



June 28, 2007

*This publication contains information on selected current developments in Korean taxation, laws and regulations compiled by the tax service group of Samil PricewaterhouseCoopers, a network firm of PricewaterhouseCoopers.*

## Contents

- Amended VAT Law on Direct Online Marketers
- Move toward a Simplified Approach to APA with China, Vietnam and India
- Public Forum on New Partnership Taxation
- Korea and Kuwait Agree to Amend an Income Tax Treaty
- MOFE Ruling on Tax Exemption for Head Office or Factory Relocation
- Accelerated Depreciation after a Spin-off

© 2007 Samil PricewaterhouseCoopers. All rights reserved. "PricewaterhouseCoopers" refers to the Korean firm of Samil PricewaterhouseCoopers or, as the context requires, the other member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

## Amended Value Added Tax Law on Direct Online Marketers

Under the amended Value Added Tax (VAT) law, which is effective July 1, 2007, open market operators, on behalf of small direct online marketers, will be required to settle credit card payments, to issue cash receipts, and to submit underlying evidences to the concerned tax offices.

For VAT purposes, the open market refers to the environment in which products are bought and sold over the Internet. The open market operator (e.g. Auction, Gmarket, etc.) refers to a value added telecommunications company prescribed by the Electricity and Communications Act, which creates and offers a cyber mall and receives commissions on online sales of goods from the supplier of goods. A direct online marketer means a vendor who provides goods or services through the open market.

The amended VAT law will allow open market operators to file aggregated VAT returns on behalf of small direct online marketers with sales volume of 6 million won to 12 million won during a 6-month VAT period. The VAT law presently requires that VAT return should be filed by each business operator. For administrative and business convenience, however, the aggregated VAT filing is allowed with prior report to the relevant tax offices.

The amended rules will also require open market operators to issue tax invoices to direct online marketers on commissions for the use of Internet sites to sell their goods.

The new rules will enable the tax authorities to more easily collect underlying documents to assess tax on online sales of goods which have grown very fast in Korea. With soaring E-commerce, the open market size is estimated to reach 7.5 trillion won in 2007, according to a press release by the Nation Tax Service (NTS).

## NTS Plans to Seek a Simplified Approach to APA with China, Vietnam and India

The NTS is seeking ways to adopt a simplified approach to advance pricing arrangements ("Simplified APA") with certain Asian countries in which Korean companies have expanded investments. As part of this, the NTS plans to organize a joint conference with China, Vietnam and India to explore the possibility of adopting a simplified APA on a reciprocal basis.

The plan was revealed as part of the NTS efforts to support Korean companies with operations in those Asian countries which have moved to strengthen the enforcement of transfer pricing regulations against foreign-investment companies.

According to the NTS, the simplified APA would apply to small and medium businesses with annual turnover below a certain level and simple functions performed. The simplified approach would focus on reducing documentation requirements, curtailing APA procedures not to last for one year or so (currently two years tend to be required for a unilateral APA) and making NTS experts' assistance available for transfer pricing reviews.

## Public Forum on New Partnership Taxation

On June 19, 2007, a public forum on partnership taxation was held by the Korea Institute of Public Finance associated with the Ministry of Finance and Economy (MOFE). In the forum, the government's plan to implement the new partnership taxation in Korea was presented and debated by academic, legal and tax professionals participating in the forum.

The MOFE has created a task force in March 2007 to prepare blueprints to implement the

new partnership taxation. The new partnership taxation is expected to constitute an important element of the Ministry's 2007 tax reform proposals. If approved at the end of December 2007, the new rules will be implemented from January 1, 2009.

Provided below is a summary of major points of the new partnership taxation in Korea discussed in the forum:

- **Applicable Scope:**

The new partnership taxation would apply to associations (*johap*) subject to the existing rules for the taxation of joint businesses under the Individual Income Tax Law (IITL), an unlimited company (*hapmyonghoesa*) and a limited company (*hapjahoesa*) which are subject to the Corporate Income Tax Law (CTL). It would also apply to new forms of entities such as limited partnership (LP, *hapja-johap*) and limited liability company (LLC, *yunhanchaegim-hwesa*). These new forms of business entities are proposed under a bill to revise the Commercial Code (please refer to the *Samil Commentary, October 31, 2006 issue*).

A taxpayer would be allowed to elect the current taxation or new partnership taxation on its own discretion, but shall not draw back the election for five consecutive years.

- **Avoidance of Double Taxation of Income**

A partnership would be treated as a conduit of income not subject to corporate income tax, but each individual partner would be subject to corporate income tax or individual income tax on his share of the profits.

