

# Guidelines for Investment



Investment in  
Korean Company

Investment in  
PE/VC Fund in Korea

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- Investment in PE/VC Fund in Korea

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Part 1

Investment in Korean Company

Foreign GP side

# I. Foreign Exchange

## 1 Reporting Obligations under the Foreign Exchange Transactions Act for Overseas Institutions, such as VC Funds, Investing in Shares of Domestic Companies

### A. Obligation to Report under the Foreign Exchange Transactions Act

- When a non-resident acquires unlisted or unregistered domestic KRW-denominated securities from a resident using an **object of investment** as defined under the Foreign Investment Promotion Act, the transaction must be reported to a foreign exchange bank (i.e., a general commercial bank in Korea). For all other cases, the report must be filed with the Bank of Korea.
- “**Object of investment**” refers to: (i) foreign currency (including checks, bills, etc.; hereinafter referred to as “**foreign currency**”) or Korean currency exchanged for foreign currency (in case foreign currency remitted from overseas to Korea is exchanged domestically), and (ii) **dividends or other proceeds generated from stocks, etc., acquired under the Foreign Investment Promotion Act.**

### B. Exceptions to Reporting Requirements under the Foreign Exchange Transactions Act

#### (1) Acquisition of KRW-denominated Securities in Accordance with the Procedures Set Forth in the Foreign Exchange Transaction Regulations (limited to the acquisition of listed stocks).

- A non-resident is not required to file a separate report under the Foreign Exchange Transactions Act when acquiring domestic won-denominated securities through the

investment procedures for foreign investors specified in the Foreign Exchange Transaction Regulations.

- However, in order to do so, the non-resident must open a dedicated investment foreign exchange account and a dedicated non-resident KRW account under their name at a foreign exchange bank, and deposit or dispose of the related funds through these accounts.

#### (2) Cases that Qualify as a Foreign Investment under the Foreign Investment Promotion Act (regardless of listed or unlisted stocks)

- To qualify as a foreign investment under the Foreign Investment Promotion Act, the below condition ① must be satisfied, and either condition ② or ③ must also be satisfied.
  - ① **Investment amount of KRW 100 million or more per person using the object of investment;**
  - ② **Ownership by a foreigner of 10/100 or more of the total number of voting shares or total equity** issued by a corporation or enterprise in Korea;
  - ③ **Ownership by a foreigner of shares or equity in a corporation or enterprise in Korea, along with dispatching or appointing an executive to that corporation or enterprise.**
- While exempt from reporting requirements under the Foreign Exchange Transactions Act, **the followings are required under the Foreign Investment Promotion Act: (i) foreign investors must submit a foreign investment report, and (ii) the foreign investor or the foreign-invested company (typically the latter handles the process in practice) must apply for the registration (or changes) of the foreign-invested company.**
- When a domestic company registered as a foreign-invested company receives a loan with a term of five years or more from its parent foreign investor (or a foreign company with a specified capital investment relationship), it is also considered foreign investment.
  - This refers to cases where an existing foreign investor provides additional long-term loans.
  - In such cases, reporting of the long-term loan is required (reporting of foreign investment and application for changes to the foreign-invested company registration are not necessary).

### C. Reporting Requirements to Foreign Exchange Banks under the Foreign Exchange Transactions Act

- Except for the above two reporting exceptions, if a non-resident acquires unlisted or unregistered KRW-denominated stocks or shares of a domestic corporation from a resident through an object of investment prescribed by the Foreign Investment Promotion Act, he/she shall report it to the foreign exchange bank.
  - Since investment funds (e.g., new technology business investment associations) are not corporations, investments in such funds are subject to reporting to the Bank of Korea, not foreign exchange banks.
  - However, investments in venture investment associations (with an investment amount of KRW 100 million or more and an investment ratio of 10% or more) are exempt from reporting under the Foreign Exchange Transactions Act. Instead, reporting is required under the Foreign Investment Promotion Act.
- Examples of reporting requirements to foreign exchange banks are as follows.
  - When the investment amount using the foreigner's object of investment is less than KRW 100 million.
  - When the foreigner owns less than 10% of the voting shares.

### D. Reporting Requirements to the Bank of Korea under the Foreign Exchange Transactions Act

- Transactions that fall outside the two reporting exceptions or the reporting requirements to foreign exchange banks must be reported to the Bank of Korea.
- Examples of transactions requiring reporting to the Bank of Korea include:
  - A foreigner acquiring convertible bonds or bonds with warrants issued by a domestic corporation, other than shares.
  - A foreigner investing in a new technology business investment association.

## 2 Reporting Procedures under the Foreign Investment Promotion Act and the Foreign Exchange Transactions Act for Overseas Institutions, such as VC Funds, Investing in Shares of Domestic Companies

### A. Reporting Procedures to Foreign Exchange Banks under the Foreign Exchange Transactions Act

#### (1) Required Documents

- Two (2) copies of the Securities Acquisition Report
- Funding verification documents: Can be confirmed with documents such as a Foreign Exchange Purchase Certificate issued by the bank; submission can be made after the fact.
- Copy of documents evidencing acquisition of shares (equity) (stock purchase agreement or issuance plan, draft articles of incorporation in case of incorporation, etc.)
- A copy of the acquirer's identification document, such as a passport or a certified copy of the corporate registration (certificate of incorporation), or any document proving the entity's establishment in the respective country.
- Power of attorney (notarization and Apostille required)
- Documents that can verify ownership relationships.
  - Can be omitted if confirmed by stock purchase agreement
  - There are cases where the bank requests a list of shareholders before and after the acquisition of shares (equity).

#### (2) Precautions in Reporting

- **Prior reporting is required before the payment of the investment funds.**
- The investor or their reporting agent must submit the report in person with identification and relevant authorization documents.

- Reporting is conducted through a branch of a foreign exchange bank.
- It takes 1-2 business days to complete the report (assuming all documents are in place).

## B. Reporting Procedures to the Bank of Korea under the Foreign Exchange Transactions Act

### (1) Required Documents

- Two (2) copies of the Securities Acquisition Report.
- Statement of reasons (detailing the background of the transaction, specific conditions/ contents of the securities to be invested, etc.)
- Documentation verifying the identity of the reporting party and the transaction (contract counterparty)
  - A copy of the passport of the reporting party (non-resident foreign investor) if an individual, or a copy of the Certificate of Incorporation if a corporation or other non-individual entity.
  - A copy of the identification of the securities issuer/transferor (resident), such as a resident registration card, passport, or driver's license (any one), or an original certified copy of the corporate registration/certificate of business registration.
- Contracts related to the acquisition of the relevant securities, such as a draft securities acquisition contract (subscription form)
- Power of Attorney
  - If a proxy applies on behalf of the principal, the original power of attorney authorizing the reporting action must be submitted (local notarization required).
- Affidavit
  - If the report is filed by a proxy, the proxy may personally prepare and affix their seal.
- Other documents deemed necessary by the head of the report-receiving institution.
  - Additional documents may be requested during the Bank of Korea's review process. For example, in the case of securities swap transactions (where a foreign investor transfers their own securities as consideration for acquiring the target securities), a valuation report verifying the appropriateness of the price of each security must be submitted.

