

SECURITIES LAWS IN KOREA AND REGULATIONS ON FOREIGN INVESTMENT

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Since the early 1960s, South Korea has enjoyed several decades of rapid economic growth.¹ At the initial stages of its economic development, Korea relied heavily on loans from overseas sources. Development of industry and a social infrastructure had been hindered by over 40 years of Japanese colonialism and further retarded by three years of civil war. Thus, Korea had to rely on overseas sources for the funding of its economic growth. In the late 1960s, however, the Korean government began to implement policies to develop a securities market for the purpose of raising more capital from domestic sources. As a result of continued efforts to cultivate the domestic securities market, approximately half of corporate financing is now achieved through securities such as stocks and bonds.²

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1. Rate of Economic Growth (source: Bank of Korea)

	1961	1965	1970	1975	1980	1985	1990	1995
GNP (in USS 1 billion)	2.1	3.0	8.1	20.8	61.5	89.7	251.8	334.0
GNP/capita (in USS)	82	105	252	590	1,592	2,194	5,883	8,483

2. Ratio of direct to indirect corporate financing (source: Ministry of Finance and Economy)

	1970	1975	1980	1985	1990	1995
Direct financing	9.9	19.9	22.0	26.2	42.4	51.0
Indirect financing	90.1	80.1	78.0	73.8	57.6	49.0

Unit: %

The rapid growth of the Korean securities market³ would have been impossible without the development of well-designed securities laws. These securities laws and regulations fulfill major policy goals such as capital market expansion, the establishment of market stability, the encouragement of fair trading and competition, the internationalization of the market, and management protection of listed corporations. These laws also reflect policies adopted to meet the challenges of an ever-changing and expanding securities market.

For example, foreign participation in the Korean market has increased significantly⁴ with the government's move to open Korea's economy, and yet barriers such as the lack of an internationally recognized reputation on the part of securities investors, steep capital requirements (minimum five billion won⁵), reciprocity barriers, and the "economic need" test still remain in order to protect both investors and the domestic securities industry.⁶

This paper introduces the major features of the Securities and Exchange Act ("SEA") to those readers unfamiliar with the securities industry in South Korea. Topics to be discussed include the definition of securities, the regulatory system, disclosure, trading, fraud, management protection of listed corporations, and the regulation of foreign participation in the capital market.

3. KSE growth (source: Korea Stock Exchange)

	1963	1965	1970	1975	1980	1985	1990	1995
Market value of all listed shares; (% of GNP)	10.0 (2)	14.5 (1.8)	97.9 (3.5)	916.0 (9.1)	2,526.5 (6.9)	6,570.4 (8.4)	79,019.6 (44.3)	141,151.4 (55.4)
Amount transacted	26.0	9.3	42.9	333.9	1,134.0	9,598.1	53,454.5	142,914.0

Unit: 1 billion won

4. Increase in foreign investment (source: Ministry of Finance and Economy)

	1992	1993	1994	1995	1996 (May)
Registered investors	1,572	2,745	3,427	4,286	4,691
Owned shares (ratio of total shares)	220.2 (4.1)	503.3 (8.7)	634.8 (9.2)	762.3 (10.0)	883.8 (11.2)
Amount transacted (ratio of total shares)	1,630.8 (1.8)	4,523.0 (2.5)	5,636.9 (2.45)	6,943.1 (4.86)	4,210.5 (4.62)

Unit: 1 billion won

5. As of July 1996, US\$ 1 was equal to 813.30 Won (Source: Korea Exchange Bank, 1996).

6. According to the economic need test in Korea, approval of new securities corporations (both domestic and foreign) is based on current and/or regional needs.

I. SOURCES OF SECURITIES LAW IN SOUTH KOREA

The SEA⁷ was enacted in 1962 to facilitate the wide and orderly circulation of securities through fair issuance and trade and to protect investors, thereby providing a good framework to raise domestic investment funds to contribute to the development of the national economy.

The scope of the SEA is not insignificant, covering the issuance and trading of securities, the functioning of securities-related organizations, the supervision of the securities market and the enforcement of SEA provisions. Matters such as corporate disclosure, proxy solicitation, acquisition of treasury stock, and restrictions on mutual ownership between companies are also covered by the SEA. The SEA also provides the legal basis for the establishment and supervision of securities firms, the Korean Securities and Exchange Commission ("SEC") and its executive organ, the Securities Supervisory Board ("SSB"), the Korea Stock Exchange ("KSE"), and the Korea Securities Depository⁸ ("KSD"). In addition, SEA provisions enforce fair trading, prohibit fraud by price manipulation and insider trading, and stipulate penalties for such violation. The SEA is the "special law"⁹ governing the securities industry, and thus its provisions override other laws on securities matters.

