

# Activity Report 2014

Joint Working Group (JWG)

August 28, 2015

# Back-ground

- Surveys on audits conducted by
  - AMCHAM
  - ECCK
  - KGCCI
  - SJC
- Joint working group on audits suggested to NTS Commissioner in 03/2014
- Kick off Joint Working Group in 06/2014

# Participants

- Representatives from NTS
- Chamber nominated industry experts
- Chamber representatives
- Tax experts

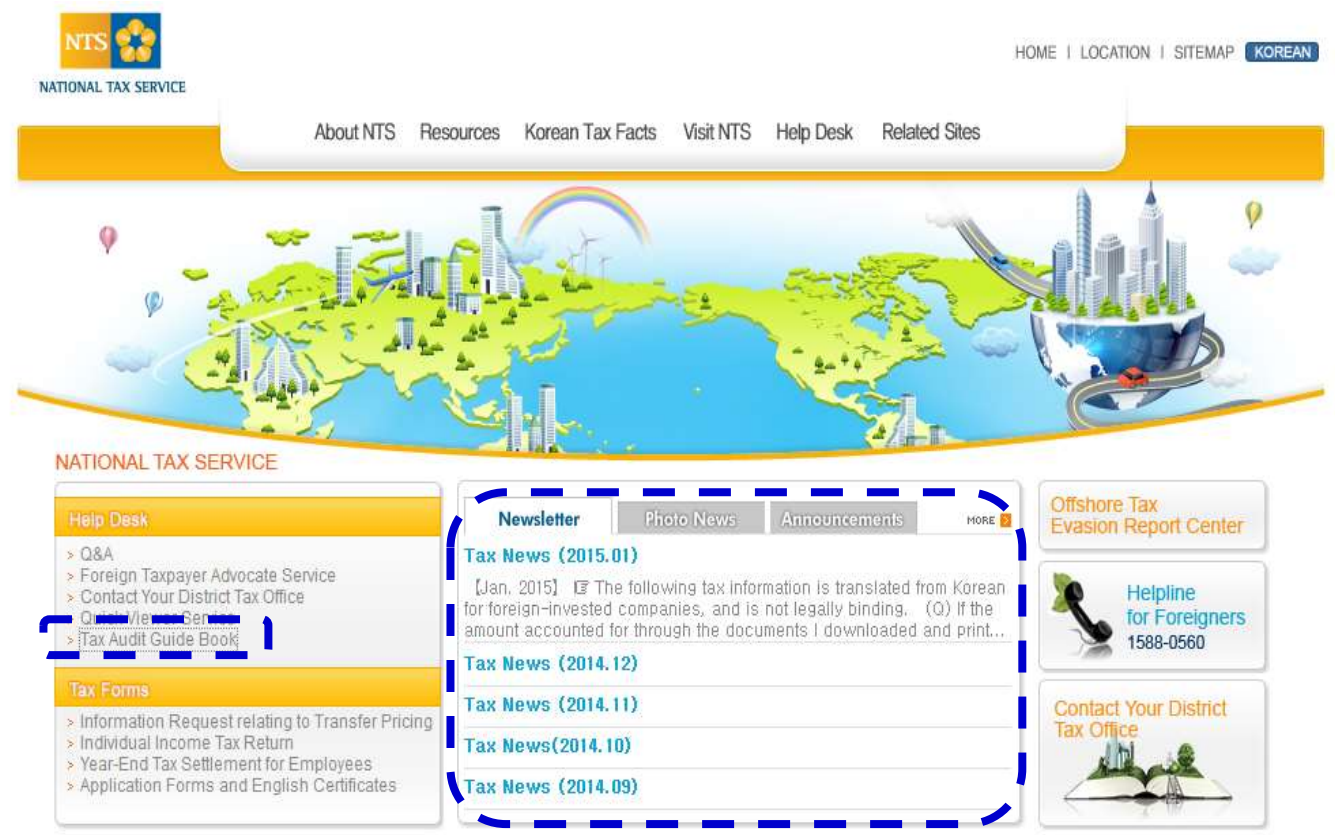
# Facts

Established 06/2014

Target: Improve mutually tax audit procedures

# Communication / Information

NTS launched various initiatives to provide to the foreign business community adequate and in time information via.....



