

# 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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## ■ Korean Tax Law Changes in 2020

Proposed tax law changes announced by the Korean government in July 2019 were approved by the National Assembly in December 2019 with several amendments and additions. We summarized below some of the major tax law changes for 2020 to keep you updated. Most of the tax law changes we discussed below came into force from the fiscal year starting, or income earned, on or after January 1, 2020 unless indicated otherwise.

### I. Corporate Income Tax Law (CITL)

#### ● Taxation on royalties for patents registered outside of Korea

While income derived from patent use is generally treated as royalties, the term ‘use’ is not clearly defined under some of the tax treaties in effect. The tax law changes have stipulated that “consideration for the use of, or the right to use other like property or rights” in the article for royalties in the tax treaty includes any payments for manufacturing know-how, technologies, or information contained in patents which are registered outside of Korea that are used in manufacturing or production activities in Korea. The revised provision is applied to payments made on or after January 1, 2020.

And also, in order to tax on compensation to overseas patent holder for infringement of a patent registered outside of Korea, such compensation would be classified as ‘other income’ which shall be subject to 16.5% income tax withholding (including 10% surtax) at source of payment. The revised provision is applied to payments made on or after January 1, 2020.

However, as there are previous cases in which the Korean Supreme Court judged that payments made for the use of patents registered outside of Korea do not constitute Korean-source income under the Korea-US tax treaty, the concerned patent holders may want to wait and see next court cases.

#### ● Increased tax limit of entertainment expenses

Where entertainment expenses exceed the tax limit which is calculated by the law, the entertainment expenses in excess of the tax limit shall not be allowed as deductible expense.

Under the tax law changes, the tax limit ((a) + (b)) of entertainment expenses has increased as given below. It is effective from the tax year beginning on or after January 1, 2020.

Tax limit amount: (a) + (b)	Criteria	Before amendment	After amendment
(a) Basic amount	SME*	KRW 12,000,000	KRW 12,000,000
	Non-SME	KRW 24,000,000	<b>KRW 36,000,000</b>
(b) Additional amount based on sales amount	Not more than KRW 10 billion	0.2%	<b>0.3%</b>
	KRW 10 - 50 billion	KRW 20,000,000 + 0.1% of sales in excess of KRW 10 billion	KRW 30,000,000 + <b>0.2%</b> of sales in excess of KRW 10 billion
	Over KRW 50 billion won	KRW 60,000,000 + 0.03% of sales in excess of KRW 50 billion	KRW 110,000,000 + 0.03% of sales in excess of KRW 50 billion

\*SME represents small and medium enterprises.

- **Increased threshold for deductible business car expense without car mileage log**

Previously, the entire amount of expenses incurred for the use of business cars were deductible unless they exceed the threshold of Won 10 million per annum where a mileage log of the business car is not prepared.

Under the tax law changes, the threshold for deductible business car expense without car mileage log has increased from Won 10 million to Won 15 million. The revised provision is effective from the tax year beginning on or after January 1, 2020.

## II. Individual Income Tax Law (IITL)

- **Totalization of ‘net capital gains’ from transfer of foreign (non-Korean) shares**

Previously, capital gains and losses arising from transfer of taxable shares had been allowed to be offset dividing domestic shares and overseas shares. And the deduction for capital gains was Won 2.5 million per annum for each division.

Under the tax law changes, a taxpayer shall totalize the net capital gains from the transfer of domestic shares and overseas shares. In addition, the deduction of Won 2.5 million is applied to the totalized net capital gains. The revised provision is applied to the transfer made on or after January 1, 2020.

## III. Others

- **Strengthened taxpayer’s burden of proof regarding abusive transaction**

Previously, burden of proof regarding abusive transaction was not specifically stated in the International Tax Coordination Law (ITCL) of Korea. Therefore, if the Korean tax authority applied the “substance over form” principle to the taxpayer who enjoyed tax treaty benefits unduly through a cross border transaction which was indirectly made via a third party or two or more transactions, the burden of proof regarding such abusive transaction was on the Korean tax authority who challenged the abusive transaction.

Under the tax law changes, when a transaction reduces the tax liability by an amount specified in the Presidential Decree of the ITCL (e.g., 50%), the burden of proof is placed on the taxpayer to prove that the transaction has a valid business purpose, without an intent of tax evasion. If the taxpayer fails to prove, the “substance over form” principle shall be applied to the transaction. This new rule is effective from the tax year beginning on or after January 1, 2020.

- **Reduction of securities transaction tax rate**

Under the tax law changes, the securities transaction tax rate will be decreased from 0.5% to 0.45% for over-the-counter transactions of listed and non-listed securities from April 1, 2020. The securities transaction tax rate on the listed securities traded in the designated stock exchange market has been lowered by 0.05% since June 3, 2019, current effective rate being 0.25% (including surtax) for the securities listed on KOSPI and KOSDAQ.