But there are, in addition to the SEA, other laws regulating various aspects of the securities market and industry. Among them are the Commercial Code¹⁰ (the legal backbone for the SEA), the Capital Market

7. The Securities and Exchange Act of Dec. 22, 1976, Law No. 2920 (as amended by Law No. 4701, Jan. 5, 1994) [hereinafter SEA].

8. The KSD is similar to an American depository receipt institution, although its scope of activities may be a little wider. In addition to its duties of handling deposits and transfers between accounts, the KSD collects securities transactions taxes and settles transactions reached at the KSE.

9. In Korean jurisprudence, a "special law" is a law which applies only under specific circumstances to people, places, and/or events. A special law contrasts with a "basic law," which applies to persons, places, events, etc., without any specific limitations. Application of a special law takes precedence over that of a basic law. In civil law countries such as Korea, the Civil Code is a basic law which applies to all sorts of legal situations, such as divorce proceedings, commercial transactions, and property disputes. On the other hand, the Commercial Code is a law dealing with commercial matters such as corporate structure and management. The application of the Commercial Code takes precedence over the Civil Code. The terms "basic" and "special" are relative. The Commercial Code is a special law vis-a-vis the Civil Code, but relative to the SEA, a special law which regulates securities, the Commercial Code is a basic law. Thus, the SEA takes priority over the Commercial Code on securities matters.

10. Commercial Code, Law No. 1000, Jan. 20, 1962 (as amended Dec. 31, 1991). The goal of the Code is the maintenance and development of corporate concerns and the promotion of smooth and secure corporate transactions.

Part 3 of the Commercial Code, dealing with companies, prescribes general provisions

Promotion Act¹¹(which supports the growth of the securities market), the Securities Investment Trust Act,¹² the Law on the External Auditing of Stock Corporations,¹³ and the Certified Public Accountant Act.¹⁴ Other laws such as the Government Bond Act,¹⁵ the Act on the Registration of Public and Corporate Bonds,¹⁶ the Act on the Trust of Collateralized Corporate Bonds,¹⁷ the Monopoly Regulation and Fair Trade Act,¹⁸ and the

concerning stock corporations (*chusik hoesa*), partnerships (*hapmyung hoesa*), and other types of companies. The SEA prescribes rules specific to the stock corporation, with an aim to promoting the smooth circulation and fair pricing of stocks. When there is a conflict between the SEA and the Commercial Code, the SEA shall be applied preferentially. For example, art. 341 of the Commercial Code in principle proscribes the acquisition of the shares of one's own corporation, while art. 189-2 of the SEA allows such ownership by listed corporations within certain limitations. Furthermore, art. 342-2 of the Commercial Code prohibits the exchangeable mutual ownership of shares between two stock corporations, yet art. 189 of the SEA limits its prohibition on the mutual ownership of shares to listed stock corporations.

11. Capital Market Promotion Act (CMPA), Law No. 2046, Nov. 28, 1987 (as amended Dec. 31, 1993). This law was promulgated to promote the sound development of capital markets. The CMPA encourages corporations to go public by setting up preferential mechanisms for public and listed corporations. It also induces the wide distribution of corporate shares through programs such as the giving of preferences to small-scale investors and employees.

12. Securities Investment Trust Act, Law No. 2129, Aug. 4, 1969 (as amended). This law was enacted with the goal of establishing a system of securities investment trusts which facilitates the investment in securities by general investors and protects the beneficiaries of securities investment trusts, thereby contributing to the development of the domestic economy.

13. Law on the External Auditing of Stock Corporations, Law No. 3297, Dec. 31, 1980 (as amended Dec. 31, 1993). This law was enacted with the purpose of protecting the various parties interested in a corporation and contributing to the sound development of the corporation. This law requires an independent outside auditor to conduct audits of stock corporations with at least 6 billion won in total assets as of the end of the previous fiscal year, thereby assuring a proper audit.

14. Certified Public Accountant Act, Law No. 1797, July 15, 1966 (as amended Dec. 31, 1993).

15. Government Bond Act, Law No.4675 Dec. 31, 1993. This law provides for basic matters relating to government bonds. The objective is the efficient execution of government bond issuance and management operations.

16. Act on the Registration of Public and Corporate Bonds, Law No.2164, Jan. 1, 1970. This law was enacted with the aim of streamlining public and corporate bond issuance and guaranteeing the rights of bond creditors, thereby contributing to the development of the Korean capital market.

17. Act on the Trust of Collateralized Corporate Bonds, Law No. 991, Jan. 20, 1962. This law was enacted with the purpose of guiding and monitoring trust-related operations regarding the issuance of collateralized corporate bonds and protecting debenture holders, thereby making it easier for the general public to invest in corporate debentures.