# JWG Activity Report 2014

## NTS Services



# Publication

NTS Newsletters in English to disseminate information

Please click [here](#) to access

【Jan. 2015】

☞ The following tax information is translated from Korean for foreign-invested companies, and is not legally binding.

(Q) If the amount accounted for through the documents I downloaded and printed out from the NTS Simplified Year-end Tax Settlement Service website is less than the actual amount I spent at medical institutions, how can I get tax credit for those unaccounted expenses?

(A) If the NTS Simplified Year-end Tax Settlement Service website does not cover all or has omitted some of your medical expenses, you can get your tax credit by asking for supporting documents (sales receipt, etc.) from individual hospitals or pharmacies, and entering that amount in the "Other Data" item in your report of exemption & deduction from wage&salary income form. The income deductions claims form should be submitted to your employer.

(Q) How do I calculate the amount of wage & salary income of an employee paid in foreign currency?

(A) The amount of wage & salary income of an employee paid in foreign currency shall be calculated follows:

# JWG Activity Report 2014

## NTS Services



This tax audit guide book explains the audit process in an easy-to-understand manner

Periodic audit

Non-Periodic audit

## Publication

Handbooks published on

- Periodical Audit
- Non-periodical Audit

Please click [here](#) to access

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### Forms

1. Tax Audit Postponement Request
2. Request to Change Audit Venue
3. Tax Audit Postponement Request
4. Power of Attorney for Tax Representation
5. Request to Suspend or Extend the Audit
6. Request for Early Decision
7. Request for Tax Deferment
8. Statement of Exemptions and Filing Status for Deferment of Collection of National and Local Taxes, etc.
9. Petition for Pre-Assessment Review
10. Petition for Pre-Assessment Review(for National Tax Service Use)
11. Form for Filing an Objection
12. Petition for Examination
13. Petition for Judgment
14. Customer Evaluation Check List



## Issue: Reconciliation of Tax and Customs Audit Results

Audit procedures for tax and customs audits need to be reconciled. It is from our point of view difficult to understand and that due to transfer price adjustment respectively lowering of import prices the taxable income is adjusted to determine tax liabilities, interests and penalties but on the other hand not offset with import prices and the respective custom duties. Additionally, financial adjustments having impact on taxes and / or custom duties should be able to off-set. Therefore, actual reconciliations should be made practically and actively according to the enacted reconciliation regulations of the corporate income tax law and the customs law. Furthermore the theoretically existing reconciliation and appeal procedures in case of conflicting assessments by tax and customs authorities should become more effective, as they are an important means to create confidence in fair and equal treatment for foreign investors.

## Response: Open

**Comment by Chambers:** The Chambers acknowledge that this area is a difficult one, involving not only the NTS but also the cooperation of the KCS. However, because it is so difficult to resolve but yet so greatly impacts many taxpayers, the Chambers urge the NTS and the KCS to continue to seek a fair and practical resolution to this issue.

**Comment by NTS:** Since Jan. 2015, advance arrangement program between transfer pricing and customs valuation has been effective. NTS and KCS currently have discussed on how to stimulate the program so far. NTS delivered a detailed explanation on the program and believes that the program will help to eliminate uncertainty in taxation.

## Issue: Disclosure of Comparables

Korea is to adhere to OECD guidelines and the Korean International Tax Coordination Law. Therefore, at tax audits comparables are to be disclosed to the company being audited. Korea as member of the OECD has agreed to follow internationally agreed rules and procedures regarding transfer pricing. A core element of these rules are the criteria according to which comparables are allowed to be selected and used for TP assessments. Examples for such criteria are the restriction to the use of 3rd party comparables only, no inter-period comparables etc. It has been experienced by member companies that Korean tax auditors were not ready to accept these restrictions.

## Response: Already Implemented

In order to determine arm's length price at TP audits, the NTS complies with OECD Transfer Pricing Guidelines. Such efforts include a disclosure of comparables to taxpayers and a collection of taxpayer opinion.



## Issue: Reliance on/Application of Prior TP Audit Results

Audit teams are in some cases coming to a different judgment than auditors at a previous audit and accordingly request profit adjustments leading to tax liabilities and penalties. It is our opinion that audit teams should acknowledge the decisions made by previous audit teams; definitely there should be neither penalties nor interests imposed as long as the previous auditor's recommendation is in line with existing rules and regulations. Unless there have been significant changes in the business model of the company or the legislation, agreed or imposed audit results should be binding for the future. This would not only give companies more security in their efforts to be compliant, but also would enable the respective partner-government to accept the audit outcome. We believe that this would also be to the benefit of Korea by avoiding conflicts with foreign authorities and reduce the number of MAPs.