### (2) Precautions in Reporting

- **Prior reporting is required before the execution of the Investment Agreement.**
- The investor or their reporting agent must submit the report in person with identification and authorization-related documents.
- It takes 3 to 5 business days to complete the report (assuming all documents are in place).

## C. Reporting Procedures under the Foreign Investment Promotion Act

### (1) Required Documents for Foreign Investment Reporting (to be filed in advance or within 60 days of the occurrence of the event).

- Two (2) copies of foreign investment report
- A copy of the certificate of incorporation of the foreign investor (in the case of an individual, a copy of the passport).
- The original power of attorney from the foreign investor (notarization and Apostille required)
- A copy of the Stock Purchase Agreement. However, in the case of participating in the issuance of new shares, the stock purchase agreement is not required.

### (2) Required Documents for Registration (or Change) of a Foreign-Invested Company (to be filed within 60 days of the occurrence of the event).

- One copy of the Application for Registration (or Amendment) of a Foreign-Invested Company
- Original certified copy of the corporate registration
- Original certificate of corporate seal
- Copy of business registration certificate
- Original Register of Shareholders (Members)
- A copy of the Foreign Exchange Purchase Certificate (if applicable).

- Original certificate of registration of the foreign-invested company (if applicable)
- Original power of attorney (can be filed by the foreign investor or the foreign-invested company)

### (3) Precautions in Reporting

- **Location:** Reports can be filed with KOTRA or a foreign exchange bank (branch)
- Foreign Investment Reporting
  - **Prior Reporting:** Required for typical stock acquisitions.
  - **Post Reporting** (within 60 days of the occurrence of the event): Acquisition of shares (existing shares) in a listed company; Acquisition of shares using dividends from previously acquired shares; Acquisition of shares through conversion of convertible bonds, exchangeable bonds, etc.; Acquisition of shares from another foreign investor (if the shares are purchased by one foreigner from another who is already recognized as a foreign investor under the Foreign Investment Promotion Act, the investment is recognized as foreign investment even if the amount is less than KRW 100 million or the ownership ratio is less than 10%).
- Application for Registration (or Change) of a Foreign-Invested Company
  - Must be filed within 60 days of the occurrence of the event.
  - Example of application for registration of change: When shares acquired by a foreign investor are transferred, or when there are changes to registered details such as the foreign investment amount or foreign investment ratio, etc.

#### Case1

**Foreign investor A purchased 20% of the voting shares of company B for KRW 200 million in accordance with the Foreign Investment Promotion Act. Afterwards, A sold 5% of the voting shares of Company B to foreigner C for KRW 50 million. Here, what are the reporting requirements for the transaction in which A sells shares to C?**

- A: As the transfer of shares is a transaction between non-residents, there is no obligation to report under the Foreign Exchange Transactions Act.
- C: Although the foreign investment ratio is less than 10%, the shares were purchased from A, who is already recognized as a foreign investor under the Foreign Investment Promotion Act, making C also qualify as a foreign investor.
  - However, as it falls under post-reporting, C must file a foreign investment report within 60 days of the occurrence of the event. Reporting under the Foreign Exchange Transactions Act is exempt.
  - Since A's prior acquisition of shares in Company B qualified as a foreign investment, C is recognized as a foreign investor even if the shares of Company B were not acquired with an object of investment.
- Company B: Since the foreign investment ratio has changed, an application for the change of the foreign-invested company registration is required.

#### Case2

**Reporting Requirements for the Case Where Foreign Investor A Acquires 15% of the Voting Shares of Unlisted Company B for KRW 500 Million Using a KRW Loan from a Domestic Bank in Korea.**

- Loans from domestic banks are not subject to object of investment. Therefore, A's investment does not constitute a foreign investment under the Foreign Investment Promotion Act.
- Since it is not an acquisition by the object of **investment, it is a matter to be reported to the Bank of Korea under the Foreign Exchange Transactions Act.**
- However, when a foreigner borrows more than KRW 1 billion, a monetary loan agreement must be reported to either a foreign exchange bank or the Bank of Korea.

Case3

Foreigner A used the investment object to purchase 5% of the voting shares of Company B for KRW 200 million won (first purchase). A also has the authority to appoint executives of Company B through a shareholder agreement. Subsequently, A purchased 2% of the non-voting shares of Company B for KRW 50 million (second purchase). Reporting requirements in this case are as follows:

- First Purchase: A's investment amount exceeds KRW 100 million, and although A's ownership ratio is less than 10%, A can appoint executives of Company B. Therefore, A's investment qualifies as foreign investment under the Foreign Investment Promotion Act.
  - A must file a foreign investment report under the Foreign Investment Promotion Act, and Company B must apply for registration as a foreign-invested company. Reporting under the Foreign Exchange Transactions Act is exempt.
- Second Purchase: The first purchase already qualifies as foreign investment. Accordingly, the second purchase also qualifies as foreign investment.
  - A must file a foreign investment report under the Foreign Investment Promotion Act, and Company B must apply for an amendment to its foreign-invested company registration.

Case4

When Foreign Investor A acquires KRW 300 million in convertible bonds of Company B using an object of investment and exercises the conversion rights to acquire 20% of the voting shares of Company B, the reporting requirements are as follows:

- A's acquisition of convertible bonds does not qualify as foreign investment **under the Foreign Investment Promotion Act, but is subject to reporting to the Bank of Korea under the Foreign Exchange Transactions Act.** However, the exercise of the conversion rights must be reported to the Bank of Korea for post-management purposes.
- When A exercises the conversion rights, A's investment amount exceeds KRW 100 million, and the investment ratio is 10% or more, qualifying it as foreign investment under the Foreign Investment Promotion Act.
  - A must file a foreign investment report, and Company B must apply for registration as a foreign-invested company.
  - Reporting under the Foreign Exchange Transactions Act is exempt.

Case 5

A, who is already a foreign investor in Company B, provided a long-term loan of KRW 500 million to Company B with a term of five years or more. A then converted the loan receivable into equity and acquired 10% of newly issued shares in Company B.

- When A provides a long-term loan to B, a long-term loan report under the Foreign Investment Promotion Act is required.
  - In the case of a long-term loan, foreign investment reporting and an application for changes to the foreign-invested company registration are not necessary.
- When acquiring shares through debt-to-equity conversion, foreign investment reporting and an application for changes to the foreign-invested company registration are required for the share acquisition.
  - The long-term loan amount is not reflected on the foreign-invested company registration certificate. Instead, when the new shares are acquired through the debt-to-equity conversion, the acquisition amount is added to the foreign investment amount.

