Tax News Flash

August 4, 2026

MOFE Announces Korea's 2026 tax reform proposals

On August 3, 2026, the Ministry of Finance and Economy (MOFE) released a comprehensive bill proposing amendments to various tax laws, with the aim of reforming corporate and international taxation in Korea. The proposals encompass a broad range of measures, including the incorporation of the OECD/G20 Inclusive Framework's Pillar Two Side-by-Side Package into Korea's domestic global minimum tax legislation, the allowance of foreign tax credits for Qualified Domestic Minimum Top-up Tax (QDMTT), and reforms to the domestic treasury share taxation regime. In addition, the government has proposed to introduce a new tax credit for the domestic production of strategically important products and adopt preferential tax incentives to promote regional R&D and investment activities. The proposals also include a reduction in the effective tax rate threshold under the Controlled Foreign Company regime to align it with the minimum tax rate under the GloBE Rules.

The proposed amendments will be subject to cabinet consultation and are expected to be submitted to the National Assembly in early September 2026. If approved, most of the changes will take effect from January 2027, unless otherwise specified.

Set out below is a summary of the key changes that may affect multinational enterprises doing business in Korea, as well as domestic corporations.

Proposed Reform of International Taxation

1. Introduction of the Side-by-Side Package into the Domestic Global Minimum Tax Rules

To align the domestic global minimum tax rules with the OECD's new package of the administrative guidance (referred to as the 'Side-by-Side Package') under the Pillar Two global minimum tax rules (the 'GloBE Rules'), the government has proposed new safe harbour rules. These include a Side-by-Side (SbS) safe harbour and an Ultimate Parent Entity (UPE) safe harbour for eligible jurisdictions, a substance-based tax incentive (SBTI) safe harbour, and a simplified effective tax rate (ETR) safe harbour. These new rules are intended primarily to prevent double taxation arising from conflicts between the GloBE Rules and domestic minimum tax regimes and to reduce compliance burdens for multinational enterprise (MNE) groups headquartered in jurisdictions that maintain minimum tax regimes consistent with the GloBE Rules. If enacted, the proposed rules will apply to GloBE Information Return or top-up tax return filings made on or after January 1, 2027.

SbS Safe Harbour

Requirements. The SbS safe harbour will be available where the Ultimate Parent Entity (UPE) of an MNE group is located in a jurisdiction with a qualified SbS regime that: (i) has an eligible domestic tax system, (ii) has an eligible worldwide tax system, and (iii) provides a foreign tax credit for QDMTTs.

Effect. Where the UPE of an MNE group is located in a qualified SbS jurisdiction that meets all prescribed requirements, the top-up tax for the MNE group's constituent entities across all their domestic and foreign operations will be deemed to be zero for the purposes of the Income Inclusion Rule (IIR) or the Undertaxed Profits Rule (UTPR).

Applicable Year. For a jurisdiction recognized as a qualified SbS jurisdiction by the OECD Inclusive Framework, based on an assessment of its pre-existing tax regimes by December 31, 2025, the SbS safe harbour will apply to fiscal years beginning on or after January 1, 2026. For jurisdictions recognized on or after January 1, 2026, the safe harbour will apply beginning in the fiscal year following the year of recognition.

UPE Safe Harbour

Requirements. The UPE safe harbour will be available where the UPE of an MNE group is located in a jurisdiction with a qualified UPE regime that has an eligible domestic tax system. To qualify, the jurisdiction must have a corporate income tax system with a nominal tax rate of at least 20% and a minimum tax regime that ensures an effective tax rate of at least 15%.

Effect. Where the UPE of an MNE group is located in a qualified UPE jurisdiction that meets all prescribed requirements, the top-up tax for the MNE group's constituent entities located in that UPE jurisdiction will be deemed to be zero for UTPR purposes.

Applicable Year. The UPE safe harbour will apply to fiscal years beginning on or after January 1, 2026.

Substance-based Tax Incentive (SBTI) Safe Harbour

The SBTI safe harbour will operate by reducing the top-up tax or domestic top-up tax (DMTT) payable in a jurisdiction through an increase in adjusted covered taxes attributable to the use of qualified SBTIs in that jurisdiction. A qualified SBTI is defined as a tax benefit calculated based on eligible expenditures or production. Examples include tax credits determined as a specified percentage of eligible R&D expenditures or tangible asset acquisition costs, or by reference to the volume of manufactured goods, electricity, extracted or refined outputs produced.

