Korean Tax Update

Samil Commentary

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Government Considers the Creation of Opportunities Zones with Tax Incentives for Companies Investing in or Relocating to These Zones

The government is considering the creation of special opportunities zones where investors in these zones may benefit from corporate income tax and acquisition tax incentives, etc. The primary goal of creating these opportunities zones is to stimulate economic development and job creation in relatively underdeveloped local regions. This initiative involves providing more than 10 types of incentives which are distinct from those currently available in existing economic zones, as outlined by the Presidential Council on New Initiative for Regional Development. In addition, the introduction of these special opportunities zones aims to address the limitations of incentives available in existing economic zones. A special opportunities zone would be created by a local government at its own discretion, and then designated and made public by the Minister of Trade, Industry and Energy (MOTIE) following consultations among the MOTIE and other relevant ministries, and then, deliberation and resolution by the Presidential Council on New Initiative for Regional Development. Tax incentives under consideration for investors in special opportunities zones include:

- Where a company relocates to an opportunities zone after selling its real estate, the deferral of individual or corporate income tax on gains arising from the sale of the real estate until it disposes of any real estate acquired within such a zone, as well as 100% individual or corporate income tax exemption for the first five years for a business start-up or a new business place in such a zone, followed by a 50% reduction for the two subsequent years;
- With respect to the real estate newly acquired by a company relocating to or starting a

business in such a zone, 100% acquisition tax exemption and 100% property tax exemption for the first five years with a 50% reduction in property tax for the subsequent five years; and

- For companies which have received family business succession benefits, substantial relaxation of the follow-up management requirements to remain eligible for these benefits.

Korea's National Tax Revenue Estimated to Be Less than the Budget by KRW59 Trillion in 2023

The national tax revenue is predicted to be KRW341.4 trillion in 2023, according to the reestimation of the tax revenue by the Ministry of Economy and Finance (MOEF). The reestimated tax revenue is KRW 59 trillion less than the Ministry's initial projection of KRW400.5 trillion for the year. Most of the decrease in the tax revenue projection is attributed to a sharp decline in corporate profits and a contraction in asset markets in the wake of a rapid slowdown in the domestic and global economy during the period from the fourth quarter of 2022 through the first half of this year. Moreover, the country's exports remained weak influenced by a recession in the semiconductor industry during the period, driving down the collection of corporate income taxes. The revenues from capital gains tax and other asset-related taxes are also expected to fall short of the initial estimations, mainly due to a downturn in real estate and other asset markets. The national tax revenue amounted to KRW241.6 trillion for the first eight months this year, a KRW47.6 trillion decrease from the same period of the previous year, according to the Ministry.

The Protocol Amending the Customs Mutual Assistance Agreement Concluded between Korea and Vietnam Takes Effect

The Protocol amending the Customs Mutual Assistance Agreement established between Korea and Vietnam went into effect on September 10, 2023. The amended protocol contains provisions related to the conclusion and implementation of the Authorized Economic Operator (AEO) Mutual Recognition Agreement (MRA). Under the AEO MRA provision, the customs authorities in one country should extend the same customs benefits as enjoyed by AEOs in the country to those certified by another country. With the implementation of the MRA, Korean exporters may benefit from practical advantages in the process of customs clearance in Vietnam, such as simplified import examinations and document submissions. In addition, the protocol amending the agreement includes a new provision on electronic origin data exchange and other information exchange to facilitate the implementation of the free trade agreement between the two countries.

Foreign Financial Account Reportings Mark a Record High of KRW186 Trillion This Year

The National Tax Service (NTS) announced that 5,419 Korean taxpayers reported a total of KRW 186.4 trillion in foreign financial accounts in 2023 including KRW 132 trillion in virtual

assets accounts. These figures mark a significant rise of 38.1% (or 1,495) and 191.3% (or KRW122.4 trillion) year on year in the number of reporting taxpayers and the amount reported, respectively. The latest reporting results represent a record high since Korea introduced the foreign financial account reporting requirements in 2011. The sharp rise in the reportings may be primarily due to virtual asset accounts which were required to be reported for the first time this year. Meanwhile, other types of financial accounts, such as bank deposit accounts and securities accounts witnessed a decline of 13.1% (or KRW 8.4 trillion), resulting in the total amount of these accounts reported at KRW 55.6 trillion this year.

In relation to virtual asset accounts which were reported from this year, it is noteworthy that a total of 73 corporate taxpayers have reported KRW120.4 trillion, representing 74.3% of the aggregate reporting amount of corporate taxpayers. The NTS attributed the primary reason behind this notable increase to the fact that crypto issuers have reported for the first time this year the cryptocurrencies they had issued and kept in overseas crypto wallets. The NTS said it has been working to align itself with the Global Crypto Asset Reporting Framework (CARF) for exchange of information on virtual asset transactions, etc. This effort is promoted by the need to address the potential risks associated with base erosion through virtual assets.