- **Allocation of Income or Loss**

A partnership's income would be allocated among the partners according to the percentage specified in the partnership agreement. The new partnership taxation would include restrictive clauses that prevent possible tax avoidance through the

manipulation of allocation percentage.

- ***Taxation of In-kind Contribution to Partnership***

The following 2 methods are now being considered for tax deferral relating to capital gains from in-kind contributions to a partnership:

- (i) When an individual contributes non-cash assets to a partnership, income tax would not apply to capital gains derived by the individual from the transfer of assets, but to gains derived by the partnership from the transfer of the contributed assets; or
- (ii) Such capital gains would be recognized at the point contributions are made, but income tax on the capital gains would be paid in three-year installments after a three-year grace period.

- ***Transactions between Partner and Partnership***

When services or goods are supplied by a partner to a partnership where the supply is not made in the course of partnership activities, such transactions would be treated as third party transactions and therefore income arising or expenses incurred from the transactions would be recognized.

## **Foreign Investment Rules Amended to Ease Criteria for Cash Grant**

Rules of the Foreign Investment Promotion Act have been amended to promote foreign investment in nonprofit organizations in high technology and research and development (R&D) areas.

The Act used to limit existing incentives to foreign investment in profit entities. The amended rules, however, extend the existing tax and other incentives for foreign direct investment in case where foreign investors or organizations invest in Korean nonprofit

entities that should meet the prescribed requirements for R&D manpower and facilities. If certain conditions are met, qualified foreign investments prescribed in the Act are eligible for the exemption from or reduction in corporate or individual income tax, acquisition and registration taxes for up to seven years and free lease of land for up to fifty years.

Amendments are also made to ease requirements for certain qualified foreign investment that receive cash grant under the existing rules. The amendments include three changes:

- the minimum capital requirements of US\$5 million is no longer required for an eligible investment in R&D area;
- the employment requirements are eased to include 10 full-time technical staff having master degrees or having bachelor degrees with at least three-year experience in R&D activities (previously required 20 staff or more); and
- cash grant is granted to investment by a foreign-invested nonprofit organization to build new or additional R&D center that should meet the minimum requirements for technical staff employment.

However, no change is made to the existing criteria for cash grant: (i) investment of USD10 million or more to establish a new or an additional manufacturing factory (business place for service industry) to operate in any one of high technology industries and industry support services eligible for tax exemption or reduction for foreign investment; or (ii) investment of USD10 million or more to establish a new or an additional factory to manufacture strategic parts and materials as prescribed in the relevant law.

The amended rules will become effective from October 27, 2007.

## Korea and Kuwait Agree to Amend an Income Tax Treaty

Korea and Kuwait have agreed to amend the existing income tax treaty which came into force in June 2000.

According to the agreement, offshore income that Korean companies earned outside Kuwait will no longer be subject to Kuwaiti taxation. This will contribute to improving the competitiveness of Korean construction companies which represent a vast majority of Korean operations in Kuwait. Under the Korea-Kuwait income tax treaty, Korean construction companies are presently subject to a 55% Kuwait corporate income tax on income arising from activities such as processing construction equipment and design engineering performed in the region outside of Kuwait.

The agreement also indicates that withholding tax rates on interest and dividends would be reduced from 10% to 5% and that interest paid to government entities would be exempt from tax.

The agreement will come into force when it is officially signed and ratified by both countries.



## Rulings

### MOFE Ruling on Tax Exemption for Head Office or Factory Relocation

MOFE issued a ruling on whether a new entity created as a result of a corporation split would continue to receive a tax exemption for the relocation of head office or factory out of a metropolitan area that the original company has enjoyed in case that the new entity continues to operate the business transferred by the original company.

The ruling upholds the continuing application of the tax exemption with respect to taxable income arising from the business the new entity has taken over from the original company. In this regard, the new entity's operation period should be reckoned including the original company's operation period in a metropolitan area, as well as the new entity's operation period in the relocated area. Accordingly, the ruling states that the new entity is entitled to the tax exemption for the remaining exemption period. (*Jaejoye-366, 2007.5.25*)

The tax law presently grants a seven-year tax exemption (100% exemption for five years and 50% exemption for two years) when a qualified company relocates its head office or factory from a metropolitan area to a non-metropolitan area. The qualified company must ensure that it has been in operations in a metropolitan area for at least three years before the relocation. Income subject to tax exemption shall be calculated according to a relocation ratio, which is the smaller ratio of (i) the number of relocated employees to the total number of employees, or (ii) the wages paid to relocated employees to the total wages.

## Accelerated Depreciation after a Spin-off

Where a spun-off company takes over the original company's assets to which the original company has applied accelerated depreciation under Special Tax Treatment Control Law, the spun-off company shall no longer benefit the accelerated depreciation, according to a ruling

issued by the National Tax Service (*Seomyon2tim-712, 2007.4.24*).