18. Monopoly Regulation and Fair Trade Act, Law No. 4198, Jan. 13, 1990 (as amended Dec. 31, 1994). This law was enacted with the purpose of promoting creative industry and protecting consumers while planning for the balanced growth of the domestic economy. This law seeks to prevent abuse of the market position of businessmen and the excessive concentration of economic power, while controlling collusive acts and other unfair transactions, so as to promote fair and free competition.

Securities Transaction Tax Act¹⁹ also regulate some securities-related businesses.

To enforce the securities-related laws, presidential decrees and ministerial decrees for each law have been promulgated.²⁰ The SEA Enforcement Decree,²¹ for example, supplements the SEA with detailed regulations. These laws and decrees, however, can not cover effectively the dynamic changes in the securities industry. Details are therefore handled by the rules set forth by the SEC which has been delegated power to do so by the SEA. The KSE rules also play an important role in regulating investors, listed corporations and securities firms. Other rules for fair business conduct by brokers are set forth and enforced by the Korean Securities Dealers Association ("KSDA"), and the KSD governs securities, certificate deposits and transfers.

II. SECURITIES REGULATORY AUTHORITY

There are several institutions which regulate the securities market in Korea. The Korean government, the SEC and its executive organ, the Securities Supervisory Board ("SSB"), the KSE, and the KSDA all share regulatory functions. In the initial stage of securities market development, market regulation was initiated mostly by the government, but regulation by the government is now gradually shifting to self-regulation with the expansion and liberalization of the securities market in Korea.

The SEC²² deliberates and passes resolutions on matters regarding the trading and issuance markets, and it oversees securities-related organs. The

19. Securities Transaction Tax Act, Law No. 3104, Dec. 5, 1978 (as amended Dec. 31, 1993). This law fixes the burden and rate of taxes upon the transfer of share rights or equity (corporate equity under the Commercial Code).

20. Presidential and ministerial decrees are those decrees proclaimed by the president or the competent ministry regarding matters that were either legislatively entrusted to the president or the ministry or which are necessary for enforcement of a legislative act. In addition to these, competent ministries promulgate enforcement regulations, in accordance with laws and decrees, to regulate those matters to which the act applies. Legislative acts take priority over decrees, and decrees take priority over enforcement regulations. In addition, among decrees, a presidential decree takes priority over a ministerial decree.

21. Presidential Decree No. 8436, Feb. 9, 1977 (as amended Apr. 30, 1994) [hereinafter Enforcement Decree].

22. Although basically similar to the Securities and Exchange Commission in the United States, the Korean SEC regulates margin trading (see article 49 of the SEA, which authorizes the SEC to fix ceilings and collateral ratio applying to margin trading, and provides for methods of collection, etc.), which, in the United States, is typically regulated by the Federal Reserve Board of the U.S. Furthermore, while enforcement functions are handled by the SEC in the U.S., this is handled in Korea by the Securities Supervisory Board (SSB).

SSB carries out the secretariat functions of the SEC, regulates the issuance markets, and performs inspections of securities-related organs. The KSE manages and operates the trading market and imposes necessary restrictions autonomously. The KSDA manages over-the-counter ("OTC") markets as provided by law. Each of these organs cooperates with the others in the coordination of each aspect of operation, and the Ministry of Finance and Economy ("MOFE"), as the supreme organ of securities policy-making under the SEA, is responsible for determining their business boundaries.

A. *Governmental Regulatory Authorities*

1. Ministry of Finance and Economy

As important economic policy-making functions in Korea are concentrated in the central government, it is not surprising that the Ministry of Finance and Economy (MOFE) is the supreme decision-making authority for securities administration. For the sake of efficiency, MOFE delegates considerable authority to the SEC, the SSB, and the KSE in accordance with the SEA, but these organizations remain subject to the management and supervision of MOFE. In addition, MOFE has the power to authorize and issue permits for securities businesses, and to call for an emergency suspension of trading of the KSE. In reality, however, much of this authority has been passed out of MOFE's hands. For example, the management of securities issuances, the maintenance of fair trading, the management of listed corporations, the supervision of securities organs, the guidance and supervision of securities companies and securities investment advisory companies, and the investigation of unfair transactions such as insider trading and price manipulation are all under the authority of the SEC and SSB.

