

Newsletter

July 2017

Bi-monthly Newsletter of Hanul Choongjung LLC



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This newsletter is prepared and issued by Hanul Choongjung LLC on a bi-monthly basis and intended to provide foreign investors with an update on tax law changes in 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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■ Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS)

The Korean government formally signed the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (“Multilateral Instrument”) in Paris on June 7, 2017. The Multilateral Instrument aims to transpose results from the OECD/G20 BEPS Project approved in November 2015 into bilateral tax treaties worldwide. If 68 countries including the OECD members sign the Multilateral Instrument, signatories to the instrument can efficiently update their treaties to reflect the measures, without the need to renegotiate each treaty with the counterpart jurisdictions. It is expected that 45 out of 91 double tax treaties of Korea may be affected due to Korea’s signing to the Multilateral Instrument (subject to the condition that both Korea and the other contracting party of the double tax treaty have ratification from the National Assembly and submit ratification instrument to the Depository of the OECD). Currently, although the Korean government signed the Multilateral Instrument, the Korean government deferred adoption of most of the articles of the Multilateral Instrument while adopting Articles 6, 7, 16, and 17. The Multilateral Instrument is expected to have the following effects among others:

Prevention of treaty abuse (Article 7): The Multilateral Instrument added a provision on the principal purpose test and limitation on treaty benefits. This provision would not grant a treaty benefit (such as non-taxation or a lower tax rate) in respect of income or capital if it is reasonable to conclude that obtaining the treaty benefit was one of the principal purposes of an arrangement or a transaction of a multinational company. This is expected to help prevent tax avoidance by misusing tax treaties. Please note that the Korean government’s provisional position is to adopt a principal purpose test only.

Modified procedures for resolution of cross-border tax disputes (Article 16): The Multilateral Instrument modifies the procedures for resolving cross-border tax disputes so that a taxpayer may file a protest against certain tax assessments with the tax authorities in both contracting parties to a tax treaty. Before the Multilateral Instrument, it can only be filed with the tax authorities in the taxpayer’s country of residence. The instrument is expected to help resolve cross-border tax disputes more quickly and strengthen taxpayers’ rights.

The Korean government plans to take follow-up measures domestically including the National Assembly’s ratification of the instrument. It will come into effect through the following two-step procedures.

- The Multilateral Instrument will take effect on the first day of the month following a three-month period after the submission of the Parliamentary ratifications to the OECD by the first five signatories to the instrument.
- The 45 bilateral treaties, which will be automatically revised by the signing of the Multilateral Instrument, will take effect on the first day of the month following a three-month period after the date on which both Korea and its other contracting parties submit their Parliamentary ratifications to the OECD.

■ Filing of the Interim Corporate Income Tax Return due by August 31, 2017

A resident corporation (and a nonresident corporation having a permanent establishment in Korea) is required to pay the interim corporate income taxes within 2 months from the end of the first six months of each fiscal year. An Interim corporate income tax return must also be filed along with the tax payment. A corporation with the December 31 calendar fiscal year-end must file the 2017 interim corporate income tax return no later than August 31, 2017.

The interim corporate income tax return can be filed using either (i) the 1/2 method (that is, paying 1/2 of the corporate tax paid in the prior year) or (ii) the book-closing method (by closing the books of accounts of the corporation for the first six-month period and calculate interim corporate tax amount based on the financial results of such first six months). When a corporation had not paid the corporate income taxes in the prior year due to tax loss or having no taxable income, only the option (ii) above should be applied. The calculation formula of interim corporate income taxes by using the book-closing method is as follows:

$$\text{Taxes payable} = [\text{taxable income for interim period} \times 12/6] \times \text{tax rates} \times 6/12$$

- (tax exemption/withholding taxes paid and taxes assessed for the interim period)

If the interim corporate income taxes payable exceeds Won 10 million, such taxes can be paid in 2 installments as below. The second installment payment is due within 1 month from the end of the filing due date (2 months in the case of defined small and medium corporation).

If total taxes payable is:		Installment payments can be broken down as below:
Over Won 10 million ~ up to 20 million	1 st installment 2 nd installment	10 million Excess over 10 million
Over Won 20 million	1 st installment 2 nd installment	50% or more of taxes payable Remaining 50% balance

- 1st installment is due together with the filing of the interim tax return within 2 months from the end of the first 6 months (i.e., August 31 for the calendar fiscal year-end).
- 2nd installment is due within 1 month from the end of the filing due date (i.e., September 30 for the calendar fiscal year-end).

Unlike the annual corporate income tax return, there is no additional local income tax payable on interim corporate income tax liability.

■ Tax Tips

● Corporate Income taxes

Corporate income taxes are assessed based on the status of the corporation. A corporation having its head office, principal office, or a place of effective management in Korea is a domestic corporation and is defined as a resident corporation. A nonresident corporation may be deemed to have a tax presence (i.e., a permanent establishment; PE) in Korea if it (1) has any fixed place of business in Korea where the business of the entity is wholly or partly carried on or (2) is represented by a dependent agent in Korea.

Exceptions to the above include fixed places used only for purchasing, storage of property not for sale, advertising, publicity, collecting or furnishing of information, or other activities that are preparatory or auxiliary to the conduct of such business. Nonresident foreign corporations without domestic places of business in Korea are generally taxed through withholding at flat rates on the gross amount of Korean source income.