For corporate income tax purposes, the spin-off refers to a corporation split where shares in the new entity are distributed to the original company's shareholders on a pro rata basis.

The information contained in this publication is for general guidance on matters of interest only and is not meant to be comprehensive. The application and impact of laws can vary widely based on the specific facts involved. For more information, please contact your usual Samil PwC client service team or professionals listed below.

David Jin Young Lee	82- 2-709-0557,	<a href="mailto:jylee@samil.com">jylee@samil.com</a>
IlHwan Oh	82-2-709-0897	<a href="mailto:ih_oh@samil.com">ih_oh@samil.com</a>
Dong-Keon Lee	82-2-709-0561,	<a href="mailto:dklee@samil.com">dklee@samil.com</a>
Dong-Bum Kim	82-2-709-7900,	<a href="mailto:dbkim@samil.com">dbkim@samil.com</a>
Sang-Keun Song	82-2-709-0559,	<a href="mailto:sksong@samil.com">sksong@samil.com</a>
Alex Joong-Hyun Lee	82-2-709-0598,	<a href="mailto:Joonglee@samil.com">Joonglee@samil.com</a>
Shin-Jong Kang	82-2-709-0578	<a href="mailto:sjkang@samil.com">sjkang@samil.com</a>

## SamilPwCAcademy Programs

### 2007 년 7 월의 교육프로그램

#### 법인세기초실무 7월 3일 (화) ~ 7월 6일 (목), 4일간 총 24시간

법인세 계산구조, 세무조정, 중소기업의 범위와 세제 지원, 손익의 귀속시기, 손익금 관련 세무조정, 법인세 신고 실무 등

#### 경영전략 전문가 과정 7월 3일 (화) ~ 7월 6일 (목), 4일간 총 24시간

전략수립 사례연구 및 Feedback을 통한 전략수립 Process의 이해, 실무자에게 적합한 실무중심의 사례분석 및 실습

#### 재무제표분석실무 7월 3일 (화) ~ 7월 6일 (금), 4일간 총 24시간

계정분석을 통한 재무제표분석, 재무비율분석, 재무제표와 현금흐름분석 재무제표와 원가구조분석, 재무제표를 통한 부실징후분석

#### 비영리법인의 회계와 세무해설 7월 4일 (수) ~ 7월 6일 (금), 3일간 총 21시간

수익사업과 목적사업의 구분과 회계처리에 대한 사례해설, 비영리법인관련 조세지원제도와 사후관리 증점해설, 학교, 의료법인, 장학재단의 회계처리방법 해설

#### 신입사원경리 실무 7월 9일 (월) ~ 7월 13일 (금) 총 5 일 (35 시간)

회계의 개념 및 흐름, 계정과목, 재무제표 읽는 법, 원가. 관리회계의 기초, 조세체계와 일반 사항 등

#### BSC도입 및 추진전략실무 7월 10일 (화) ~ 7월 10일 (화), 1일간 총 4시간

BSC 모델의 지속적인 발전추세 및 국내·외 도입현황 파악, BSC와 EIS 통합 시스템에 대한 삼일PwC의 사례 검토

#### 원가 및 관리회계입문 7월 11일 (수) ~ 7월 13일 (금), 3일간 총 21시간

원가 및 관리회계에 대한 기본이론, 관리회계정보를 활용한 의사결정 및 성과평가방법 사례

#### 소비성경비지출 증빙에 따른 세무회계처리 7.13(금) 총 1 일 (7시간)

접대비 개념, 판례와 해석상 접대비로 본 주요 사례, 50만원 이상 접대비 업무관련성 입증, 신용카드 매출전표와 매입세액 공제 등

#### 개정 재무제표 작성기준과 자본변동표(기업회계기준서 21호를 중심으로) 7월 13일 (화) ~ 7월 13일 (금), 1일간 총 4시간

기존 재무제표 작성기준과 개정 재무제표 작성기준의 주요 차이, 사례를 통한 재무제표 작성 실습

위의 교육과정은 이론 및 실무, 그리고 사례 연구 등 실무능력향상에 중점을 둔 교육으로 「고용보험법 및 근로자 직업훈련촉진법」에 의해 교육훈련비의 일부를 정부로부터 지원 받는 교육과정으로 지정되어 있으며 (일부 과정은 제외) 교육 7일 전까지 신청하셔야 교육훈련비의 일부를 지원 받으실 수 있습니다. 자세한 사항에 대한 문의는 ☎: 02-3781-3429로 하시기 바랍니다.