



# Newsletter

April 2007

*This newsletter is prepared by Horwath Choongjung (Choongjung Accounting Corp.) and intended to provide foreign investors with an update on tax law changes in Korea and other related subjects of special interests to foreign investors. The information provided herein should not form a basis of any decision as to a particular course of action, nor should it be relied upon as a substitute for a detailed advice in individual cases.*

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*Please contact any of the following individuals with any inquiries or comments.*

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*(You may find this newsletter and other items of interest at <http://www.horwath.co.kr>)*

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## Horwath Choongjung News

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### **Gyeonggi Provincial Government Office Appointed Horwath Choongjung as a Professional Firm of Accounting and Taxation for Foreigners and Foreign Invested Companies**

On February 8, 2007, Gyeonggi Provincial Government Office hosted an open competition for professional consultative companies to construct the supporting systems for foreigners and foreign invested companies, and Horwath Choongjung Accounting Corp. (“Horwath Choongjung”) was selected as one of the professional firms that provide accounting and taxation services. Based on the partnership with Gyeonggi Province, Horwath Choongjung is to provide professional services including audit and assurance, taxation, accounting and business advisory services to the foreign invested companies in Gyeonggi Province and Gyeonggi Province itself for the next 3 years. The agreement signing ceremony was held on March 9, 2007 between Mr. M. S. Kim, the governor of Gyeonggi Province, and Mr. H. J. Hwang, the managing partner of Horwath Choongjung.



## Horwath Choongjung News

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### **DAEDEOK INNOPOLIS Nominated Horwath Choongjung as the Professional Consulting Firm for the Ventures in its Boundary**

On March 2, 2007, Horwath Choongjung was nominated by the DAEDEOK INNOPOLIS (a special industrial zone designated for research and development) as one of the professional consulting firms which will provide professional consulting services, including consultations on accounting, finance, IPO, M&A, etc., to the small and medium enterprises and the new startups in the DAEDEOK INNOPOLIS which are faced with managerial difficulties in doing business.

Horwath Choongjung will identify problems and set directions by analyzing some of the most common difficulties experienced by the small and medium enterprises and venture companies located in DAEDEOK INNOPOLIS, and provide professional consulting services to them to enhance their competitiveness and sustainable growth.

### **Horwath Choongjung Opened a New Branch Office in Daegu**

Horwath Choongjung established and opened a new Branch Office in Daegu on April 2, 2007. Horwath Choongjung Daegu Branch Office will offer to its clients a full range of professional services including audit and assurance, taxation and professional business advisory services such as consultation services related to IPO and M&A, domestic/foreign investment inducement, venture/company setup, outbound investment, etc.

The Daegu Branch Office is headed by Mr. Chang-Hoon Lee, a former Partner of Ernst & Young Korea (Hanyoung). The Office Opening Reception was held on April 6, 2007 at the Daegu Branch office located at the 15th Floor, Hosoo Bldg (Woorideul Hospital Bldg), 50-3, Dongin-dong 2-ga, Jung-gu, Daegu (Tel: 053-212-6500).

### **The Korea Tax Times Carried a Featured Article on Horwath Choongjung**

The Korea Tax Times (Hankuk Sejung Shinmoon) carried an article about an interview with Mr. Heung Ju Hwang, Managing Partner of Horwath Choongjung, on March 23, 2007. This article introduced the process how Horwath Choongjung was selected as the professional consultative firm for foreign-invested companies by Gyeonggi Provincial Government Office, the profiles, major clients, good reputation, and strengths of Horwath Choongjung.

## Tax Law Changes – Presidential Decree

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We summarize below some of the major changes to keep you up-to-date on tax law changes (Presidential Decree) in Korea. Most of the tax law changes we discuss below came into force effective from the fiscal year starting (or for payments/investments made or income earned) on or after January 1, 2007 unless indicated otherwise.

1. **Rights of Filing Amended Tax Return Claiming Refund of Taxes Withheld Are Granted to Non-residents as well**

Under the revised tax law of Korea, non-resident taxpayers and foreign corporations (defined), who have borne taxes through withholding by a payer, shall be allowed to file tax returns claiming refunds of taxes withheld within 3 years.