### 3 KYC PROCEDURE

#### A. KYC (Know-Your-Customer): A System for Verifying Customers and Identifying the Ultimate Beneficial Owner (UBO)

#### B. Reason for Reporting

- Under the customer due diligence obligations of financial institutions, when a foreign corporation establishes an account in Korea for financial transactions or remits investment funds exceeding USD 10,000, the corporation must disclose its beneficial owner (individual) (Article 2(2)(b) of the Act on Reporting and Using Specified Financial Transaction Information, Article 3(1)(3) of its Enforcement Decree, and Article 5-2(1)(1) of the same Act).
- The customer due diligence obligations of financial institutions for corporate customer is carried out in the following order (Article 10-3 and 10-5 of the Enforcement Decree of the Act on Reporting and Using Specified Financial Transaction Information).

**Stage 1** Persons who **own equity securities of 25/100 or more** (verified through the shareholder register)

- (If verification cannot be made in Stage 1)

**Stage 2** Choose between 1, 2, or 3 (in practice, only ② is typically verifiable).

- (1) A shareholder (individual) who has **appointed** the majority of representatives, executives, or managing members
- (2) The person holding the **largest equity securities**
- (3) A person who effectively controls the corporation or organization, aside from ① or ②.

If the largest equity securities holder under ② is a corporation or organization, the financial institution does not immediately proceed to stage 3 but instead traces the ultimate controlling individual by reviewing the shareholder register of the largest equity-holding corporation. In practice, since it is rare to identify individuals through each shareholder register, the “representative of the corporation or organization” in stage 3 is often substituted as the beneficial owner .

- (If verification cannot be made in Stage 2)

**Stage 3** The **representative** of the corporation or organization

#### Case

The sole shareholder of foreign investor A is Corporation B, and the sole shareholder of Corporation B is Corporation C. If no individual holding 25% or more of the shares or the largest shareholding in Corporation C can be identified:

- In such cases, the representative of A, Individual X, may be regarded as the Ultimate Beneficial Owner.
- A **Shareholder Structure Chart** may be submitted in place of the shareholder registers of A, B, and C.
- Typically, when A is an offshore fund, it is uncommon to identify an individual Ultimate Beneficial Owner, so KYC must be conducted based on the General Partner (GP).
- Notably, the method of conducting KYC for offshore funds varies by foreign exchange bank, so prior consultation with the bank is necessary.

C. Required Documents

Matters	Required Documents
Where an individual controlling shareholder is identified in the foreign investor shareholder register	<ul style="list-style-type: none"> <li>- Register of Foreign Investors</li> <li>- Passport copy of the foreign investor</li> <li>- Passport copy of the representative of the foreign investor</li> </ul>
Where the controlling shareholder who is an individual is not confirmed in the shareholder register of a foreign investor and the largest shareholder is a corporation	When an individual controlling shareholder is identified in the shareholder register of the largest shareholder corporation <ul style="list-style-type: none"> <li>- Shareholder register of the foreign investor</li> <li>- Shareholder register of the largest shareholder corporation of the foreign investor</li> <li>- Passport copies of individual shareholders of the largest shareholder corporation.</li> <li>- Passport copy of the representative of the foreign investor</li> </ul>
	When an individual controlling shareholder is not identified in the shareholder register of the largest shareholder corporation (the representative of the foreign investor may be substituted as the beneficial owner) <ul style="list-style-type: none"> <li>- Shareholder register of the foreign investor (investor)</li> <li>- Shareholder register of the largest shareholder corporation of the foreign investor (parent company)</li> <li>- Shareholder register of the largest shareholder corporation of the parent company (grandparent company)</li> <li>- Passport copy of the representative of the foreign investor</li> <li>- Beneficial Owner Verification Form signed (or sealed) by the representative of the foreign investor (or legal representative), including the representative's name, date of birth, and nationality</li> </ul>

- The required documents for KYC vary by foreign exchange bank, so prior consultation is necessary.

II. Taxation

1 Tax System Related to the Repatriation of Investments in Domestic Companies Made by Non-resident Venture Capital (“VC”)

A. Overview of Tax Related to Investment Repatriation

(1) Taxation System Outline

- Overview of the taxation system for domestic source income

In principle, when a non-resident VC invests in a domestic company and generates domestic source income, the provisions of the domestic tax law are generally applied. However, for the residents of countries with which Korea has entered into a tax treaty with, the tax treaty takes precedence over domestic tax law.

(2) Tax System under the Internal Revenue Code

- Taxation Principles

- ① Domestic source income that is effectively attributable to the non-resident VC is subject to taxation.
- ② The non-resident VC's domestic source income is taxed based on the income classification pursuant to the domestic tax law.
- ③ If the non-resident VC does not have a place of business/permanent establishment in Korea, its tax liability on domestic source income is fulfilled through withholding tax. (Provided, however, that (i) in the case of capital gains from transfer of assets such as real estate, and (ii) if there is a permanent establishment and domestic source income is attributed to the place of business/permanent establishment, there is an additional tax reporting obligation other than the withholding tax).

- Method of Taxation on Domestic Source Income of Non-Resident VC Under the Domestic Tax Law

Domestic Source Income	Place of Business/ Permanent Establishment O	Place of Business/ Permanent Establishment X	Withholding Tax Rate (Domestic Tax Law)
Interest Income	Comprehensive Taxation Filing and Payment	Separate Taxation Withholding Final Settlement	22%
Dividend Income			22%
Capital Gains From Transfer of Securities			Min (Transfer Price * 11%, Capital Gain From Transfer* 22%)

- Case Study

Case

A, a resident of a country that does not have a tax treaty with Korea, acquired 100,000 shares of X Corporation, a Korean corporation, for USD 1 million.

Resident A does not have a place of business/ permanent establishment in Korea

**Q1** What is the withholding tax if A received USD 10,000 in dividends from X in 2024?

**A1** USD 2,200 (=USD10,000 \* 22%)

**Q2** If A transfers all of A's shares in X to B, a Korea resident, for USD 3 million in 2024, what is the withholding tax amount?

**A2** USD 330,000 (=Min [USD 3 million\* 11%, (USD 3 million - USD 1 million) \* 22%])

(3) Application of Tax Treaties

- Relationship Between Tax Treaties and Domestic Tax Law

Tax treaties take precedence over domestic tax law.

- Requirements for Application of Tax Treaties

- ① A tax treaty must have been entered into between the country of residence of the non-resident VC and Korea.
- ② Non-resident VC must be the actual beneficiary of the domestic source income.
- ③ In order for a non-resident VC to be exempted from taxation in accordance with the tax treaty, an application for deduction or exemption must be submitted to the withholding agent, and in order to be subjected to the reduced tax rate, the non-resident VC must submit an application for a reduced tax rate to the withholding agent (Details of the required documents and procedures for exemption, deduction, and application for reduced tax rate are explained in Section B.)

