VI

Bond Market Costs and Taxation

This chapter details the typical costs incurred by issuers and investors in the Korean bond market, with a particular emphasis on costs associated with bond or note issuance and settlement.

For ease of reference, the descriptions of the types of costs are given in the context of the actions to be taken by issuers or investors (as explained in this document) and follow the lifecycle of a bond or note in the Korean bond market.

A. Costs Associated with Bond and Note Issuance

1. Application for Issuance via Public Offer (Mandatory)

Issuers intending to offer bonds or notes via a public offering need to file an SRS with the FSS. For the process of SRS submission and review, the FSS levies a fee on the issuer, referred to as allocated contribution. The rate of allocated contributions is determined by the FSC, pursuant to Article 388 in the Enforcement Decree of FSCMA (Table 6.1). The fee is payable at the time the SRS is submitted to the FSS.

Table 6.1: Allocated Contributions for Submission of Securities Registration Statement

Condition	Fee rate
Maturity ≤ 1 year	0.05% of total issue value
1 year < Maturity ≤ 2 years	0.06% of total issue value
2 years < Maturity	0.07% of total issue value

Source: Financial Supervisory Service.

2. Registration of Bonds in the Over-the-Counter Market

KOFIA administers the OTC market in the Republic of Korea. Bonds and notes to be traded on K-Bond need not be registered with KOFIA by default. Only bonds and notes issued by private placement to be traded among QIBs (QIB-eligible securities) are required to be registered with KOFIA.

At present, KOFIA does not charge a fee for the registration of bonds and notes in the QIB Market.

3. Managing Company Fee

The appointment of a managing company in the Korean bond market is not mandatory. The managing company is, among other roles, responsible for the submission of issuance applications, issuance documentation and disclosure items, and supporting information to the relevant regulatory authorities.

The managing company and underwriters will charge a fee, which should be expected to follow established market practice and may be subject to negotiations between the issuer and the managing company and underwriters. Under current market practice, KRW20~KRW25 per KRW10,000 face value of the bonds or notes is charged as the total fee. Of the total fee charged, a portion of about KRW5 per KRW10,000 face value (or about 20%–25%) is distributed to the managing company. The share of a managing company tends to increase with the introduction of a book-building system.

4. Underwriter Fee

Issuers are not required by law to appoint one or more underwriter(s) in the Republic of Korea; often, the managing company performs the role of underwriter as well. However, some offers of bonds and notes may require the services of one or more underwriters to place the debt securities with institutional investors or distribute the issuance to the public.

Underwriters charge a fee, typically commensurate with the effort and risk of taking over parts or all of a bond or note issue from the issuer. This fee or service charge is charged to the issuers as part of the total cost billed by the managing company, and should be expected to follow established market practice and may be subject to negotiations between issuer and underwriter(s). After the share due to the managing company, the remaining fee amount (about KRW15–KRW20 per KRW10,000 face value) is distributed to the underwriters proportional to the amount of the bonds or notes underwritten by each underwriter.

5. Agent Fees

The appointment of a number of agents in the context of a bond or note issuance is mandated to ensure effective and professional administration of the issue, a division of duties, and the observance of international best practice. The managing company will administer the issuance process of debt instruments into the market, while a paying agent is responsible for handling the cash flow at issuance and for benefits arising from the issue and upon redemption. The indenture trustee holds the fiduciary responsibility toward the bond- or note-holders, and acts in the case of default or distress.

The paying agent and the indenture trustee are also remunerated for their services based on market practice. The standard contract for an indenture trustee for non-guaranteed corporate bonds stipulates that the fee for, and costs incurred by, the indenture trustee are paid by the issuing company.

6. Korea Securities Depository Registration Fees

KSD charges a registration fee for the creation of new debt securities in its book-entry system, as shown in Table 6.2. The fees differ between the debt securities issued by resident and nonresident issuers, and have a maximum amount.

