

Korea

Corporate tax guide

1. Jurisdiction

Parameters for determining income or gain subject to corporate income tax

Corporations are classified primarily as domestic or foreign. A domestic corporation is one whose head office or main office is in Korea, or a foreign corporation having a place of effective management in Korea. A foreign corporation is one whose head office or main office or a place of effective management is located outside the jurisdiction of Korea.

A domestic corporation is subject to Korean taxes on its worldwide income and capital gains, while a foreign corporation is subject to Korean taxes only on income and capital gains incurring from Korean sources.

Foreign corporations are taxed substantially in accordance with provisions applied to a domestic corporation.

2. Major taxes on corporations

Corporate income tax

Corporate income tax is assessed on the taxable income for each fiscal year at the rate of 11% for the first KRW 100 million and at the rate of 22% for the amount in excess of KRW 200 million.

There are certain tax incentives available to qualified foreign invested corporations under the Foreign Direct Investment Law (see **Investment Incentives** for further details).

Corporations enjoying tax incentives have to pay minimum tax at least 13% (7% for small and medium size companies) of the tax base, calculated under the assumption that no tax incentives are allowed.

Resident Tax

A surcharge at the rate of 10% of the corporate income tax amount is levied as the resident tax.

Consolidated tax return system

Korea has recently introduced the consolidated tax return system, which will take effect from the fiscal year commencing on or after 1 January 2010. It is aimed to impose corporate tax on aggregate income of a parent or subsidiary corporation by deeming them as a tax unit according to their economic substances, in case a parent corporation and a subsidiary corporation are combined economically.

The tax payer may make an election; however it cannot be repealed for at least five years after the election.

3. Organisations taxable as corporations

Principal forms of business entities subject to the corporation income tax

Joint Stock Company ("Chusik Hoesa")
Private Limited Liability Company ("Yuhan Hoesa")
Limited partnerships ("Hapja Hoesa")
General partnerships ("Hapmyong Hoesa")

4. Taxable income of resident corporations

Tax base

Taxable income is defined as assessable income less allowable deductions.

Assessable income is simply gross income adjusted to include receipts deemed to be income by the Corporation Income Tax Law of Korea and to remove tax-exempt income items.

Allowable deductions include most expenses recognised for financial accounting purposes. There are, however, exceptions whereby certain expenses recognised in financial accounting are not fully recognised in tax. Examples are entertainment

expenses, donations and contributions, allowance for employee severance pay, etc. The Corporation Income Tax Law provides various formulae for the calculation of deductible amounts for these expense items.

Depreciation

Depreciation is based on the total acquisition cost of tangible assets. Buildings are depreciated by straight-line method, and for other assets both straight-line and declining-balance methods are permissible. Depreciation is deductible only if it is recorded in the financial accounts.

Useful lives to be used in the calculation of depreciation are prescribed by law and their use within 25% variation is mandatory. Tax purpose useful lives of fixed assets reasonably approximate the economic lives thereof.

Expenditure on intangible assets such as patents, goodwill and trademarks must be amortised on a straight-line basis over the statutory useful lives of the assets, ranging from 5 to 20 years.

Capital gains

Capital gains of corporations are subject to taxation as ordinary income.

If the price of the real estate in a certain region increases by more than 3% or 10%, the government may designate the region to be a taxable region and impose a 10% tax on the capital gains arising from land and buildings. The surtax is assessed at a rate of 10% (20% for property transferred without registration) on the gains derived from the sale of land, buildings, or the rights thereto, and unlisted stock of certain category. The land and residential house, not-for-business operation are taxed at 30% (40% for property transferred without registration).

Net operating losses

Operating losses can be carried forward for up to five years. Generally loss carry back relief does not apply. Loss carry back applies only to small and medium size companies for the prior fiscal year.

Transfer pricing

Under the Law for the Coordination of International Tax Affairs, the tax authorities reserve the right to adjust the transfer price based on an arm's length price and to determine or recalculate a resident's taxable income when the transfer price of a Korean company and its foreign related party is either below or above an arm's length price.

Transfer pricing is becoming one of the most important international tax issues that multinational companies doing business in Korea face. The National Tax Service of Korea stated that the enforcement of transfer pricing compliance is one of their high priorities, including introduction of transfer pricing documentation requirements and routine examination of intercompany transactions during tax audits.

