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Global Minimum Tax in Korea: Implementation Upcoming

Korea recently published new regulations containing detailed implementation guidance in regard to Global Minimum Tax (OECD Pillar Two). The new regulations are published in the Presidential Decrees to the International Tax Coordination Law and are effective January 1st, 2024. In this newsletter, Lee & Ko's International Tax Team provides an update on the status of the latest domestic implementation guidance and differences from the OECD Pillar Two, implications for multinationals in Korea, and timetable for implementation of IIR, UTPR and the Transitional Safe Harbours, among others.

With the top-up tax aspect of the OECD Pillar Two Global Minimum Tax (**GMT**) set to take effect in Korea from January 1, 2024 onwards, the Lee & Ko team reviews the latest status of domestic GMT legislation and its implementation, and discusses the implications for multinationals operating in Korea.

1. *GMT in Korea – a Short History*

The OECD released its Pillar Two Model Rules (the **OECD Model Rules**) on December 20, 2021, and in the same month, Korea's Ministry of Economy and Finance (**MOEF**) announced that work would begin on drafting amendments to domestic legislation in order to incorporate the OECD Model Rules into Korean tax law.

In July 2022, a draft of the revisions was published by the MOEF, with which the OECD Model Rules could be incorporated into the International Tax Coordination Law (**ITCL**). The MOEF initially proposed that both the income inclusion rule (**IIR**) and undertaxed payments rule (**UTPR**) would take effect from January 1, 2024. However, since no other country in the world at that time was proposing to bring the UTPR into effect from 2024, there was widespread unease amongst in-scope Korean companies at the prospect of Korea being the first country in the world to implement the UTPR.

It therefore came as no surprise when in July 2023 the MOEF published a further revised draft of the ITCL, which postponed the introduction of the UTPR by one year in Korea, such that it is now scheduled to take effect from January 1, 2025 (with the IIR still scheduled to come into effect on January 1, 2024). This is in line with the implementation timeline in many other countries.

More recently still, on November 9, 2023, the relevant Presidential Decree was published, which contains more detailed implementing regulations that have been introduced by the OECD through a series of

administrative guidelines after the initial legislation of the GMT in Korea in July 2022. This Presidential Decree is scheduled to take effect on January 1, 2024.

2. *Korean v. OECD Rules*

Similar to the UK and EU, Korea has re-drafted the OECD Model Rules and then inserted them into its domestic tax legislation, and more specifically into the ITCL. By contrast, some countries, such as Switzerland, have incorporated the OECD Model Rules into their domestic legislation by way of a reference to the OECD Model Rules.

Generally speaking, the amended Korean legislation closely mirrors the OECD Model Rules, as it should, due to the importance of consistent interpretation and implementation by participating jurisdictions under the so called 'Common Approach'. The Korean GMT rules are now contained within Chapter 5 of ITCL, in Articles 60-86. Key provisions include:

- the threshold for a multinational group to be in-scope (Art. 62(1));
- excluded entities (Art. 62(3));
- the IIR (Art. 72);
- the UTPR (Art. 73); and
- the de minimis exclusion (Art. 74(1)).

Prior to the amendment, Chapter 5 of the ITCL contained penalty provisions, but the penalty provisions have now been pushed back such that they constitute Chapter 6 of the ITCL (Art. 87 – 91).

The Korean version of the GMT legislation as contained within the ITCL is not self-contained legislation, but contains frequent references to the Presidential Decree. The Presidential Decree, released on November 9, 2023, contains more granular or procedural detail about how the GMT rules are to be implemented in Korea, some of the details of which we set out below.

There are three key charging concepts in the OECD Model Rules, the first two of which are present in Korea's domestic GMT rules, namely: the IIR, the UTPR, and the domestic override, also known as the Qualified Domestic Minimum Top-up Tax or 'QDMTT'. Unlike the IIR and UTPR, Korea has yet to adopt the QDMTT, partly because Korea already has an unqualified minimum tax regime in place that requires an Effective Tax Rate (**ETR**) of at least 17%.