Table 6.2: Debt Securities Registration Fee at Korea Securities Depository

Classification	Fee Rate
Domestic entity issuing bonds	• KRW10 billion and less: KRW100,000 • KRW10 billion and more: Registration amount x 1/100,000 (ceiling: KRW500,000)
Foreign entity issuing bonds	• KRW10 billion and less: KRW500,000 • KRW10 billion and more: Registration amount x 5/100,000 (ceiling: KRW10,000,000)

Source: Korea Securities Depository.

Information on the public and corporate debt securities registration fee and fee levels is available in the fee schedule published on the KSD website (presently only in Korean).[34]

B. Listing Fees

In the Republic of Korea, only bonds and notes issued via a public offering may be listed on KRX. A listing is optional. If an issuer decides to list its debt securities, KRX applies the following fees to such listings. Listing fees are paid when the listing request is made, but for shelf-listed bonds, fees are paid when the results of the issuance are announced.

1. Listing Review Fee

KRX requires prospective issuers—both resident and nonresident—to submit to a listing eligibility review prior to actual listing. If a listing is intended for a public offer, the issuer should include the results of a listing eligibility review in its SRS to be filed with the FSC.

KRX charges a listing review fee of between KRW100,000 and KRW1.7 million for the review of the issuer's, as well as a bond's or note's, listing eligibility, depending on the size of the issue. The fee is not refundable in case of an unsuccessful application. KRX does not charge for the listing eligibility consultation for a foreign issuer.

2. Annual Listing Fee [or another continuous fee, as applicable]

KRX also levies an annual listing fee, fixed at KRW100,000, payable for the first 5 years or depending on the maturity of the debt securities, whichever comes first. If a bond has a maturity beyond 5 years, the issuer will pay a maximum of KRW500,000 in annual listing fees.

The current listing fee schedule is available from the KRX website.[35]

C. Ongoing Costs for Issuers of Corporate Bonds and Notes

Once an issuer has issued bonds or notes in the Korean market, regardless of whether those are listed, and whether they are traded in the OTC market or on exchange, a number of recurring costs may apply throughout the lifecycle of the bonds

[34] See http://www.ksd.or.kr/static/KB1200000000.home?menuNo=84
[35] See http://global.krx.co.kr/contents/GLB/03/0303/0303080400/GLB0303080400.jsp

or notes. These recurring costs may be charged by agents or service providers appointed by the issuer, such as a paying agent or an indenture trustee.

1. Paying Agent Fees [as applicable]

Corporate bond issuers may appoint a paying agent, who will remit principal and interest payments to KSD for further distribution. The paying agent is expected to charge a fee commensurate with the role and in line with market practice.

KSD distributes principal and interest payments for the corporate bonds and notes deposited in its book-entry system to its participants who, in turn, onward distribute the payments to their clients. At the time of compilation of this Bond Market Guide, KSD did not charge the issuer for the provision of interest payments or redemption processing.

2. Indenture Trustee [as applicable]

The issuer of corporate bonds offered or sold to the public shall appoint an indenture trustee. The indenture trustee will charge a fee commensurate with the expectations of its function, which is expected to follow market practice.

D. Costs for Deposit and Withdrawal of Bonds and Notes

The Korean market is considered immobilized. Securities continue to coexist with securities created and kept as book-entry records only. In the event that an investor or their agent, as KSD participant, wishes to deposit physical securities certificates into an account with KSD, a deposit fee is applicable (Table 6.3).

Likewise, should an investor or KSD participant choose to withdraw securities from their account with KSD in the form of physical certificates, KSD would charge a withdrawal fee.

1. Deposit Fee

The deposit fee policy was amended in January 2010 to compensate for the costs incurred by KSD in executing its deposit-related operations, which grew in proportion with the increasing deposit balance of a particular security.

