Gaseong Industrial District Foundation(GIDF)
Foreign Investment Support Center(FISC)

TAX accounting in GIC

GIDF
FISC

CONTENTS

Chapter 1. Accounting regulations in the Gaeseong Industrial Complex

Section 1. Outline of accounting regulations in the complex

The complex's accounting regulations include rules that an company must abide by in the accounting process. An company is required to follow the company accounting standards written and announced in detail by the complex's management committee.

The following are major regulations that any company residing in the complex must abide by in the accounting process.

(1) Write figures in USD in an account book.

(2) Fiscal year : January 1~December 31(the first fiscal year falls on the business opening day)

(3) Accounting balance sheet and investigation

A company should write an accounting balance sheet that includes a balance sheet, a statement of profit and loss, receipts of profit appropriation, a deficit reconciliation statement, documents of cash flow, annotations of a balance sheet and documents of financial conditions. The accounting balance sheet should be written within two months after a fiscal year and should be verified by an accounting investigation office.

Section 2. Accounting verification

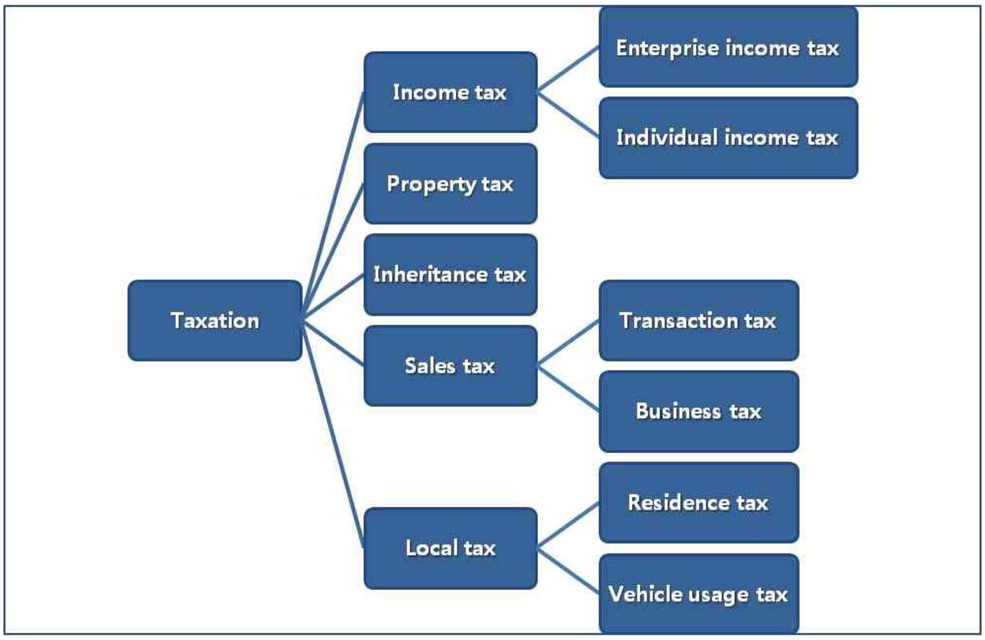
According to the complex's regulations on accounting verification, branches, sales offices and individuals as well as registered companies whose investment has exceeded more than USD 1 million or who have earned more than USD 3 million in sales and service profits last year should get their accounting verified by an accounting investigation office installed in the complex

Chapter 2. Taxation in the complex

Section 1. The complex's taxation system

Matters concerning tax payment should be handled in accordance with the complex's related regulations. The regulations include tax provisions and detailed regulations of enforcement. The following is a list of taxes that are applicable to the complex under the regulations.

<The complex's taxation system>



Section 2. Income tax

Ⅰ. Company income tax

company income tax in the complex is the equivalent of South Korea's corporate tax. According to the detailed rules of tax enforcement, the accounting regulations and the corporate finance regulations of the complex, an company's total income will be decided, which is the equivalent of South Korea's income of each fiscal year.

1. Tax requisitions

(1) Taxpayer : The taxpayer is companies, branches, sales offices and individuals that make profits in the complex.

(2) Range of taxable income : The following income that occurs in the complex is regarded as taxable income.

① Income from business activities : profits from sales of products, transfer of properties, fares and fees

② Others : income from interests, dividends, rentals, property sales, offering intellectual property rights or know-how, service and endowed income

(3) Fiscal year and tax rate

① Fiscal year : The fiscal year in the complex is from January 1 to December 31. For new companies in the complex, the fiscal year starts from its opening day to December 31. For companies that close their business, the fiscal year starts from January 1 of the closing year to the closing day.