Foreign tax credits

Where a domestic corporation has paid, or is liable to pay, foreign corporate tax abroad, the tax amount paid or payable abroad is deducted from the corporate tax up to an amount equivalent to the ratio of the income from foreign sources to the taxable income. If the foreign tax amount paid or payable exceeds the creditable limit against the corporate tax payable for the year, the excess portion may be carried over for five years.

5. Taxation of non-resident corporations

Taxation of permanent establishments of foreign corporations

A foreign corporation which has a permanent establishment in Korea is liable to the Korean corporate income tax as are domestic corporations, on its income attributable to the permanent establishment.

Taxation at source of income paid to foreign corporations

If a foreign corporation has neither a permanent establishment nor real estate income in Korea, it will be taxed only on certain types of Korean source income, and only by withholding at source as follows, unless relevant tax treaties provide otherwise:

Interest, dividends, royalties and other income	22%
Bond interest income from government or company	15.4%
Personal service income	22.0%
Lease income on vessels, aircraft, registered automobiles and heavy equipment	2.2%
Gains from the transfer of securities: lesser of 11% of gross receipts or 22% of net gain	

The withholding constitutes the final liability.

6. Liquidations

Taxation of liquidation gains

A domestic corporation is subject to tax on its liquidation gains. Gains from the liquidation of a branch in Korea of a foreign corporation are not subject to Korean taxes.

Liquidation gains are the excess of the fair market value of properties to be distributed to the

shareholders over their respective shareholdings in the equity of the corporations being liquidated. Liquidation gains are taxed at the ordinary income tax rates.

Business income generated during the liquidation period is normally included in the liquidation gains.

Taxation of shareholders of a liquidated corporation

Liquidation gains distributed to a Korean corporation or a resident individual are included in the respective corporation's or individual's income for the purpose of calculating corporation or individual income taxes, as appropriate.

Liquidation gains distributed to foreign shareholders are subject to the 22% withholding tax, unless otherwise provided by the relevant tax treaties. The withholding constitutes the final liability.

7. Taxation of shareholders (corporations and individuals)

Taxation at source of investment income paid to non-residents

Dividends and interest paid to non-residents are subject to the 22% withholding tax unless otherwise provided by the relevant tax treaties. The withholding constitutes the final liability.

Capital gains realised by non-residents

Capital gains arising from transactions involving land, buildings, rights to real estate, antiques and unlisted stocks in Korea are taxed at rates ranging from 6.6% to 77%, depending on the amount of gains, the holding period, or whether the title to the land or building is registered under the seller's name, etc.

Taxation of domestic shareholders of foreign Corporations

Dividends received by Korean shareholders from a foreign corporation are fully taxable, subject to relief for foreign taxes paid.

8. Returns

Taxable period

The taxable period is the fiscal year of a corporation and normally covers a period of 12 months.

However, a corporation can choose to have a fiscal year shorter than a 12-month period. A fiscal year will be deemed in the cases of incorporating a new corporation, liquidation and changing a fiscal year.

Filing requirements

Every corporation is required to file an annual tax return. Generally, a corporation must submit its return within 3 months from the fiscal year end.

Corporations are generally not eligible for filing extensions.

Assuming the corporation's accounting period exceeds six months, it will be required to file an interim tax return within two months from the end of the first six months of the period.

Remittance of tax payments is generally expected at the time of filing both the interim and final returns. However, corporations having a tax liability in excess of KRW 10 million are allowed to make instalment payments over a period of 30 days (45 days for a small and middle size corporation) from the time of filing.

Statute of limitation

The statute of limitation is generally five years, and it can be extended to seven to ten years where tax avoidance is due from cheating or other wrongdoings.

9. Investment incentives

The Foreign Investment Promotion Act ("FIPA") of Korea offers various tax incentives in order to induce foreign investors to invest in projects which accompany advanced technology; in projects to be located in a Foreign Investment Zone as defined in the FIPA; and in other projects designated as projects for which a tax deduction is essential to induce foreign investment.

Qualified foreign invested enterprises under the FIPA are generally exempt from corporation or individual income tax, as appropriate, for three to five years from the year reporting taxable income, and receive a 50% reduction in corporation tax or individual income tax for the further two subsequent years. Foreign invested enterprises accompanying advanced technology under the FIPA are exempt from corporation or individual income tax for the initial year reporting taxable income, and for three to five years thereafter, and receive a 50% reduction in corporation tax or individual income tax for the further two subsequent years. However, these exemptions apply only to that portion of income generated from qualified projects and are given in proportion to the foreign equity holding ratio in the qualified foreign invested enterprises.