A resident corporation and a nonresident corporation which has a PE in Korea are required to pay interim corporate income taxes within 2 months from the end of the first six months of the fiscal year and annual corporate income taxes within 3 months from the fiscal year-end. Annual and interim corporate tax returns must also be filed along with the tax payment.

The corporate income tax and local income tax rates are as follows.

Taxable income	Tax rates	
	Corporate Income Tax	Local Income Tax
Up to Won 200 million	10%	1%
Over Won 200 million and up to Won 20 billion	20%	2%
Over Won 20 billion	22%	2.2%

In addition to these corporate income tax rates, a local (provincial) income tax is levied at 10% on income tax liability.

● Tax Obligations with and without PE

If a foreign company has a PE, the foreign company should file tax returns and pay taxes on business income from its operation in Korea in the same manner as a domestic company. Where a foreign company does not have a PE, business profits from the Korean source earned by the foreign company are non-taxable if the home country of the foreign company has entered into a tax treaty with the Korean government, exempting such income from taxation.

Once a PE of a foreign company as the principal/supplier is deemed to exist in Korea, the profits of the foreign company, as the principal/supplier from the sale of products to Korean customers made through a dependent agent that are attributable to Korea, are subject to the Korean corporate taxes. In the case where a PE exists through a physical presence, profits from Korean sources associated with the PE will be subject to the Korean corporate taxes under the arm's length principle.

Where a PE exists, the foreign company should report, pursuant to the provisions of the Corporate Income Tax Law, the establishment of a PE within two months from the day the PE is established. The report should be filed with the district tax office which has jurisdiction over the PE along with various documents. In addition, under the Value Added Tax Law of Korea, a foreign company which carries on business through a PE in Korea should also apply for a business registration at the district tax office which has jurisdiction over its place of business within 20 days from the day of starting business. For a foreign company, the place of business is the place where it carries on its business wholly or partly in Korea.

An office including a liaison office that does not constitute a PE can apply to the district tax office for its own identification number, which is given to a tax exempt entity and is similar to a business registration of the taxable business entity. Even if an office does not apply for the number, the district tax office which has jurisdiction over the office can issue the number, at its discretion, at the time of an audit. District tax offices audit such liaison offices regularly or on occasion in order to confirm their tax status.

In addition to the foregoing, there may be separate legal requirements under the Foreign Exchange Transaction Law and the Commercial Code of Korea for the foreign companies to establish or register a PE in the form of a branch office or a subsidiary company, etc.

■ Other Tips

● Statutory Social Insurance Rates in Effect in 2017

Monthly ceiling of national pension amount was increased from KRW 390,600 to KRW 404,100 (**KRW 202,050 each** for employer and employee) **from July 1, 2017**. All other statutory social insurance rates remain unchanged in 2017 as summarized below.

Social Insurances:	Employee portion	Employer portion	Total	Remark
National Pension (NP)	4.5%	4.5%	9.0%	Won 202,050 of monthly ceiling each
National Health Insurance (HI)				
a. Health Insurance(HI)	3.06%	3.06%	6.12%	Won 2,389,860 of monthly ceiling each
b. Long-term Care Insurance for the Elderly (HI-LTCI)	6.55%	6.55%	13.10%	Assessed at 6.55% of HI premium in a. above
Employment Insurance (EI)	0.65%	0.9% ~1.5%	1.55% ~2.15%	Vary depending on the number of employees
Industrial Accident Compensation Insurance (IACI)	NIL	0.76%~ 32.36%	0.76%~ 32.36%	Vary depending on type of business

● Key Notes to Consider for Foreigner(Non-Korean) Employees

For foreigner (non-Korean) employees, we summarized the key notes that need to be considered in relation to individual income tax and 4 statutory social insurances in Korea when the company sets up their payroll initially as below.

	Key notes
Individual income tax withholding	<p>Foreigner (non-Korean) employees may choose to be applied the flat 20.9% tax rate scheme (19% income tax plus 1.9% local income tax), which is more favorable than the progressive tax rate scheme applied to Korean nationals (rates ranging between 6.6% ~44.0% depending on the income brackets).</p> <p>This flat tax rate scheme is available for the first five (5) year period (limited to the taxable year ending December 31, 2018).</p> <p>When such flat 19% tax rate is applied, however, provisions concerning income taxation, such as tax exemption (non-taxable income), deduction, reduction or exemption, and tax credit allowed under the Individual Income Tax Law and the Special Tax Treatment Control Law are not applicable.</p>

National pension	<p>A foreigner employee working in Korea shall not be subject to the Korean national pension obligations if <u>the social security agreement is established between Korea and his/her home country.</u></p> <p>An application for waiver should also be filed with the government agency together with submission of document of proof (i.e., Certificate of Coverage).</p>
National health insurance	<p>A foreigner employee may be exempt from participation in the statutory national health (medical) insurance program in Korea <u>if such foreigner is covered for medical benefit in accordance with the relevant laws, insurance policy or the agreement with the employer of his/her home country during his/her stay in Korea, which is equivalent to the medical benefits offered under the statutory medical insurance program of Korea.</u></p> <p>A certificate for proof of coverage of medical benefits or insurance policy (with its English translation) should be submitted to the government agency in Korea together with the exemption application.</p>
Unemployment insurance (UI)	<p>A foreigner employee may choose to participate in the unemployment insurance depending on his/her visa type and nationality.</p>
Industrial accident compensation insurance (IACI)	<p>Foreigner employees should be covered under the IAIC, but the company is solely responsible to pay for this insurance premium with no contribution required from the employee.</p>

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

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