TECHNICAL EXPLANATION OF THE CONVENTION BETWEEN THE UNITED STATES OF AMERICA AND THE REPUBLIC OF KOREA FOR THE AVOIDANCE OF DOUBLE TAXATION AND THE PREVENTION OF FISCAL EVASION WITH RESPECT TO TAXES ON INCOME AND THE ENCOURAGEMENT OF INTERNATIONAL TRADE AND INVESTMENT, SIGNED AT SEOUL ON JUNE 4, 1976

GENERAL EFFECTIVE DATE UNDER ARTICLE 31: 1 JANUARY 1980

It is the practice of the Treasury Department to prepare for the use of the Senate and other interested persons a Technical Explanation of the tax conventions which are submitted to the Senate for its advice and consent to ratification.

An Income Tax Convention with Korea was signed June 4, 1976, and submitted by the President to the Senate on September 3, 1976. On July 19 and 20, 1977 and on June 6, 1979, the Senate Committee on Foreign Relations held hearings and this Technical Explanation was presented. The Senate voted its advice and consent on July 9, 1979, and instruments of ratification were exchanged on September 20, 1979.

TABLE OF ARTICLES

ARTICLE 1
Taxes Covered

Paragraph (1) designates the taxes of the Contracting States which are the subject of the Convention. In the case of the United States, the subject taxes are the Federal income taxes imposed by the Internal Revenue Code ("Code") (referred to as "United States tax"). However, in certain situations described in paragraph (8) of Article 4 (General Rules of Taxation), the United States reserves its right to impose taxes under Sections 531 (accumulated earnings tax) and 541 (personal holding company tax), except as provided in such paragraph (8).

In the case of Korea, paragraph (1) provides that the subject taxes are the income tax and the corporation tax (referred to as "the Korean tax"). In an exchange of notes, Korea has agreed that the term "Korean tax" also includes the Korean Defense tax assessed on the taxes referred to in paragraph (1).

Pursuant to paragraph (2), the Convention will also apply to taxes substantially similar to those covered by paragraph (1) which are imposed in addition to, or in place of, existing taxes, after June 4, 1976 (the date of signature of the Convention).

Under paragraph (3), for the purpose of Article 7 (Nondiscrimination), the Convention will apply to taxes of every kind imposed at the national, state, or local level; and for purposes of Article 28 (Exchange of Information), the Convention will apply to taxes of every kind imposed at the national level.

ARTICLE 2
General Definitions

Paragraph (1) sets out definitions of certain basic terms used in the Convention. A number of important terms, however, are defined elsewhere in the Convention.

The term "United States" means the United States of America. When used in a geographical sense, the term means the states of the United States and the District of Columbia. Thus, the Convention does not apply to possessions of the United States or the Commonwealth of Puerto Rico. The term "Korea" means the Republic of Korea.

When used in a geographical sense, the term "Korea" means all territory in which the laws relating to Korean tax are in force, and the terms "United States" and "Korea" also include

their respective territorial seas and, in general accord with the principles of section 638 of the Code, their continental shelves.

The term "Contracting State" means the United States or Korea as the context requires.

The term "person" includes an individual, a partnership, a corporation, an estate, a trust or any body of persons.

The term "United States corporation" or "corporation of the United States" is defined as a corporation which is created or organized under the laws of the United States, any state thereof, or the District of Columbia, or any unincorporated entity treated as a United States corporation for United States tax purposes. A "Korean corporation" or "corporation of Korea" is defined as a corporation (other than a United States corporation) which has its head or main office in Korea, or any entity treated as a Korean corporation for Korean tax purposes.

With respect to the United States, the term "competent authority" means the Secretary of the Treasury or his delegate. With respect to Korea, it means the Minister of Finance or his delegate.

The term "State" means the United States, Korea or any other National State.

The term "citizen", in the case of the United States, is defined as a citizen of the United States, and in the case of Korea, the term is defined as a national of Korea.

Paragraph (2) provides that any term used in the Convention which is not defined therein shall, unless the context otherwise requires, have the meaning which it has under the laws of the Contracting State whose tax is being determined. However, where a term has a different meaning under the laws of Korea and the United States or where the meaning under the laws of one of the Contracting States is not readily determinable, the competent authorities may for purposes of the Convention establish a common meaning in order to prevent double taxation or to further any other purpose of the Convention.

ARTICLE 3
Fiscal Domicile

This Article sets forth rules for determining the residence of individuals, corporations, and other persons for purposes of the Convention. Residence is important because, in general, only a resident of one of the Contracting States may qualify for the benefits of the Convention.

In paragraph (1), the term "resident of Korea" is defined as a Korean corporation (as defined in Article 2 (General Definitions)) and any person (except a corporation or any entity treated under Korean law as a corporation) resident in Korea for purposes of its tax. Similarly, "resident of the United States" means a United States corporation (as defined in Article 2 (General Definitions)) and any person (except a corporation or any unincorporated entity treated as a corporation for United States tax purposes) resident in the United States for purposes of its

tax. Thus, a resident of the United States includes a resident alien individual and a resident citizen but under no circumstances a foreign corporation. A citizen of the United States or Korea is not automatically a resident of the United States or Korea for purposes of this Convention.

The Convention provides that a person acting as a partner or fiduciary is considered a resident of a Contracting State only to the extent that the income derived by such person is subject to tax in such Contracting State as the income of a resident. For example, under United States law, a partnership is never, and an estate or trust is often not, taxed as such. Under the Convention, income received by a partnership, estate, or trust will not be treated for purposes of the Convention as income received by a resident of the United States unless such income is subject to tax in the United States as the income of a resident. Thus, the treatment of income received by a partnership will be determined by the residence and taxation of its partners for United States tax purposes with respect to that income. To the extent the partners are subject to United States tax as residents of the United States, the partnership will be treated as a resident of the United States. Similarly, the treatment of income received by a trust or estate will be determined by the residence and taxation of the person subject to tax on such income, which may be the grantor, the beneficiaries or the trust or estate itself, as the case may be.

Paragraph (1) also provides that in determining the residence of a partnership which makes a payment, that partnership shall be considered a resident of the State under the laws of which it was created or organized. This paragraph is to be used in the determination of the source of interest. Thus, if a partnership organized in the United States pays interest to a resident of Korea, the source of the interest would be the United States even if none of the partners are residents of the United States.

Under paragraph (2), an individual who is a resident of both Contracting States under paragraph (1) will, for purposes of the Convention, be deemed to be a resident of the Contracting State in which he has his permanent home (where an individual dwells with his family), his center of vital interests (closest economic and personal relations), a habitual abode, or his citizenship, in the order listed. If the issue is not settled by these tests, the competent authorities will decide by mutual agreement the one Contracting State of which he will be considered to be a resident.

Since the definitions of residence in this Article apply for purposes of the entire Convention, an individual who is deemed to be a resident of one Contracting State and not a resident of the other Contracting State by reason of paragraph (2) will be deemed to be a resident only of the first-mentioned Contracting State for all purposes of the Convention, including Article 4 (General Rules of Taxation). For example, if an individual is determined to be a resident of Korea under paragraph (2) and is also considered to be a resident of the United States under the laws of the United States, such individual would continue to receive the exemptions and special benefits granted by the Convention to residents of Korea, unless the individual is a citizen of the United States (see the saving clause of paragraph (4) of Article 4 (General Rules of Taxation)).