Foreign investors receiving dividends from their investment will receive a similar 100% or 50% tax-exemption privilege, provided the income subjected to dividends is generated during the tax-exempted period described above from a qualified project and the dividends subject to tax-exemption have accrued based on the foreign equity holding ratio in the qualified foreign invested enterprise.

Acquisition tax and property tax on property acquired for use in the qualified projects are also similarly tax exempted.

The above tax exemptions will be given only upon filing application for the available tax benefits along with the application for the approval of foreign investment, and when approval thereof is granted by the Ministry of Strategy and Finance.

Capital goods imported pursuant to the approval of a confirmation by the Ministry of Strategy and Finance for use in a qualified project are generally exempted from customs duties, value added tax and special consumption tax at the rate of 100% for advanced technology projects.

In case of an increase in the capital of a qualified foreign invested enterprise, the tax exemption privileges outlined above are generally also available for the increased portion of foreign investment in the qualified foreign invested enterprise.

Licence or royalty payments to a foreign supplier of technology under a technology inducement contract confirmed under the FIPA are also exempted from income taxes for five years, provided that the technology meets designated criteria.

Foreigners engaged in services under a technical inducement contract may be exempt from wage and salary income tax for five years.

Also, under the Individual Income Tax Law of Korea, the amount equivalent to 30% of gross salary income of foreign expatriates or employees would not be taxable in Korea. In this case, salary income deduction, tax credits and the graduated tax rate are applied to the taxable income as the residents' tax calculation.

Foreign expatriates and employees will be able to opt to apply for a flat income tax rate of 16.5% (including resident surtax) on their salary income. In this case, 30% deduction of salary income, any other income deduction and tax credit will not be allowed. The tax amount is calculated by multiplying the 16.5% tax rate to total salary income without any deduction and tax credit. If a foreign expatriate or employee wants to choose the 16.5% flat tax application, he/she is required to submit an application.

Expenses incurred by an employer in connection with providing housing to its employees (including expatriate employees) are recognised as deductible items in arriving at the taxable income of the employer and would be excluded from the taxable

income of beneficiary employees, provided that certain conditions are met.

10. Other significant taxes

Value Added Tax

Goods and services sold within Korea or imports to Korea by individuals or corporations licensed to carry on business under the Value Added Law of Korea are subject to value added tax at the rate of 10% of selling price of goods or services, or gross value in money of the goods being imported.

Any tax paid on inputs (purchases) can be used as a credit against tax collected in connection with outputs (sales). A zero tax rate applies to exports and certain other goods and services that earn foreign currency. A corporation that exports all of its products will obtain refunds of the tax paid on its purchases.

Acquisition Tax

A 2% acquisition tax is levied primarily on the acquisition cost of property such as land, buildings, motor vehicles, ships, heavy equipment and forests. However the acquisition tax rate on new factories or expansion of existing factories in the "major cities" is three times the normal rate.

Property Tax

The annual property tax at rates between 0.2% and 5% of the acquisition cost or revaluation value is levied by the local authorities. Property tax rates on new factories or expansions of existing factories in the "major cities" are five times the normal rate.

Registration Tax

A 0.3% to 2% registration tax is levied on the public registration of an acquisition, transfer, change, or abolition of title to property and other rights, or the public registration of an incorporation and a capital increase of a company. However, in case of a company located in "major cities", the registration tax rates for the acquisition of land and buildings, the incorporation and the capital increase will be three times the normal rates.

Business Place Tax

Business entities with over 50 permanent employees are subject to a tax at the rate of 0.5% of monthly employee compensation. Additionally, business entities having working premises in the form of a building larger than 330 square metres are taxed at 250 Won for each 1.0 square metres.

Education Tax

The education tax applies to those liable to liquor tax, special consumption tax and certain other local taxes at the rates ranging from 10% to 30% of the related

tax amount, and to corporations engaged in banking and insurance business at the rate of 0.5% of the revenue amount.

Special Consumption Tax

A special consumption tax is assessed on certain items

Securities Transaction Tax

Currently, Korea does not impose the capital gains tax on the sale or transfer of listed equity securities. Instead, Korea imposes the securities transaction tax at the point of sale or transfer of the stock or ownership interest at the rate of 0.15% to 0.5%.

