KRW 150 mil	38.5%	Same as left	Same as left
KRW 150 mil ~ KRW 300 mil	41.8%	Same as left	Same as left
KRW 300 mil ~ KRW 500 mil	44%	Same as left	Same as left
Exceeding KRW 500 mil	46.2%	KRW 500 ~ KRW 1 bil	46.2%
		Exceeding KRW 1 bil	49.5%

■ COVID-19 Update: Introduction of new re-entry permit and medical certificate submission requirement in Korea

The South Korean government implemented the new requirements involving re-entry permit and medical certificate submission for foreigners effective from June 1, 2020 to protect the health and safety of its citizens and foreigners staying in South Korea in response to the global spread of COVID-19, which can be summarized as below.

- (1) Registered aliens (regardless of their nationality) seeking re-entry into South Korea after they travel outside of South Korea on or after of June 1, 2020, an Application for Re-entry Permit has to be submitted at the airport at departure. Re-entry will be restricted if a foreigner leaves South Korea without obtaining a re-entry permit in advance and his/her alien registration card will be revoked automatically if he/she does not apply for re-entry permit at their departure.
- (2) **A diagnosis report** issued by a local medical institute must be presented when boarding, and submitted to the Korean immigration authorities, which is issued within 2 business days (excluding holidays) before the departure date. Those without a written diagnosis report are not permitted to re-enter South Korea. The following important note shall be included on "Diagnosis Report".
 - A diagnosis report must be written either in Korean or English and be issued by an authorized local medical institute. However, under exceptional circumstances, a diagnosis report written in languages other than English or Korean, can be accepted when submitted with a full English or Korean translation with 'translation certificate' (notarization for the translation is NOT required).
 - It must include the date of examination (valid only when examined within 48 hours in advance of departure date), and the presence or absence of fever, cough, chills, headache, difficulty of breathing, muscle pain, and pulmonary symptoms (X-ray scans are not required), and must be signed by a medical examiner (it does not have to include a COVID-19 test result).

■ Korean Labor Law Update

● Change in the expiration date of annual leave for the new hire

Under Article 60 of the Labor Standards Act (LSA) of Korea, employers shall grant its employees 15 days of paid annual leave if the employees fulfilled at least 80% attendance during one (1) year. With respect to employees who have worked for less than one (1) year, employers shall grant one (1) day of paid leave for each completed month of service. Before amendment of the LSA, however, the paid leave days used during the first year were able to be deducted from the 15 days to be granted in the second year (Article 60, Paragraph 3).

Effective from May 29, 2018, the paid leave days earned and used in the first year are not deducted from the 15 days to be granted in the second year (Articles 60, Paragraph 3 was deleted). Employees are granted one (1) day of paid leave for each completed month of service in their first year and separately, employees should be granted 15 days in the second year if fulfilled 80% attendance requirement.

Before revision, the paid leave days earned and unused in the first year (maximum 11 days) may be used for 1 year from the date the paid leave days earned. Effective from March 31, 2020, however, the unused paid leave days earned in the first year can be used for 1 year from the employment date.

This new rule shall be effective for the annual leave earned after March 31, 2020.

■ Special Tips for Companies Having Foreign (non-Korean) Employees

● At hire/initial payroll setup

Under the Individual Income Tax Law (“IITL”), the individual income tax liabilities of foreigner workers (excluding daily employed workers) on earned income from the rendering of his/her services to companies in Korea including foreign invested companies can be finalized by applying the 19% flat income tax rate (excluding local income tax by 10% of the income tax) on gross earned income for the first five (5) year period notwithstanding Article 55 (1) of the IITL (Article 18-2, Special Tax Treatment Control Law of Korea; STTCL). For foreigners who have already been working in Korea as at Jan 1, 2014, however, the 19% flat income tax rate application was allowed only up to December 31, 2018, and as such, the progressive tax rate should apply from Jan 1, 2019 and onward for the foreigners concerned.

When the flat 19% tax rate is applied, provisions concerning income taxation, such as tax exemption (non-taxable income), deduction, reduction or exemption, and tax credit allowed under the IITL as well as this STTCL shall not be applicable to the foreigners concerned. At the year-end settlement in February after each calendar year-end, annual settlement calculations under both the 19% flat rate and the progressive tax rate scheme will be simulated, and more favorable scheme based on the comparison will be applied for the foreign employees.

The employer (withholding agent) should submit the flat tax rate application form to the competent tax office by the 10th day of the following month.

● Statutory social insurance participation obligation by visa type

Statutory social insurance participation obligation may vary depending on the visa type, which can be summarized by most common visa types of foreigners in Korea as below:

Visa type		Medical insurance	National pension	Unemployment insurance	Industrial accident compensation insurance
D-2	Student 유학	statutorily required	NOT statutorily required	NOT statutorily required	statutorily required
D-7	Expatriate 주재원		statutorily required	may elect to participate in the insurance at their discretion.	
D-8	Investment 기업투자자				
F-4	Overseas Korean 재외동포				
D-10	Employment 구직		NOT statutorily required		

Unless the foreign (non-Korean) employee concerned is eligible for waiver of statutory social insurances and submits waiver applications with proper supporting documents thereof required by the Korean social insurance agencies, the foreign employee shall be subject to participation in the statutory social insurance programs in Korea mandatorily.

● At permanent departure from Korea: Korean national pension refunds (lump-sum refunds)

Obligation to participate in the statutory national pension scheme in Korea and the possibility of withdrawal/refunds of contribution made into statutory national pension scheme in Korea upon permanent departure of an employee will vary depending on the employee’s nationality and the social security agreements entered into between the countries. Refunds of contribution made to statutory national pension in Korea is generally based on the “principle of reciprocity”.

Please contact any of the following individuals with any inquiries or comments.

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