ARTICLE 4

General Rules of Taxation

Under paragraph (1), a resident of one Contracting State may be taxed by the other Contracting State on any income from sources within that other Contracting State and only on such income, subject to any limitations set forth in the Convention. For this purpose, the source rules contained in Article 6 (Source of Income) are to be applied. However, if the resident is a citizen of the other Contracting State, that other Contracting State may tax the resident without regard to this paragraph because of the saving clause of paragraph (4) of this Article.

Paragraph (2) contains the customary rule that the Convention will not restrict in any manner any exclusion, exemption, deduction, credit, or other allowance now or hereafter accorded by the laws of a Contracting State in the determination of a tax imposed by it, or by any other agreement between the Contracting States. This rule reflects the principle that a convention should not increase the tax burden on residents of the Contracting States.

Paragraph (3) provides that the provisions of the Convention shall not affect Korean law so as to deny benefits accorded residents of the United States under the provision of the Korean Foreign Capital Inducement Law No. 2598 of March 12, 1973 as amended or any similar law to encourage investment in Korea. This paragraph applies only with respect to Korean law, and has no impact on United States tax on the Korean source income which may benefit from such provisions.

Paragraph (4) contains the traditional saving clause under which the United States reserves the right to tax its citizens and residents (as determined under Article 3 (Fiscal Domicile)) as if the Convention had not come into effect. However, under paragraph (5), the saving clause does not apply in several cases in which its application would contravene policies reflected in the Convention. Thus, the saving clause does not affect the provisions with respect to relief from double taxation, nondiscrimination, social security payments, or the mutual agreement procedure. Moreover, the saving clause does not affect the benefits of the Convention to teachers, students and trainees, and individuals performing governmental functions, who are neither citizens of, nor have immigrant status in, the Contracting State imposing the tax. In the case of the United States, "immigrant status" means the individual has been admitted to the United States for permanent residence. The saving clause is reciprocal.

Paragraph (6) authorizes the competent authorities of the Contracting States to prescribe regulations necessary to carry out the provisions of the Convention. On the United States side, this authority is also provided by section 7805 of the Code.

Paragraph (7) allows, for purposes of United States tax, in the case of a resident of Korea who is not a resident of the United States, a deduction for personal exemption (subject to the conditions prescribed in sections 151 through 154 of the Code as in effect on June 4, 1976) for the spouse of the taxpayer and for each child of the taxpayer present in the United States and residing with him in the United States at any time during the taxable year. These additional deductions shall not exceed that proportion of the taxpayer's entire income from all sources, for any taxable year, which is from sources within the United States and which is treated as effectively connected with the conduct of a trade or business within the United States within the

meaning of section 864(c). These additional deductions are to continue as long as section 873 of the United States Internal Revenue Code provides only one personal exemption for a taxpayer who is a resident of Korea and not a resident of the United States.

Paragraph (8) reserves the right of the United States to impose its personal holding company tax (section 541 of the Code) and its accumulated earnings tax (section 531 of the Code) notwithstanding any provision of the Convention. However, paragraph (8) also provides that a Korean corporation will be exempt from the personal holding company tax in any taxable year if all of its stock is owned, directly or indirectly, by one or more individuals who are residents of Korea (and not citizens of the United States) for that entire year. In addition, a Korean corporation will be exempt from the accumulated earnings tax in any taxable year unless it is engaged in trade or business in the United States through a permanent establishment at any time during such year. Even if a Korean corporation is engaged in trade or business in the United States through a permanent establishment at any time during the taxable year it may be subjected to the accumulated earnings tax only with respect to any income derived from sources within the United States. See Regulation section l.532-1 (c).

ARTICLE 5
Relief from Double Taxation

Under paragraph (1), the United States agrees to allow a United States citizen or resident as a credit against the United States tax the appropriate amount of Korean tax in accordance with the provisions and subject to the limitations of the law of the United States (as it may be amended from time to time without changing the principles of paragraph (1)). In addition, in the case of a United States corporation owning at least ten percent of the voting power i.e., voting stock) of a Korean corporation from which it receives dividends in any taxable year, the United States will allow credit for the appropriate amount of Korean tax paid by the Korean corporation paying such dividends with respect to the profits out of which such dividends are paid. The appropriate amount will be based upon the amount of tax paid to Korea, but the credit shall not exceed the limitations (for the purpose of limiting the credit to the United States tax on income from sources within Korea or on income from sources outside of the United States) provided by United States law for the taxable year. This provision does not require the United States to maintain a per-country or overall limitation in the future so long as the general principle of a foreign tax credit remains in effect. For the purpose of applying the United States credit in relation to taxes paid to Korea, the rules set forth in Article 6 (Source of Income) will be applied to determine the source of income.

Paragraph (2) contains a reciprocal provision under which, in accordance with the provisions and subject to the limitations of Korean law (as it may be amended without changing the general principles of the Treaty Article), Korea will allow to its citizens and residents a credit against Korean tax for the appropriate amount of income taxes paid to the United States. Furthermore, in the case of a Korean corporation owning at least ten percent of the voting power of a United States corporation from which it receives dividends in a taxable year, Korea shall allow a credit for the appropriate amount of taxes paid to the United States by the United States corporation paying the dividends with respect to the profits out of which such dividends are paid.

The appropriate amount will be based on the amount of tax paid to the United States, but the credit may not exceed that portion of Korean tax which such citizen's or resident's net income from sources within the United States bears to his entire net income for the same taxable year. For the purpose of applying the Korean credit in relation to taxes paid to the United States, the rules set forth in Article 6 (Source of Income) shall be applied to determine the source of the income.

ARTICLE 6
Source of Income

This Article contains the source rules which are to be used in applying the provisions of the Convention, such as Article 5 (Relief from Double Taxation). Under Article 4 (General Rules of Taxation), one Contracting State may tax a resident of the other Contracting State only on income from sources within the first-mentioned Contracting State (provided the resident is not a citizen of the first-mentioned Contracting State).

Paragraph (1) provides that dividends will be treated as income from sources within a Contracting State only if paid by a corporation of that Contracting State.

Under paragraph (2), with two exceptions, interest will be treated as income from sources within a Contracting State only if paid by that Contracting State, a political subdivision or a local authority thereof, or by a resident of that Contracting State. Under the first exception, if the person paying the interest (whether or not such person is a resident of a Contracting State) has a permanent establishment in a Contracting State in connection with which the indebtedness on which the interest is paid was incurred and such interest is borne by the permanent establishment, the interest will be deemed from sources within the Contracting State in which the permanent establishment is situated. For example, if a resident of France has a permanent establishment in Korea which borrows money from a resident of the United States and bears the interest, the interest will be deemed to be from Korean sources. Thus, if the limitation in paragraph (2) of Article 13 (Interest) is applicable, this interest will be taxed in Korea at the reduced rate. As provided in paragraph (8) of Article 9 (Permanent Establishment), the principles of Article 9 will be applied to determine whether the resident of France has a permanent establishment in Korea.

Under the second exception, paragraph (2) also provides that if the person paying the interest is a resident of a Contracting State and has a permanent establishment in a State other than a Contracting State in connection with which the indebtedness on which the interest is paid was incurred and such interest is paid to a resident of the other Contracting State, and such interest is borne by the permanent establishment, the interest will be deemed from sources within the State in which the permanent establishment is situated. This interest will be exempt from tax in the Contracting State where the payor is a resident if paid to a resident of the other Contracting State because, under Article 4 (General Rules of Taxation), a resident of one Contracting State, not a citizen of the other Contracting State, may be taxed by that other Contracting State only on income from sources within that other Contracting State.