2. The Securities Exchange Commission and the Securities Supervisory Board

The SEC and the SSB were established as specialized administrative agencies for the management and supervision of the securities market under the 1976 revised provisions of the SEA.²³ The SEC is an

23. SEA, *supra* note 7, arts. 118, 130.

administrative committee which is comprised of nine commissioners.²⁴ Resolutions are adopted by this body by a two-thirds vote, as long as a quorum of at least two-thirds of the commissioners are present.²⁵ The Korean SEC was modeled after the U.S. SEC, though in content the Korean one differs substantially. That is, the Korean SEC is composed mainly of civilians, not governmental officials; commissioners are usually selected from among experts in the securities industry or academia. The SEC has quasi-legislative powers, yet no corresponding quasi-judicial powers.²⁶ All resolutions adopted by the SEC must be reported to MOFE, which may cancel or suspend the resolution if it is deemed illegal or highly inappropriate. Such an action, however, has rarely been taken. The SSB is an executive organ of the SEC which aims to secure fairness in the issuance and trading of securities through the supervision and inspection of securities-related institutions and the overseeing of listed companies.²⁷

B. *Self-regulatory Institutions*

1. Korea Stock Exchange

The KSE was set up in 1956 for the fair and stable formation of securities prices and the smooth trading of securities under the SEA. The KSE is the only stock exchange in Korea and the SEA prohibits the opening of a market similar to the KSE. As a non-profit organization, the KSE runs under a membership system. A member must be a securities company satisfying requirements stipulated by the Charter of the KSE.²⁸ As

24. The nine commissioners are provided for under article 119 of the SEA. The president of the Bank of Korea, the Chairman of the Korean Stock Exchange, and the Vice-minister of MOFE automatically assume the position of non-standing commissioners, and the remaining six (three of whom are standing commissioners and three are non-standing) are chosen by the President from among candidates recommended by MOFE for their securities expertise and integrity.

25. SEA, *supra* note 7, art. 125.

26. In Korea, exclusive authority over arrests and prosecutions is held by the Prosecutor's Office. Thus, unlike in the United States, a quasi-judicial role has not been recognized for the Korean SEC.

27. SEA, *supra* note 7, art. 135.

28. Art. 10 of the KSE Charter limits membership to those securities companies receiving approval to establish an office under art. 28 of the SEA. Arts. 11-16 fix certain further requirements, such as amount of capital investment, dues, deposit funds, disclosures, documentation, etc. which must be submitted or observed. Arts. 19 to 21-2 fix matters regarding membership application, membership fees, etc., while arts. 28-29 provide for disciplinary measures. In addition, the portion of the KSE operating rules starting from art. 39 provides for inspection of members suspected of engaging in aberrant trading, in order to achieve market stability and fair pricing. Furthermore, it provides for measures such as suspension of trading, imposition of fines, and demanding of employee

of August, 1996, there are 36 members, among which three are foreign securities houses.²⁹ The basic function of the KSE is to operate the securities market, including the securities index futures markets. To this end, the KSE engages in sub-functions such as listing, trade matching, corporate disclosure, surveillance and member administration, and the auctioning of unlisted securities.

As for its regulatory functions, the KSE may take disciplinary actions³⁰ against its members to ensure fairness of securities trading in the exchange market. If a member fails to settle transactions or make payment to the KSE, the KSE may take measures to suspend trading and/or membership or to expel a member. In cases where a member's actions violates the Charter, relevant laws, rules and regulations, or provisions of the KSE or other authority, the KSE may also suspend trading and/or membership as well as request members to take disciplinary measures against their own responsible officers or employees.

2. Korea Securities Dealers Association

The KSDA was established as a non-profit organization to maintain order among securities companies and to protect investors through fair securities trading. This agency is not merely an independent association but a self-regulatory institution promulgated under the SEA.³¹ The association provides rules and oversees members' business practices on investment recommendations and customer management, advertisements, and employment. The SEC may direct the KSDA to examine and report on the status of transactions in securities and on matters relating to the protection of investors, and the SEC may also order the KSDA to take necessary measures to maintain orderly commercial transactions among securities companies.³² Under these rules and regulations, member securities companies are required to comply with relevant regulations and are encouraged to give priority to the investor's interests in their dealings, investment recommendations, and customer management. To protect potential investors, members are required to make appropriate claims in

disciplinary action, in the case of a violation of law, falsification of documents, or obstruction of an inspection.

29. The three foreign investment houses are Jardine Fleming, ING Baring, and Morgan Stanley.

30. Art. 28 of the KSE Charter.

31. SEA, *supra* note 7, arts. 162-172.

32. SEA, *supra* note 7, art. 166.

their advertisements³³ and should be clear in stipulating the criteria for employment of investment advisors or member employees, the responsibilities of the above-stated positions, and the qualifications of investment advisors for the responsible supervision of employees.

