

# Transfer pricing for Korea

## Overview

The Law for the Coordination of International Tax Affairs (“LCITA”) was enacted in 1995 and took effect from 1996, in an effort to conform the Korean transfer pricing regulations to internationally recognized rules. Before then, transfer prices charged on intercompany transactions were governed by the Corporate Income Tax Law of Korea. The LCITA is based on the arm’s length principle and generally consistent with the OECD Transfer Pricing Guidelines. The provisions for the Advanced Pricing Agreement (“APA”) were also introduced in 1997.

The LCITA states that in an international transaction where one party to the transaction is a foreign related party, if the price is either below or above an arm’s length price, the tax authorities may determine or recalculate taxable income and tax of the resident based on the arm’s length price.

## Regulatory environment in Korea

Transfer pricing is becoming one of the most important international tax issues multinational companies doing business in Korea face. The National Tax Service (“NTS”) of Korea stated that the enforcement of transfer pricing compliance is one of their high priorities, including introduction of transfer pricing documentation requirements, routine examination of intercompany transactions during tax audits, and training of field auditors to enhance their transfer pricing audit capabilities.

## Special features of transfer pricing in Korea

The NTS is actively conducting tax audits of multinational companies with significant foreign related party transactions. The emphasis of tax audits is on the level of documentation multinational

companies have to verify that international transactions are in fact at arm's length. The NTS outlined a four step process that it expects taxpayers to follow, involving:

- identifying transactions, functions and risks
- selecting appropriate pricing methods
- adopting proper pricing by undertaking comparable analyses
- reviewing the appropriateness of pricing.

## What it means for Korean businesses

Multinational companies doing business in Korea need to carefully examine their foreign related party transactions and to prepare a detailed transfer pricing documentation to support their transfer price. In case of tax audits, tax auditors usually request the submission of the transfer pricing study.

## Recent development in Korea

In 2008, the Ministry of Strategy and Finance (“MOSF”) of Korea announced the important amendment to the transfer pricing regulations, which took effect from 2009 – the under-reporting penalty relief.

The under-reporting penalty may be waived if, as a result of the Mutual Agreement procedure, it is confirmed that the taxpayer is not liable for any negligence with regard to the difference between the reported transfer price and the arm’s length price. In addition, the under-reporting penalty may be waived if:

- the taxpayer’s transfer pricing documentation is prepared and maintained at the time of filing of corporate tax return; and
- it is confirmed that the transfer pricing method is reasonably selected and applied.

## How Grant Thornton helps you

As a leading tax adviser, Grant Thornton understands the need to comply with the transfer pricing regulations in a way which is cost-effective and does not waste management's time.

Our transfer pricing group can provide a comprehensive solution suited to your needs, after understanding management's objectives and the exact nature of the international transactions. The process may include the following:

- fact-finding exercise, where an analysis of the functions performed and risks assumed by each entity is conducted
- selection of the appropriate transfer pricing method and identification of the tested parties
- benchmarking analysis - comparable companies are identified using global/local databases, and an economic and financial analysis is conducted
- documentation - results are collated into a report and the required documentation is prepared
- negotiate the Advanced Pricing Agreement on your behalf
- dispute resolution - assist your business defending your transfer pricing policies before the tax authorities
- international compliance assessment to meet standards in other jurisdictions
- transfer pricing risk assessment
- transfer pricing planning.

Grant Thornton's practical approach to provide transfer pricing solutions protects your business from incurring onerous tax penalties on transfer pricing adjustments and non-compliance with legislative requirements. Grant Thornton can also identify beneficial changes to business processes that may result in both substantial worldwide tax savings and other commercial benefits to your business.

**If you require any additional information or have a specific question, please contact:**

Dong-Bum Kim  
Tax Partner  
T +82 2 2056 3706  
E dongb.kim@dmgt.co.kr

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