Paragraph (3) provides that royalties described in paragraph (4) of Article 14 (Royalties)

for the use of, or the right to use, property or rights other than as provided in paragraph (5) with respect to ships or aircraft, described in such paragraph will be treated as income from sources within a Contracting State only to the extent that such royalties are for the use of, or the right to use, such property or rights within that Contracting State.

Paragraph (4) provides that income from real property and royalties from the operation of mines, quarries, or other natural resources (including gains derived from the sale of such property or the right giving rise to such royalties) will be treated as income from sources within a Contracting State only if such property is situated in that Contracting State.

Paragraph (5) provides that income from the rental of tangible personal (movable) property will be treated as income from sources within a Contracting State only if such property is situated in that Contracting State. Income from the rental of ships or aircraft derived by a person not engaged in the operation of ships or aircraft in international traffic shall be treated as income from sources within a Contracting State only if the lessee is a resident of that Contracting State.

Under paragraph (6), income received by an individual for his performance of labor or personal services, whether as an employee or in an independent capacity, or for furnishing the personal services of another person and income received by a corporation for furnishing the personal services of its employees or others, will be treated as income from sources within a Contracting State only to the extent that such services are performed in that Contracting State. Income from personal services performed aboard ships or aircraft operated by a resident of a Contracting State in international traffic will be treated as income from sources within that Contracting State if rendered by a member of the regular complement of the ship or aircraft. For purposes of this paragraph, income from labor or personal services includes pensions (as defined in paragraph (3) of Article 23 (Private Pensions and Annuities)) paid in respect of such services. However, remuneration described in Article 22 (Governmental Functions) and payments described in Article 24 (Social Security Payments) will be treated as income from sources within the Contracting State only if paid by or from the public funds of that Contracting State or local authority thereof.

Paragraph (7) provides that income from the purchase and sale of intangible or tangible personal (including movable) property (other than gains defined as royalties by paragraph (4) (b) of Article 14 (Royalties)) will be treated as income from sources within a Contracting State only if such property is sold in that Contracting State.

Paragraph (8) contains a general qualification to the preceding source rules. It provides that industrial or commercial profits attributable to a permanent establishment which the recipient, a resident of one Contracting State, has in the other Contracting State will be treated as income from sources within that other Contracting State. Industrial or commercial profits attributable to such permanent establishment may include any item of income described in paragraphs (1) through (6) if the item of income is "effectively connected" with the permanent establishment. See the discussion of paragraph (6) (b) of Article 8 (Business Profits) for a discussion of the effectively connected concept.

Under paragraph (9) the source of any item of income to which paragraphs (1) through (8) are not applicable will be determined by each Contracting State in accordance with its own law. However, if the source of any item of income under the laws of one Contracting State is different from its source under the laws of the other Contracting State or if its source is not readily determinable under the laws of one of the Contracting States, the competent authorities of the Contracting States may, in order to prevent double taxation or further any other purpose of the Convention, establish a common source of the item of income for purposes of the Convention.

Several of the source rules set out in this Article differ to some degree from those existing in the Code. Since Article 4 (General Rules of Taxation) provides that the Convention will not increase a person's United States tax, a taxpayer is not required to apply the Convention rules in calculating his United States tax liability.

ARTICLE 7
Nondiscrimination

Paragraph (1) provides that a citizen of one Contracting State who is a resident of the other Contracting State will not be subjected in that other Contracting State to more burdensome taxes than a citizen of that other Contracting State who is a resident thereof. The determination whether there is more burdensome taxation is to be made by comparing the treatment of individuals who are in comparable positions. Thus, for example, a citizen of Korea who is a resident of the United States and who otherwise meets the requirements specified in section 911 of the Code would under this Article be eligible for the benefits of section 911 even though not a citizen of the United States. On the other hand, just as a United States citizen who becomes a nonresident alien at any time during a taxable year or whose spouse is a nonresident alien at any time during a taxable year cannot file a joint return for that year, a Korean citizen would not be entitled to file a joint return with his spouse if either is a nonresident alien at any time during the taxable year.

Paragraph (2) provides that a permanent establishment which a resident of one Contracting State has in the other Contracting State will not be subject in that other Contracting State to more burdensome taxes than a resident of that other Contracting State carrying on the same activities. However, this does not obligate a Contracting State to grant to individual residents of the other Contracting State any personal allowance, reliefs, or deductions for taxation purposes on account of civil status or family responsibilities which it grants to its own individual residents.

Paragraph (3) prohibits one Contracting State from subjecting a corporation of such Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State to any taxation or any requirement connected with taxation which is other or more burdensome than those applicable to corporations of the first-mentioned Contracting State carrying on the same activities, the capital of which is wholly or partly owned or controlled by one or more residents of the first-mentioned Contracting State.

Under paragraph (3) of Article 1 (Taxes Covered), the provisions of this Article extend to taxes of every kind imposed at the National, state or local level.

ARTICLE 8
Business Profits

Paragraph (1) sets forth the general rule that industrial or commercial profits of a resident of one Contracting State are exempt from tax by the other Contracting State unless the resident is engaged in industrial or commercial activity in that other Contracting State through a permanent establishment situated therein. Where the resident is so engaged, only the industrial or commercial profits attributable to the permanent establishment can be taxed by that other Contracting State, unless the resident is a citizen of the other Contracting State. (See the saving clause in paragraph (4) of Article 4 (General Rules of Taxation).) Under paragraph (8) of Article 6 (Source of Income), industrial or commercial profits whether from sources within or without a Contracting State attributable to a permanent establishment which a resident of one Contracting State has in the other Contracting State will be considered to be from sources within the other Contracting State. Thus, items of income described in section 864(c)(4)(B) of the Code attributable to a permanent establishment situated in the United States will be subject to tax by the United States.

In determining the proper attribution of industrial or commercial profits under the Convention, paragraph (2) provides that both Contracting States will attribute to the permanent establishment such profits which would be attributable to it if it were an independent entity engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the resident of which it is a permanent establishment. Under paragraph (3), expenses which are reasonably connected with profits attributable to the permanent establishment, including executive and general administrative expenses, whether incurred in the Contracting State in which the permanent establishment is situated or elsewhere, will be allowed as deductions in determining the industrial or commercial profits of the permanent establishment. However, in determining the amount of the deduction under paragraph (3) for expenses incurred by the head office, the deduction generally will be limited to the expense incurred without including a profit element for the head office.

Paragraph (4) provides that no profits shall be attributed to a permanent establishment merely because of the purchase of goods or merchandise by that permanent establishment, or by the resident of which it is a permanent establishment, for the account of such resident. Paragraph (2) of the Article does not override paragraph (4). Thus, where a permanent establishment purchases goods for its head office, the industrial or commercial profits attributed under paragraph (2) or to the permanent establishment with respect to its other activities will not be increased by adding a notional figure for profits from purchasing.