Computation. Qualified SBTIs for a fiscal year will be determined by the type of incentive, as follows:

For a tax credit, the relevant amount is the reduction in covered taxes due to the tax credit claimed in the fiscal year.

For an excess deduction, the relevant amount is the excess deduction claimed in the fiscal year multiplied by the applicable corporate income tax rate.

For an income exemption or preferential tax rate, the relevant amount is the exempt income multiplied by the applicable corporate income tax rate, or the preferential income multiplied by the difference between the applicable corporate income tax rate and the preferential tax rate.

Cap. The benefit of the SBTI safe harbour will be subject to a substance cap at 5.5% of the greater of: (i) eligible payroll costs, or (ii) eligible depreciation expenses on eligible tangible assets. Alternatively, if a five-year election is made for the jurisdiction, a cap equal to 1% of the book value of eligible tangible assets may apply.

Applicable Year. The SBTI safe harbour will apply to fiscal years beginning on or after January 1, 2026.

Simplified Effective Tax Rate (ETR) Safe Harbour

Requirement. The simplified ETR safe harbour will be available where an MNE group did not have a top-up tax or domestic top-up tax liability for a jurisdiction in every fiscal year beginning within 24 months before the first day of the relevant fiscal year.

Effect. Where the requirement is met, the MNE group may calculate its simplified ETR using simplified income and simplified taxes instead of the full GloBE income and adjusted covered taxes computations. Where the jurisdiction has a simplified ETR of at least 15% or a simplified loss, the top-up tax or domestic top-up tax in the jurisdiction will be deemed to be zero for the fiscal year.

Applicable Year. The simplified ETR safe harbour will apply to fiscal years beginning on or after December 31, 2026.

2. Reduction in the Effective Tax Rate Threshold under the Controlled Foreign Company Regime

Under Korea's Controlled Foreign Company (CFC) regime, the undistributed earnings of a foreign company in a low-tax jurisdiction may be treated as if those earnings had been distributed to its Korean shareholder and may therefore be taxed in the hands of that shareholder if certain prescribed conditions are met. One of the key conditions is that the foreign company's effective tax rate must not exceed a prescribed threshold, which is currently 17.5%, calculated as 70% of the highest marginal corporate income tax rate. The proposal would lower this effective tax rate threshold from 17.5% to 15%, thereby aligning the CFC regime with the minimum tax rate under the GloBE Rules. The other CFC conditions, including the ownership, control and substantive business activity tests, would remain unchanged. As a result, certain foreign companies with effective tax rates above 15% and up to 17.5%, which are currently within the scope of the CFC regime, may no longer be subject to the regime if the proposed amendment is enacted.

3. Clarification of the Scope of Non-Compliance with Transfer Pricing Documentation Requirements Subject to Fines

The proposed revision seeks to clarify the scope of administrative fines applicable to transfer pricing documentation requirements. Under the current rules, fines may be imposed where a taxpayer fails to submit the required documentation by the statutory deadline or submits false documentation. The proposed amendment clarifies that documentation containing material omissions or significant errors will also be treated as non-compliance and therefore subject to fines. As a result, fines may apply not only to non-submission or false submissions, but also to documentation that is materially incomplete or inaccurate. The change is intended to provide greater certainty regarding the circumstances in which fines may be imposed and to encourage the submission of complete and accurate transfer pricing documentation.

Tax Reform for Reinforcing Future Growth Engines and Regional Economic Growth

1. Introduction of a Domestic Production Tax Credit

To support the domestic production of strategically important products in sectors where Korea's domestic manufacturing bases remains relatively weak, the government has proposed a new domestic production tax credit. The proposed tax credit would provide corporate income tax and individual income tax benefits based on the production volumes of qualifying products that are directly produced and sold in Korea.