- System of Application of Tax Treaties by Type of Income

- Interests and Dividends: In the case of a country with a tax treaty, the tax treaty's provisions for exemption or reduced tax rates apply (Varies by different tax treaties but generally within the range of 5-15%)
- Capital Gains on Securities: Most of the tax treaties adopt the method of taxation of the country of residence, meaning that capital gains from transfer of securities of non-resident VCs are taxed in the country of residency and not in Korea. However, if the securities related to real estate (i.e., shares of a corporation which real estate constitutes 50% or more of its total assets) or if the shares are held by a majority shareholder (typically owning 25% or more of the shares) are transferred, there may be tax obligation in Korea, the source country (Relevant tax treaties may need to be reviewed for specific details).

- Case Study

**Case1**

A, a resident of the US with whom Korea has entered into a tax treaty with, acquired 100,000 shares (not real estate shares) of X Corporation, a Korean corporation, for USD 1 million.

Resident A does not have a place of business/ permanent establishment in Korea

Assuming that the reduced tax rate and exemption under the Korea-U.S. Tax Treaty are as follows:

(Dividend income: 11%, Capital Gains on Securities: Not Taxed in Korea. Provided, however, that capital gains from the transfer of real estate shares shall be taxed in Korea).

**Q1** What is the withholding tax if A received USD 10,000 in dividends from X in 2024?

**A1** USD 1,100 (=USD 10,000 \* 11%)

\* Under the domestic tax law, the withholding tax rate on dividend income is 22%, however, the reduced tax rate in accordance with the Korea-U.S. Tax Treaty which amounts to 11% will be applied.

**Q2** What is the withholding tax if A transfers all of A's shares in X to B, a resident of Korea, for \$3 million in 2024?

**A2** No withholding tax

\* According to the domestic tax law, the withholding amount for capital gains on securities is USD 330,000, however, pursuant to the Korea-U.S. Tax Treaty, the tax is exempted.

**Case2**

In contrast to the fact pattern of Case 1 above, A is a paper company established in Iceland that has a tax treaty with Korea, and the sole shareholder of the paper company is C, a U.S. resident. A acquired 100,000 shares (not real estate shares) of X Corporation, a Korean corporation, for USD 1 million.

Assume the reduced tax rate and exemption under the Korea-Iceland Tax Treaty are as follows:

(Dividend Income: 5%, Capital Gains from Securities: not subject to taxation in Korea)

• Where A is the beneficial owner: Korea-Iceland Tax Treaty Applies

**Q1** What is the withholding tax if A received \$10,000 in dividends from X in 2024?

**A1** USD 500 (= \$10,000 \* 5%);

\* Under the domestic tax law, the withholding tax rate on dividend income is 22%, however, the reduced tax rate of 5% under the Korea-Iceland Tax Treaty is applied.

**Q2** What is the withholding tax if A transfers all of A's shares in X to B, a resident of Korea, for \$3 million in 2024?

**A2** No Withholding tax

\* According to the domestic tax law, the withholding amount for capital gains on securities is USD 330,000, however, pursuant to the Korea-Iceland Tax Treaty, the tax is exempted.

• Where C is the beneficial owner: Korea-U.S. Tax Treaty Applies

**Q1** What is the withholding tax if C received \$10,000 in dividends from X in 2024 through A?

**A1** USD 1,100 (= \$10,000 \* 11%)

\* Under the domestic tax law, the withholding tax rate on dividend income is 22% and the reduced tax rate under the Korea-Iceland Tax Treaty is 5%. However, as the dividend income is effectively attributed to C, a resident of the US, the reduced tax rate pursuant to the Korea-U.S. Tax Treaty which amounts to 11% applies.

**Q2** What is the withholding tax if A transfers all of A's shares in X to B, a resident of the Republic of Korea, for \$3 million in 2024, and the transfer price is substantially attributable to C?

**A2** No withholding tax

\* According to the domestic tax law, the withholding amount for capital gains on securities is USD 330,000, however, pursuant to the Korea-U.S Tax Treaty, the tax is exempted.

**- Withholding Tax Rate**

- Where there is no tax treaty (Taxation in accordance with the domestic tax law)

Domestic Source Income	Withholding Tax Rate (including Local Income Tax)
Interest Income	22%
Dividend Income	22%
Capital Gains on Securities	Min (Transfer Price* 11%, Capital Gain from Transfer* 22%)

- Where there is a tax treaty

Domestic Source Income	Withholding Tax Rate
Interest Income	Withholding at the reduced rate under the tax treaty;
Dividend Income	Withholding at the reduced rate under the tax treaty;
Capital Gains on Securities	Exemption from the taxation in accordance with the principle of taxation by country of residence under the tax treaty (Provided, however, taxation may apply to real estate shares, etc.)

**(2) Procedures for Non-Taxation, Exemption and Application of Reduced Tax Rates Under Tax Treaties**

**① When paid directly to the beneficial owner;**

- Applicable when the non-resident VC is the actual beneficiary of the income received.
- Non-resident VCs must submit (i) a non-taxation/exemption application for capital gains from transfer of securities or an application for the reduced tax rate on interest or dividend income, and (ii) documentation proving the actual beneficiary (example: certificate of residence) to the entity or person paying the income. In the event a foreign investment vehicle<sup>1</sup> is deemed to be the actual beneficiary of domestic source income<sup>2</sup>, a special declaration form for foreign investment vehicles must also be submitted.

<sup>1</sup> An organization established overseas that acquires, disposes of, or otherwise manages investable assets with property value, such as money collected through soliciting investments, and distributes and reverts the results thereof to investors.

<sup>2</sup> A foreign investment vehicle must satisfy certain requirements specified by the tax treaty to bear tax liability in the country where it was established and be eligible to apply the non-taxation, exemption, or reduced tax rates set forth in the tax treaty.

**(4) Adjustment of Double Taxation**

When a non-resident VC invests in a domestic company and pays withholding tax on domestic source income to Korea, the non-resident VC may be eligible to receive a tax credit in its country of residence for the taxes paid in Korea. However, as the tax laws vary by country, it is necessary to verify the tax laws for each jurisdiction.

**B. Reporting Procedures**

**(1) Withholding**

- Withholding Method: When a non-resident VC or others receive domestic source capital gains, interest income, or dividend income, the withholding tax obligation arises. The payer of the income withholds and remits the tax, thereby fulfilling the tax liability.
- Withholding Agent: The entity or person paying the domestic source income to the non-resident VC or others (\*)
- (\*) For securities transferred through a securities company, the securities company is withholding agent.
- Timing of Withholding and Payment: The withholding tax is to be withheld when the domestic source income is paid to the non-resident VC or others, and the tax must be remitted to the tax office by the 10th day of the month following the month in which the withholding occurred.
- Submission of Payment Statement: The payer of the income must submit a payment statement to the tax office having jurisdiction over taxpayer by the end of February of the year following the year to which the payment date falls.

- Applications, etc. submitted does not need to be submitted within three (3) years from the date of submission; provided, however, that if there is a change thereof, such change shall be submitted.