Under paragraph (5) the term “industrial or commercial activity” includes the conduct of manufacturing, mercantile, insurance, banking, financing, agricultural, fishing or mining activities, the operation of ships or aircraft, the furnishing of services, and the rental of tangible

personal property (including ships or aircraft when the rental is not covered by Article 10). The term does not include the performance of personal services by an individual either as an employee or in an independent capacity.

Paragraph (6)(a) defines the term "industrial or commercial profits" to include income derived from industrial or commercial activity, and income derived from real property and natural resources and dividends, interest, royalties (as defined in paragraph (4) of Article 14 (Royalties)), and capital gains but only if the property or rights giving rise to such income, dividends, interest, royalties, or capital gains is effectively connected with a permanent establishment which the recipient, being a resident of one Contracting State, has in the other Contracting State, whether or not such income is derived from industrial or commercial activity. See paragraph (3) of Article 12 (Dividends), paragraph (4) of Article 13 (Interest), paragraph (3) of Article 14 (Royalties), and paragraph (1)(b) of Article 16 (Capital Gains).

Paragraph (6)(b) contains criteria for determining whether property or rights are effectively connected with a permanent establishment. Factors to be taken into account include whether the rights or property are used in or held for use in carrying on industrial or commercial activity through a permanent establishment and whether the activities carried on through such permanent establishment were a material factor in the realization of the income derived from such property or rights.

For this purpose, due regard shall be given to whether or not such property or rights or such income were accounted for through such permanent establishment. The effectively connected test in this paragraph is substantially similar to the effectively connected test in section 864(c) of the Code.

Under paragraph (7), where industrial or commercial profits include items of income which are dealt with separately in other articles of the Convention, the provisions of those articles will, except as otherwise provided therein, supersede the provisions of this Article. Thus, for example, taxation of interest income will be controlled by Article 13 (Interest) and not by this Article unless, as provided by paragraph (4) thereof, the interest is effectively connected with a permanent establishment.

ARTICLE 9
Permanent Establishment

This Article defines the term "permanent establishment." The existence of a permanent establishment is relevant under Article 8 (Business Profits) to the taxation of industrial or commercial profits and in determining the applicability of other provisions of the Convention.

Under paragraph (1), the term “permanent establishment” means a fixed place of business through which industrial or commercial activity is carried on. Illustrations in paragraph (2) of a fixed place of business include a branch; an office; a factory; a workshop; a warehouse; a store or other sales outlet; a mine, quarry or other place of extraction of natural resources; and a building Site or construction or installation project which exists for more than six months. As a

general rule, any fixed facility or premises through which a resident conducts industrial or commercial activity for an indefinite or substantial period of time will be treated as a fixed place of business unless it is used only for one or more of the activities described in paragraph (3).

Under the construction or installation project rule the six month period begins only when work physically commences in the other Contracting State. A series of contracts or projects which are inter-dependent both commercially and geographically is to be treated as a single project for the purpose of applying the six month test.

Paragraph (3) specifically provides that a permanent establishment does not include a fixed place of business used only for one or more of the following:

> "(a) The use of facilities for the purpose of storage, display, or delivery of goods or merchandise belonging to the resident;
>
> "(b) The maintenance of a stock of goods or merchandise belonging to the resident for the purpose of storage, display, or delivery;
>
> "(c) The maintenance of a stock of goods or merchandise belonging to the resident for the purpose of processing by another person;
>
> "(d) The maintenance of a fixed place of business for the purpose of purchasing goods or merchandise, or for collecting information, for the resident;
>
> "(e) The maintenance of a fixed place of business for the purpose of advertising, for the supply of information, for scientific research, or for similar activities which have a preparatory or auxiliary character, for the resident; or
>
> "(f) The maintenance of a building site or construction or installation project which does not exist for more than 6 months."

As noted, these exceptions are cumulative and a fixed place of business used only for one or more of these purposes will not be considered a permanent establishment under the Convention.

Paragraph (4) provides that even if a resident of one of the Contracting States does not have a permanent establishment in the other Contracting State, under paragraphs (1) through (3) of this Article, he shall nevertheless be deemed to have a permanent establishment in the other Contracting State if he engages in trade or business in that other Contracting State through an agent who has authority to conclude contracts in the name of that resident and regularly exercises that authority in that other Contracting State, unless the exercise of the authority is limited to the purchase of goods or merchandise for the account of the resident, or who maintains in that other Contracting State a stock of goods or merchandise belonging to that resident from which he regularly fills orders or makes deliveries.

Under paragraph (5), notwithstanding subparagraphs (a), (c) and (d) of paragraph (3), if a resident of one of the Contracting States has a fixed place of business in the other Contracting State and goods or merchandise are either:

> (1) subjected to processing in that other Contracting State by another person (whether or not purchased in that other Contracting State), or
>
> (2) are purchased in that other Contracting State (and such goods or merchandise are not subjected to processing outside that other Contracting State) then such resident shall be considered to have a permanent establishment in that other Contracting State, if

all or part of such goods or merchandise is sold by or on behalf of such resident for use, consumption or disposition in that other Contracting State.

On the other hand, notwithstanding the provisions of paragraphs (4) and (5), paragraph (6) provides that a resident of one Contracting State will not be deemed to have a permanent establishment in the other Contracting State merely because such resident engages in industrial or commercial activity in such other Contracting State through a broker, general commission agent, or any other agent of an independent status, where such broker or agent is acting in the ordinary course of his business.

Under paragraph (7), the fact that a resident of one Contracting State is a related person with respect to a resident of the other Contracting State or with respect to a person who engages in industrial or commercial activity in that other Contracting State (whether through a permanent establishment or otherwise) shall not be taken into account in determining whether the resident of the first-mentioned Contracting State has a permanent establishment in that Contracting State. As defined in Article 11 (Related Persons), a person is related to another person if either person owns or controls directly or indirectly the other, or if any third person owns or controls directly or indirectly both such persons.

Paragraph (8) provides that the principles set forth in this Article are to be applied in determining whether there is a permanent establishment in a State other than one of the Contracting States or whether a person other than a resident of one of the Contracting States has a permanent establishment in one of the Contracting States. This is necessary for the proper application of paragraph (2) of Article 6 (Source of Income). This paragraph is not intended to extend the benefits of the Convention to persons other than residents of the two Contracting States.

ARTICLE 10
Shipping and Air Transport

The Article provides that, notwithstanding Article 8 (Business Profits), income derived by a resident of one of the Contracting States from the operation in international traffic of ships or aircraft will be exempt from tax by the other Contracting State. Income derived from the operation in international traffic of ships or aircraft is defined to include income incidental to such operation, such as income derived from the use or lease of containers, trailers from the inland transportation of containers and other related equipment. It does not, however, include other income from the inland transportation of containers.

This Article is subject to the saving clause of paragraph (4) of Article 4 (General Rules of Taxation). Therefore, a Contracting State may tax the income from international traffic derived by a resident of the other Contracting State without regard to this Article if such resident is a citizen of the first-mentioned Contracting State.

ARTICLE 11

Related Persons

This Article complements section 482 of the Code and confirms the authority of the United States under that section. Where a person subject to the taxing jurisdiction of one of the Contracting States and any other person are related and where such related persons make arrangements or impose conditions between themselves which are different from those which would be made between independent persons, under paragraph (1) any income, deductions, credits or allowances which would, but for those arrangements or conditions, have been taken into account in computing the income or loss of, or the tax payable by, one of such persons, may be taken into account in computing the amount of the income subject to tax and the taxes payable by such person.

