

## Recent Unanimous Decision of the Supreme Court: “Trustee has Taxpayer Liability for VAT on Trust Assets”

(Supreme Court Decision 2012Doo22485, May 18, 2017)

This recent Supreme Court Decision clarifies who bears taxpayer liability of value added tax (“VAT”) in the case of trust assets, which has been a controversial issue until now. The following is a summary of the background, rationale and impact of this landmark decision.

### **Absence of Statutory Provision**

The Value Added Tax Act of Korea (the “VAT Act”) states that “the taxpayer of VAT is the party who independently provides goods or services as part of its business” and does not provide further guidance on whether the Trustor, Trustee or Beneficiary is liable for payment of VAT in the context of a trust.

### **Overtaken Precedents**

In the past, the Supreme Court has ruled that the liability for payment of VAT lies with the Trustor (Supreme Court Decision 2000Da33034, April 25, 2003) or the Beneficiary (Supreme Court Decision 99Da59290, April 25, 2003; Supreme Court Decision 2006Doo8372, December 24, 2008), as the case may be, because the profits and expenses arising out of the disposal or management of trust assets ultimately belong to the Trustor, or in the case of a trust with a third party beneficiary, to the Beneficiary. Such precedents imposing tax liability on the Beneficiary have been largely criticized for various reasons as follows: (i) the assignment or transfer of the beneficial interest itself can hardly be viewed as “providing goods” since the Beneficiary derives benefits from the trust solely on the basis of the beneficial interest; (ii) even if the Beneficiary is a mere investor without any business presence, the Beneficiary needs to register itself as a business because the Beneficiary is deemed a business for purposes of VAT payment; and (iii) it is against the fundamental principles of VAT to hold the Beneficiary as a provider of goods.

### **Rationale Behind Recent Supreme Court Decision**

On May 18, 2017, the Supreme Court rendered a unanimous decision ruling that the Trustee has taxpayer liability for VAT in the case of trust assets, overturning the above precedents imposing taxpayer liability on the Trustor or Beneficiary (Supreme Court Decision 2012Doo22485, May 18, 2017). The Supreme Court provided the following rationale for overturning the prior decisions: “When the Trustee provides goods in the course of management or disposal of trust assets (which have been transferred to the Trustee by the Trustor), the Trustee is conducting the business of the trust by becoming a party to a contract, in its capacity as the owner of the rights and obligations of the trust assets, and as such the Trustee (who has entered into a transaction where the goods are provided by the Trustee and the rights to use and consume the goods are transferred to the transaction counterparty) is liable for payment of VAT. It does not make a difference whether the profits and expenses arising from the management or disposal of the trust assets ultimately belong to the Trustor or the Beneficiary. In addition, given the nature of the VAT as a multi-level transactional tax which requires the issuance and delivery of a tax invoice, if the Trustee is viewed as the taxpayer and as the party providing goods pursuant to the disposal of trust assets, (i) it is easy to determine the transaction counterparty under the VAT Act in relation to the trust and (ii) any confusion regarding the tax event or the price of goods can be avoided.”

### **Significant Impact**

The recent Supreme Court Decision is expected to cause a change in the tax authorities’ interpretation of this issue. In the past, based on the above Supreme Court precedents, the tax authorities have issued rulings to the following effect: “In principle, the Trustor is the taxpayer of the VAT on trust assets. However, in the case of trusts with third party beneficiaries, the Trustor is deemed to have provided goods at the time the actual control of the real estate which constitutes trust assets (“Trust Property”) is transferred to the Beneficiary from the Trustor. Thus, the Trustor should collect VAT by delivering a VAT invoice to the Beneficiary. Thereafter, the Beneficiary shall be the taxpayer liable for VAT on the Trust Property.” (Jae-so-bi-113 August 31, 2005; Jae-boo-ga-737 November 23, 2011; Bub-kyu-boo-ga 2013-233 July 12, 2013; Sa-jun-bub-ryung-boo-ga-119 May 15, 2015). It is likely that the tax authorities will shortly issue a ruling that the Trustee has taxpayer liability for VAT when providing (i.e., selling) trust assets.

### **Our Recommendation**

The significance of this recent Supreme Court Decision is that the Trustee has become both the legal owner and taxpayer of the trust assets. As a result, the interests of the parties comprising a trust have been aligned, allowing further use of trusts in structured financing and other types of transactions.

Going forward, the Trustee should be designated as the taxpayer liable for VAT on trust assets pursuant to this recent Supreme Court Decision. Tax issues may arise if the Trustor or Beneficiary is designated as the taxpayer in accordance with overturned court precedents and prior rulings from the tax authorities, which were based on the transfer of actual control of the trust assets. At this stage, it is important to constantly monitor the tax authorities’ position on this issue. Accordingly, it is advisable to seek professional advice in relation to payment liability of VAT on trust assets. In particular, entities acting as Trustees should reevaluate their current practice and obtain professional advice to establish VAT payment procedures as part of their services.

### **Download**

Full Korean Text of the Supreme Court Decision 2012Doo22485, May 18, 2017  
(Revocation of Order Imposing VAT)

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