Chapter 23

Republic of Korea (South Korea)

BY TAE-IL LEE*

From as early as 50 B.C. (the Three Kingdom period), payment of land tax has been one of the basic duties Korean citizens have had to perform, along with military service and service for public works. The ownership of land was traditionally considered to be in the hands of the royal dynasty and the king, and the land tax was an in-kind charge for the right to cultivate assigned farmlands. Although the structures and the implementation schemes differed substantially from dynasty to dynasty, and even during different periods of the same dynasty, a similar principle more or less persisted until the end of the 19th century.

With the opening of the 20th century, modern techniques of land resource management were eventually introduced to Korea by the Japanese colonial government (from its own motives of pillage); these include a cadastral survey of the entire country, land-value taxation, and a land use planning system. In the course of the first national cadastral survey (1910–1918), the primitive, loosely organized land ownership pattern that had prevailed previously virtually disintegrated, and a clearer land title concept was enforced, with corresponding tax liability. In this modern concept of real-estate as introduced to Korea, the land and its improvements

*Tae-Il Lee, Ph.D., Texas A&M University, is the director of the Chungbok Development Institute. He served for 15 years as senior research fellow and director of the Land Policy Research Division, Korea Research Institute for Human Settlements; and has been an advisor to the Minister of Construction, a visiting scholar at the Harvard Graduate School of Design, and a visiting fellow at the Lincoln Institute of Land Policy. His publications include a book, The Land Policy Problems in East Asia: A Search for New Choices (1994), and various book chapters, articles, and working papers dealing with Korean land policy.
were treated as separate entities, and property taxes thus levied separately upon them.

I

Land-Related Tax System in Modern Korea

A. An Overview of Land Taxes

As is the case for most other countries, land taxes by the central government in Korea are basically imposed on the income stream from the property and the capital gains realized at the time of transaction, while the local property taxes are levied on acquisition and registration, and on ownership. Table 1 shows the array of different land taxes currently being imposed on Korea in each sequential stage of land ownership cycle.

<table>
<thead>
<tr>
<th>Imposed On</th>
<th>National Tax*</th>
<th>Local Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Acquisition</td>
<td>Inheritance Tax</td>
<td>Acquisition Tax</td>
</tr>
<tr>
<td></td>
<td>Gift Tax</td>
<td>Registration Tax</td>
</tr>
<tr>
<td>Holding</td>
<td>Income Tax**</td>
<td>Comprehensive Landholding Tax</td>
</tr>
<tr>
<td></td>
<td>Corporate Income Tax**</td>
<td>City Planning Tax</td>
</tr>
<tr>
<td></td>
<td>Land-Value Increment Tax</td>
<td></td>
</tr>
<tr>
<td>Transfer</td>
<td>Transfer Income Tax</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Special Surtax on Corporate Income Tax</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Corporate Income Tax</td>
<td></td>
</tr>
</tbody>
</table>

Notes: *Stamp Tax is surcharged.
**Imposed on rental income.

It should be noted that, before the beginning of the local autonomous political system in 1995, the central government made virtually all the rules in Korea. Instead of having governors, mayors, and county heads appointed by the Ministry of Home Affairs (MOHA), local citizens now elect their administrators through
direct vote. Besides these elections, however, not many changes have been made yet in overall local administration.

**B. Administration of Property Tax**

MOHA is the central government agency responsible for overseeing the activities of the local governments, and even for taxes labeled as local taxes. Tax codes used to be and are still largely established by MOHA, which defines the details of tax bases, rate structures, exemptions and reductions, and collections as well as appeal procedures. Formerly, local property taxation in Korea was simply an extension of the central government’s activities, part of it (e.g., collection) being delegated to municipalities and counties. The levying and management of property taxation, which usually constitutes a major portion of any local government’s revenues, did not at all reflect each locality’s distinctive financial situation.

As has already been pointed out, all the property-related local taxes in Korea make a clear distinction between land and buildings. The distinction apparently is not derived from the influence of Henry George, since buildings are also taxed, possibly at even higher rates, by the same property taxes as those on land. Currently, the land portions of the property tax are levied in the spring of each year and the building portions in the autumn.