It is anticipated that if an adjustment is made in accordance with paragraph (1) by a Contracting State to the income of one of its residents, the other Contracting State will, if it agrees with such redetermination and if necessary to prevent double taxation, make a corresponding adjustment to the income of a person in such other Contracting State related to such resident. If the other Contracting State disagrees with the redetermination, it is intended that the two Contracting States will endeavor to reach agreement in accordance with the mutual agreement procedure in Article 27 (Mutual Agreement Procedure).

Paragraph (2) provides that for purposes of the Convention a person is related to another person if either person owns or controls directly or indirectly the other, or if a third person or persons own or control directly or indirectly both. "Control" includes any kind of control, whether or not legally enforceable, and however exercised or exercisable.

ARTICLE 12
Dividends

Paragraph (1) provides that dividends derived from sources within one Contracting State by a resident of the other Contracting State may be taxed by both Contracting States. However, paragraph (2) limits the rate of tax imposed by the Contracting State of source to a rate not in excess of fifteen percent of the gross amount of the dividend. If the dividend recipient is a corporation, the rate of tax imposed by the Contracting State of source may not exceed ten percent of the gross amount of the dividend if during the part of the paying corporation's taxable year which precedes the date of payment of the dividend and during the whole of its prior taxable year (if any), at least ten percent of the outstanding shares of the voting stock of the paying corporation was owned by the recipient corporation, and not more than twenty-five percent of the gross income of the paying corporation for such prior taxable year (if any) consists of interest or dividends (other than interest derived from the conduct of a banking, insurance, or financing business and dividends or interest received from subsidiary corporations, fifty percent or more of the outstanding shares of the voting stock of which is owned by the paying corporation at the time such dividends or interest is received). These rate limitations do not affect the taxation of profits of the corporation which pays the dividends.

Paragraph (3) provides that the limitations of paragraph (2) will not apply if the dividend

recipient, being a resident of one Contracting State, has a permanent establishment in the other Contracting State and the shares with respect to which the dividends are paid are effectively connected with the permanent establishment. In such a case, the dividend will be treated as industrial or commercial profits subject to Article 8 (Business Profits). If the dividend recipient is a citizen of the source Contracting State, that Contracting State may tax the recipient without regard to this Article because of the saving clause of paragraph (4) of Article 4 (General Rules of Taxation).

ARTICLE 13
Interest

Paragraph (1) provides that interest derived from sources within one Contracting State by a resident of the other Contracting State may be taxed by both Contracting States.

Paragraph (2) provides that the rate of tax imposed by one of the Contracting States on interest derived from sources within that State by a resident of the other Contracting State shall not exceed 12 percent of the gross amount of the interest.

Paragraph (3) provides that, notwithstanding paragraphs (1) and (2), interest derived from sources within one of the Contracting States shall be exempt from tax by that Contracting State if it is beneficially derived by the Government of the other Contracting State, by any local authority thereof, the central bank of that other Contracting State, or any instrumentality wholly owned by that Government or that central bank or both, not subject to tax by that other Contracting State on its income. In the case of the United States, examples of "instrumentalities" wholly owned by the government are the Export-Import Bank and the Overseas Private Investment Corporation. The "central bank" in the case of Korea would be the Bank of Korea, and in the case of the United States, the Federal Reserve Banks.

Paragraph (4) provides that paragraph (2) will not apply if the interest recipient, being a resident of one Contracting State, has a permanent establishment in the other Contracting State and the indebtedness giving rise to the interest is effectively connected with the permanent establishment. In such a case, the interest will be treated as industrial or commercial profits subject to Article 8 (Business Profits).

If excessive interest is paid to a related person, paragraph (5) provides that the provisions of the Article do not apply to the excessive portion of the payment. The excessive portion may be taxed by each Contracting State according to its own law, including the provisions of the Convention where applicable. In the case of the United States, the excessive portion may be taxed as a dividend, in which case the provisions of Article 12 (Dividends) will apply.

Paragraph (6) defines the term "interest" for purposes of the Convention as income from bonds, debentures, Government securities, notes, or other evidences of indebtedness, whether or not secured and whether or not carrying a right to participate in profits, and debt-claims of every kind, as well as all other income which, under the taxation law of the Contracting State in which the income has its source, is assimilated to income from money lent.

This Article is subject to the saving clause of paragraph (4) of Article 4 (General Rules of Taxation). Therefore, interest derived by a citizen of the source Contracting State may be taxed by that Contracting State without regard to this Article.

ARTICLE 14
Royalties

Paragraph (1) provides that tax imposed by one of the Contracting States on royalties derived from sources within that Contracting State by a resident of the other Contracting State shall not exceed fifteen percent of the gross amount thereof, except as provided in paragraphs (2) and (3).

Under paragraph (2) royalties derived from copyrights, or rights to produce or reproduce any literary, dramatic, musical, or artistic work, by a resident of one Contracting State, as well as royalties received as consideration for the use of, or the right to use, motion picture films including films and tapes used for radio or television broadcasting, may not be taxed by the other Contracting State at a rate of tax which exceeds ten percent of the gross amount of the royalties.

Paragraph (3) provides that paragraphs (1) and (2) will not apply if the royalty recipient, being a resident of one Contracting State, has in the other Contracting State a permanent establishment and the property or rights giving rise to the royalty is effectively connected with such permanent establishment. In such a case, the royalty will be treated as industrial or commercial profits subject to Article 8 (Business Profits).

Paragraph (4) defines the term "royalties" as payment of any kind made as consideration for the use of, or the right to use, copyrights of literary, artistic, or scientific works, copyrights of motion picture films or films or tapes used for radio or television broadcasting, patents, designs, models, plans, secret processes or formulae, trademarks, or other like property or rights, or knowledge, experience, or skill (know-how), or ships or aircraft (but only if the lessor is a person not engaged in the operation in international traffic of ships or aircraft). The term also includes gains derived from the sale, exchange, or other disposition of any such property or rights (other than ships or aircraft) to the extent the amounts realized on such sale, exchange or other disposition for consideration are contingent on the productivity, use, or disposition of the property or rights. If the amounts realized are not so contingent, the provisions of Article 16 (Capital Gains) will apply. The term "royalties" as used in the Convention does not include any royalties, rentals or other amounts paid in respect of the operation of mines, quarries, or other natural resources, which are covered by Article 15 (Income from Real Property).

If excessive royalties are paid to a related person, paragraph (5) provides that the provisions of the Article do not apply to the excessive portion of the royalty. The excessive portion may be taxed by each Contracting State according to its own law, including the Convention where applicable. Thus, in the case of the United States, the excessive portion may be treated as a dividend or interest, or in whatever other manner is appropriate.

As noted under paragraph (3) of Article 6 (Source of Income), royalties described in paragraph (4), including contingent gains, will be treated as income from sources within a Contracting State only to the extent they are payments for the use of, or the right to use, property or rights described in paragraph (4) within that Contracting State.

This Article is subject to the saving clause of paragraph (4) of Article 4 (General Rules of Taxation). Therefore, royalties derived by a citizen of the source Contracting State may be taxed by that Contracting State without regard to this Article.