Eligibility Requirements. To qualify for the proposed domestic production tax credit, a Korean taxpayer, such as a domestic corporation, must directly manufacture and sell qualifying products in Korea. For this purpose, the domestic production requirements include: (i) performing key manufacturing processes in Korea and maintaining a prescribed minimum ratio of domestic expenditures to total qualifying production costs; and (ii) not claiming the integrated investment tax credit for business-use tangible assets directly used in domestic production. In addition, the domestic sales requirements include that: (i) the products must be supplied in Korea, subject to exceptions such as exports to be prescribed by the Presidential Decree, (ii) the products must be sold during the year of production or the following fiscal year, (iii) the products must not constitute used products, and (iv) where the products are sold to a related party, the taxpayer must submit prescribed supporting documentation demonstrating that the transaction was undertaken for bona fide business purposes.

Application Period. The proposed regime will apply to production and sales occurring in fiscal years beginning on or after January 1, 2027, and will remain available through December 31, 2036.

Qualifying Products. The proposed domestic production tax credit will apply to products in six sectors: solar power, wind power, secondary batteries, semiconductors, critical materials, and AI and robotics components. These sectors were selected based on three key criteria: strategic importance, future growth potential, and necessity. Specifically, (i) they are strategically important from the perspectives of the green transition and economic security; (ii) domestic production is necessary to maintain or strengthen competitiveness given their future growth potential; and (iii) the domestic production base for such products remains relatively weak. The specific list of qualifying products will be prescribed by the Presidential Decree.

Tax Credit Amount. The amount of the domestic production tax credit will be determined by multiplying the following three factors: (i) a base credit amount prescribed by the Presidential Decree, taking into account production costs and sales prices; (ii) a regional weighting factor, and (iii) a phase-out factor. To encourage regional investment, higher regional weighting factors will apply to production activities undertaken outside the Seoul metropolitan area. In addition, the phase-out factor will apply to the tax credit during the last three years of the regime, with the applicable rates reduced to 75%, 50%, and 25%, respectively, before the regime expires at the end of 2036.

Category (*)	Weighting Factor
Seoul Metropolitan Area	1.0
Provincial Metropolitan Cities and Designated Seoul Metropolitan Regions	1.1
Other Non-metropolitan Areas and Designated Provincial Metropolitan Cities	1.3
Other Designated Non-metropolitan Areas	1.5

(*) Detailed classifications of provincial metropolitan cities other than the Seoul metropolitan area and designated preferential areas will be prescribed by the Presidential Decree, taking into account factors such as distance from Seoul, population levels, and economic and social conditions.

Further, taxpayers claiming the domestic production tax credits may not claim certain other tax reductions or credits for the same fiscal year, including the integrated investment tax credit.

Tax Credit Limit. The annual credit will be limited to the lesser of: (i) 50% of qualifying production costs incurred during the relevant fiscal year, or (ii) 50% of the cumulative investment in business-use tangible assets directly used to manufacture qualifying products, reduced by any domestic production tax credits previously claimed. Any unused portion of the credit may be carried forward and utilized within the subsequent ten fiscal years.

Filing Procedures and Recordkeeping Requirements for Domestic Production Tax Credit. Taxpayers claiming the domestic production tax credit will be required to submit a written tax credit application to the competent district tax office when filing their tax return for the relevant fiscal year. In addition, taxpayers must retain supporting documentation, including records relating to production costs, production volumes, and sales volumes, for up to ten years after the expiration of the applicable tax credit period and submit such documentation upon request by the tax authorities. Detailed filing and documentation requirements will be specified by the Presidential Decree.

2. Adjustment of Deduction Limits for Environmentally Friendly Company Vehicles

The proposal would revise the annual tax deduction limits for depreciation and disposal losses relating to company vehicles. The annual deduction limit for electric and hydrogen-powered vehicles would increase from the current KRW 8 million to KRW 10 million per vehicle, while the limit for other vehicles will decrease from the current KRW 8 million to KRW 7 million per vehicle. This change is intended to promote the use of environmentally friendly vehicles. The proposed changes will apply to company vehicles newly acquired or leased on or after January 1, 2027.

3. Expansion of the Hydrogen Sector into the Future Energy Sector under National Strategic Technologies

The proposal seeks to expand the current hydrogen sector under Korea's national strategic technologies category into a broader future energy sector. As a result, tax incentives currently available for national strategic technologies may be extended to a wider range of next-generation energy technologies beyond hydrogen. The specific technologies eligible for the incentives will be prescribed by the Presidential Decree. This change is intended to support the development of advanced strategic industries and will apply to R&D expenditures incurred or investments made on or after January 1, 2027.