## ■ Year-End Settlement and Declaration of Payroll Withholding Taxes for 2019 (due filing by March 10, 2020)

The employer as a tax withholding agent must perform the year-end settlement of exact payroll withholding taxes for and on behalf of its employees in February of following year after each year end mandatorily as required by the IITL of Korea.

In this connection, the employer should reflect the results of year-end settlement in the February payroll of the following year accordingly. Any overpayment resulting from year-end settlement is used to offset the payroll taxes due in February of the following year and onward until fully utilized. For any underpayment resulting from the year-end settlement, the employer should withhold additionally from the February payroll and remit it to the tax office as scheduled by March 10 of the following year (by March 10, 2020 for year 2019).

For the year-end settlement processing, the employees should gather and submit supporting documents to claim tax deductions/credits.

By the year-end settlement and filing, employees having only salary income may fulfill his/her annual individual income tax reporting obligations in Korea. On the other hand, employees having other source of income exceeding certain thresholds than salary income are required to file additionally an annual individual income tax return together with tax payment on or before May 31 of the following year additionally (i.e., by June 1, 2020 for 2019 income).

## ■ Major Changes in 2019 Year-End Settlement of Payroll Withholding Taxes

### ● Addition of postnatal care center expenses to the tax credit for medical expenses

Employees having annual gross salary of less than KRW 70 Million are eligible for medical expenses tax credit up to KRW 2 Million per birth for the expenses paid to a postnatal care center.

### ● Expansion of tax credit for donation

2018		2019	
Donation amount	Tax Credit Rate	Donation amount	Tax Credit Rate
KRW 20 Million or less	15%	<b>KRW 10 Million or less</b>	<b>15%</b>
Over KRW 20 Million	30%	<b>Over KRW 10 Million</b>	<b>30%</b>

### ● Expansion of carry-over period for tax credit for donation

2018	2019
Carry-over period for donation tax credit	Expansion of carry-over period for donation tax credit
<ul style="list-style-type: none"> <li>o Carry-over period: 5 years</li> <li>o Effective for: donation made on or after January 1, 2008</li> </ul>	<ul style="list-style-type: none"> <li>o Carry-over period: <b>10 years</b></li> <li>o Effective for: donation made on or after <b>January 1, 2013</b></li> </ul>

● **Expansion of tax credit for monthly housing rent**

Previously, the tax credit for monthly housing rent was applicable only when the rented house was in the size of national housing unit defined in the Housing Act.

Under the amended Special Tax Treatment Control Law (STTCL), tax credit for monthly housing rent can also be applied for the house which is larger than the size of national housing unit (net 85m<sup>2</sup> or below) as long as the government published standard market price of the rented house is KRW 300 Million or less.

2018	2019
Tax credit for monthly housing rent <ul style="list-style-type: none"> <li>o Eligible taxpayer: employees having annual gross salary of less than KRW 70 Million</li> <li>o Eligible house: in the size of national housing unit</li> <li>o Deduction rates: 10% (12% for employees having annual gross salary of 55 Million or less)</li> <li>o Max deduction: KRW 7.5 Million</li> </ul>	Expansion of tax credit for monthly housing rent <ul style="list-style-type: none"> <li>o Same</li> <li>o Eligible house: in the size of national housing unit <b>or the standard market price of the rented house is KRW 300 Million or less</b></li> <li>o Same</li> <li>o Same</li> </ul>

● **Expansion of income deduction for interest payments on long-term mortgage loans**

2018	2019
Income deduction for interest paid on the long-term mortgage loans <ul style="list-style-type: none"> <li>o Deductible amount: KRW 3 Million ~ 18 Million</li> <li>o Eligible taxpayer: The head of household with no house or one house owned by the household</li> <li>o Eligible house: the standard market price does not exceed KRW 400 Million at the time of acquisition</li> </ul>	Income deduction for interest paid on the long-term mortgage loans <ul style="list-style-type: none"> <li>o Same</li> <li>o Same</li> <li>o Eligible house: the standard market price does not exceed <b>KRW 500 Million</b> at the time of acquisition</li> </ul>

- **Adjustment to scope of tax credit for children**

2018	2019
Children eligible for tax credit claim <ul style="list-style-type: none"> <li>o Children aged 6 or more</li> </ul>	Children eligible for tax credit claim <ul style="list-style-type: none"> <li>o Children <b>aged 7 or more</b> (including children aged younger than 7 enrolled in elementary school)</li> </ul>

- **Exclusion of amount spent in duty free shops from income deduction for amount spent on credit card**

2018	2019
The amounts excluded from income deduction for amount spent on credit card <ul style="list-style-type: none"> <li>o National health insurance premium, college tuitions, costs for merchandise coupons, monthly rental fees, etc.</li> </ul>	The amounts excluded from income deduction for amount spent on credit card <ul style="list-style-type: none"> <li>o Same</li> <li>o <b>Amounts spent in duty free shops (added)</b></li> </ul>

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