2. **Judgment Criteria for Determination of Unfair Transactions between the Specially Related Parties Is Supplemented**

Under the revised Article 88 (3) of the Presidential Decree of the Corporation Tax Law (“CTL”) of Korea and Article 98 (2) of the Presidential Decree of the Individual Income Tax Law of Korea, the transactions between the specially related parties shall be regarded as being unfair if the difference between the fair market value and the consideration of the transactions is more than 5% of the fair market value or more than Won 300 million. This tax law changes became effective on or after February 28, 2007.

3. **Introduction of Re-review Procedure Before Making Final Decision on Tax Exemption Applications for High Technology and Industry Support Business**

To enhance transparency and fairness in review process of tax exemption application with relation to high technology and industry support businesses under Paragraph 2, Article 116-3 of the Presidential Decree of the Special Tax Treatment Control Law of Korea, an applicant may request a second review of the application by submitting supplemental documents, after receiving a notice of disqualification for tax exemption from the first review. This tax law changes became effective on or after February 28, 2007.

4. **Discount Offered after Provision of Goods or Services Excluded from the Value-added Tax (VAT) Base**

Discount offered after providing goods or services shall be excluded from a VAT base under Article 13 (3) of the revised VAT Law of Korea.

## Bilateral Tax Treaty Development

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### 1. Tax Treaties with Albania and Venezuela Took Effect

#### (1) Albania - Korea Tax Treaty

The tax treaty entered by and between Albania and Korea on May 17, 2006 came into force on January 13, 2007. According to the tax treaty, withholding taxes (including resident surtax) are limited to 10% for interest income, certain dividend income, and royalties. Regarding dividend income, the 5% withholding tax rate shall be applied on gross dividend income if the beneficial owner is a company (other than a partnership) which holds directly at least 25% of the capital of the company paying the dividends and in all other cases, the 10% withholding tax rate shall be applied.

The limited withholding tax rates prescribed in the treaty shall be applied on or after January 1, 2008, and the relevant articles in the treaty on other incomes such as real estate income and business income shall be applied from the calendar year starting on or after January 1, 2008.

#### (2) Venezuela - Korea Tax Treaty

The tax treaty between Venezuela and Korea came into force on January 15, 2007. Under the treaty, generally, the taxes withheld at source shall not exceed 10% (excluding resident surtax) for interest income, dividend income and royalties. The limited withholding tax rates shall be applied on or after January 1, 2008. Also, the relevant articles under the treaty on other incomes such as real estate income and business income shall be applied from the calendar year on or after January 1, 2008.

However, there are some exceptional cases of applying the 5% limited withholding tax rate. For interest income, if a recipient of interest income is a bank as a beneficial owner, only 5% of the interest income shall be withheld. Regarding dividend income, the 5% withholding tax rate shall be applied if the beneficial owner is a company (other than a partnership) which holds directly at least 10% of the capital of the company paying the dividend. For royalty income, 5% of the royalties shall be withheld provided that the royalties are paid for the use of, or the right to use, industrial, commercial, or scientific equipment.

## New Rulings

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### 1. Income Classification of Consideration for Software

The National Tax Service of Korea (“NTS”) issued a new ruling (*Seomyon 2team-342, 2007.2.26*) that in the case where a Korean corporation receives master CDs from a Japanese corporation which does not have a permanent establishment in Korea and pays consideration according to the number of the master CDs copied, such consideration shall be classified as royalties under Article 12 of the tax treaty between Japan and Korea and Article 93 of the CTL. Therefore, the taxes on such royalty payment shall be withheld according to the said tax treaty and the CTL.

However, in the case where a software is ready to sell in the market as a product and cannot be altered and /or transformed additionally, and the end-users have the right to use the software permanently without additional payment, the consideration for the software shall not be considered as royalties under Article 12 of the said tax treaty and Paragraph 9, Article 93 of the CTL.

### 2. Taxation on Payment Guarantee Transaction

A new ruling was issued by the NTS that if a Korean corporation provides a payment guarantee by opening a stand-by L/C for its Chinese subsidiary (which is an overseas specially related party under Article 2 of the International Tax Coordination Law (“ITCL”) of Korea), the payment guarantee transaction concerned shall be classified as an international transaction under Paragraph 1-1, Article 2 of the ITCL and subject to the Korean taxes based on an arm’s length principle (*Seomyon 2team-255, 2007.2.6*).

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