**II**

**Public Concept in Land (To-Ji-Gong-Gae-Nyom)**

**A. Background**

The bad memories of nation-wide land speculation in the late 1970s had scarcely faded when land prices soared again in the late 1980s. Although the rate of increase was not the highest Korea had ever seen, the absolute level of prices was such that the social and political problems generated posed a serious potential threat to the national integrity. For example, the total sum of the value of the nation’s landed resources was estimated to be more than nine times the size of the GNP in 1990, much higher than the figure for most other countries and even higher than in Japan.
The magnitude of the “capital” gains from the price appreciation in the year of 1989 alone was estimated to be 35 percent more than the local aggregate income earned by all urban workers in the same year. For a number of reasons, however, most of these unearned gains were virtually free from the recapturing efforts of tax authorities.

The government recognized that, if not properly taken care of, these issues could not only shatter the nation socio-politically, but also create a bottleneck for future economic growth. Thus from 1987 to early 1989, when the land price increase began to show signs of letting-up again, the government introduced a set of new policies, popularly known by the comprehensive term, “To-ji-gong-gae-nyom” (Public Concept in Land).

Interpreted as measures to enhance pubic interests in land-related matters, they include: the comprehensive landholding tax, a new system of land assessment, a reinforced land title registration system, and three completely new measures which some regard as rather radical—the ceiling on urban residential land per household, the development charge, and the land-value increment tax. However, since the ceiling on urban residential land, and the development charge are not exactly tax measures, they will not be discussed in this chapter.4

B. Comprehensive Landholding Tax

Korea’s landholding tax used to be levied at fixed rates on the value of each land parcel. In the late 1980s, a broad consensus emerged that this tax should be increased to deter speculative withholding. Also, as the true dimension of ownership concentration became evident, a heavy tax burden was called for also to discourage large land holdings.5 For these reasons, the comprehensive landholding tax was introduced in 1988.

Thus, the levying scheme of the conventional property tax (land portion) has been revised so that progressive rates could be applied for large holdings. Basically, it is a tax on the sum of the value of landed parcels all over the country registered under the same owner. A progressive rate structure is certainly not desirable in terms of neutrality, horizontal equity, administrative costs, or
the fiscal autonomy of local jurisdictions, but the decision was made to selectively increase the tax burden of large land owners so as to render them more likely to dispose of their excess holdings. It was anticipated that this would lessen the concentration of ownership and at the same time lower the market price of land.

Table 2

<table>
<thead>
<tr>
<th>Classification</th>
<th>Land Type</th>
<th>Number of Tax Brackets</th>
<th>Rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed Rates</td>
<td>Factory site</td>
<td></td>
<td>0.3</td>
</tr>
<tr>
<td></td>
<td>Farmland tilled by owner</td>
<td></td>
<td>0.1</td>
</tr>
<tr>
<td></td>
<td>Luxury property</td>
<td></td>
<td>5.0</td>
</tr>
<tr>
<td>Progressive</td>
<td>Speculative land and</td>
<td>9</td>
<td>0.2-5.0</td>
</tr>
<tr>
<td>Rates</td>
<td>residential land</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Commercial land</td>
<td>9</td>
<td>0.3-2.0</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

It was clear from the beginning of this measure that the tax burden on ordinary homes, agricultural lands owned by working farmers, and factory sites in operation would not increase and, indeed, would sometimes even decrease. In its final form, the measure constituted an amalgam of three principles: first, the indiscriminate aggregation of all land holdings registered under the same owner; second, the penalization of "obviously speculative" holdings; and third, opposition to any tax increase for "innocent" holdings. The tax rate structure includes three fixed rates and two progressive rates as shown in Table 2. Low fixed rates for factory sites and farm land, and a high rate for luxury land are the same as in the old property tax, but now residential land, commercial land, and land held presumably for speculation are subject to one of two progressive rates.