4. Preferential Tax Incentives for Regional R&D and Investment Activities

The proposal would introduce preferential tax treatment for R&D tax credits and integrated investment tax credits in order to support balanced regional development. Under the proposed rules, the applicable credit rate will be determined by multiplying the existing credit rate by a regional weighting factor, with higher factors applying to business operations located outside the Seoul metropolitan area. The existing credit rates range from 2% to 40% for R&D tax credits and from 1% to 30% for integrated investment tax credits. The proposed regional weighting factors are 1.0 for the Seoul metropolitan area, 1.1 for provincial metropolitan cities and designated Seoul metropolitan regions, 1.3 for other non-metropolitan areas and designated provincial metropolitan cities, and 1.5 for other designated non-metropolitan areas.

To apply the regional preferential treatment, taxpayers would be required to separately account for eligible activities by business location. In addition, the preferential credit rate for R&D tax credits would be subject to an overall cap of 50%. The proposed rules will apply to R&D expenditures incurred or investments made on or after January 1, 2027.

Reform of Tax Incentives and Preferential Tax Regimes

1. Increased Flat Tax Rate for Foreign Employees

Eligible foreign employees may currently elect to be taxed under a special tax regime that applies a flat tax rate of 19% (20.9% including local income tax) in lieu of the progressive individual income tax rates, which range from 6% to 45% (6.6% to 49.5% including local income tax). Foreign employees who elect this regime are generally not eligible for most tax exemptions, deductions, or tax credits and may apply the regime for up to 20 years from the commencement of their employment in Korea. This special tax regime was scheduled to expire at the end of the year. Without the proposed extension, foreign employees commencing employment in Korea on or after January 1, 2027, would not have been eligible to elect the regime.

Under the proposal, the flat tax rate would increase from 19% to 21% (23.1% including local income tax), while the application period of the regime would be extended through December 31, 2029. These proposed changes will apply to income arising on or after January 1, 2027.

2. Introduction of Applicability Periods for Specific Technologies and Facilities under New Growth and Source Technologies

To ensure that tax incentives remain aligned with technological developments and policy priorities, the proposed rules would introduce applicability periods for individual technologies and facilities classified as New Growth and Source Technologies or National Strategic Technologies, under which the continued eligibility of such technologies and facilities would be periodically reassessed.

R&D Tax Credit. Under the current rules, applicability periods are prescribed only at the technology category level rather than for individual technologies. Under the proposal, applicability periods would be introduced for specific technologies, with the expiration date determined based on the year in which the relevant technology was designated, as follows:

<table>
<tr><th rowspan="2">Year of Specific Technology Designation</th><th colspan="2">Applicability Period</th></tr>
<tr><th>Semiconductor</th><th>Other than Semiconductor</th></tr>
<tr><td>On or before 2017</td><td>Dec 31, 2027</td><td></td></tr>
<tr><td>2018-2020</td><td>Dec 31, 2028</td><td></td></tr>
<tr><td>2021</td><td>Dec 31, 2029</td><td rowspan="3">Dec 31, 2029</td></tr>
<tr><td>2022</td><td>Dec 31, 2030</td></tr>
<tr><td>2023 or later</td><td>Dec 31, 2031</td></tr>
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Integrated Investment Tax Credit. The proposed rules would introduce an applicability period through December 31, 2029, for commercialization facilities relating to new growth industries. In addition, applicability periods for specific commercialization facilities would be determined based on the year in which the relevant facility was designated, as follows:

Year of Specific Facility Designation	Applicability Period
On or before 2017	**Dec 31, 2027**
2018-2020	**Dec 31, 2028**
2021 or later	Dec 31, 2029

3. Revision of the Integrated Employment Tax Credit

The integrated employment tax credit is intended to encourage businesses to increase and maintain employment, particularly among certain categories of workers, including young workers, older workers, and persons with disabilities. The amount of the tax credit available for each increase in the number of qualifying full-time employees varies depending on the size of the employer. Small and medium-sized enterprises are generally eligible for the largest tax credits, whereas large companies are entitled to reduced tax credit amounts and may claim the credit only with respect to increases in the number of employees within these categories. For this purpose, Korean subsidiaries of multinational groups with worldwide consolidated assets exceeding KRW 10 trillion (approximately USD 7 billion) are generally classified as large companies.

