Korean Tax Update

Samil Commentary

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Taxpayers Filing Reports of Overseas Financial Accounts Increase 16.6% from a Year Ago

The Threshold for Non-taxable Gain from Exercising Stock Options in Venture Businesses Would Be Increased to KRW50 Million in 2022

NTS Launches Investigation of Unfair Tax Evasion Practices

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Taxpayers Filing Reports of Overseas Financial Accounts Increase 16.6% from a Year Ago

The National Tax Service (NTS) announced that a total of 3,130 taxpayers reported a total balance of KRW59 trillion (KRW9.4 trillion for individuals and KRW49.6 trillion for corporations) held in accounts at foreign banks and financial institutions during 2020 by the due date (i.e., June 30, 2021). The number of taxpayers who filed the reports increased 16.6% from a year ago while the reporting amount declined 1.5% during this period. The increase in the number of such taxpayers was largely driven by the expanded scope of reporting obligations with the reporting threshold lowered in 2019 from KRW1 billion to KRW500 million. This increase was also attributed to improved public awareness of voluntary reporting and the NTS guidance on reporting overseas financial accounts. On the other hand, the NTS attributed the decline in the reporting amount to the decreased issuance of asset-backed securities under the low interest rate environment. The NTS will analyze and examine non-compliance with the foreign financial account reporting requirements by utilizing inter-governmental exchanges of financial information, etc. In addition, the NTS scrutiny will be focused on identifying suspicious offshore donations to children and young people and offshore tax evasion.

삼일회계법인

The Threshold for Tax-exempt Gains from Exercising Stock Options in Venture Businesses is Proposed to Be Increased to KRW50 Million in 2022

The Ministry of SMEs and Startups announced on September 30 its plan to expand tax benefits for gains from exercising stock options granted by venture businesses. Currently, gains from exercising such stock options are exempt from individual income tax to the extent of KRW30 million per year. The Ministry's plan calls for raising the threshold for tax-exempt gains to KRW50 million beginning from 2022. The Ministry also plans to prepare standard contracts and guidelines to facilitate the practical implementation of stock option plans in venture companies. To improve the method of unlisted share valuations, the Ministry will amend the Presidential Decree of the Act on Special Measures for the Promotion of Venture Businesses. In addition, even in the case of stock options granted at a lower price than the market price, the Ministry will consider applying a special tax treatment whereby employees do not pay income tax when they exercise stock options for shares but pay capital gains tax when they sell the shares. Currently, in case of certain qualified stock options granted by venture firms (subject to some conditions), employees may choose not to pay income tax at the time of exercise. This plan is part of efforts to provide an institutional framework for venture businesses to effectively use stock options to attract and retain talented employees.

NTS Launches Investigation of Unfair Tax Evasion Practices

The National Tax Service (NTS) has launched tax investigations on 74 taxpayers with an increased focus on income earned through online platform businesses. The latest NTS audit has also targeted certain professionals with work experience in government service. Specifically, the recent audit targets 16 social media influencers who deliberately evaded taxes through sponsorship platforms and 17 persons who sought to conceal their income earned through sharing economy platforms while operating unregistered shared lodging businesses. Audit targets also include those who have not paid their fair share of taxes, including 28 attorneys, certified tax accountants and other consultants who are highly paid based on their career experiences of working for government agencies; and 13 multi-property owners who bought a number of highly valuable real properties.

As part of these examinations, the NTS said there has been international exchanges of information with foreign tax authorities to obtain data on specific target groups rather than individual targets and analyzed overseas payments and settlement service data to identify new or irregular tax evasion practices using domestic as well as international online platforms. The NTS will continue to strengthen its capabilities to obtain and analyze domestic and foreign tax information in order to discover patterns of tax evasion in various economic and social sectors and collect taxes owed.

Korea's National Assembly Budget Office Publishes a Report Analyzing the Tax Reform Proposals for 2021

The National Assembly Budget Office has recently published a report on Korea's tax reform proposals for 2021 presenting an analysis and projections of the government budget and tax revenue. In the report, the Budget Office projects a KRW5.8 trillion decrease in tax revenue over the next five years, which is KRW1.3 trillion less than the level of reduction estimated by the government (KRW7.1 trillion). The recent analysis indicates that the government's tax reform bill for 2021 focuses on securing future growth engines, encouraging the recovery of job markets and promoting investment and consumption as measures responding to the post-pandemic situation. It also states that the reform bill addresses fiscal and tax policies to increase support for small and midsize enterprises and ordinary citizens. Further, the report presents an analysis of what should be taken into consideration in the process of reviewing tax reform proposals. They include: i) the implications of the tax reform proposals in terms of tax revenue expected and those who will ultimately bear the burden of taxes, ii) whether government spending was sufficiently streamlined, iii) increasing tax incentives for national strategic industrial technologies; and iv) a higher level of the income threshold for earned income tax credits.

Moreover, the report sets forth an evaluation of the government's tax reform bill for 2021 as summarized below:

- The government's reform bill addresses the need for continued fiscal support to ensure inclusive economic recovery and measures to facilitate investment to secure future growth engines.
- The recent trends show that the types of investments receiving the government's tax breaks are more likely to be research and development activities in high-tech industries, rather than simple physical facilities. In terms of the effectiveness of investment incentives, however, there is a concern that the complexity in institutional frameworks and economic inefficiency might increase or be intensified due to the reform bill that proposes to add national strategic technologies eligible for special tax treatments.
- In order to restore fiscal soundness harmed by the COVID-19 pandemic and ensure sustainable fiscal management, taxation should focus on its intrinsic function of securing more stable sources of fiscal revenues.