The first progressive rate, which applies to speculative land as well as residential land is a penalty only to the truly large land holders, since it reaches a one percent marginal rate only when the assessed value is as high as 500 million Won (roughly US$650,000). The second progressive rate with more mild progressivity is applied to commercial building sites which usually occupy expensive land in downtown areas.
Applying progressive rates is most feasible when the ownership of all land is computerized nationwide. After five years of preparation, the Ministry of Home Affairs currently runs a computerized land ownership record system and determines the amount of tax for each individual. The amount of land owned is then divided in proportion to land values among localities in which the owner holds land, and each local government is responsible for collecting its share.

C. The Tax Base and Assessment Ratio

At the core of the problems of land taxes, both national and local, is the issue of assessment. For the purpose of local taxation, Korea’s local government officials are supposed to assess the unit value of each land parcel every year and set the Standard Value for Taxation (SVT), which is then written on the official record of the parcel. However, until recently, local governments had not bothered to accurately assess land values. Even when land prices increased rapidly, the SVT was raised only slightly, partly because of political reasons but also because of the knowledge that much revenue shortfall would be supplied by the central government anyway.

Nationwide, the SVT ranges somewhere between 15 and 20 percent of the market price. As we have seen, holding tax rates are quite low for most properties, but it is the low assessment ratio that makes the tax almost insignificant to landowners and renders land taxation ineffective in achieving any policy goal. Table 3 shows the effective average tax rates for eight land values which correspond to the bracket boundaries of Progressive Rate I. In 1990, 93.56 percent of taxpayers belonged to the lowest rate bracket, and over 99.9 percent of them paid less than 0.09 percent of their land values. Whatever the policy objective of the tax may be, it cannot be achieved with such a low effective rate.

Another problematic aspect is that the present assessment ratio shows a great deal of variation among regions, land uses, and individual parcels. Usually, when there is a time lag between the actual market price change and the assessment, land with higher prices and higher rates of price increase tends to be assessed at a
lower ratio; thus, the wealthy pay relatively less tax. In addition to the inequity problem, lack of assessment uniformity poses an obstacle in using the tax as a land policy tool.

Table 3

<table>
<thead>
<tr>
<th>A. Tax Base (Assessed Value)</th>
<th>B. Amount of Tax</th>
<th>C. Market Value of Land</th>
<th>D. Average Effective Rate of Tax (B/C, %)</th>
<th>E. Cumulative Rate of Taxpayer (1990, %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>20</td>
<td>0.04</td>
<td>133.3</td>
<td>0.03</td>
<td>93.56</td>
</tr>
<tr>
<td>50</td>
<td>0.13</td>
<td>333.3</td>
<td>0.04</td>
<td>98.42</td>
</tr>
<tr>
<td>100</td>
<td>1.38</td>
<td>666.7</td>
<td>0.0</td>
<td>99.46</td>
</tr>
<tr>
<td>300</td>
<td>1.78</td>
<td>2,000.0</td>
<td>0.09</td>
<td>99.91</td>
</tr>
<tr>
<td>500</td>
<td>11.28</td>
<td>6,666.7</td>
<td>0.17</td>
<td>99.98</td>
</tr>
<tr>
<td>3,000</td>
<td>51.28</td>
<td>20,000.0</td>
<td>0.26</td>
<td>100.00</td>
</tr>
<tr>
<td>5,000</td>
<td>111.28</td>
<td>33,333.0</td>
<td>30.53</td>
<td>100.00</td>
</tr>
</tbody>
</table>

Notes: 1. Assessment Ratio is assumed to be 15 percent. Number of total taxpayers subject to the Progressive Rate I was 7,549,350.
2. 1 million Won is equivalent to approx. 1,280 Dollars (US$1 is approx. 780 Korean Won).

D. Land-Value Increment Tax

One of the most controversial of the new measures adopted was a new tax called land-value increment tax. The land-value increment tax was to institute and, in fact, to strengthen the windfall recapture system by taxing away a significant portion of the unearned income from land value appreciation even before it is actually realized, thus deterring landowners from holding onto lands because of speculative anticipations.