ARTICLE 15
Income from Real Property

Under paragraph (1), income from real property, including royalties and other payments in respect of the exploitation of natural resources and gains derived from the sale, exchange or other disposition of such property or of the right giving rise to such royalties or other payments, may be taxed by the Contracting State in which the real property or natural resources are situated. However, income from real property does not include interest on indebtedness secured by real property (e.g., mortgages) or secured by a right giving rise to royalties or other payments in respect of the exploitation of natural resources. Such interest income is covered by Article 13 (Interest).

Paragraph (1) applies to income derived from the usufruct, direct use, letting, or use in any other form of real property.

ARTICLE 16
Capital Gains

Under paragraph (1), a resident of one Contracting State will be exempt from tax by the other Contracting State on gains from the sale, exchange, or other disposition of capital assets, e.g., stock or securities. However, the exemption does not apply if

(1) the gain is from the sale, exchange or other disposition of property described in Article 15 (Income from Real Property) situated within the other Contracting State;

(2) the recipient of the gain has a permanent establishment in the other Contracting State and the property giving rise to the gain is effectively connected with the permanent establishment or

(3) the individual recipient of the gain maintains a fixed base in the other Contracting State for a period or periods aggregating 183 days or more during the taxable year and the property giving rise to the gain is effectively connected with the fixed base, or the individual recipient of the gain is present in the other Contracting State for a period or periods aggregating 183 days or more during the taxable year.

The term “day” for purposes of the physical presence tests contained in the Convention with respect to an individual means a calendar day during any portion of which the individual is physically present in the relevant Contracting State.

Under paragraph (2), the provisions of Article 15 (Income from Real Property) will apply to real property gains, and the provisions of Article 8 (Business Profits) will apply to gains effectively connected with a permanent establishment.

If the recipient of the gain is a citizen of the other Contracting State, that Contracting State may tax the recipient without regard to this Article because of the saving clause of paragraph (4) of Article 4 (General Rules of Taxation).

ARTICLE 17
Investment or Holding Companies

This Article provides that a corporation of one Contracting State deriving dividends, interest, royalties or capital gains from sources within the other Contracting State will not be entitled to the benefits of Articles 12 (Dividends), 13 (Interest), 14 (Royalties) or 16 (Capital Gains) if by reason of special measures the tax imposed on such corporation by the first-mentioned Contracting State with respect to such dividends, interest, royalties or capital gains is substantially less than the tax generally imposed by such Contracting State on corporate profits, and twenty-five percent or more of the capital of such corporation is held of record or is otherwise determined, after consultation between the competent authorities of the Contracting States, to be owned, directly or indirectly, by one or more persons who are not individual residents of the first-mentioned Contracting State (or, in the case of a Korean corporation, who are citizens of the United States). For purposes of applying this Article it is intended that the requisite direct or indirect ownership be tested at the individual shareholder level.

The purpose of this Article is to deal with potential abuse which could occur if one of the Contracting States provided preferential rates of tax for investment or holding companies. In the absence of this Article, residents of third countries could organize a corporation in the Contracting State extending the preferential rates for the purpose of making investments in the other Contracting State. The combination of low tax rates in the first Contracting State and the reduced rates or exemptions in the other Contracting State would enable the third country residents to realize unintended benefits. Existing Code provisions dealing with the taxation of capital gains do not make this Article applicable with respect to capital gains.

ARTICLE 18
Independent Personal Services

In dealing with the taxation of income from personal services the Convention distinguishes between "independent" and "dependent" personal services.

Personal services performed in an independent capacity, or independent personal services, are services performed by an individual for his own account where he receives the income and bears the losses arising from such services. If an individual is an independent contractor he is considered as rendering independent personal services. Generally, services

rendered by physicians, lawyers, engineers, architects, dentists and accountants performing personal services as sole proprietors or partners are independent personal services.

Under paragraph (1), income derived by an individual resident of one Contracting State from the performance of personal services in an independent capacity may be taxed by that Contracting State. Except as permitted by paragraph (2), such income will be exempt from tax by the other Contracting State.

Under paragraph (2) such income derived in the other Contracting State may be taxed by that other Contracting State if

(1) the individual is present therein for a period or periods aggregating 183 days or more in the taxable year;

(2) the income exceeds $3,000 or its equivalent in Korean won in the taxable year; or

(3) the individual maintains a fixed base therein for a period or periods aggregating 183 days or more in the taxable year (but only on such income attributable to the fixed base).

Under paragraph (4) of Article 4 (General Rules of Taxation), the other Contracting State may also tax any individual who is a citizen of that Contacting State without regard to this Article.

ARTICLE 19
Dependent Personal Services

Under paragraph (1), subject to Articles 20 (Teachers), 21 (Students and Trainees), 22 (Governmental Functions) and 23 (Private Pensions and Annuities), wages, salaries, and similar remuneration derived by an individual who is a resident of one Contracting State from labor or personal services performed as an employee may be taxed by that Contracting State. Except as provided by paragraph (2), such remuneration derived from sources within the other Contracting State may also be taxed by that other Contracting State. It is intended that for purposes of the Convention the term "wages, salaries and similar remuneration" includes income from services performed as an officer of a corporation.

Under paragraph (2) such remuneration derived by an individual resident of one Contracting State will be exempt from tax by the other Contracting State if:

(a) the individual is present in that other Contracting State for a period or periods aggregating less than 183 days in the taxable year;

(b) the individual is an employee of a resident of the first-mentioned Contracting State or of a permanent establishment maintained in the first-mentioned Contracting State by a resident of a State other than that first-mentioned State;

(c) the remuneration is not borne as such by a permanent establishment which the employer has in that other Contracting State; and

(d) the income does not exceed $3,000 or its equivalent in Korean won.

Such income may nevertheless be taxed by that other Contracting State if the individual is a citizen of that Contracting State, because of paragraph (4) of Article 4 (General Rules of Taxation).

Under paragraph (3), notwithstanding paragraph (2), remuneration derived by an individual from the performance of labor or personal services as an employee aboard ships or aircraft operated by a resident of a Contracting State in international traffic will be exempt from tax by the other Contracting State if such individual (even if a resident of a State other than a Contracting State) is a member of the regular complement of the ship or aircraft. However, this paragraph is also subject to the saving clause of paragraph (4) of Article 4 (General Rules of Taxation) so that the other Contracting State may tax a citizen or resident of that other Contracting State without regard to this paragraph.

ARTICLE 20
Teachers

Paragraph (1) provides that where a resident of one Contracting State is invited by the Government of the other Contracting State, a political subdivision, or a local authority thereof, or by a university or other recognized educational institution in that other Contracting State to come to that other Contracting State for a period not expected to exceed two years for the purpose of teaching or engaging in research, or both, at a university or other recognized educational institution, and such resident comes to that other Contracting State primarily for such purpose, his income from personal services for teaching or research at the university or educational institution will be exempt from tax by that other Contracting State for a period not exceeding two years from the date of his arrival in that other Contracting State.

Since a temporary visit may be of such a duration that an individual may lose his status as a resident of the Contracting State of which he was a resident at the time he became eligible for the benefits of this Article, the individual need only be a resident of such Contracting State at the beginning of his visit. However, if the individual becomes a citizen of, or acquires immigrant status in, the other Contracting State, that other Contracting State may tax the individual without regard to this Article. See paragraphs (4) and (5)(b) of Article 4 (General Rules of Taxation). If the individual's visit exceeds a period of two years from the date of his arrival, the exemption applies only to the income received by the individual before the expiration of such two year period.

