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Supreme Court of Korea – En Banc Ruling[1] on Royalties for Foreign-Registered Patents

Unsettles three decades of Treaty Interpretation, impliedly follows Ambulatory Approach

Snapshot

In a landmark ruling, the Supreme Court of Korea (*en banc*) overturned over three decades of precedent by holding that royalties paid for the use of foreign-registered patents (not registered in Korea) may still constitute Korean-source income if the patented technology is used in Korea. The Court clarified that "use" under the Korea–U.S. Tax Treaty and Corporate Tax Act refers not merely to exercising patent rights within the country of registration but also to the factual use of patented technology in domestic manufacturing, sales, or operations. The judgment is also noteworthy in that it implicitly adopts a dynamic (ambulatory) approach—allowing later domestic law to inform the meaning of undefined treaty terms—rather than a static approach that freezes meaning at the time of treaty signing.

Background

Historically, Korean courts interpreted the term "use of a patent" narrowly. Since 1992, the Supreme Court had held that because of the territoriality principle of patents, "use" could occur only in the country of registration. Thus, royalties paid for foreign patents were not Korean-source income unless those patents were also registered in Korea.

Prior to the 2008 amendment, Corporate Tax Act (CTA) Article 93(8) only considered royalties taxable in Korea if the patent or right was registered domestically or if the royalty was paid within Korea. This meant that technology from foreign-registered but unregistered patents could be used in Korean manufacturing without giving rise to Korean-source royalty income, because the law tied taxability to domestic registration.

In 2008, Korea amended CTA Article 93(8) to expand source taxation: even if patents are not registered in Korea, if their technology is used in Korea (e.g., in manufacturing or sales), the royalties are deemed Korean-source income. Despite this amendment, the Supreme Court continued to apply its old precedent until 2025, effectively neutralizing the new law by invoking the treaty context and territoriality principle.

[1] *Case No. 2021Du59908 | Decision Date: 18 September 2025*

Arguments by the Parties

Taxpayer's Arguments	Tax Authorities' Submissions
Royalties related to patents registered abroad but not in Korea; under Treaty, these should not be taxable as Korean-source.	2008 amendment to CTA Article 93(8) expanded taxability; even if patents are registered abroad, factual use in Korea makes royalties taxable.
Since Korean law did not recognize use of foreign-registered patents domestically, royalties could not be considered Korean-source income.	The Treaty does not define 'use'; Article 2(2) requires reliance on domestic law, which expressly includes factual use of technology.
Relied on Supreme Court precedent since 1992 which excluded such royalties from Korean taxation.	Royalties are taxable if technology is used in Korea, consistent with the 2008 domestic law amendment.
Payments were in substance for U.S. patent rights and settlement of U.S. litigation, not for Korean use.	Royalties are for technology exploited in Korea regardless of registration status; withholding obligations attach if technology is deployed domestically.

Decision of the Korean Supreme Court

In its en banc decision, the Supreme Court departed from over three decades of consistent precedent and fundamentally reshaped the approach to royalty taxation under Korean law. The Court observed that the issue turned on the interpretation of the term "use" in Article 14 of the Korea–U.S. Tax Treaty and Article 93(8) of the Corporate Tax Act. Contrary to earlier rulings that had equated "use" solely with the exercise of patent rights in the country of registration, the Court held that "use" encompasses the factual and economic deployment of patented technology in Korea, such as in manufacturing processes or the sale of goods, even where the patents themselves are not registered domestically. By adopting this interpretation, the Court placed emphasis on the economic reality of technology use rather than the formalities of registration and enforceability of patent rights. It further reasoned that the Treaty text contains no contextual basis to restrict the meaning of "use" narrowly, and that Article 2(2) of the Treaty expressly directs undefined terms to domestic law. Since the 2008 amendment to CTA Article 93(8) defines "use" to include factual use of foreign registered patents in Korea, the Court accepted this as the applicable standard. In conclusion, the Supreme Court reversed the High Court's decision that had sided with the taxpayer and remanded the case for fact finding on whether the patented technology was indeed used in Korea in a manner giving rise to Korean source royalty income.

Earlier Korean Supreme Court Rulings and Their Rationale

From 1992 through 2022, the Court consistently held that royalties for patents registered abroad were not Korean-source income. This interpretation was based on the territoriality principle: patent rights exist only in the country of registration, and 'use' was equated with exercising exclusive rights within that country.

Even after the 2008 amendment to CTA Article 93(8), the Court adhered to this position, citing concerns of treaty override and emphasizing that foreign inventions were in the public domain in Korea. It characterized royalties as payments for foreign patent rights and foreign market access, not domestic use.