The lands which are subject to this tax are basically unbuilt, idle lands and non-business lands owned by firms, and excess residential lands beyond the permitted ceiling. This tax is normally levied at three year intervals, and a flat 50 percent rate is applied to the "excessive profits from lands" (land value increase over the national average during the three year period). However, when the land value increase of a certain district is so rapid that it exceeds 1.5 times the national average (speculation prone
districts), the land in question is taxed annually instead of every three years.

The new tax was levied for the first time in June 1991 with 27,441 individuals and firms being affected. It exhibited a tremendous impact on the real estate market, sharply reducing speculation-oriented land ownership. As might be expected, it did not meet with universal approval. It was criticized for being levied on unrealized gains and for violating the principle of “ability to pay.” Actually, according to the initial version, an owner might have to reduce the number or size of his housing plots or farming paddies just to pay the tax.

Also, there have been numerous successful instances of evasion by landowners who managed to avoid the “idle lands” classification by building unnecessary and often unsightly “improvements.” Besides being an aesthetic blight, during a period in 1990–1992 much of this building exacerbated a shortage of materials and skilled labor that might otherwise have been used for genuinely needed construction.8

Strong and organized complaints from the landowners culminated in their bringing the issue of land-value increment tax to the constitutional court in 1995. The court eventually ruled that the tax was not conforming to the spirit of the Constitution and ordered a substantial modification. Besides, the stabilized land market since 1991 made the number of taxable cases decrease rapidly and, at the moment of this writing, the practical viability of the land-value increment tax in the future is rather slim.

E. Unified Official Land Price Assessment System

There were in the past a number of different official land price quoting systems by different agencies or ministries corresponding to the needs of their respective functions. Problems with these existing official land prices were two-fold. One was that, although each agency had its own rationale, ordinary citizens were confused as to how the government was assessing the value of their properties and were reluctant to accept the official prices, especially since they varied widely from one agency to another. Also, land was so grossly under-assessed (roughly 15–20 percent of the
market value), any policy tools—taxes being most critical—could not exert their intended effects. Even the most stiff nominal tax rate would turn out to be a very meager tax burden for landowners.

These problems of assessment were well recognized, and the Ministry of Construction managed to get a law passed in 1989 to improve land assessment. Under its provision, all these official land prices were unified to one single system, and more importantly, full market value was made the criterion for land assessment.

The first nationwide assessment of all private lands, under the new criterion, was completed during the summer of 1990, and from 1991 national taxes on land have been imposed on that base. To-ji-gong-gae-nyom measures have also adopted the new assessment base. The government, however, failed to link the new assessment system with the comprehensive landholding tax because of objection from the National Assembly which feared that the new assessment standard would abruptly raise the tax burden. The government nevertheless planned to adopt the new assessment system as the base for the comprehensive landholding tax by 1998. But, it also planned to simultaneously adjust the nominal tax rates lest the change in the assessment standard should result in a sudden tax increase for most land owners.

\textit{F. Land Title Registration System}

Formulation and implementation of any policy requires accurate information, but the current land-related record system needs a great deal of improvement. Currently, two official records exist for each parcel of land. One is used for taxation and other administrative purposes, and the other, kept by the judicial courts, shows various legal property rights related to the parcel and concerned individuals. The problem is that one or both of the records may frequently contain defective information, and they often conflict with each other.

The proposals made for improvement include: first, unification of the two records into a single system, correctly representing all related information; second, computerization of the information
with a broader scope (links to resident identification card and household database, and to building records); and third, the initiation of a Land Census which will update necessary information once and for all.

As the first step toward improvement, the National Assembly passed the Compulsory Property Registration Act in July, 1990, which makes non-registration of property a criminal offense. Despite some doubts of its conformity to the principle of free transaction, this law will deter major causes of tax evasion and enhance the effectiveness of land taxes.

III

Financial Crisis and Recent Changes in Land Policy

The bailout by the International Monetary Fund in November 1997 marked a critical turnover in the nation's overall economic policy environment. Originating from the mismanagement of excessive short-term borrowing from abroad by local financial institutions, the crisis swept through the entire spectrum of the economic system, quickly drying up the financial market. Faced with severe lack of liquidity, business firms hurriedly let go of their real properties, and the banks also poured real properties and other assets held as collateral into the market. The real estate market in general and the land market in particular thus suddenly became flooded, and prices dropped to fire-sale levels. Since a large proportion of their portfolios consisted of real properties, this asset deflation further aggravated the threat to financial institutions. It also posed a threat to average families that held their savings in the form of housing.