In addition, if a member is found to have violated the SEA or its related regulations in its securities trading or to have violated regulations for investor protection, the association may take the case to its board of directors. The board of directors has the power to issue disciplinary actions including warnings, fines, or the suspension/expulsion of membership. Under the supervision of the SEC, and in accordance with the trend towards deregulation to strengthen the competitiveness of the Korean securities market, the association will play a greater role in enhancing the self-regulatory function in the securities business.

III. SECURITIES

Securities, as defined in Article 2 of the SEA, include national and local government bonds, corporate bonds or debentures, bonds and certificates of capital contribution issued by a corporation incorporated under special legislation,³⁴ and stock certificates or instruments representing a preemptive right to subscribe to new shares. Securities also include certificates or instruments issued by a foreign country or corporation which are of the same nature as those listed above and designated by MOFE, and include other certificates or instruments which are similar or related to those listed above and designated by Enforcement Decree (e.g., beneficial certificates issued pursuant to the Trust Business Act or the Securities Investment Trust Act). Rights to be represented by any of the securities enumerated above are themselves securities even in cases where the certificates thereof have not been issued.

The SEA provides enumerated and narrowly defined categories of securities whereas the U.S. laws define securities in a broad manner as determined in the Securities Act of 1933, the Securities and Exchange Act of 1934, and under Blue Sky Laws. In contrast, securities under the SEA

33. According to art. 4 of the KSDA Advertising Regulations, making "appropriate claims" refers to "a prudent manner of advertising which will not compromise the judgment of investors."

34. The Bank of Korea, for example, established under the Bank of Korea Act (Law No. 138, May 5, 1950, as amended Dec. 31, 1982), may issue currency stabilizing securities in accordance with arts. 90-92 of that Act. Furthermore, the Korea Industrial Bank, incorporated under the Korea Industrial Bank Act (Law No. 302, Dec. 30, 1953, as amended Jan. 5, 1995), may issue industrial financing bonds.

have been defined narrowly, being limited to investment securities for corporate finance, held by investors with the purpose of investment, and issued by firms to raise funds. Korean academics in the field of civil and corporate laws interpret securities narrowly as investment securities based on the concept of civil and traditional proprietary rights. They also explain trading of securities as a contract by which the proprietary right and the payment of proceeds are exchanged. Therefore, for example, an investment contract is not considered to be a security under Korean law.

Korea has had little need to expand its legal definition of securities to a more comprehensive one because its economy is still in the initial stages of securitization of finance. Also, there has been concern that a broad legal definition of securities might cause conflicts among financial intermediaries concerning their respective roles in the business community. Because Korean law strictly demarcates the role of different financial institutions within the financial industry, a slight legal change can have a significant impact on the interests of these institutions. However, Article 2 of the SEA does provide a basis to designate which certificates or instruments must be regulated as securities by Enforcement Decree for the protection of investors. It is inevitable that several types of derivatives will be incorporated into the definition of securities in the future. It is also likely that in the future newly developed corporate finance securities, asset-backed securities, and other marketable securities will fall under the jurisdiction of the SEA when required.

As a recent example, a 1994 revision of the SEA provided for a separate definition of financial products related to securities-indices as securities.³⁵ As mentioned above, the SEA definition of securities is based on the concept of capital securities. Thus, under traditional concepts of proprietary rights, it could be disputed whether securities indices, which take the form of balance payments, not involving the transfer of proprietary rights, could be considered securities at all. The SEA chose to regard these financial products as quasi-securities in a separate article, rather than to include them among the current list of securities.

IV. CORPORATE DISCLOSURE

In order to promote the timely disclosure of information that may affect the value of securities or investment decisions, the SEA requires all listed and registered corporations to submit periodic reports and timely

35. SEA, *supra* note 7, art. 2-2. *See infra* Part V(C).

disclosures of corporate information to the SEC and/or to the KSE. Registration is required for any corporation described in Article 3 of the SEA. Corporate disclosures prescribed in the SEA fall into two categories, issuing market disclosure and trading market disclosure.

A. *Disclosure in the Issuing Market*

The registration statement and the prospectus are the principal sources of information in the issuing market. The registration statement, which is filed with the SEC, contains a wide range of information about a corporation desiring to make a public offering. This information includes the outlook on the corporation,³⁶ description of the public offering, the proposed use of the funds to be raised, and relevant financial statements. The prospectus must be disclosed to the public at the time of the public offering and must be consistent with the information contained in the registration statement.³⁷ Securities issuers are required to keep copies of the prospectus in the issuer's place of business (main and branch offices), at the SEC, at the KSE, and with the underwriters and dealers, so that it can be viewed by the public.³⁸