Table 6.3: Deposit Fee at Korea Securities Depository

Range	Fee Rate per KRW 10,000 Face Value
KRW1 trillion and less	KRW0.00125
More than KRW1 trillion up to KRW3 trillion	KRW125,000 + KRW0.001
More than KRW3 trillion	KRW325,000 + KRW0.00075

Source: Korea Securities Depository.

For registered bonds that do not exist in physical form, KSD applies a discount rate of 50%.

2. Withdrawal Fee

There is no withdrawal fee. KSD now only accepts bonds in registered form without physical certificates, with the exception of National Housing Bond Type 2.

E. Costs for Account Maintenance and Safekeeping at Korea Securities Depository

KSD does not impose an account maintenance fee on its participants. Participants are charged either the deposit fee or the securities company fee.

F. Costs Associated with Bond and Note Trading

Bonds and notes issued in the Korean market may be traded in the OTC market or, for publicly offered debt securities only, listed and traded on KRX. The fees applicable to a debt securities transaction differ between these two trading options, as further explained in this section.

1. Exchange Trades

Investors carry out transactions in debt securities on the exchange by submitting an order to, or via, investment brokerage companies, which are members of KRX.

a. Brokerage Fee (investor pays to securities firm)

A securities firm may levy brokerage fees on investors for a trade in bonds or notes on the KRX market. When fee levels and methods are determined or changed, this should be notified to KRX within 5 business days. Securities firms apply their own fee levels, but they determine the levels corresponding to the remaining time to maturity of bonds traded.

b. Trading Fee (securities firm pays to Korea Exchange)

KRX may levy a trading fee on a securities firm when the firm conducts principal trading on its own account or executes trading orders received from investors for the KRX market. A trading fee is determined by multiplying the traded amount by the fee level; the trading fee for KRX KTB is KRW10,940 per trade amount up to a value of KRW10 billion.

c. Clearing and Settlement Fee (securities firm pays to Korea Exchange)

KRX also levies a clearing and settlement fee since every order placed within the KRX market needs to be processed via the clearing and settlement system of KRX. The clearing and settlement fee for KRX KTB is KRW1,710 per trade amount up to a value of KRW10 billion.

The securities firm may decide to defray its costs incurred for an exchange trade by including it into the securities price or its own fee, or bill these fees to the investor as out-of-pocket expenses.

2. Over-the-Counter Trades

Market participants trading debt securities for their investor clients in the OTC market may charge a brokerage fee or levy other such charges for each trade, subject to their own conditions and considerations.

Such brokerage fees in OTC trading are determined by each broker company. Typical brokerage fee rates are set as follows: for bonds or notes with residual time to maturity of less than 1 year, the fee is set at around KRW0.5 per KRW10,000 face value; for bonds and notes with residual time to maturity of 1 year or more, the fee is set at around KRW1 per KRW10,000 face value.

G. Costs for Settlement and Transfer of Bonds and Notes

To defray its cost of settlement and depository operations, KSD levies a settlement fee and a book-transfer fee for transactions instructed by its participants. The fees are levied on a transaction basis and billed to the KSD participant on a monthly basis, payable by the 20th day of the following month.

1. Settlement Fee

KSD applies a settlement fee for bonds and notes that are transacted in the OTC market as well as on the exchange. The fee is charged at 0.001646 basis points on the total transacted amount.

2. Book-Transfer Fee

KSD also charges a fee for conducting the book transfer activities, being one of the major cost centers that require great amount of resources. As a result, KSD charges a transfer fee (official name: book-transfer fee) of KRW1,000 to the transferor of a given transaction.

There are exceptions to this rule however. Book-entry transfers that are made upon request from the transferor who wishes to use services offered by KSD such as securities borrowing and lending and repo are exempt from book-transfer fee obligations.

H. Taxation Framework and Requirements

The tax authority in the Republic of Korea is the National Tax Service. The provisions for the taxation of income and capital gains from debt securities are contained in the Income Tax Act and the Corporate Tax Act, for individual and institutional investors, respectively. Nonresidents are also subject to income tax in the same manner as residents. However, individuals or corporates resident in any country that has a tax treaty with Korea are taxed on their income in accordance with the relevant tax treaty.