## Response: Addressed

Previous audit decision may be changed depending on different facts and circumstances (e.g., changes in organizational structure, function & risk) or law amendments. However, the NTS will deliver sufficient instructions for auditors to explain why they have to change the audit decision.

## Issue: Written Explanation of Audit Assessments

The calculation of a tax payable needs to be transparent, predictable and logically understandable; thus internal harmonized procedures needs to be in place. The JWGC wishes that the procedures applied are transparent and appropriately explained to the management of the audited company. It would be wished to have the possibility to have a written explanation of the rationales of re-assessment by Tax audit team.

## Response: Already Implemented

Certain programs are already in operation (e.g., Interim Explanation Program, Tax Consultation Day) to explain results of tax audit to auditee. In particular, the NTS revised a form attached to [Notice on Tax Audit Result] to inform taxpayer of tax types, taxable period, relevant statutory provisions and whether the auditee pays penalty taxes for unlawful act.

## Issue: Employee Interviews During Audit

Auditors have to conduct interviews with company employees in order to get a clear picture on various areas. If auditors present the interview subjects to audited companies before the interviews to employees to have enough time to prepare well, the interview would be much more helpful and efficient for both parties.

## Response: Addressed

The NTS will provide taxpayers with preparatory time within the availability of audit period where an interview is to be conducted. The NTS will deliver sufficient instructions for auditors to have a proper and appropriate attitude during the interview process.

## Issue: Periodic and Non-periodic Audits

The procedures for regular audits are in general quite clear; which is not necessarily the case for special audits (due to a lower number of occurrences). An overview would definitely help to avoid lengthy discussions at any beginning of a special audit, including which additional rights the NTS has in comparison to a general audit. This overview shall include as well hints on under which circumstances a regular audit can turn into a special one and under which circumstances a special audit can turn into a general audit.

## Response: Addressed

In 2013, special audit was abolished. Periodic and non-periodic audits are divided based on audit selection reason. Non-periodic audit is conducted where any specific suspicions of tax evasion is found under the Framework Act of National Taxes as follows.

✕ **Ground for non-periodic audit** : where a taxpayer does not comply with tax compliance obligations under the Korean Tax laws, where transactional facts are not in line with what was reported (e.g., transaction without authentic documentation, fraud transaction), where a specific suspicions of tax evasion is reported, where a clear evidence of tax evasion or error is found from the submitted documentation

Auditees of non-periodic audit are informed audit procedure by receiving Tax Audit Guidebook from 2014.



## Issue: Publication of Internal Audit Guidelines

Audit assessment results and procedures are often influenced by "internal instructions" within the NTS. Audited companies often only learn about such guidance through informal channels (e.g. consultants' internal contacts), which makes it difficult to comply with the expectations of the audit. Furthermore such internal instructions seem to be sometimes results-driven. More transparency, e.g. by making important internal guidance public, would not only enable companies to comply with them, but also contribute to trust-building between the NTS and (potential) investors, who monitor the audit environment in Korea very closely.

## Response: Already Implemented

The NTS opened 'Guidance on Tax Audit Procedure' which defines basic rules and procedure of tax audit to the public since 2006 via NTS website. However, the level of disclosure is similar to the level of foreign tax administrations, and it is difficult to open selection method of tax audit subject as seen in other tax administrations.



## Issue: Requests for Foreign Affiliate Data/Documentation

Legal entity audited is legally registered in Korea. An audit team shall concentrate on all data and documents related to that company. Data and documents are requested to be provided from foreign affiliates.

Multinational companies registered in Korea have neither power nor the right to request data from overseas affiliates. Korean authorities should concentrate on data and documents possessed by the company operating in Korea. This includes the requests from auditors to provide e.g. income statements – company- or business-unit-based – from overseas affiliates. In cases in which the auditors think that documents from other companies than the auditee are necessary for the tax assessment (e.g. in the area of transfer pricing), the official process for bilateral request for documents as defined in most double taxation treaties between the respective countries is to be followed. Under no circumstances unreasonable pressure shall be exerted on the auditee to circumvent this official process.

