



Attorneys at Law
YULCHON

Textile Center 12F, 944-31 Daechi 3-dong
Gangnam-gu, Seoul 135-713, Korea
TEL +822 528 5200 FAX + 822 528 5300
mail@yulchon.com www.yulchon.com

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Mr. Owens. Jeffrey Esq.
Director
OECD Center for Tax Policy and Administration
2, rue Andre Pascal,
75775 Paris, France

RE: Issues re Foreign source or non-domestic comparables

Dear Mr. Owens,

As members of the Tax Group at Yulchon, Attorneys at Law, a full-service law firm in Korea, we are pleased to have this opportunity to provide comments as attached hereto on the recently announced proposed revision of chapters I to III of the OECD transfer pricing guidelines (the "Proposed Guidelines").

Our firm, Yulchon, is one of the fastest-growing and most respected law firms in Korea, providing a wide spectrum of advisory services to corporate clients relating to international and local tax issues, including transfer pricing issues.

Our comments herein, though rather brief, are duly prepared and reviewed by our tax professionals with in-depth knowledge and expertise in transfer pricing issues, arising particularly in the Korean tax jurisdiction.

Should you have any comments or questions regarding the contents of this letter and the attachment, please do not hesitate to contact us.

Respectfully Yours,

Kyung Geun Lee / Duk Won Suh

Foreign Source or Non-Domestic Comparables

According to paragraph 3.34 of the Proposed Guidelines, “foreign source or non-domestic comparables” should not be automatically rejected just because they are not domestic (hereinafter “the paragraph 3.34”). Determination as to whether non-domestic comparables are reasonably reliable has to be made on a case-by-case basis and by reference to the extent to which they satisfy the five comparability factors.

According to the Korean Law for Coordination of International Tax Affairs (“LCITA”), arm’s length price means the price which is applied or would have been applied in an ordinary transaction between a resident, a domestic corporation or a permanent establishment and an unrelated third party other than the related party overseas. Based solely on the wording of the LCITA provisions dealing with arm’s length principles, there seems to be no basis for the Korean tax authorities to preclude the use of non-domestic comparables outright. However, in practice, the Korean tax authorities have not allowed the use of non-domestic comparables to date, as is the case in other jurisdictions as well. The main reasons for this practice are believed to be that the regional market difference and accounting standards between Korea and other countries are so significant that they cannot be reasonably adjusted no matter what method or adjustment measure is adopted. However, it is envisaged that this practice will soon be seriously reconsidered in the near future once the Proposed Guidelines are finalized and announced.

Even with the new enactment of the paragraph 3.34, however, differences in conditions among markets and countries would still be a material factor in terms of comparability criteria. Accordingly, it seems essential for the proper application of the paragraph 3.34 in practice that a consensus be formed between taxpayers and the tax authorities concerned that this type of differences can be reasonably adjusted for via appropriate methods.

In view of the foregoing, we opine that by incorporating in the Proposed Guidelines specific examples of possible adjustment factors (e.g., interest rate, price of land, standard of living, etc.), as suggested in the May 2006 publication titled “Comparability: Public Invitation to comment on a series of draft issues notes (the

“Issue Notes”),¹ the Proposed Guidelines would prove to be particularly more useful and practicable in terms of applicability in Korea and other countries that currently disallow the use of non-domestic comparables for transfer pricing purposes.

In addition to the factors suggested in the Issue Notes, we believe various industry-specific indicators readily available worldwide may also be used as adjustment criteria. Further, in appropriate cases, multi-year financial data (e.g., the level of operating margins of the specific line of business concerned) extracted from reliable commercial databases used nationwide in a given market or a country may be used as the weighting factor in the adjustment process.

The last sentence of paragraph 3.34 reads “Difficulties may also arise from differing accounting standards.” However, it would be more appropriate to add that these difficulties will be lessened as the number of countries adopting the Internal Financial Reporting Standard (IFRS) is on the rise. Indeed, a majority of the countries worldwide have actually announced their plans to introduce IFRS in the near future.

¹ Refer to paragraph 38, page 43 of the Issue Notes.