Table 6.4 provides an overview of the taxes relevant for investments in the bond market in the Republic of Korea and their applicable rates, with relevant details explained in the subsequent sections.

For their individual tax treatment and the applicability of double taxation treaties, entities investing or wanting to invest in the Korean bond market are encouraged to seek tax advice from a professional firm.

Table 6.4: Duties and Taxes on Fixed-Income Securities in the Republic of Korea

Duties and Tax	Type of Bonds	Tax Rate
Corporate Income Tax	Government	10%–22%[a]
	Corporate	10%–22%[a]
Withholding Tax	Government	15.4%[b]
	Corporate	15.4%[b]
Capital Gains Tax	Government	10% or 22%[c]
	Corporate	10% or 22%[c]
Stamp Duty	N.A.	N.A.
VAT	N.A.	10%

N.A. = not applicable, VAT = value-added tax.
[a] Depending on tax base of individual corporation.
[b] 15.4% applicable for government bonds and domestic corporate bonds, which constitute almost all debt securities issued in the Korean bond market.
[c] 10% of gross proceeds from sale, or 22% from net capital gains, whichever is lower.
Source: Clearstream, KPMG.

1. Corporate Income Tax

The corporate income tax in the Republic of Korea ranges from 10% to 22%, depending on the amount of the tax base (assessable income). Other related taxes may be levied in individual years of assessment.

A corporation is considered to reside in the Republic of Korea if the corporation has its head or main office, or place of effective management, in the country. A resident corporation is liable in the Republic of Korea for corporate income tax on its worldwide income. Resident corporations include the subsidiaries of foreign corporations, but not their branches.

A nonresident corporation is liable for corporate income tax on income from Korean sources only.[36]

The Corporate Tax Act stipulates that corporate tax shall be imposed on all income of a company for each business year, including interest income and capital gains from bonds and notes. In the case of interest income from bonds, the tax must be withheld at the time the income is generated. The amount of tax withheld shall be deemed to be prepaid as corporate tax and, thus, is deducted in computing and levying the corporate tax.

2. Taxable Income

According to the Income Tax Act, interest and discount amounts are considered taxable interest income.

[36] This and other relevant information was adapted by SF1 consultants from KPMG. 2015. *Korea Tax Profile*. https://home.kpmg.com/content/dam/kpmg/pdf/2015/10/korea-2015.pdf

The taxable discount amount stipulated in the Income Tax Act only refers to the issuance discount (the amount according to the market interest rate at the point of bond issuance), not the market discount (the amount according to the market interest rate at the point of early bond redemption). Persons redeeming their bonds before maturity only have to pay tax on the amount of interest accrued during the possession of the bonds.

To help promote and develop the government bond market, exemptions exist for (i) government bonds, (ii) industrial finance bonds, (iii) deposit protection fund bonds and compensation fund bonds for deposit protection fund bonds, and (iv) MSBs issued by BOK in the open market. In these cases, only the amount of interest accrued by the coupon rate exclusive of the discount amount is considered to be taxable interest income, pursuant to Article 22-2 (2) of the Enforcement Decree of the Income Tax Act.

Under normal circumstances, persons transferring their bonds to another person before maturity could accrue capital gains due to the difference between the interest rate at the point of bond issuance and at the point of the transfer. But the Republic of Korea's taxation law does not levy tax on capital gains accrued from the transfer of bonds. When calculating taxable income, the amount of interest income shall be included in the total gross income accrued during the corresponding year, pursuant to Article 16 (2) and Article 17 (3) of the Income Tax Act.

As a result, expenses incurred by an investor during the disposal or sale of securities are not recognized as tax-deductible expenses.