Pursuant to paragraph (2), this Article does not apply to income from research undertaken primarily for the private benefit of a specific person or persons.

ARTICLE 21
Students and Trainees

Paragraph (1) provides that an individual who is a resident of one Contracting State at the time he becomes temporarily present in the other Contracting State and who is temporarily present therein for the primary purpose of studying at a university or other recognized educational institution in that other Contracting State, securing training required to qualify him to

practice a profession or professional specialty, or studying or doing research as a recipient of a grant, allowance, or award from a governmental, religious, charitable, scientific, literary, or educational organization, will be exempt from tax by that other Contracting State for a period not exceeding five taxable years from the date of his arrival in that other Contracting State on:

(1) Remittances from abroad for the purpose of his maintenance, education, study, research or training;

(2) The grant, allowance, or award; and

(3) Income from personal services performed in the other Contracting State not in excess of $2,000 or its equivalent in Korean won for any taxable year.

Under paragraph (2), an individual who is a resident of one Contracting State at the time he becomes temporarily present in the other Contracting State and who is temporarily present therein as an employee of, or under contract with, a resident of the first-mentioned Contracting State, for the primary purpose of acquiring technical, professional, or business experience from a person other than that resident of the first-mentioned Contracting State or other than a person related to such resident, or studying at a university or other recognized educational institution in that other Contracting State, will be exempt from tax by that other Contracting State for a period of twelve consecutive months, on income from personal services not in excess of $5,000 or its equivalent in Korean won.

Under paragraph (3), an individual who is a resident of one Contracting State at the time he becomes temporarily present in the other Contracting State and who is temporarily present therein for a period not exceeding one year, as a participant in a program sponsored by the other Contracting State, for the primary purpose of training, research, or study, will be exempt from tax by the other Contracting State with respect to his income from personal services in respect of such training, research, or study performed in that other Contracting State in an aggregate amount not in excess of $10,000 or its equivalent in Korean won.

Under paragraph (4), the benefits provided in paragraph (1) and the benefits provided under Article 20 (Teachers) may extend only for such period of time, not to exceed five taxable years from the date of the individual's arrival, as may reasonably or customarily be required to effectuate the purpose of the visit.

If an individual qualifies for the benefits of more than one of the provisions of Articles 20 (Teachers) and 21 (Students and Trainees), such individual may choose the most favorable provision but may not claim the benefits of more than one provision in any taxable year as a means of avoiding the limitations provided. Thus, for example, an individual who comes to the other Contracting State for the primary purpose of studying may be able to qualify under either paragraph (2) or (3) of this Article. However, he cannot combine the maximum exclusion limits in those two paragraphs to exclude $15,000 during the taxable year. The exclusions permitted by the Convention are in addition to any exclusions, exemptions, deductions, credits or other allowances to which the individual is entitled under the laws of the Contracting States. If the individual becomes a citizen of, or acquires immigrant status in, the other Contracting State, that other Contracting State may tax the individual without regard to this Article. See paragraphs (4) and (5)(b) of Article 4 (General Rules of Taxation).

ARTICLE 22
Governmental Functions

Under this Article, wages, salaries, and similar remuneration, including pensions or similar benefits, paid from public funds of one Contracting State to a citizen of that Contracting State for labor or personal services performed as an employee of that Contracting State or instrumentality thereof in the discharge of governmental functions will be exempt from tax by the other Contracting State.

If the citizen becomes a citizen of, or acquires immigrant status in, the other Contracting State, that other Contracting State may tax the individual without regard to this Article. See paragraphs (4) and (5)(b) of Article 4 (General Rules of Taxation).

ARTICLE 23
Private Pensions and Annuities

Except as provided in Article 22 (Governmental Functions), pensions and other similar remuneration paid to an individual who is a resident of a Contracting State in consideration of past employment will be taxable under paragraph (1) only in that Contracting State. Thus, private pensions and similar remuneration derived from sources within one Contracting State by an individual resident of the other Contracting State in consideration of past employment are exempt from tax in the first-mentioned Contracting State. The term "pensions and other similar remuneration" is defined in paragraph (3) as periodic payments made after retirement or death in consideration for services rendered, or by way of compensation for injuries received in connection with past employment. The term does not include social security payments covered in Article 24 (Social Security Payments).

Paragraph (2) provides that alimony and annuities paid to an individual resident of a Contracting State will be taxable only in that Contracting State. The term "annuities" is defined in paragraph (4) as a stated sum paid periodically at stated times during life or during a specified number of years, under an obligation to make the payments in return for adequate and full consideration (other than for services rendered). The term "alimony" is defined in paragraph (5) as periodic payments made pursuant to a decree of divorce, separate maintenance agreement, or support or separation agreement which is taxable to the recipient under the internal laws of the Contracting State of which he is a resident. Thus, the term "alimony" would not include a payment which would not be taxable to the recipient under the laws of the Contracting State in which the recipient is a resident even though such payment is made pursuant to a decree of divorce or of separate maintenance agreement.

This Article is subject to the savings clause of paragraph (4) of Article 4 (General Rules of Taxation). Therefore, individuals who are citizens of a Contracting State may be taxed by that Contracting State without regard to this Article.

ARTICLE 24
Social Security Payments

This Article provides that social security payments and other public pensions, e.g., railroad retirement benefits, paid by one Contracting State to an individual who is a resident of the other Contracting State (or in the case of such payments by Korea, to an individual who is a citizen of the United States, i.e., such payments by Korea to United States citizens or residents will be exempt from tax by the United States) will be taxable only in the first-mentioned Contracting State. Payments described in Article 22 (Governmental Functions) are not covered by this Article.

ARTICLE 25
Exemption from Social Security Taxes

This Article provides an exemption from social security taxes for Korean residents working in Guam, on a temporary non-immigrant basis, similar to the exemption contained in the Internal Revenue Code for residents of the Philippines working in Guam.

Specifically, paragraph (1) provides for an exemption from taxes imposed under Chapter 21 of the Internal Revenue Code with respect to wages paid for services performed in Guam by a resident of Korea while in Guam on a temporary basis as a nonimmigrant alien admitted to Guam pursuant to section 101(a)(15)(H)(ii) of the United States Immigration and Nationality Act (8 U.S.C. 1101(a)(15)(H)(ii)).

Paragraph (2) provides that the exemption shall continue only so long as the similar exemption for residents of the Republic of the Philippines provided by section 3121(b)(18) of the Internal Revenue Code.

ARTICLE 26
Diplomatic and Consular Officers

This Article provides that nothing in the Convention will affect the fiscal privileges of diplomatic and consular officials under the general rules of international law or under the provisions of special agreements. This is merely a special case of the general rule provided in paragraph (2) of Article 4 (General Rules of Taxation).

ARTICLE 27
Mutual Agreement Procedure

When a resident of one Contracting State considers that the action of one or both Contracting States results or will result for him in taxation not in accordance with the Convention, he may, notwithstanding the remedies provided by the national laws of the Contracting States, present his case to the competent authority of the Contracting State of which

he is a resident. A resident of a Contracting State need not, although it is anticipated that in the normal situation he will, exhaust his other administrative or judicial remedies prior to resorting to the use of the mutual agreement procedure. If the claim is considered to have merit by the competent authority, that competent authority must endeavor to come to an agreement with the competent authority of the other Contracting State with a view to the avoidance of taxation contrary to the Convention.