① Tax rate : Companies are taxed at 14 percent out of their profits in general, while those in encouraged industries are taxed at 10 percent out of their profits. The abovementioned "encouraged industries" include infrastructure construction, light industry, and advanced scientific technology.

(4) Tax base : Tax base refers to quantities or price of taxation articles under the complex's taxation regulations. The tax amount is measured by multiplying the tax base by tax rate. For company income tax, the company's profits become the tax base.

2. How is the tax amount calculated?

The total amount of company income tax is measured by applying the tax rate to the company's closing profits. According to Article 32 of the detailed regulations on taxation enforcement, the company's closing profits, gross income and expenses that occurred concerning the gross income are indicated as each fiscal year's income, the total Article 25 of the Gaeseong Industrial Complex's company Finance Regulations amount of profits and the total amount of loss.

(1) Calculation of tax base : The tax base refers to the amount with business loss that has occurred within five years after the business opening day, deducted from the year's total income.

※ Each fiscal year's income - the amount of business loss = tax base

1) Each fiscal year's income : Each fiscal year's income refers to the amount with the total amount of loss that has occurred in the fiscal year, deducted from the total amount of the fiscal year's profits.

2) The amount of business loss : When the company's total income is short of its amount of loss, the shortfall is regarded as the amount of business loss. The amount of business loss can be made up for in the next fiscal year, and the make-up period is within five years.

(2) How is the tax amount calculated?

☞ The tax amount is measured by multiplying the tax base by tax rate.

※ Tax amount = tax base×tax rate(14%, 10%)

1) Tax rate for general companies : 14%

2) Tax rate for encouraged industries : 10%

* The abovementioned "encouraged industries" include infrastructure construction, light industry, and advanced scientific technology.

3. Profits

Profits refer to the amount of money that the company has made within the fiscal year, the amount that has increased the company's net assets. However, the amount of its capital or investment and the list of exclusive profits are not included in "profits."

4. Loss

The amount of loss refers to losses and expenses that have cut down the company's net assets. However, the losses and expenses don't include the amount that occurred in capital or investment returns and the amount that occurred in surplus appropriation. They only include the amount related to the company's business and expenses.

(1) List of losses that are not regarded as "losses"

The complex's company finance regulations and detailed regulations on taxation enforcement stipulate a list of losses that are not regarded as "losses," as can be seen below.

1) losses from capital transactions

2) losses from fines that the company paid when it violated laws or regulations

3) losses from appraised assets

Losses from appraised assets are not included except for the following losses.

① losses from appraised assets that include inventory properties, securities, foreign currencies and debts

② losses from property accounts that are recognized in particular cases

4) losses from deprecation expenses for fixed properties

Only deprecation expenses that are measured by the rate of redemption cost based on the period of depreciation for fixed properties are included in losses, but the surplus is not included.

5) losses from expenses that occurred in foreign business(for example, entertainment expenses for South Korean personnel)

Expenses from foreign business are regarded as losses in principle, as they reduce the company's net assets. However, excessive expenses from foreign business may cause overconsumption and a decline in the company's competitiveness, so there is a limit on the expenses in place, and only losses within the limit are regarded as "losses."

6) losses from any excessive expenses

7) losses from expenses that occurred regardless of businesses

8) losses from interest payments

Interests paid for the company's debts are just losses that reduced its net assets, so the interest payment is regarded as "losses" in principle. However, no interest payment is included when the creditor is not accurate or it is an interest payment for construction funds.

9) losses from excesses that occurred in paying retirement subsidies

The limit of retirement subsidies that is regarded as "losses" is within 5 percent out of the monthly wages for employees who have worked more than one year and the personnel in administrative positions.

10) losses from excesses that occurred due to appropriation for a bad /irrecoverable debt.

Only within a certain range of debt balances as of the closing day of a fiscal year are excesses that occurred due to appropriation for a bad/irrecoverable debt regarded as "losses."

5. Withholding tax

(1) Withholding taxpayers

Companies, economic organizations and groups working outside of the complex which have earned incomes from interests, dividends, rents for fixed properties, property sales and businesses are the withholding taxpayers.

Only incomes that belong to Permanent Establishment are taxed, while incomes that don't belong to Permanent Establishment are not taxed. Therefore, companies outside of the complex that do not belong to Permanent Establishment in the complex are taxed for business taxes, not for company income tax, in accordance with the double tax avoidance agreement, when they earn incomes from businesses in the complex.