② **When paid to the actual beneficial owner through a foreign investment vehicle.**

- When domestic source income is paid to the actual beneficial owner through a foreign investment vehicle (foreign fund)
- The foreign investment vehicle must (i) receive an application for non-taxation/exemption on capital gains on securities or application for reduced tax rate on interest or dividend income from the actual beneficial owner, (ii) prepare a statement of the actual beneficial owner, and (iii) submit the above to the withholding agent by attaching the above to the declaration form for foreign investment vehicle before receiving the domestic source income.
- Applications, etc. submitted does not need to be submitted within three (3) years from the date of submission; provided, however, that if there is a change thereof, such change shall be submitted.

## Part 2

### Investment in PE/VC Fund in Korea

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Foreign LP side

# I. Introduction

This guideline is for foreign investors interested in investing through indirect investment vehicles (i.e., funds) in Korea. In Korea, the most representative indirect investment vehicles include venture capital (“VC”) funds, such as venture investment associations, new technology business investment associations, and private equity (“PE”) funds. Below, we will introduce the structure of Korean funds and their related tax system.

## II. Governance Structure

### 1 Comparison of Korean and Foreign Fund Structures

#### - Comparing Korean Funds with US Private Equity Funds:

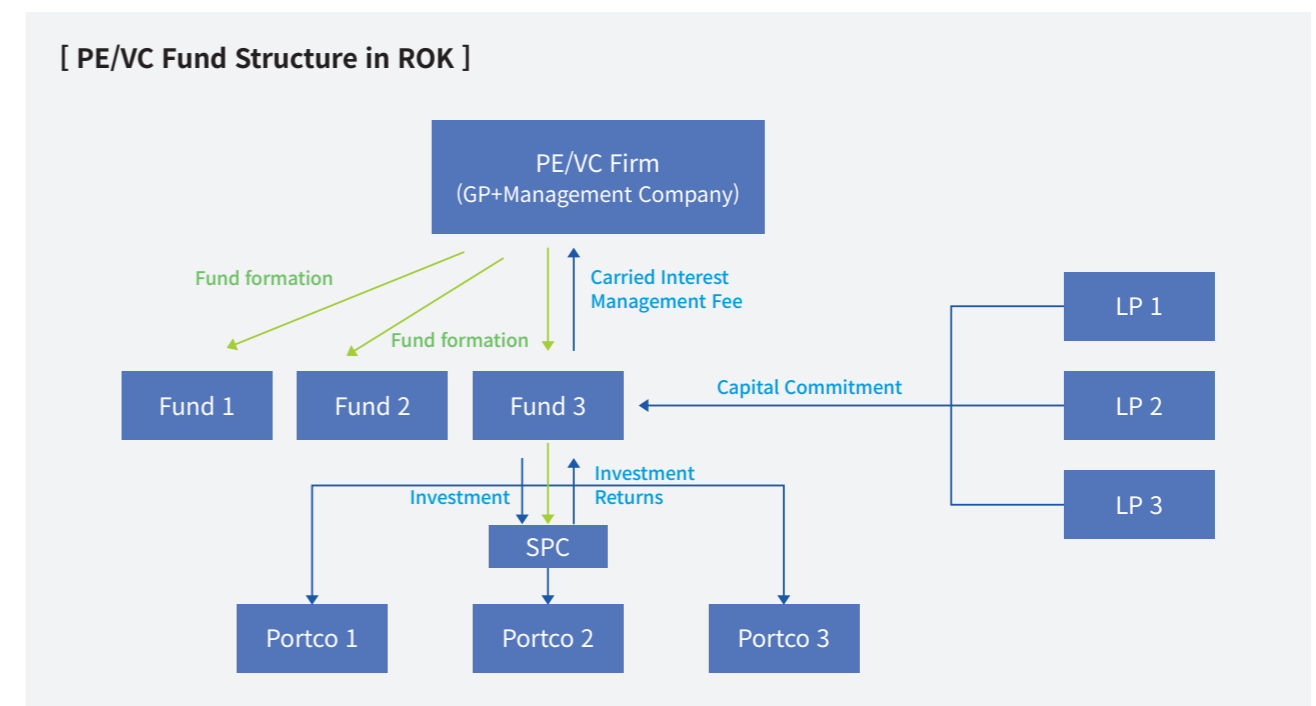
- Establishment: In the US, it is common to establish a limited partnership that serves as a fund, with investors joining as limited partners during a specific fundraising period, with the option to continue adding limited partners afterward. In contrast, Korean funds typically complete investor recruitment first before establishing and registering the fund.
- Structure: In the US, to prevent a general partner’s liabilities from affecting private investment companies or other funds, it is common to establish a separate legal entity for the general partner for each fund. In Korea, private investment companies typically directly participate as the general partner of a fund, and it is conventional for a single general partner to manage multiple funds.
- Fees: In the US, the general partner receives performance-based fees, and a separate investment management company under the private investment company may be entrusted with fund asset management and receive management fees. However, in Korea, the general

partner (private investment companies) receives both management and performance-based fees.

#### - Institutional measures to ensure independence of Korean funds: Korean funds generally have the following independence measures in place (details may vary by fund type)

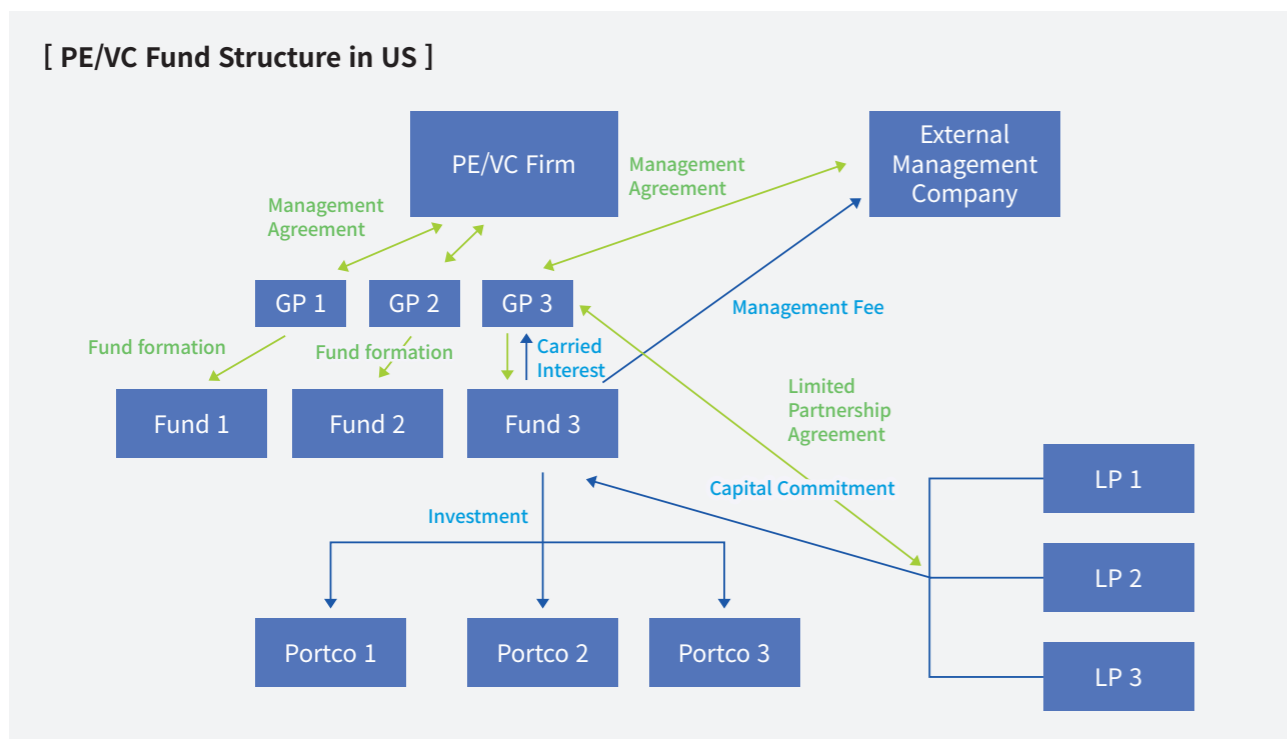
- Transactions between the general partner or their affiliates and the fund are restricted.
- Fund assets are entrusted to a trustee and managed separately with independence.
- Limited partners should not, in principle, be involved in the essential duties of the general partner (such as selection of investment target companies for PEF and other operation-related activities)
- Fund regulations specifically define the expenses to be borne by the fund.