A prospectus should include the following information as contained in the registration statement: (1) matters pertaining to the public offering and secondary distribution, such as the manner in which the offering will be conducted, the objectives to be achieved through the use of received capital, the opinions of underwriters, the evaluations of financial analysts; and other matters required for investor protection; and (2) matters pertaining to the issuer, such as the general conditions of the company, the nature of business, financial matters, opinions of auditors; conditions of related companies, stock-related matters, employee-related matters; transactions with interested parties, attached specifications, and other related matters.³⁹ In addition to the aforementioned items, the prospectus should also contain the date that the registration statement takes effect, the prices of securities, the period of public offering, the payment period, and the places where the registration statement and the prospectus will be made public.⁴⁰

36. Unlike the United States, Korea has avoided problems relating to the disclosure of soft information and forward-looking statements. However, discussion of such issues has begun in academic and industry circles.

37. SEA, *supra* note 7, art. 12.

38. Enforcement Decree, *supra* note 21, art. 8.

39. SEC Regulations.

40. MOFE Ministerial Decree.

As in the United States, all activities aimed at persuading investors to purchase securities are considered a solicitation for subscription by the SEC. Such activities include informing investors of securities issuance and sales and of acquisition procedures by sending letters, holding conferences on investment opportunities, distributing promotional literature, and advertising through television, newspapers, magazines, radio, etc.

The issuer of securities may draw up and use a preliminary prospectus during the period between the SEC's acceptance of registration statement and its effective date. In this case, the issuer must submit the preliminary prospectus in addition to submitting the registration statement to the SEC. The final prospectus should be submitted on the day the registration statement takes effect.

1. Corporate Registration

Corporate registration was introduced in 1976 to promote the growth of the securities market and to induce public offerings by corporations.⁴¹ This was done at a time when the securities market was underdeveloped and there were so few public corporations that corporations had difficulty raising working capital. From the time it was introduced until 1990, there were a number of corporations which had to register under SEC mandate. Since 1990, however, there have been no cases of corporations which were required to register.

The SEA requires the following issuers of securities to register with the SEC:⁴²

- (1) corporations that intend to list their securities on the securities market;
- (2) unlisted corporations that intend to make a public offering or secondary distribution of securities;
- (3) unlisted corporations that intend to merge or consolidate with a listed corporation;
- (4) unlisted corporations that intend to trade their securities outside the exchange market in accordance with Art. 94 of the SEA;
- (5) legal entities that are in the process of being incorporated through public offerings; and

41. SEA, *supra* note 7, chapter II, arts. 3-6.

42. *Id.* art. 3.

(6) corporations designated by the SEC from among those corporations falling under standards set by the Enforcement Decree.

Securities for which registration is required include corporate stock, subscription rights certificates of new shares, debentures, and foreign securities designated by MOFE. Issuers of government bonds, municipal bonds, bonds and capital securities issued by corporations established under special legislation,⁴³ and beneficial securities issued by trust companies and securities investment trust companies are exempt from registration.⁴⁴

A registered corporation must submit its financial statements and report important matters such as changes in corporate name, the amount of capital stock, corporate control, and mergers to the SEC.⁴⁵ The SEC is required to make this information available for public perusal (to the extent that it does not involve trade or other secrets) usually for a period of two years.⁴⁶ Furthermore, the SEC may prescribe criteria for the management of registered corporations and make recommendations regarding matters such as the financing of corporations and improvements to the financial structure.⁴⁷

2. Registration of Public Offerings

Unless grounds for exemption can be established, a public offering can commence only after the issuer files a registration statement⁴⁸ which is declared effective by the SEC.⁴⁹ Basically, there are two types of exemptions: (1) exemptions for certain kinds of securities, including government bonds, municipal bonds, bonds and capital securities issued by corporations established under special legislation, and, under Article 5-3

43. "Corporations established under special legislation" include entities such as the Bank of Korea, the Korea Industrial Bank, etc. See *supra* note 34.

44. SEA, *supra* note 7, art. 3.

45. *Id.* art. 4.

46. Enforcement Decree, *supra* note 21, art. 8.

47. SEA, *supra* note 7, art. 6. In accordance with this provision, the SEC formulated the Regulations on Management of Registered Corporations, which set forth the appropriate criteria.

48. It should be noted that corporate registration is different from the registration of a public offering. Corporate registration applies to the corporations mentioned in the previous section, whereas the registration of a public offering applies to those corporations intending to offer their securities publicly. Thus, before a corporation may engage in a public offering, it must first register the corporation and then register the offering.