This vicious cycle of problems caused serious concern on the part of government policy makers, who swiftly relaxed much real estate related regulation in order to buoy up the market. This approach mainly took the form of permitting foreigners (who had previously been excluded) to buy real estate, and of various exemptions and reductions in transfer income tax. In addition, the urban residential land ceiling regulation and the land value increment tax, both part of the Public Concept in Land package
introduced in the late 1980s, have been lifted. The development charge, also part of the package, was temporarily halved until the end of 1999.

Another line of policy change consisted of the introduction of mortgage-backed securities (MBSs) and asset-backed securities (ABAs), to make real estate a more easily assessable option to the general investor. With this move, the real estate and financial markets have slowly begun to be integrated.

IV

Summary and Conclusions

KOREA’S PAST LAND policy was so obsessed with the speculation problem that the land-related taxes were primarily regarded as measures for recapturing the unearned “capital” gains between the transactions; e.g., transfer income tax and special surtax on corporate income tax. However, due to the numerous cases of exemption and defective market information, these taxes were not able to hold down speculative transaction and ownership.

The To-ji-gong-gae-nyom policy package was thus introduced in the late 1980s as an effort to rectify the situation by structurally affecting the land ownership pattern itself. The comprehensive landholding tax, which is a much reinforced version of the already existing local property tax (land portion), was adopted to increase the tax burden of those with large holdings. The land-value increment tax was also introduced for recapturing unearned land price appreciation regardless of transaction. The focus has, therefore, shifted from the transaction point to the holding stage of the land ownership cycle.

While the rationale behind the comprehensive landholding tax is relatively well received by the public, some problems still persist including the argument about the nature of this particular tax, namely that local taxes such as the comprehensive landholding tax should not carry too heavy a national policy objective. Uneven level of assessment is another problem that has to be solved for the effective administration of the comprehensive landholding tax. The land-value increment tax, on the other hand,
is facing a serious setback by a rule of the constitutional court which could dwindle its viability.

In general, the importance and effectiveness of the landholding tax depend largely upon the share of the tax among local revenue sources. If it is a major revenue source with high effective rate, every minute detail of the tax code will draw attention from taxpayers and the tax will have significant effects on the economy. However, in many developing countries, the landholding tax is only a minor revenue source and the effective tax rate is low for various reasons: the ownership of the land may be unclear, record keeping defective, identification of land parcels difficult, and assessment techniques primitive. Under such conditions, the government’s efforts should be focused on building up an essential information base to make the tax workable. A number of measures taken by the Korean government during the late 1980s and early 1990s such as mandatory title registration and an improved assessment system, reflect such endeavors.

The government should also refrain from using the landholding tax as a tool for too many policy goals, especially when the effective tax rate is low. If a tax measure carries diverse motives, it becomes unmanageably complicated, and altogether ineffective. Also, when the central government has the power to institute tax exemptions and reductions for national purposes, it can further distort the proper tax administration and may cause revenue loss for the local governments.

Notes

1. From this point on, the name “Korea” refers only to the non-communist part of the divided nation, or South Korea.

2. Property tax (land and building portions together) makes up roughly 30-80 percent of each local government’s annual revenue.

3. Since then, the ratio between land value and GNP has shown a declining trend; in 1995, it was estimated to be around five to one.


5. A government statistic on land ownership, first revealed in 1988, indicated that 65.2 percent of the nation’s total landed resources was owned by the top 5 percent of landowners in the country.

7. Ibid., p. 276.

8. Such difficulties exemplify the pitfalls of introducing roundabout methods such as classification to try to achieve the benefits of straightforward land-value taxation. If all parcels were assessed at full market value and taxed at the same percentage thereof, with improvements exempted correspondingly, no owner would have any incentive to erect unnecessary and shoddy structures, but neither would he be penalized for erecting high-grade ones that serve a useful purpose.