(2) Tax rate for withholding taxes

① Income from interests: 10% out of the total income

② Incomes from dividends and fixed property rents: 10% out of the rest of the amount, with 70% deducted from the total income

③ Incomes from property sales and offering intellectual property rights and technical know-how, and from service activities: 10% out of the rest of the amount, with 30% out of the total income deducted from the income

(3) Person responsible for withholding

The person responsible for withholding is the one who pays the incomes of the withholding taxpayer.

(4) Reporting and paying withholding taxes

The person who pays incomes that are subject to withholding taxes should pay withholding taxes by the tenth day of the next year.

6. Tax Break

(1) Companies in encouraged industries and in the manufacturing sector are given tax break They are exempt from the company income taxes that spanned five years from the year that they started making profits. Then they will be given a 50% reduction in the related taxes over the next three years.

(2) Companies that have been running for more than 10 years in the service sector. They are exempt from company income taxes over two years starting from the year that they started making money. Then they will be given a 50% reduction in the related taxes over the next year.

(3) Tax break on reinvestment

For companies that have run for more than three years by reinvesting in business with profits that they earned with business before, 70% of their company income taxes for this year will be deducted from the next year's taxes.

(4) Reduced or exempted taxes to be collected

Companies which have their company income taxes exempted or deduced thanks to tax break are required to pay the reduced or exempted taxes if they close business or withdraw their reinvested capital.

Ⅱ. Individual income tax

Individuals who earn income from their labor or interests in the complex are obliged to pay individual income taxes. Individual income taxes are imposed according to progressive tax rates or a single tariff system, not in the way it is done in South Korea, where individual income taxes are included in general taxation after tallying up the total amount of individual incomes.

1. Taxpayer

(1) labor income : Labor incomes that South Korean residents earned in North Korea are taxed on the North side only if the incomes don't meet the second clause of Article 15 of the double tax avoidance agreement struck between the two Koreas.

(2) Other incomes : Individuals who earned incomes in the complex are required to pay individual income taxes.

2. How to calculate taxable incomes

(1) Labor income is taxed when the amount with 30% deducted from the monthly labor wage comes to more than USD 500.

(2) Incomes from dividends and fixed property rents are taxed with 70% deducted from the total income amount.

(3) Incomes from property sales, offering intellectual property rights and technical know-how and from management and service are taxed with 30% deducted from the total income amount as necessary expenses.

3. Tax rate

The following tax rates apply to individual income taxes.

(1) Incomes from interests, dividends, fixed property rents, property sales, offering intellectual property rights and technical know-how and from management and service: 10%

(2) labor income(Currency unit : US$)

4. Reports and payments

(1) Withholding agent or taxpayer

Companies that pay incomes from labor, interests, dividends, fixed property rents, offering intellectual property rights and technical know-how and from management and service are obliged to deduct withholding taxes every time they pay. Then they are required to write a tax return and a statement of payment for withholding taxes within 10 days in the next month.

For individual income taxes on incomes from property sales and endowed income, the income earner is obliged to report and pay the taxes within 30 days after the incomes occurred.

(2) How to turn taxes into a foreign currency unit

When individual income taxes are paid in the South Korean currency, the won should be converted into USD according to exchange rates set by the Seoul Money Brokerage(SMB).

Section 3. Sales tax

Sales taxes refer to taxes on transactions of all kinds of products or service. Sales taxes are measured by the amount of sales involving all kinds of goods and service transactions. Sales taxes in the complex refer to transaction taxes and business taxes, while sales taxes in South Korea refer to value-added taxes.

Ⅰ. Transaction taxes

1. Taxpayer : companies in the production sector

2. Taxation articles and tax rate

No	Production sector	Tax rate
1	electricity, electronics, metal and machinery	1%
2	fuel, minerals, chemicals, building materials and rubber	1%
3	fabric, shoes, ordinary utensils, leather and other industrial products	1%
4	food, agricultural products, livestock products, marine products	2%
5	alcohol, cigarettes, other items of personal preference	15%

3. How to calculate taxes to be paid

☞ The total amount of taxes
= the proceeds from the sales of products × applied tax rate

4. Transaction tax exemption

When products produced in the complex are carried into South Korea or exported to other countries, the company will be exempted from transaction taxes.

5. Reports and payments

Transaction taxes should be reported and paid within 20 days in the next month after a quarter.

* Even when the company is exempted from transaction taxes, it should write a tax refund and submit it.

6. Form of tax refund : See the section about the form for business taxes

Ⅱ. Business tax

1. Taxpayer : companies in the service sector

2. Taxation articles and tax rate

No	Production sector	Tax rate
1	construction and transportation sectors	1%
2	finance sector	1%
3	commerce sector	2%
4	sectors involving protecting forests, tourism, running inns, advertisements and hygiene	1%
5	education, culture, sports and other service sectors	1%
6	real estate transactions	2%
7	entertainment sector	7%

3. How to calculate taxes to be paid

☞ The total amount of taxes
= the total income from service × the applied tax rate

4. Business tax exemption

Companies involved in producing energy substances such as electricity, gas and heating materials or in investing in water supply and drainage and in roads are exempted from business taxes.