#### - Fund structure diagram for US and Korea



\* In Korean PEFs, investment is often made through special purpose companies (“SPC(s)”) for operational flexibility, leverage effects, and quick liquidation. For VC funds, while there are no legal restrictions, the frequency of using SPC vehicles is relatively lower.

[ PE/VC Fund Structure in US ]



\* US fund companies either have internal management companies and enter into separate management agreements with individual funds, or enter into contracts with external management companies. In Korea, PE/VC firms perform fund management and operation duties without separate contracts.

## 2 Establishment and Legal Governance of Domestic PE/VC<sup>3</sup> Funds

### A. Venture Investment Association

#### (1) Fund Composition and Contribution

<sup>3</sup> While these are not legally defined terms, this section will review the investment vehicles commonly used as PE/VC funds: (i) institutional private collective investment schemes under the Capital Market Act ("PEF(s)"), (ii) venture investment associations under the Act on the Promotion of Venture Investment (assuming they are private venture investment associations; hereinafter "Venture Investment Associations"), and (iii) new technology business investment associations under the Specialized Credit Financial Business Act (assuming they are private new technology investment associations, hereinafter "New Technology Business Investment Associations").

For PEFs, Venture Investment Associations, and New Technology Business Investment Associations, the general partner corporate entity itself becomes the general partner. They do not establish a separate legal entity as a general partner for each investment deal. This is a characteristic arising from domestic regulatory environments and practices. However, it would be difficult to definitively state that this integrated structure is less flexible compared to overseas organizational structures that operate separate general partner entities for individual funds.

#### ① Composition and Qualifications of Partners

- A Venture Investment Association is composed of one or more general partners who are responsible for the association's business operations and have unlimited liability for the association's debts, and limited partners who have limited liability up to the amount of their contribution.
- The number of limited partners in a Venture Investment Association must not exceed 49. **There are no qualification restrictions on limited partners in the Venture Investment Association Act, and therefore, individual investors can participate.**

#### ② Commitment Method and Related Restrictions

- Partners of a Venture Investment Association may invest the entire amount of commitment in a lump sum or in installments as specified in the association agreement. The specific method of commitment can be stipulated in the specific association agreement, but typically a capital call method is used.
- The general partner's commitment share must be at least 1 percent of the total commitment amount.
- **The minimum value of one unit of commitment shall be at least KRW 1 million.**

#### ③ Recovery of Commitment

- Transfer of shares: Transfer of a general partner's shares requires unanimous consent from all other partners, and the transfer of limited partners' shares follows the provisions in the association agreement.
- Withdrawal from the association: Partners can withdraw from the association according to the conditions specified in the association agreement, and specific procedures for commitment refunds are determined by the association agreement.

#### (2) Governance Structure

##### ① Managing Authority and Internal Decision-Making Body

- The general partner is the representative who executes the business of the venture investment association. A joint general partner structure is also possible. The general partner may delegate some of its duties to the limited partners of the venture investment association according to an agreement.
- Typically, an association partners' meeting is established as the internal decision-making body, with provisions for resolving certain agenda items through a meeting

with a specified quorum of partners.

② **Conflict of Interest Management**

- When executing the Venture Investment Association's business, the general partner is **prohibited from**: (i) using the association's assets for the benefit of themselves or a third party, (ii) selling the association's assets to the general partner or their affiliates, or purchasing shares owned by the general partner or their affiliates with the association's assets, or (iii) extending credit to the general partner or their affiliates.
- In addition to these explicit restrictions, it is common for the association agreement to require a resolution at the association partners' meeting for other potentially conflicting transactions agreed upon by partners.
- Limited partners can review the accounting books, balance sheet, and other documents at the end of the fiscal year and inspect the association's business and financial status.
- The general partner must entrust the assets of the Venture Investment Association to a trustee, and the association assets must be managed separately.

③ **Distribution**

- Partners can agree to specify the specific distribution timing, criteria, and priority in the association's agreement.

(3) **Expenses Incurrence, Distribution and Compensation**

① **Compensation for the Manager**

- Typically, according to the association agreement, the general partner receives (i) a regular management fee not directly linked to investment performance and (ii) a performance fee based on investment performance.<sup>4</sup>

② **Other Fund-Related Costs**

- It is common for the association agreement to specifically define the costs that the Venture Investment Association will bear related to business execution. For example, costs incurred in acquiring or disposing of securities belonging to the Venture Investment Association are recognized as operating expenses.

**B. New Technology Project Investment Association**

(1) **Fund Composition and Contribution**

① **Composition and Qualifications of Partners**

- A new technology business finance company manages and operates the association's capital, serving as the general partner responsible for executing the association's business and bearing unlimited liability for the association's debts. It is possible for entities other than a new technology business finance company to become a joint general partner alongside the new technology business finance company.
- **There are no specific qualification restrictions for limited partners.**

② **Commitment Method and Related Restrictions**

- There are no special restrictions, and the specific commitment method is determined by the association agreement. The capital call method is typically used, and unlike Venture Investment Associations, there is no explicit requirement for the general partner to commit a specific minimum amount.