How the Court Treated Undefined Treaty Terms, Later Domestic Amendments, and Treaty-Override Concerns

1) **Majority's method (Article 2(2) of the Korea–U.S. Treaty)**

   The Treaty does not define "use." The Court therefore applied Article 2(2): unless the context requires otherwise, undefined terms take their meaning from the domestic law of the taxing state. The majority examined the Treaty's text, structure, object and purpose, and found no contextual basis to restrict "use" only to the exercise of registered patent rights. On that footing, it looked to Corporate Tax Act (CTA) Article 93(8) (as amended in 2008), which treats "use" as the factual use of technology in Korea (manufacturing, sales, etc.), and held that royalties tied to such use are Korean-source income.

2) **Temporal question — can later domestic law supply the meaning?**

   The majority did not frame this as a treaty-override problem. By invoking Article 2(2), it effectively adopted a dynamic (ambulatory) reference to domestic law at the time of taxation. Because the Court found no contrary "context" in the Treaty, it saw no obstacle to using the 2008 amendment to supply the operative meaning of "use." In other words, the sequencing (Treaty first, statute later) did not bar the statute from informing the Treaty term; the key was whether the Treaty's own context displaced domestic law — and the majority said it did not.

3) **Why this is not, in the majority's view, treaty override**

   Treaty override arises when domestic law negates or displaces the Treaty. The majority characterized its approach as Treaty-conforming: the Treaty itself (Art. 2(2)) points to domestic law for undefined terms. The majority also rejected the earlier reliance on patent territoriality as lacking grounding in the Treaty's context, thus removing the basis for excluding domestic law's broader, technology-use meaning.

4) **The dissent's rebuttal on override and dynamic interpretation**

   The dissent argued that the Treaty's text and context already fix "patent" as a legal right and "use" as the exercise of that right, so Article 2(2) should not be triggered. In their view, importing the 2008 CTA amendment to redefine "use" amounts to a de facto treaty override and an improper use of dynamic interpretation — contrary to Vienna Convention Article 27 and OECD Commentary cautions — because it lets a later domestic statute alter the Treaty's agreed meaning.

5) **Practical takeaway**

   Post-ruling, Korean courts and tax authorities will read undefined royalty terms through the lens of current domestic law unless the Treaty's context clearly compels a different reading. Taxpayers should document where technology was actually used and be prepared for allocation debates; doctrinally, expect arguments to focus on whether a Treaty's "context otherwise requires" a narrower meaning.

What Changes in Korea Now?

The ruling marks a significant turning point in Korea's approach to royalty taxation. By abandoning its long standing territoriality based interpretation, the Supreme Court has clarified that royalties for foreign registered patents can be taxed in Korea if the patented technology is factually used within the country. This expands Korea's source taxing rights considerably and aligns domestic law more closely with the broader "place of use" principle seen in many tax treaties. The decision also means that Korean companies paying royalties abroad must now assess more carefully whether the technology licensed under foreign patents is deployed in their Korean operations. If so, they will bear withholding obligations even in the absence of Korean registration of those patents. At the same time, the Court's approach opens the door to new challenges. Questions of how to determine factual use, how to apportion royalties between Korean and foreign use in global agreements, and how to avoid double taxation will likely dominate future disputes. In effect, the judgment strengthens Korea's fiscal position but adds compliance complexity and elevates the importance of documentation and fact finding for cross border royalty arrangements.

KCM Comments

Korea's en-banc judgment illustrates how a court can lawfully reach a technology-use (place-of-use) outcome by invoking the treaty's Art. 3(2) analogue—i.e., borrowing domestic-law meaning for an undefined term—and, crucially, by treating a post-treaty domestic clarification as operable because the treaty text/context did not pre-empt it. Transposed to India, the operative hierarchy remains: if a treaty term is undefined in the treaty but defined in Indian law, India applies the Act's definition with section 90(2) protection; the treaty's "context otherwise requires" gateway is not engaged here and instead appears only in the residuary cases under the Income-tax Act, 2025 section 159(7)(b)/(c) (where the term is defined in neither the treaty nor the Act), for which the 2025 Act expressly adopts an ambulatory timing rule (meaning taken as at the time of application). The Korean approach is therefore most analogous to India's position when the treaty is silent and the Act supplies the meaning—with one important caveat: unlike the explicit ambulatory rule in section 159(7)(b)/(c), the 2025 Act is silent on timing where the term is defined in the Act (static vs ambulatory). Practically, Indian authorities and courts often read domestic definitions as in force for the relevant year, but because section 159 does not say so expressly for Act-defined terms, a timing ambiguity remains.

For further analysis and discussion, you may please reach out to us.

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