



TP News Flash

Release of BEPS Combined Report of International Transactions

February 18, 2016

Summary

In accordance with the G20/OECD Base Erosion and Profit Shifting (“BEPS”) project, the Ministry of Strategy and Finance (“MOSF”) announced the amendments to the Law for the Coordination of International Tax Affairs (“LCITA”) to strengthen transfer pricing documentation requirements on 15 December 2015. Following the announcement, Article 21-2 of the Presidential Enforcement Decree (“PED”) of the LCITA was newly established on 5 February 2016, requiring all domestic corporations and foreign corporations with international related party transaction amounts in excess of KRW 50 billion and sales revenue in excess of KRW 100 billion to annually submit the Master file and Local file by the time of the corporate tax return filing. Guidance on the party responsible for preparing the Master File and related details are now provided in the pre-announced amendments to the Enforcement Regulations (“ER”) of the LCITA released on 16 February 2016.

Contents of the Combined Report of International Transactions (“CRIT”)

The CRIT is comprised of the **Master file** and the **Local file** (Article 21-2, Paragraph 2).

- Master file: Provides an overall perspective on the entity, including organization structure, business description, intangible assets, and financing activities
- Local file: Contains specific transfer pricing information including organizational structure, business information, and financial summary of the local entity

Details including document formats and contents of the CRIT are outlined in the proposed amendments to the ER, which are generally consistent with the BEPS Final Report for Action Plan 13 released by OECD. Through the submission of a uniform Master file in various tax jurisdictions, MNCs will now need to prepare Local files for all relevant entities which are consistent with group-wide transfer pricing policy.

Corporations subject to submission of CRIT

Under the newly established PED and pre-announced ER, the CRIT is applicable to domestic corporations and foreign corporations with a domestic place of business having international related party transactions in excess of KRW 50 billion and sales revenue in excess of KRW 100 billion during the corresponding taxable year.

Whether or not a company exceeds the related party transaction threshold amount of KRW 50 billion can be determined by the total amount of related party goods and service transactions as well as lending and borrowing transactions on Appendix Form 8 of the Statement of Related Party Transactions.

In addition, related parties that should be covered under the CRIT shall be limited to entities that are part of group consolidated financial statements in accordance with the International Financial Reporting Standards.

The entity responsible for preparing the CRIT should be the ultimate parent company that is responsible for preparing the group consolidated financial statements.

The initial draft of the proposed amendments to the PED released at the end of 2015 stated that “the Master file should be submitted by the corporation submitting the Local file or the ultimate parent company within the business segment that owns voting shares of the corporation or has substantial influence on business operations.” The proposed amendments also provided exception for cases where the ultimate parent company is not located in Korea or is not subject to submission of the Master file in the country in which it is located, or performs business operations wholly different to those of its subsidiaries, by allowing the corporation responsible for submitting the Local file to obtain the Master file from the ultimate parent company within the same business segment for submission in Korea. However, in anticipation of potential issues on defining and implementing the concept of “voting shares of the corporation and ultimate parent entity having substantial influence on business operations within the same business segment,” this language has been deleted from the newly released amendments to the PED and instead, the company responsible for the preparation of the Master file (i.e. the company responsible for preparing the group consolidated financial statements) has now been aligned to the entity responsible for preparing the OECD BEPS Country-by-Country Report as defined by the OECD.

Further, in accordance with Article 21-2, Paragraph 3 of the PED and Article 6-1, Paragraph 4 of the proposed amendments to the ER, “when two or more taxpayers are equally subject to consolidation of financial statements, ***the ultimate parent company may submit the Master file*** as the representative.” With the removal of the “exception” clause previously mentioned in the proposed amendments, this can be interpreted as meaning that the ultimate parent company is responsible for preparation and submission of the Master file.

However, given that there may often be cases where the ultimate parent company does not engage in the transactions and is unable to prepare and submit the Master file, the new amendments should be supplemented so that a secondary parent company within the business segment to act as a delegate for the ultimate parent company in preparing and submitting the Master file. Samil is continuing to engage with the MOSF and related authorities to express opinions on the new amendments and make changes where necessary to enhance clarity and facilitate implementation of the new legislation.

The newly released amendments to the ER now provide clear guidance on which entities should be subject to the CRIT. As a result, relevant corporations should take into consideration the following:

- The Master file is to be submitted by the ultimate parent company that is also responsible for preparing the group-wide consolidated financial statements. Accordingly, the parent company should identify the entities that are subject to group consolidated financial statements and prepare the Master file that covers all such entities. The parent company should also be aware of which entity is responsible for preparing the Master file under the regulations of the tax jurisdiction in which each local affiliate is located.
- With respect to MNCs, the Master file is required to be prepared by the ultimate parent company abroad, which should then be provided to the subsidiary in Korea for submission to the local tax authority. As such, it is important to identify the ultimate entity that is responsible for the consolidation of the financial statements and such entity’s submission requirements of the Master file in its respective country, including the filing due date.
- Whether or not a corporation is required to prepare and submit the CRIT is dependent on the intercompany transaction volume and sales revenue during the taxable year. However, even if the sales revenue or international related party

transaction volume does not exceed the threshold amounts, corporations will still be subject to submission of transfer pricing documentation upon request by the tax authority (typically in the event of a tax audit) according to Article 11, Paragraph 3 of the LCITA.

Period of submission and extension

Submission of the CRIT is required by the time of corporate tax return filing for the fiscal year beginning 1 January 2016. In reality, it may be difficult for the CRIT to be submitted by the corporate tax return filing date, considering the short preparation period (i.e. within three months of fiscal year-end) to file the corporate tax return in Korea and different submission due dates for Master files in countries in which the foreign ultimate parent company is located (i.e. due date may be later than that of Korea). An additional complication is that the taxpayer's obligation to submit the CRIT may be uncertain until year-end closing of the fiscal year in which the intercompany transaction volume and sales revenue become fixed.

In such cases, the taxpayer may apply for an extension for submission of CRIT by no later than 15 days prior to the submission due date, for an extension period of up to one year.

For reference, the current regulations under the LCITA allow an extension for circumstances where the taxpayer incurs a significant amount of time for gathering and preparation of the required documents and cannot submit such documentation within the required timeframe, or where there are legitimate reasons for the delay. It is important to note that the extension is granted at the discretion of the local tax office in the respective jurisdiction, and the extension period is not automatically one year but may be shortened depending on the actual time

required for preparation and submission.

The legislation currently stipulates that the ***CRIT should be documented and submitted in Korean***. While the Master file may initially be submitted in English, it must be accompanied by the Korean translation within one month from the date of submission.

Accordingly, corporations that are subject to the CRIT requirements will need to prepare relevant documentation in advance for timely submission.

Conclusion

This pre-announcement of the ER provides clearer guidance on the contents to be included in the CRIT and the entity responsible for preparing the Master file. The contents to be included in the CRIT are mostly consistent with the OECD BEPS Action Plan 13, and the entity responsible for preparing the Master file has also been aligned with the entity defined by the OECD for preparing the BEPS Country-by-Country Report. However, given the existence of situations where the ultimate parent company of the group is not in the position to prepare and submit the Master file, the new legislations should be supplemented so that the responsibility can be delegated to a secondary parent company within the business segment.

Samil is continuing to engage with the MOSF and the National Tax Service, as well as other key stakeholders, to share our opinions regarding the proposed amendments and promise the timely delivery of any new information and appropriate tax strategies to our clients. If there are any additional questions regarding the matters above, please contact the Samil PwC Transfer Pricing Team.

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