5. Withholding taxes

When South Korean companies or individuals without Permanent Establishment are involved in any business activities in the complex, their residing businesses and sales offices are obliged to report and pay business taxes after withholding them.

6. Report and payment

Business taxes are to be reported and paid within 20 days in the next month after a quarter.

Section 4. local taxes

Ⅰ. Residence taxes

Residential tax and business place tax are imposed according to the South Korean Local Tax Law. Meanwhile, for the North Korean Taxation Law for non-Koreans, residence taxes are imposed on foreign investment companies and residential foreigners to help manage public facilities including parks, roads and sanitation facilities.

1. Taxpayer

The following are persons who are liable for residence taxes.

① Companies that pay employees for their labor

② Individuals who stay in the complex for more than 182 days and earn labor income

③ Individuals who earn income from interests, dividends, rents and property sales in the complex

2. Taxation articles

Residence taxes are measured by multiplying the following taxation articles by their tax rate.

① Company : the total amount of monthly wages paid to employees, which is appropriated in the account book

② Individual : the total amount of incomes from labor, interests, dividends, and property sales

3. Tax rate

Tax rates of 0.5% are applied to both companies and individuals

4. Reports and payments

Companies and individuals should report and pay taxes as follows.

① Company : Report and pay taxes to be paid on a monthly basis within 10 days in the next month

② Individual : Report and pay taxes within 10 days in the next month after the income

* When companies pay residence labor income taxes that were imposed on individuals, they should report and pay the taxes after withholding the amount.

Ⅱ. Vehicle use tax

1. Taxpayer

Companies or individuals who own a vehicle, from January 1 every year

2. Taxation articles

Passenger cars, buses, trucks, trains, special vehicles(cranes, tankers, forklifts, cement carriers, excavators, bulldozers, freezer trucks, etc.)

3. Taxes to be paid

No	Category		Tax amount(US$)
1	passenger cars	per vehicle/year	40
2	bus with a capacity of 15 seats with a capacity of 13-30 seats with a capacity of more than 31 seats	per vehicle/year per vehicle/year per vehicle/year	40 50 60
3	trucks	per shipping ton/year	3
4	trains	per vehicle/year	10
5	special vehicles	per vehicle/year	20

4. Payment

The complex's tax office sends out a notice of payment for vehicle use taxes in February every year → Taxpayers are obliged to pay taxes within 30 days after they received the payment notice.

* Those who own a vehicle during the tax year are obliged to pay vehicle use taxes measured based on the use days, within 30 days after the car was registered.

Section 5. Property tax

1. Taxpayer

companies and individuals that own permanent property in the complex

2. Taxation articles

Property taxes are imposed based on registered building prices. The registered building prices are the amount set by the time the owner acquired it. When the prices have changed, the owner is required to submit a certificate of the new price to the committee and to have the building newly registered.

3. Tax rate

No	Purpose of building	Tax rate(%)
1	Building for production activities	0.1
2	Residential building	0.2
3	Commercial building	0.5
4	Entertainment building	1.0

4. How to calculate taxes

Registered building prices × applied tax rate

5. Property tax exemption

Companies or individuals that own a newly constructed building are exempted from property taxes for five years after the building was registered.

6. Payment

The complex's tax office sends out a notice of payment in February every year. Taxpayers are obliged to pay property taxes within 30 days after they received the payment notice.

Section 6. Taxation agreement struck between South and North Korea

The Double Tax Avoidance Agreement, an agreement that aims at revitalizing economic exchanges between North and South Korea by preventing double taxation for incomes that occurred in transactions between the two Koreas, was signed in 2000, and came into effect as of August 20, 2003.

Although it was signed in the form of a written agreement and not a treaty between the two nations, due to the distinct characteristics of the two Koreas, the basic content in the agreement is equivalent to that in other tax treaties, as it is designed to prevent double taxation.

The agreement stipulates how to impose taxes for company profits, for investment profits, for personal service income, and other incomes, as well as how to prevent double taxation, a prohibition on discrimination against residents from both sides and an agreement procedure.

The inter-Korean agreement adopted through a series of discussions between the two governments in order to develop the economy in a balanced manner with the goal of boosting economic exchanges and cooperation between the two Koreas, will be applied in preference to the tax regulations adopted in the Gaeseong Industrial Complex.