③ **Recovery of Commitment**

- Transfer of shares: Transfer of a general partner's shares requires unanimous consent from all other partners, and the transfer of limited partners' shares follows the provisions in the association agreement.
- Withdrawal from the association: Partners can withdraw from the association according to the conditions specified in the association agreement, and specific procedures for commitment refunds are determined by the association agreement.

(2) **Governance Structure**

① **Managing Authority and Internal Decision-Making Body**

- Unless otherwise stipulated in the association agreement, each general partner has the right and obligation to execute and represent the association's business.

<sup>4</sup> Management fees are fundamentally a base fee that provides the general partner with the resources necessary to operate the fund (e.g., staffing, fund management). On the other hand, performance fees are designed to incentivize the general partner to generate high returns. Given that the general partner's primary source of income is derived from performance fees linked to investment outcomes, it is difficult to argue that the simultaneous receipt of both management and performance fees diminishes the general partner's motivation. This argument also applies to discussions regarding New Technology Project Investment Partnerships and PEFs.

- An association partners' meeting is established as the internal decision-making body, with provisions for resolving certain agenda items through a meeting with a specified quorum of partners.

## ② Conflict of Interest Management

- No specific regulations are explicitly defined. However, the general partner must consider the interests of the New Technology Business Investment Association and its investors.
- General partners cannot engage in transactions in the same business category without other partners' consent, establishing a basic structure to prevent potential conflicts of interest.
- In addition to these explicit restrictions, it is common for the association agreement to require a resolution at the association partners' meeting for other potentially conflicting transactions agreed upon by partners.
- Limited partners can review the accounting books, balance sheet, and other documents at the end of the fiscal year and inspect the association's business and financial status.
- While there's no explicit requirement under Specialized Credit Finance Business Act to entrust collective investment assets to a trustee, it is common to select a trustee through association resolution. Since the New Technology Business Investment Association does not have a separate legal entity, its assets are legally considered directly owned by the partners. Therefore, investment performance of one association managed by the same general partner is not expected to directly impact the assets of another association.

## (3) Expenses Incurrence, Distribution and Compensation

### ① Compensation for the Manager

- A New Technology Business Investment Association may distribute a portion of the **investment profits** to the general partner as compensation for business execution, not exceeding 20% of investment returns, as specified in the association agreement.
- Typically, according to the association agreement, the general partner receives (i) a regular management fee not directly linked to investment performance and (ii) a performance fee based on investment performance

## ② Other Fund-Related Costs

- It is common for the association agreement to specifically define the costs that the New Technology Business Investment Association will bear related to business execution. For example, costs incurred in acquiring or disposing of securities belonging to the New Technology Business Investment Association are recognized as operating expenses.

## ③ Distribution

- Partners can agree to specify the specific distribution timing, criteria, and priority in the association's agreement.

## C. Institutional Private Equity Fund

### (1) Fund Composition and Contribution

#### ① Composition and Qualifications of Partners

- A PEF consists of one or more unlimited liability partners and one or more limited liability partners, with a total of no more than 100 partners.
- The PEF must designate at least one general partner for business execution in its articles of incorporation, and can have two or more general partners.
- **PEF limited partners are restricted to institutional investors and equivalent entities who are not individuals** (excluding foreigners, and excluding executives and operating personnel of the general partner), which is a significant difference from Venture Investment Associations and New Technology Business Investment Associations.
- **Particularly for foreigners, they must meet one of the following conditions under the Capital Market Act to be considered qualified as a PEF limited partner.** Each foreign individual's eligibility as a limited partner in a private equity fund must be assessed on a case-by-case basis.
  - Entities equivalent to financial institutions or financial public institutions;
  - Parent company of the PEF's general partner; or
  - Foreign corporations with no Korean shareholders that invest KRW 10 billion or more in the PEF.

## ② Commitment Method and Related Restrictions

- The primary contribution method for PEF partners is cash, with an exceptional provision to contribute securities if objective valuation is possible, there is no risk of harming the interests of the partners, and if all other partners agree.
- Partners can contribute through a capital call method, where the general partner requests contributions. Unlike Venture Investment Associations, there is no explicit requirement for the general partner to contribute a specific minimum amount.

## (2) Governance Structure

### ① Managing Authority and Internal Decision-Making Body

- The general partner has the authority to execute the PEF's business. **Limited partners are principally prohibited from involvement in the general partner's essential business functions** (such as selecting investment target companies).
- For internal decision-making matters not involving essential business functions, it is common to establish a partners' general meeting with resolutions based on legal requirements and agreements.

### ② Conflict of Interest Management

- The **general partner is principally restricted from transactions with interested parties** when managing the PEF's collective investment assets, with exceptions only when such transactions are limited in principle and are exceptionally advantageous to the PEF or with the consent of all partners.
- The general partner, through the PEF, is prohibited from acquiring securities of (i) the general partner's affiliated companies or (ii) affiliated companies of the limited partners with ownership of 30% or more in the PEF, in both cases exceeding 5% of the PEF's collective investment assets.
- Beyond these explicit restrictions, it is common to require partners' general meeting approval for other potentially conflicting transactions agreed upon by partners.
- Each PEF is a separate legal entity with assets managed separately from other PEFs, and the general partner must entrust the custody of collective investment assets to a trust company.

## (3) Expenses Execution, Distribution and Compensation

### ① Compensation for the General Partner

- The PEF can define profit distribution or priority in its articles of incorporation.
- Typically, the general partner receives (i) a regular management fee not directly linked to investment performance and (ii) a performance fee based on investment performance

### ② Other Fund-Related Costs

- The PEF's articles of incorporation typically specify operational costs to be borne by the PEF, with other business execution costs typically borne by the general partner.

### ③ Distribution

- Profits from collective investment asset management must be distributed in cash to investors. However, as stipulated in the articles of incorporation, the distribution of profits may be reserved to the PEF, and the distribution may be made in cash in excess of the profits.
- Partners can agree to specify the specific distribution timing, criteria, and priority in the PEF's articles of incorporation.

### III. Taxation

#### 1 Taxation Related to Domestic PE<sup>5</sup> Funds/VC<sup>6</sup> Funds

##### A. Taxation Structure – Application of Partnership Tax to PE Fund/VC Fund

###### (1) Contribution Phase

- If non-resident LPs invest in domestic PE funds or VC funds, there are no particular taxation issues.

###### (2) Operational Phase – Where the Fund Earns Revenues From the Management of Its Assets

- PE Fund and VC Fund: No taxation such as corporate tax, etc.
- Income Distributed from PE Funds and VC Funds to Non-Resident LPs:
  - Principle: In principle, distributed income shall be classified as dividend income.
  - Exception: In the case of institutional private equity funds (“**Institutional PE Funds**”), income is separately classified and taxed by source(\*) in accordance with the Korean Corporate Tax Act or applicable tax treaties.

※ In the case of capital gains from the transfer of securities, no taxation applies if a tax treaty is in effect and the securities do not qualify as real estate shares

- Withholding: PE funds and VC funds must withhold tax on income distributed to non-resident LPs and submit payment statements.