Rulings Update

Whether the loss carryback rules for SME would apply to the domestic company engaged in finance and insurance business

In general, a domestic company is allowed to carry forward losses to use in future years (loss carryfoward) under the Corporate Income Tax Law (CITL, Article 13(1)). Also, where a domestic company qualifies as a small and midsize enterprise (SME) under Article 6(1) of the Special Tax Treatment Control Law (STTCL) and Article 2 of the Presidential Decree of the STTCL, it can choose to carry back losses for one year and seek a refund of tax paid in the previous year by offsetting the tax losses (loss carryback) under the CITL (Article 72(1)).

In a recent authoritative interpretation, the National Tax Service clarified that the loss carryback rules can apply to a domestic company engaged in finance and insurance business, provided that the company qualifies as a SME (*Seomyeon-2022-Beobin-4397, 2023.4.19*). This interpretation appears to take into account that finance and insurance business falls within the scope of SME businesses that can be carried on by a SME under the so-called negative list system. Under this system, introduced with the amendments to Article 2 (Scope of SME) of the Presidential Decree of the STTCL (on February 7, 2017), most businesses are considered as SME businesses, except certain businesses explicitly excluded (for example, consumption-oriented businesses such as hotels), effective for fiscal years beginning on or after January 1, 2017. Prior to this amendment, the positive list system applied and only the 52 categories of businesses were listed as SME businesses, which included agriculture, manufacturing and construction activities, etc. but notably excluded finance and insurance business.

This authoritative interpretation implies that starting from fiscal years beginning on or after January 1, 2017, domestic companies carrying on business in finance and insurance, real estate rental and other sectors, which were formerly excluded from the scope of SME businesses under the positive list system, will have access to loss carrybacks as well as tax credits and deductions, etc. that are available for SMEs if they meet other conditions for SMEs such as their corporate size and independence (between ownership and management).

Regarding the timing for determining whether a domestic company qualifies as a SME eligible for the loss carryback, an authoritative interpretation clarified that the determination should be based on the fiscal year when the losses were incurred, rather than the immediately preceding year when the loss carryback is applied. (*Seomyeon-2017 Beobin-1732, 2017.11.30, Corporation Tax Disvision-624, 2009.5.28*). This means that even if a company failed to meet the conditions for SME in the immediately preceding year when losses were to be offset, it can still carry back those losses if it meets the conditions for SME in the fiscal year when the losses are incurred.

Separately, it is worth noting that finance and insurance business falls under the scope of SME businesses, but is excluded from the category of businesses which can be carried on by middle standing enterprises (*Articles 6-4(1)(2) and 9(4)(2)(b) of the Presidential Decree of the STTCL, Article 2(2)(2) of the Presidential Decree of the Special Act on the Promotion of Growth of Middle-standing Enterprises*). As such, if a domestic company engaged in finance and insurance business does not meet the conditions for SME, it should be classified as a large corporation, rather than a middle-standing enterprise, for Korean tax purposes.

Whether the tax incentive for startup SMEs would continue to apply if a startup SME is relocated back out of the designated metropolitan area

The Korean tax law provides for tax incentives for youth and other startup SMEs incorporated outside the 'designated overconcentration control region of the Seoul Metropolitan area' ('designated metropolitan area' or 'designated area'). The tax incentives include 100% income tax exemption for youth startup SMEs incorporated outside the designated area, and 50% income tax reduction for youth startup SMEs incorporated in the designated area and other startup SMEs incorporated outside the designated area during the first five years under Article 6(1) of the STTCL. Also, where a startup SME, incorporated outside the designated area, relocates into the designated area, the startup SME will be treated as if it were originally incorporated in the designated area, and eligible for the tax incentives during the remainder of the first five year period, beginning from the fiscal year in which the relocation takes place under Article 5(25) of the Presidential Decree of the STTCL ('provision at issue')

However, while the provision at issue addresses situations where a startup SME was incorporated outside a designated area and relocates into the said area, it does not cover a specific case where a startup SME, which was incorporated outside the designated area and relocated into the designated area, is later relocated back out of the designated area.

A recent advanced tax ruling concerns this case on whether a youth startup SME would be eligible for 100% income tax exemption during the remainder of the first five year period where the youth startup SME was incorporated outside the designated area (100% tax exemption claimed), relocated into the designated area (10% tax exemption claimed) and later relocated back out of the designated area. The ruling provided that the 100% tax exemption would apply during the remainder of the first five-year period from the fiscal year in which the youth startup SME were relocated back out of the designated area, as if it were incorporated outside the designated area. (*Advance Ruling-2023-Beobgyubeobin-0165, 2023.5.2*).

In this regard, it is necessary to consider that the tax incentive applicable to youth or other startup SMEs can continue to be available for the remainder of the first five year period if the startup SME is relocated back out of the designated area, even though it was not eligible for such tax incentives during the years in which it was relocated in the designated area.

The content is for general information intended to facilitate understanding of recent court cases and authoritative interpretations. It cannot be used as a substitute for specific advice and you should consult with a tax specialist for specific case.

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