49. SEA, *supra* note 7, art. 8.

of the Enforcement Decree, beneficial securities issued by trust companies and securities investment trust companies;⁵⁰ and (2) exemptions for securities issued in public offerings not exceeding 100 million won.⁵¹ The registration statement must include all pertinent information and documents related to the affairs of the issuer and to the offering in particular. The registration will take effect five to twenty days after being received by the SEC. A waiting period is specified by Ministerial Decree pertaining to each type of offering as follows:⁵²

- (1) twenty days for an initial public offering of shares (seven days for an issuance of new shares to preemptive rights holders);
- (2) ten days for a public offering of new shares by listed corporations;
- (3) fifteen days for a public offering of corporate bonds;
- (4) five days for a public offering of collateralized secured bonds; and
- (5) seven days for a public offering of the bonds through shelf registration.

When a registration statement is filed (if it includes all the information required by the SEC),⁵³ it shall be deemed to have been accepted by the SEC and will take effect after the lapse of the above-stated waiting period. If the statement does not satisfy the requirements, or if there are omissions in material information, the SEC may order a corporation to amend the statement and the statement shall not be considered to have been accepted. On the other hand, a corporation may voluntarily submit an amended statement when there are changes in the statement it has submitted. In this case, the waiting period shall begin anew from the date the amended statement was submitted.

In most cases, before filing a registration statement, it is the general practice for a corporation to discuss with and receive advice from the SEC. A statement may be filed without specifying the issuing price, since that price is yet to be determined. In such a case, an amended statement is filed

50. *Id.* art. 7.

51. *Id.* art. 8.

52. MOFE Ministerial Decree.

53. SEA, *supra* note 7, art. 8(2). Under the SEC 'Regulations on Reporting of Securities,' the statement must include: the general health of the company, the purpose of the offerings, the usage of funds, financial statements, the opinion of an underwriter, and other matters related to the corporation.

as soon as the issuing price is determined. Similarly, when there are changes in the original information submitted, such as a change in the issuing price, an issuer may submit an amended statement.

As for the registration of bonds (with the exception of equity-related bonds such as convertible bonds, bonds with warrants, and participation bonds), issuers may use the shelf registration system. This system allows the filing of a registration statement for bonds to be issued within one year. At the time of issuance, if there are any changes, a corporation may present an amended shelf registration statement, and an amended statement may be ordered by the SEC when deemed necessary. Expected issuing price and issuing period, however, may not be changed.

If a subscriber or purchaser of the offered securities suffers monetary damages due to the issuer's submission of false information or the omission of material information required in the registration statement, the corporate executives at the time of filing the registration statements or any person who has prepared or delivered the prospectus is liable for such damages.

After a registration statement becomes effective, a prospectus must be prepared and made available to the public. The prospectus must contain the same information and be consistent with the registration statement.⁵⁴

B. Disclosure in the Trading Market

1. Periodic Reports

Pursuant to the SEA, a listed company must file a semi-annual report with the SEC and the KSE within 45 days after the end of the first half of the business year and an annual report within 90 days following the end of each fiscal year.⁵⁵ These reports must contain a general description of the corporation, a description of its business operations, matters relating to its financial position, and an audit by a certified public accountant ("CPA"). The SEC and the KSE is required to make these reports available to the public for two years.

In cases where a listed corporation is a controlling company of a subsidiary, it must file consolidated financial statements and an audit report on the statements issued by a CPA with the SEC and the KSE. A "controlling company" includes owners of 50% or more of the total

54. SEA, *supra* note 7, art. 12.

55. *Id.* arts. 92-93.

number of shares issued by a subsidiary or shareholders with a plurality of 30% or more of the shares of a subsidiary.

2. Timely Disclosure of Material Information

The SEA requires listed corporations to make full and prompt disclosure of important corporate developments.⁵⁶ A listed company should publicly disclose important corporate actions or events stipulated in the SEA to the SEC and the KSE without delay (i.e., within one day of the event's occurrence). Such events include the suspension of trading with a bank, suspension of business activities, the filing of an important lawsuit regarding the listed securities, the sale or acquisition of the entire or a substantial part of the business, merger or consolidation,⁵⁷ the occurrence of events leading to dissolution, and the occurrence of any event significantly influencing corporate management.

In addition, the SEA empowers the KSE to request a listed company to clarify rumors or news about the company.⁵⁸ Response to such a request is mandatory. In cases where the shares of the company show a significant change in price or trading volume, the KSE may also request a company to disclose whether or not there exist any material information not made public. In fact, failure to disclose material information is a violation in itself. If a listed company fails to fulfill the disclosure requirements, the KSE may notify the SEC of the fact.⁵⁹ The SEC, in turn, may place restrictions on the issuance of securities by the corporation and recommend that the corporation remove the officer responsible for the insufficient disclosure procedures.⁶⁰

56. *Id.* art. 186.