###### (3) Sale of Fund Interests

- **Capital gains from the sale of PE fund or VC fund interests by non-resident LPs to a third party are deemed capital gains from the transfer of securities.**

<sup>5</sup> Private Equity Fund

<sup>6</sup> New technology business investment associations, venture investment associations, etc.

- The person making the payment must withhold tax (\*) on capital gains from the transfer of securities.

※ No withholding tax applies if a tax treaty is in effect and the securities do not qualify as real estate shares.

###### (4) Liquidation of the Fund

- If the fair market value of assets distributed to the non-resident LP upon the liquidation of the Fund exceeds the equity value of the non-resident LP, the excess amount shall be deemed dividend income.

- A party/person distributing the assets must withhold tax on the dividend income.

##### B. Description of Withholding Tax and the Application of Tax Treaties For Non-Resident LP Income

###### (1) Withholding Tax System For Domestic Source Income of Non-Resident LPs

- In principle, the withholding tax on domestic source income distributed to non-resident LPs is governed by the provisions of domestic tax law. However, for residence of countries with which Korea has a tax treaty, the tax treaty takes precedence over the domestic tax law.

- Withholding Tax Rate

Domestic Source Income	Withholding Tax Rate Under the Domestic Tax Law (including Local Income Tax)	Tax Treaty Withholding Tax Rate
Interest Income	22%	Reduced Tax Rate (0~15%)
Dividend Income	22%	Reduced Tax Rate (0~15%)
Capital Gains on Securities	Min (Transfer Price *11%, Capital Gain from Transfer* 22%)	Exemption from the taxation in accordance with the principle of taxation by country of residence under the tax treaty (Provided, however, taxation may apply to real estate related shares, etc.)

## (2) Application of Tax Treaties

### - Requirements for Application of Tax Treaties

- ① A tax treaty must have been entered into between the country of residence of the non-resident VC and Korea.
- ② Non-resident VC must be the actual beneficiary of the domestic source income subject to tax treaties
- ③ In order for a non-resident VC to be exempted from taxation in accordance with the tax treaty, an application for deduction or exemption must be submitted to the withholding agent, and in order to be subjected to the reduced tax rate, the non-resident VC must submit an application for a reduced tax rate to the withholding agent

### - System of Application of Tax Treaties by Type of Income

- Interests and Dividends: In the case of a country with a tax treaty, the tax treaty's provisions for exemption or reduced tax rates apply (Varies by different tax treaties but generally within the range of 0-15%)
- Capital Gains on Securities: Most of the tax treaties adopt the method of taxation of the country of residence, meaning that **capital gains from securities of non-resident LPs are taxed in the country of residency and not in Korea**. However, for real estate shares (i.e., shares of a corporation which real estate constitutes 50% or more of its total assets) or if the shares are held by a majority shareholder (typically owning 25% or more of the shares) are transferred, there may be tax obligation in Korea, the source country (Relevant tax treaties may need to be reviewed for specific details).

## (3) Adjustment of Double Taxation

When a non-resident LP invests in a PE fund or a VC fund and pays withholding tax on distributed domestic source income to Korea, the non-resident LP may be eligible to receive a tax credit for the taxes paid in Korea. However, as the tax laws vary by country, it is necessary to verify the tax laws for each jurisdiction.

## C. Simulation (Example)

### - Basic Assumptions

- ① Application of partnership tax to PE funds or VC funds
- ② Tax Treaty – It is assumed that a tax treaty in effect between the country where the non-resident LP is located and Korea
- ③ Contribution Phase – Non-resident LPs invest 100 to PE funds or VC funds in Korea, and PE funds or VC funds invest 100 in domestic venture companies to acquire shares
- ④ Income generated during the operation phase - Dividend income 10, Capital gain from transfer of securities 150 (Transfer Price 250).
- ⑤ Sale of Fund Interests - Transfer Price 300
- ⑥ Liquidation of the Fund - The fair market price of the PE Fund or VC Fund at the time of liquidation is 300
- ⑦ Tax Treaty Withholding Tax Rate – Dividend income is subject to a 10% withholding tax (including local income tax) while capital gain from transfer of securities is exempt from taxation)

### - Simulation Results: Withholding Tax

Classification	Investments in Institutional PEFs		Investments in Other Funds	
	General Shares	Real Property Shares	General Shares	Real Property Shares
1. Contribution Phase	No Taxation			
2. Operational Phase	<b>1</b>	<b>28.5</b>	<b>16</b>	<b>16</b>
2.1 Dividend Income	1 <sup>(1)</sup>	1 <sup>(1)</sup>	1 <sup>(1)</sup>	1 <sup>(1)</sup>
2.2 Capital Gains from Transfer of Shares	- <sup>(2)</sup>	7.5 <sup>(3)</sup>	15 <sup>(4)</sup>	15 <sup>(4)</sup>
3. Sale of <sup>7</sup> Fund Interests	-	.8 <sup>(5)</sup>	-	.8 <sup>(5)</sup>

<sup>7</sup> It is assumed that the sale of fund interests and the fund liquidation are mutually exclusive events.

Classification	Investments in Institutional PEFs		Investments in Other Funds	
	General Shares	Real Property Shares	General Shares	Real Property Shares
4. Upon liquidation of the Fund	4 <sup>(*6)</sup>	4 <sup>(*6)</sup>	4 <sup>(*6)</sup>	4 <sup>(*6)</sup>
<b>5. Total withholding tax;</b>				
<b>5.1 Upon Sale of Fund Interests (=1+2+3)</b>	1	37.3	16	24.8
<b>5.2 Upon liquidation of the Fund (=1+2+4)</b>	5	32.5	20	20

(\*1) 10x10% (Applying the reduced tax rate of 10% under the tax treaty with respect to dividend income)

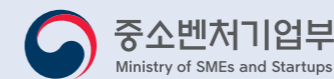
(\*2) Non-taxation on capital gains from transfer of securities pursuant to tax treaties

(\*3) Min [(250 -100) x22%, 250 x11%] (Non-taxation on capital gains from the transfer of securities cannot be applied to real estate shares under the tax treaty, and may be taxed under the domestic tax law)

(\*4) (250 -100) x 10% (Capital gains from the transfer of securities distributed from funds other than Institutional PE Funds are deemed dividend income, and the reduced tax rate under the tax treaty is applied at 10%)

(\*5) Min [(300 - 260<sup>8</sup>) x22%, 300 x11%] (The capital gain on the sale of the Fund's interests shall be deemed capital gains from the transfer of securities)

(\*6) (300-260) x 10% (the portion in which the fair market value of the fund exceeds the value of the fund's interests constitute dividend income, and the reduced tax rate of 10% under the tax treaty is applied with respect to dividend income)



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<sup>8</sup> Fund's equity value: Initial acquisition price (100) + increase in equity value due to dividend income (10) + increase in equity value due to capital gains from transfer of shares (150).