Other features of the Korean domestic GMT regime, such as the EUR 750 million threshold for the multinational group to be in-scope, the types of entities excluded from the regime, and the de minimis exclusion, are all broadly the same as the equivalent concepts in the OECD Model Rules.

3. *Ultimate Parent Entities (**UPEs**) in Korea – GMT Impact*

For UPEs in Korea, it will first be necessary to determine whether the UPE is part of a multinational group that is within the scope of the Korean GMT rules.

The rules apply to entities which are part of a multinational group of entities, referred to as Constituent Entities (**CEs**), when the annual consolidated revenues of the multinational group are over EUR 750 million in at least two of the four fiscal years immediately preceding the fiscal year being tested. In addition to the revenue threshold, the GMT rules only apply to entities that are not specifically prescribed as 'Excluded Entities' under the rules (excluded entities include governmental entities, pension funds, international or non-profit organizations, or investment funds which are a UPE).

After determining that the rules apply, it is then necessary to perform fairly complex calculations, on an entity-by-entity and jurisdiction-by-jurisdiction basis, to determine whether the ETR is lower than 15% in any jurisdiction where the CEs of the in-scope multinational group are located.

If the ETR is lower than 15% for any CE of a multinational group, then the IIR is activated and 'top-up tax' needs to be paid by the UPE in the jurisdiction of the UPE, in proportion to the UPE's ownership interests in the CE that is subject to an ETR of less than 15%. To the extent that the CE with a low ETR is owned by a UPE in Korea, the 'backstop rule', i.e. the UTPR, will not apply. This is because the UTPR only applies where the under-taxed entity is held through a chain of ownership that does not result in income being taxed under the IIR; but since Korea has implemented the GMT rules, whenever the UPE of an undertaxed CE is located in Korea, then under-taxed income will be taxed under the IIR in Korea.

As far as domestic compliance in Korea is concerned, all domestic CEs that are part of a multinational group will have to submit to their local tax office in Korea: (i) a Global Anti-Base Erosion (**GloBE**) Information Return; and (ii) a Top-up Tax Allocation Return. During the first year of application, these reports will have to be submitted within 18 months from the end of the year to which the reports apply, and thereafter, within 15 months. In other words, the first such reports will need to be submitted in Korea by June 30, 2026, in respect of the business year January 1, 2024 – December 31, 2024.

4. *Transitional Safe Harbours*

Korea's GMT rules, following the OECD Model Rules, contain transitional CbCR Safe Harbour provisions that will apply to business years beginning on or before December 31, 2026, and ending on or before June 30, 2028.

The safe harbour conditions involve simpler calculations, derived from a smaller pool of data, as compared with the default calculation methods set out in the GMT rules. Also, the data that is required under the safe harbour conditions is for the most part already available.

The safe harbour conditions set out three different routes by which the top-up tax arising from a specific jurisdiction will be deemed to be nil, even if some top-up tax would have been due by operation of the regular GMT rules. Specifically, if any of the three following conditions are satisfied, then the top-up tax in that jurisdiction will be deemed to be nil:

(1) *De Minimis Condition*: in respect of all CEs in a certain jurisdiction, the jurisdiction has: (i) average revenues of less than EUR 10 million; and (ii) a profit (loss) before income tax (**PBT**) of less than EUR 1 million; or

(2) *Simplified ETR test*: a simplified version of the ETR calculation, which should be calculated by dividing the income tax expense accrued by the profit before income tax, results in an ETR of less than 15% in 2024, 16% in 2025, or 17% in 2026; or

(3) *Routine Profits test*: the PBT in respect of all CEs in a certain jurisdiction is smaller than or equal to the amount of the Substance-based Income Exclusion (or substance carve-out), which is equal to 10% of qualified payroll costs and 8% of qualified tangible assets, with these carve-out percentages declining to 5% over time.

Please do not hesitate to contact us if you have any further questions or queries about any of the above.