Branch Tax

According to the tax treaties between Korea and some countries including France, Canada, Australia, Indonesia, Philippines, Brazil, Morocco and Kazakhstan, a branch of the company in the above mentioned countries is subject to the branch tax of 5.5% to 16.5% of its tax base (including the resident tax) in addition to the normal corporate income tax. The branch tax is not applied to subsidiaries of a foreign company.

11. Tax treaties and withholding tax rates

Modification of tax principles by treaty

Tax treaties modify the general principles of taxation described herein, and have been concluded with the countries noted in the table below.

Withholding Tax Rates

Treaty Country	Interest (%)	Dividend (%)	Royalty (%)
Japan	10	5 to 15	10
Thailand	10	15 to 25	15
Germany	10	5 to 15	2 to 10
United Kingdom	0 to 10	5 to 15	2 to 10
Denmark	15	15	10 to 15
Belgium	10	15	10
United States	12	10 to 15	10 to 15
Canada	15	5 to 15	15
France	10	10 to 15	10
Singapore	10	10 to 15	15
Switzerland	10	10 to 15	10
Netherlands	10 to 15	10 to 15	10 to 15
Finland	10	10 to 15	10
Sweden	10 to 15	10 to 15	10 to 15
Malaysia	15	10 to 15	10 to 15
New Zealand	10	15	15
Australia	15	15	15
Norway	15	15	10 to 15
Bangladesh	10	10 to 15	10
Turkey	10 to 15	15 to 20	10
Sri Lanka	10	10 to 15	10
India	10 to 15	15 to 20	15

Treaty Country	Interest (%)	Dividend (%)	Royalty (%)
Philippines	10 to 15	10 to 15	10 to 15
Luxembourg	10	10 to 15	10 to 15
Pakistan	12.5	10 to 12.5	10
Austria	10	5 to 15	2 to 10
Indonesia	10	10 to 15	15
Tunisia	0 to 12	15	15
Hungary	0	5 to 10	0
Brazil	10 to 15	15	15 to 25
Ireland	0	10 to 15	0
Poland	10	5 to 10	10
Italy	10	10 to 15	10
Mongolia	5	5	10
Egypt	10 to 15	10 to 15	15
Vietnam	10	10	5 to 15
Republic of China	10	10 to 15	10
Rumania	10	7 to 10	7 to 10
Spain	10	10 to 15	10
Mexico	5 to 15	0 to 15	10
Fiji	10	10 to 15	10
Czech Republic	10	5 to 15	10
Bulgaria	10	5 to 15	5
Russia	N/A	5 to 10	5
South Africa	10	5 to 15	10
Israel	0 to 10	5 to 15	2 to 5
Portugal	15	10 to 15	10
Malta	10	5 to 15	0
Papua New Guinea	10	15	10
Greece	8	5 to 15	10
Uzbekistan	5	5 to 15	2 to 15
Kazakhstan	10	5 to 15	10
Kuwait	10	10	15
Morocco	10	5 to 10	5 to 10
Ukraine	5	5 to 15	5
Nepal	10	5 to 15	15
Belarus	10	5 to 15	5
Chile	10 to 15	5 to 10	5 to 15
Slovak Republic	10	5 to 10	10
Myanmar	10	10	10 to 15
UAE	10	5 to 10	-
Jordan	10	10	10
Laos	10	5 to 10	5
Oman	5	5 to 10	8
Slovenia	5	5 to 15	5
Algeria	10	5 to 15	2 to 10
Croatia	5	5 to 15	0
Albania	10	5 to 10	10
Venezuela	5 to 10	5 to 10	5 to 10
Lithuania	0 to 10	5 to 10	5 to 10

According to the new withholding tax rule of Korea which took effect from July 2006, in case a foreign corporation is located in a foreign jurisdiction designated by the Ministry of Strategy and Finance,

any Korean source income of the foreign corporation will be subject to the domestic tax rate without any tax treaty benefit. Labuan is the only jurisdiction designated so far.

The foreign corporation may claim the refund for any excess withholding tax within 3 years by proving that it is entitled to the reduced tax treaty rate.

Corporation tax calculation

The following is an example of a Korean corporation tax calculation.

	In Korean won
Net income before income taxes	310,000,000
Depreciation expense exceeding tax limit	30,000,000
Entertainment exceeding tax limit	5,000,000
Reversal of disallowed depreciation expenses	<u>(15,000,000)</u>
Taxable income	330,000,000
Tax loss carried over from prior years	<u>(130,000,000)</u>
Tax base	<u>200,000,000</u>
Corporation tax	38,000,000
Resident surtax	<u>3,800,000</u>

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