3. Receipt Date of Income

The date of receipt of income in the form of bond interest shall be the date of receipt of such payments for interest and discount amounts in the case of bearer public bonds, and the payment date under the agreement for interest and discount amount in the case of non-bearer public bonds, according to Article 45 (2) (3) of the Enforcement Decree of the Income Tax Act. The receipt date of income accrued from coupon interest shall be the date of the coupon. As for the discount, the receipt date of income shall be the date of the maturity, which is the receipt date of such payment.

In the case of the sale of bonds before maturity, the receipt date of income from interest shall be the sale date of the relevant bonds. Therefore, when discount bonds are sold before maturity, the receipt date of income from the sale of the relevant bonds shall be the sale date, and if the bonds were redeemed at maturity, the date of redemption at maturity shall be the date of income from such payment according to Article 45 (10) of the Enforcement Decree of the Income Tax Act.

In contrast, in the case of commercial notes or cover notes (discounted notes) with short maturity terms traded using a passbook held in custody, the receipt date of income shall be the date of the sale of the notes at a discount, if the owner of the notes decides to pay the withholding tax on the same day. Consequently, such bonds are referred to as prepaid interest bonds.

4. Withholding Tax

Interest paid to a nonresident is subject to a withholding tax of 15.4% for interest on bonds issued by the Government of the Republic of Korea, a local government, or a domestic corporation, unless the withholding tax rate can be reduced under a tax treaty.

5. Capital Gains Tax

The capital gains and losses of a resident corporation are included in its taxable income and taxed at the standard corporate income tax rates.

Generally, nonresidents of the Republic of Korea are liable for capital gains tax on domestic securities at the lower of the following rates:

- 11% of the gross proceeds realized from the sale (including the 10% surtax), or
- 22% of the net capital gains (including the 10% surtax).

Residents of countries that have concluded a Double Taxation Treaty with the Republic of Korea, or countries with reciprocity rules, will either be exempted or taxed depending on the Double Taxation Treaty.

The selling broker is responsible for the calculation and withholding of the capital gains tax and for its payment to the National Tax Service.[37]

6. Stamp Duty

There is no stamp duty withheld on transactions in securities held with custodians. A stamp duty may, however, be payable on specific transactions, typically related to direct investment.

7. Value-Added Tax

The standard rate of VAT is 10%.

8. Double Taxation Treaty

As of 2017, the Republic of Korea had signed treaties for the avoidance of double taxation with 92 countries, including most of the ASEAN+3 countries.

The provisions of an applicable tax treaty shall preferentially apply to the classification of domestically sourced income of a nonresident or foreign corporation, notwithstanding the provisions in the Income Tax Act and the Corporate Tax Act, respectively.

Article 29 of the Adjustment of International Taxes Act prescribes that the lower of the limited tax rate provided by a tax treaty or any of the tax rates in the Income Tax Act or Corporate Tax Act shall apply to interest that constitute the domestically sourced income of a nonresident or foreign corporation under the tax treaty.

9. Tax Exemption for Nonresident Investors

The Republic of Korea had previously exempted nonresident investors from withholding tax on interest income earned from investment in KTBs and MSBs. The exemption, however, was abolished in 2011. Currently, nonresident investors may avail themselves of tax relief under applicable tax treaties.

[37] This and other relevant information was adapted by SF1 consultants from Clearstream Luxembourg. *Market Taxation Guide 2018.*

10. Tax Treatment of Investment Funds

Investment funds are subject to a specific treatment under the Corporate Income Tax Law. The provisions focus on the legal beneficiary level. While the IRC is set at the fund level, the tax form submission requires disclosure of the holding shares of the various domiciles of the fund holders. Thereafter, a blended tax rate is formed according to the relevant double taxation treaties for the domiciles declared. This practice only applies to funds or investment vehicles with more than 100 beneficial owners. In case a fund or investment vehicle has fewer than 100 beneficial owners, the details of each investor must be submitted. The necessary information is collected and submitted to the tax authorities by the custodian, as the standing proxy of the investor, here being the fund or investment vehicle.