## Response: Addressed

While it is inevitable to request for foreign affiliate-related data for the purpose of calculating arm's length price at TP audit, the NTS will deliver sufficient instructions to auditors (also monitor whether the instructions are well operated) in order to minimize documentation burden of companies.

## Issue: Timelines for Appeals

Clear timeline by authorities, e.g. that a decision on an appeal is made within a reasonable period of time such as max 90 days as prescribed in the laws and informed back to the company.

## Response: Addressed

NTS made most of decisions on appeals within 90 days, but some of cases require substantial amount of time to proceed because it takes some time to receive opinions from authoritative organizations or taxpayers.

## Issue: Length of Audits

The length of on-site audits differs remarkably ranging from two to six months. We expect that time standards are set for companies considering the complexity and the size of the legal entity. Actually, it must be also in the interest of the authorities to conduct audits in an efficient way and if completed according to the original audit scope to close them accordingly and not to extend the audit scope only because there is still time left.

## Response: Already Implemented

Each audit period is unequal according to various reasons (e.g., size and business types of an entity). As for extension of audit scope, the audit team is unable to arbitrarily extend the scope as the extension requires permission by taxpayer advocacy committee. Also, while the NTS will put its efforts to follow the arranged timeline, the NTS explained it is difficult to disclose criteria for allocating audit period.

## Issue: Quantity of Data Requested

The quantity of reports, documents and data requested by authorities in many cases reaches an excessive number. The same is true for “necessary” documentation to prove that e.g. management fees from either a local holding- / lead-company or global/regional headquarters are justified. It is our opinion that the Korean government strives for deregulation and accordingly we would more than appreciate if documentation requests and needs could be reviewed to make lower in number and less complex and could be defined and published.

## Response: Addressed

See Response/Comment to Request for Foreign Affiliate Data/Documentation Issue (slide 14)

## Issue: Length of Audits

Considerable long periods after on-site audit to deliver the final audit conclusion to the company. It is for sure mainly based on the fact that members of the audit team are in some cases assigned shortly after the on-site audit to a different audit team which makes a finalization more difficult. The JWGC wishes that the audit team involved in that audit, shall firstly complete the audit report before being taking over new assignments. In this respect, we also expect a clear timeline by the authorities, e.g. that a final report is to be issued latest three months after the on-site audit.

## Response: Already Implemented

The NTS is providing the final audit results within 20 working days after having finished the on-site audit. In case of facing complex tax situation, which requires internal reconciliation, it may require more than 20 days until the final audit conclusion is delivered. In such case the NTS provides a reasonable and clear justification to the taxpayer, as well as a formal status update at least every 30 days.



## **Issue: Simultaneous Audits by Different Authorities**

Companies have been audited at the same time by either different authorities or by the same authority with different teams and a different scope. This leads automatically to the effect that efficiency decreases and that the provision of data and documents is delayed etc. We request that authorities do not schedule multiple regular audits at the same time.

## **Response: Already Implemented**

A company can apply for a postponement of NTS audit if documents are currently not available due to double audits (or investigations) by different government authorities. The NTS itself schedules only one audit per company at a time. The JWGC pointed out that in some cases it might be different legal entities at which an audit is conducted at the same time but supported by the same centralized shared accounting service team located at the lead company. It was suggested to have coordination meetings on senior level with other regulatory bodies (e.g. customs service) to align the timing of different audits. The NTS considers this as difficult, due to the different legal basis for the respective audits, but will rather consider a postponement of a tax audit if it interferes with other audits.

## **Issue: Request for Translation of Documents**

During the course of an audit, a substantial number of documents are requested. Multinational companies in many cases have defined their company language to be English. It has been observed that auditors request translation into Korea which we find not adequate – neither financially nor from an efficiency point of view. The JWGC recommends that documents in English are accepted and that only a limited number of documents on outstanding important issues / areas are to be provided in Korean. Documents or data requested to be provided need to have audit relevance; although it could be observed also non-audit-relevant documents have been requested.

## **Response: Addressed**

According to the Enforcement Decree of the Adjustment of International Taxes Act, documentation shall be prepared and submitted in Korean and the submission of documentation prepared in English is allowed in limited cases.

The NTS will deliver a message to audit team to request English-Korean translation within the limited scope necessary to conduct the audits.



# Thank you !