Rulings Update

Whether a late payment penalty would be exempt in case of the non-filing of gift tax return under the deemed gift tax provision

According to Article 45-5 of the Inheritance and Gift Tax Law (IGTL), where a related party corporation of a controlling shareholder, etc. is engaged in certain transactions prescribed under the IGTL with a specific corporation (e.g., a free supply of property or services by a related party corporation to a specific corporation), an 'amount of profits calculated pursuant to the IGTL shall be deemed to have been donated from the related party corporation to the controlling shareholder, etc. through the transactions' (the "deemed gift of profits") and be subject to gift tax on the controlling shareholder, etc. For this purpose, a specific corporation

refers to a corporation where a controlling shareholder, etc. directly or indirectly holds 30% or more of shares in the corporation.

Meanwhile, Article 47-4 of the Basic National Tax Law states that where a taxpayer underpays taxes or receives an excess refund of taxes by the statutory due date, a late payment penalty, calculated on a daily basis, shall be imposed. However, this Article further provides that a late payment penalty shall be exempt (limited to the period from the date following the statutory due date to the payment notice date) in cases where an amount of the deemed gift of profits under Articles 45-3 through 45-5 of the IGTL is changed due to the determination or reassessment of corporate income tax base and tax amount pursuant to Article 66 of the Corporate Income Tax Law (with some exceptions), among others.

In this case, a district tax office applied the rule for denial of unfair transactions between related parties, arguing that the related party corporation purchased products from the specific corporation at a higher price than the market price (the "transaction in question"), and assessed corporate income tax to the related party corporation for the difference from the market price. In addition, the tax office considered that the deemed gift of profits was made from the related party corporation to the controlling shareholder of the specific corporation through the transaction in question according to Article 45-5 of the IGTL, and it assessed gift tax to the controlling shareholder with a late payment penalty for the gift tax. The controlling shareholder (i.e., the appellant) filed an appeal with the Tax Tribunal against the tax office's assessment, asserting that the late payment penalty should be exempt on the basis that the deemed gift of profits was changed due to the reassessment of corporate income tax to its related party corporation.

The tax office took the position that the late payment penalty can be exempt only when a taxpayer originally filed a gift tax return by the statutory due date and as such, the penalty should not be exempt in this case since the appellant did not file a gift tax return by the original due. However, the Tax Tribunal decided against the tax office and held that the late payment penalty should be exempt if the deemed gift of profits occurred due to the determination or reassessment of corporate income tax base and tax amount, regardless of whether there was a gift tax return originally filed by the taxpayer or the related gift tax assessed by the tax authority. The Tribunal further ruled that the late payment penalty should be exempt even in the case where the deemed gift of profits is changed due to the determination or reassessment of corporate income tax to the related party corporation as well as to the specific corporation. *(Joshim 2021seo782, 2021. 10. 21.)*

This case is considered important in that it is the first case that ruled that, although a taxpayer failed to file the deemed gift of profits under the deemed gift tax provisions with the tax office, the late payment penalty can be exempt in cases where such profits are increased due to the determination or reassessment of corporate income tax to the specific corporation or to the related party corporation of the taxpayer.

How to determine the holding period of shares transferred via a tax qualified merger in applying the dividend received deduction rule

Based on Article 18-3 of the Corporate Income Tax Law, the dividend received deduction (DRD) rule provides that where a Korean holding company under relevant laws receives

dividends from its subsidiary whose shares have been held by the holding company for at least three months as of the dividend record date, a certain portion of the dividends received by the holding company shall be excluded from its taxable income for corporate income tax purposes.

In this ruling, the Korean company owning several subsidiaries was merged into the Korean holding company with the holding company as the surviving company via a tax qualified spin-off whereby the subsidiary shares held by the Korean dissolving company were transferred to and acquired by the holding company. The holding company subsequently received dividends from one of the subsidiaries whose shares were acquired on the merger. In computing the holding period of shares, the holding company in question was deemed to have held the subsidiary shares for more than three months if the holding period began from the acquisition date of the subsidiary shares by the dissolving company, but for less than three months if the period started from the registration date of the merger between the holding company and the dissolving company.

In applying the DRD rule for the dividends received by the holding company, the issue in this case was whether the holding period for the subsidiary shares being transferred to the holding company via a tax qualified merger should be calculated starting from the share acquisition date of the dissolving company or the merger registration date. Regarding this, the National Tax Service (NTS) replied that whether the shares deriving dividends were acquired within three months before the dividend record date should be determined based on the share acquisition date of the dissolving company. (*Advance Ruling-2021-Beobryeonghaeseokbeobin-1167, 2021. 10. 12.*)

In previous NTS rulings, it was interpreted that the holding period of shares transferred to a new spun-off entity from an existing entity via a tax qualified spilt-off should be calculated based on the share acquisition date of the existing entity. (*Corporate Taxation Division-103, 2010.2.2, etc.)* It may therefore be necessary to consider the previous interpretation in addition to the recent NTS advance ruling.

A short YouTube video on one of the topics in the latest issue is available on the Samil PwC YouTube Channel link. →PwC Korea YouTube Channel

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