

Setting up your Business in Republic of Korea

Issues to consider



The Republic of Korea (ROK) is the world's 12th largest economy and experienced 2.1 percent growth in 2012. Despite market jitters and slowing growth, the ROK has so far weathered the global economic uncertainty and continues to remain a generally favorable destination for foreign investment. Also, the World Bank has rated the ROK as the 7th country in the world and 3rd country in the Asia for ease of doing business.

However there are a number of issues which you must consider when you are looking to set up your business in ROK. This document takes you through some of the common questions we come across and gives you practical information about the issues you need to consider.

What type of Business Structure should we use?

There are advantages and disadvantages to all of them, and there is no one correct answer, it's all dependent on your specific business circumstances and needs. A brief overview of the main structures is below:

Establishment (a branch of your overseas business)

- Not a separate legal entity but an extension of the overseas parent company
- No limited liability or ring-fencing of the ROK operations
- If have a permanent establishment in ROK then profits from this PE are liable to ROK Corporation tax
- Must file **parent company accounts**, prepared under ROK Company Law, at Companies House for public inspection, even if these are not made publically available overseas

A foreign company appoints the representative of Korean branch. It also complies with the establishment procedure of a branch under the provision of the Foreign Exchange Control Act and requires the registration of a court. A branch can operate its business activities to make earnings in Korea. Therefore, the same corporate tax rate as that of a common Korean company is applied to the branch's earnings made from the business operating in Korea.

Limited Company:

- Provides limited liability and ring-fencing to ROK operations
- Gives a perception of a local business, with longevity
- Corporation tax to be paid on company profits
- Accounts require auditing if in **group as (1) a whole Gross Assets \geq ₩10,000m or (2) a whole Gross Assets \geq ₩7,000m & Liabilities \geq ₩7,000m or (3) a whole Gross Assets \geq ₩7,000m & the number of employees \geq 300**

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Limited Liability Partnership:

- Members (partners) have limited liability
- Profits are allocated to members who then pay Income Tax on these profits personally
- The tax residence of the member, and where the profits in the LLP originated will determine in what jurisdiction and how these profits are taxed

How much Corporation Tax will the business pay?

Current Corporation Tax rates in ROK (sum of national and local) are:

Tax rate (%)		Taxable profit (₩)
Small co rate	11	0 – 200,000,000
Intermediate rate	22	200,000,001 – 20,000,000,000
Full rate	24.2	Over 20,000,000,000

(NB: rates are for the tax year to 31/Dec/2014)

What if we make cross-border transactions between group companies?

ROK is the 29th member of the OECD. The Korean transfer pricing regulations are largely based on the OECD Guidelines. ROK follows internationally recognized **Transfer Pricing (TP)** rules where cross-border trading and financial transactions between affiliated entities have to be conducted on an arm’s length basis. The price and terms should be the same as if the transactions had been between completely independent parties.

Typical transactions between affiliated entities that are covered by TP regulations are:

- Sale and purchase of goods
- Provision of management services
- Property rental charges
- Transfer of intangible assets e.g. trademarks, patents
- Sharing of knowledge, expertise, business contacts etc.
- Provision of financial support e.g. inter-group loans and charging a “market” interest on loans

A business will need to prepare a Transfer Pricing Report proving the arm’s length basis of transactions. The report will include a functional and risk analysis, analysis of the adopted pricing model and benchmarking of the arm’s length basis.

Although there is no concept of immateriality (or a de minimis transaction) in the Korean

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regulations, a taxpayer is not required to submit the Declaration of Transfer Pricing Method form at the time of filing the corporate income tax return if the taxpayer is engaged in cross-border inter-company goods (or service) transactions that accumulatively amount to below Korean won (KRW) 5 billion (KRW 500 million for service transactions) or amount to below KRW 1 billion (KRW 100 million for service transactions) per transaction party. Likewise, the taxpayer is not required to submit a Summary of Income Statements of Overseas Affiliates if it is engaged in cross-border inter-company goods (or service) transactions that amount to below KRW 1 billion (KRW 100 million for service transactions) per transaction party or if the taxpayer has submitted a list of overseas affiliates and their summarized financial statements in accordance with the Corporate Income Tax Law (CITL).

However even if an entity is exempt from the ROK's transfer pricing regime it may fall under the scrutiny of the other international tax jurisdictions where it transacts. There may also be other tax regulations which ensure transactions are undertaken at a commercial value.

What Employment Taxes and Social Security will need to be paid?

If an individual is resident in ROK then they are subject to ROK tax laws. Any necessary expenses are deducted from aggregate income amounts. Tax is imposed on the adjusted incomes by applying the aggregate tax rate of between 6~35%.

We would advise any new entrant to ROK or person who spends time working in ROK to take professional advice to determine whether they are ROK tax resident.

Current Personal Income Tax rates in ROK(sum of national and local) are:

Band of income (₩)	Tax rate (%)
0 – 12,000,000	6.60
12,000,000 – 46,000,000	16.50
46,000,000 – 88,000,000	26.40
88,000,000 – 300,000,000	38.50
Over 300,000,000	41.80

(NB: rates are for the tax year to 31/Dec/2013)

Employers and employees also have to pay ROK 4 social securities, which is called “four major social insurance”



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Current Social Security rates of Incomes are:

4 Social Securities	National Pension	Health Insurance & Long term Medical Care Insurance	Employment	Industrial Disaster Compensation Insurance
Employer	4.5%	3.09%	0.80%	
Employee	4.5%	3.09%	0.55%	0.6~3.4%
Total	9.0%	6.18%	1.35%	0.6~3.4%

NB: (rates are for the tax year to 31/Dec/12)

It is the employers’ legal responsibility to pay over employee’s tax and social security deductions to the ROK tax authorities.

What is Value Added Tax (VAT) and should the business be registered?

VAT is a “goods and services tax” on supplies made, the standard rate of which is 10%. If a business makes taxable supplies in excess of ₩ 48,000,000 in any 12 months then it **MUST** be registered for VAT.

There are three types of supply

- Taxable – must charge VAT on supplies, can reclaim input VAT
- Exempt – cannot charge VAT nor reclaim input VAT
- Outside the scope – not in the ROK VAT system

The supply of most types of goods and services in ROK would be classed as Taxable supplies. However when these supplies are made to companies which are outside of the ROK advice needs to be sought as to what rate of VAT, if any, to use.

Can we provide Share Option plans to our staff?

Many companies see Share Option plans as being an important way of attracting, motivating and retaining key staff.

ROK has a number of “approved” Share Option plans which give tax benefits to employees and employers alike and it is often possible to adapt an overseas stock option plan to fit into one of these “approved” plans.

However this is a very technically complex area and careful planning needs to be undertaken as soon as share option plans are being considered for implementation in ROK.



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How else can we compensate our employees?

ROK has a very comprehensive range of compensation and benefit options available for companies to offer their employees.

Pensions, private medical insurance, life and disability cover are now commonplace benefits provided by many ROK businesses to their workforce.

Flexible benefit packages are also gaining in popularity, giving employees options on how they wish to “spend” their benefits allowance; which can range from “purchasing” additional holiday entitlement to obtaining full family medical cover.

To discuss your requirements please contact the International Office on +44 (0) 1245 449266 or email us directly.

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