Under the proposal, large companies would no longer be eligible for the integrated employment tax credit, even with respect to increases in the number of employees within the aforementioned categories. The revised rules will apply to tax credits claimed for fiscal years beginning on or after January 1, 2027.

Technical and Administrative Tax Reforms

1. Reform of the Treasury Share Taxation Regime

Following the amendments to the Korean Commercial Code, which characterize the acquisition of treasury shares as a capital transaction and require treasury shares to be cancelled upon acquisition, the proposal would align the tax treatment of treasury share transactions with their treatment under company law.

Deemed Dividend Treatment. Under the current rules, from a shareholder's perspective, the tax treatment of a disposal of shares to the domestic issuing company depends on whether the treasury shares are acquired for cancellation or for subsequent resale. Depending on the purpose of the acquisition, the shareholder's income may be treated either as deemed dividend income or as capital gains. The classification of such income may affect the applicable tax treatment, particularly for foreign shareholders, as different withholding tax rules apply to dividends and capital gains.

Under the proposed rules, where a domestic company acquires treasury shares from a shareholder, the excess of the consideration received by the shareholder over the acquisition cost of the shares will be treated as deemed dividend income, regardless of the purpose for which the treasury shares are acquired. The proposed rules will apply to treasury shares acquired on or after January 1, 2027. Treasury shares acquired before that date will remain subject to the current rules.

Gains and Losses from the Treasury Share Transaction. Under the current rules, although gains or losses arising from treasury share transactions are not recognized as profits or losses for accounting purposes, corresponding taxable gains or losses are recognized through book-to-tax adjustments.

Under the proposed rules, consistent with the treatment of treasury share transactions as capital transactions rather than taxable transactions, gains or losses arising from such transactions will not be included in the taxable income of the domestic issuing company for corporate income tax purposes. The proposed rules will apply to treasury shares disposed of on or after January 1, 2027.

2. Foreign Tax Credit on Qualified Domestic Minimum Top-up Tax

Under the current rules, foreign tax credits are generally available for taxes imposed on taxable income, surtaxes imposed on such taxes, etc., without explicitly including the Qualified Domestic Minimum Top-up Tax (QDMTT) among the taxes eligible for foreign tax credits. QDMTT is a domestic minimum top-up tax imposed by a jurisdiction when constituent entities of a multinational enterprise group located in that jurisdiction are subject to an effective tax rate below the 15% minimum rate under the GloBE Rules.

Under the proposed rules, QDMTT will be added to the list of creditable foreign taxes. By allowing QDMTT to qualify for foreign tax credits, the proposed rules will align with the OECD's global minimum tax framework and mitigate potential double taxation resulting from the application of QDMTT.

Contacts

Corporate Tax

Henry An
+82-2-3781-2594
henry.an@pwc.com

Michael Kim
+82-2-709-0707
michael.kim@pwc.com

Chang-Ho Jo
+82-2-3781-3264
changho.jo@pwc.com

Yun-Jung Yang
+82-2-3781-9278
yunjung.yang@pwc.com

Il-Gyu Cha
+82-2-3781-3173
il-gyu.cha@pwc.com

Young-Ok Kim
+82-2-709-7902
young-ok.kim@pwc.com

Robert Browell
+82-2-709-8896
robert.browell@pwc.com

Kyu-Young Han
+82-2-3781-3105
kyu-young.han@pwc.com

Jeong-Eun You
+82-2-709-8911
jeong-eun.you@pwc.com

Seung-Ryul Lee
+82-2-3781-2335
seung-ryul.lee@pwc.com

Ji-Young Yoon
+82-2-3781-9958
jiyoung.yoon@pwc.com

Hyun-Kyu Park
+82-2-3781-2301
hyun-yu.park@pwc.com

Se-Young Yoon
+82-2-3781-9096
se-young.yoon@pwc.com

Kyoung-Soon Lee
+82-3781-9982
kyoungsoon.lee@pwc.com

Paul (Eunho) Lee
+82-709-0413
paul.eh.lee@pwc.com

Transfer Pricing

Won-Yeob Chon
+82-2-3781-2599
won-yeob.chon@pwc.com

Young-Joo Kim
+82-2-709-4098
young-joo.kim@pwc.com

삼일회계법인

samil.com