Paragraph (2) requires the competent authorities of the two Contracting States to endeavor to resolve by mutual agreement any difficulties or doubts arising as to the application of the Convention. In particular, the competent authorities may agree to the same attribution of industrial or commercial profits to a resident of one Contracting State and its permanent establishment situated in the other Contracting State; the same allocation of income, deductions, credits, or allowances between a resident of one Contracting State and any related person; the same determination of the source of particular items of income; uniform accounting for income and deductions; and the same meaning of any term used in this Convention.

Under paragraph (3), the competent authorities may communicate with each other directly and, when advisable, meet together for an oral exchange of opinions, for the purpose of reaching an agreement.

Under paragraph (4), in cases in which the competent authorities reach an agreement, taxes will be imposed on such income, and refund or credit of taxes allowed, by the Contracting States in accordance with such agreement. This permits the issuance of a refund or credit notwithstanding procedural barriers otherwise existing under a Contracting State's law, such as the statute of limitations. However, it does not authorize imposition of additional taxes after the statute of limitations has run.

ARTICLE 28
Exchange of Information

Paragraph (1) provides for a system of administrative cooperation between the competent authorities of the two Contracting States by requiring an exchange of information pertinent to the carrying out of the Convention and for the prevention of fraud or for the administration of statutory provisions concerning taxes to which this Convention applies provided the information is of a class that can be obtained under the laws and administrative practices of each Contracting State with respect to its own taxes. The competent authorities may exchange information in connection with tax compliance generally, not merely illegal acts or crimes.

Under paragraph (2) information exchanged must be treated as secret and cannot be disclosed except when disclosed to persons concerned with, or made part of a public record with respect to the assessment, collection, enforcement or prosecution in respect of taxes which are the subject of the Convention. Thus, disclosure is not prohibited as a part of a public proceeding before a court or administrative body.

Under paragraph (3) no information shall be exchanged which would be contrary to

public policy.

Under paragraph (4) and if specifically requested by the competent authority of one of the Contracting States, the competent authority of the other Contracting State shall provide information in the form of depositions of witnesses and copies of unedited original documents (including books, papers, statements, records, accounts, or writings), to the same extent such depositions and documents can be obtained under the laws and administrative practices of each Contracting State with respect to its own taxes.

Under paragraph (5) the exchange of information may be on either a routine basis or on request with reference to particular cases. The competent authorities may agree on the list of information to be furnished on a routine basis.

Paragraphs (6) and (7) provide for notification and text transmittal at least once a year of amendments of the tax laws referred to in paragraph (1) of Article 1 (Taxes Covered), of adopted taxes referred to in paragraph (2) of that Article, or of published material concerning application of the Convention, whether in the form of regulations, rulings or judicial decisions.

Under paragraph (3) of Article 1 (Taxes Covered), the provisions of this Article extend to taxes of every kind imposed at the National level.

ARTICLE 29
Extension to Territories

Under paragraph (1), either Contracting State may, at any time while the Convention continues in force, by a written notification given to the other Contracting State through diplomatic channels, declare its desire that the Convention, either in whole or in part or with such modifications as may be found necessary for special application in a particular case, shall extend to all or any of the areas (to which the Convention is not otherwise applicable) for whose international relations it is responsible and which impose taxes substantially similar in character to those which are the subject of the Convention. When the other Contracting State has, by a written communication through diplomatic channels, signified to the first-mentioned Contracting State that such notification is accepted in respect of such area or areas, and the notification and communication have been ratified and instruments of ratification exchanged, the Convention, in whole or in part, or with such modifications as may be found necessary for special application in a particular case, as specified in the notification, will apply to the area or areas named in the notification and will enter into force and effect on and after the date or dates specified therein. None of the provisions of the Convention will apply to any such area in the absence of such acceptance and exchange of instruments of ratification in respect of that area.

Under paragraph (2), at any time after the date of entry into force of an extension under paragraph (1), either Contracting State may, by six months' prior notice of termination given to the other Contracting State through diplomatic channels, terminate the application of the Convention to any area to which it has been extended under paragraph (1). In such event the Convention will cease to apply and have force and effect, beginning on or after the first day of

January next following the expiration of the six-month period, to the area or areas named therein, but without affecting its continued application to the United States, Korea, or to any other area to which it has been extended under paragraph (1).

Pursuant to paragraph (3), in the application of the Convention in relation to any area to which it is extended by notification by Korea or the United States, reference to "Korea" or the "United States", as the case may be, shall be construed as referring to that area.

Under paragraph (4), termination in respect of the United States or Korea of the Convention under Article 32 (Termination) will unless otherwise expressly agreed by both Contracting States, terminate the application of the Convention to any area to which the Convention has been extended under this Article by the United States or Korea.

ARTICLE 30
Assistance in Collection

This Article provides for mutual assistance in the collection of taxes where required to ensure that the benefits of the Convention will only be extended to persons entitled to such benefits. It does not in any way affect rights of residents of the Contracting States under the Convention.

Paragraph (1) provides that each Contracting State will endeavor to collect on behalf of the other Contracting State such taxes imposed by that other Contracting State as will ensure that any exemption or reduced rate of tax granted under the Convention by that other Contracting State will not be enjoyed by persons not entitled to such benefits.

Paragraph (2) makes clear, however, that in no case shall this Article be construed to impose upon a Contracting State the obligation to carry out measures at variance with the laws, administrative practices, or public policy of either Contracting State with respect to the collection of its own taxes.

ARTICLE 31
Entry into Force

This Article provides that the Convention is subject to ratification and for the exchange of instruments of ratification. The Convention will enter into force on the thirtieth day following the exchange of instruments of ratification. The Convention shall first have effect with respect to the rate of withholding taxes and Article 25 (Exemption from Social Security Taxes), to amounts paid on or after the first day of the second month following the date on which this Convention enters into force; and with respect to other taxes for taxable years beginning on or after January 1 of the year following the date on which this Convention enters into force.

ARTICLE 32

Termination

This Article provides that the Convention will remain in force indefinitely, but that it may be terminated by either Contracting State at any time after five years from the date it enters into force. A Contracting State seeking to terminate the Convention must give at least six months' notice through diplomatic channels. If the Convention is terminated, such termination will be effective with respect to income of taxable years beginning (or, in the case of withholding taxes and social security taxes, payments made) on or after January 1 next following the expiration of the six month period.

EXCHANGE OF NOTES

In notes exchanged at the time of the signing of the treaty the United States noted that the Korean Government had stressed the need for provisions in the Convention which would constitute special incentives to promote the flow of United States capital and technology to Korea. While observing that the United States could not agree to such provisions, the United States did offer assurances that, when circumstances permit, the United States would be prepared to resume discussions with a view to incorporating provisions into the Convention which will minimize the interference of the United States tax system with incentives offered by the Government of Korea. These provisions would be consistent with income tax policies of the United States Government regarding other developing countries.

In the same exchange of notes, the Korean Government confirmed that the definition of Korean tax in paragraph (1) of Article 1 of the Convention includes the Korean Defense Tax assessed on the taxes referred to in that definition, i.e., the Korean income tax and corporation tax. The Defense Tax is levied as a surcharge on a number of Korean taxes including the income tax and the corporation tax. The treaty applies only to those parts of the Defense Tax levied with respect to the income and corporation taxes.