57. In the case of mergers or consolidations, listed corporations are required to make public disclosure at the moment of the formation of the relevant contract. However, the KSE may demand confirmation of any rumor or news of an impending merger. In these circumstances, the listed company has the obligation of confirming or denying such rumors, and more concrete information should be disclosed at the moment of certainty.

58. SEA, *supra* note 7, art. 186(2).

59. *Id.* art. 186(3).

60. *Id.* art. 193.

V. TRADING OF SECURITIES

A. Exchange Market Trading

As indicated previously, the KSE is the only stock exchange allowed by the SEA. Providing stipulations on the systems of membership, listing, trading and settlement, the SEA states that only the KSE may open a securities market in order to create a centralized and continuous market.⁶¹

The SEA stipulates that a member of the KSE must satisfy requirements provided in the Charter of the KSE⁶² and make contributions to the KSE⁶³ and that no one other than a member of the KSE can trade in the securities market.⁶⁴ The SEA ensures the public function of the KSE by stipulating that the chairman of the KSE must be elected from among those people with experience, knowledge, and integrity by a general meeting of KSE members, with the subsequent approval of MOFE.⁶⁵

Generally, a company listing is made by application. In certain cases, however, MOFE may order a company to list its shares.⁶⁶ Listing securities requires approval by the SEC.⁶⁷ The law emphasizes the public interest and investor protection in approving listings, and it delegates concrete criteria

61. *Id.* art. 76.

62. Article 28 of the SEA stipulates that a KSE member must be a securities company licensed to conduct brokerage or dealing activities under art. 28 (2). However, banks, trust companies, short-term financing companies, general financing companies, and insurance companies which are allowed to carry out securities-related businesses under SEA art. 29 are excluded.

63. These contributions totaled approximately 15.5 billion won as of the end of June, 1996.

64. SEA, *supra* note 7, art. 86.

65. *Id.* art. 78.

66. The policy behind this provision has been scrapped, and it is now a dead provision. This compulsory order system was established to help foster the Korean securities market during the early years of Korean securities market when there were very few companies listed on the KSE. However, it has not been enforced at all over the past 20 years.

67. SEA, *supra* note 7, art. 88.

to regulations of the KSE.⁶⁸ The listing regulations must be reviewed by the SEC and authorized by MOFE.

The SEA empowers the KSE to promulgate 'Entrustment Contract Rules' which require members to enter contracts with clients when opening accounts.⁶⁹ The contents of the contracts must include matters relating to the establishment of an account, procedures for placing orders, settlement procedures and procedures for payments of good faith deposits and brokerage commissions.

The SEA prohibits a securities company from receiving orders in places other than the company's head office, branch offices, and other business posts.⁷⁰ Moreover, securities companies are required to process customers' orders through the KSE market unless asked not to do so by the customer. In addition, securities companies may not act concurrently as a principal and as a broker, an intermediary or an agent for another party with respect to the same transaction. For the trading of securities in the exchange market, however, securities companies can compete with other sellers or buyers, as there are a majority of unspecified investors. Article 111 of the SEA prohibits stop orders.⁷¹

68. The main criteria for listing securities under the KSE 'Securities Listing Regulations' are as follows:

1. Five years having passed since the foundation of the corporation.
2. Initial paid-in capital greater than three billion won, equity capital greater than five billion won, and more than 300,000 total outstanding shares.
3. Average revenue greater than 15 billion won during the three most recent fiscal years and revenue greater than 20 billion won during the latest fiscal year.
4. The corporation must have issued and floated stock within the most recent year. The total number of issued and floated shares and shares with voting rights must be greater than 10 million shares, and each must be greater than 30 percent of total number of shares or 10 percent of total number of shares with voting rights, respectively, at the time of the application for listing securities.
5. The following requirements related to the operation of business must be satisfied: 1) debt ratio of the latest fiscal year of less than 150% of the average debt ratio in same business; 2) operating profits, ordinary profits, and quarterly profits during the past three most recent fiscal years; 3) no capital encroachment; and 4) the value of assets and profits must be 150 percent and 100 percent of the stock par value, respectively.
6. The auditor's opinions in the audit reports of the financial statements of the most recent three years must have been without irregularities.
7. The corporation must not have defaulted or been involved in any controversial incidents such as a lawsuit having significant effect on the corporation's management within the past year.

69. SEA, *supra* note 7, art. 110.

70. *Id.* art. 109.

71. A "stop order" is an instruction to purchase stocks when their price increases above a point designated by the customer and to sell those stocks when the price falls below a designated point.

The SEA mandates that the KSE create operating rules that stipulate trading units, trading hours, settlement methods⁷² and deadlines.⁷³ The KSE is legally responsible for the settlement of transactions at the KSE market. Thus, settlements executed exclusively by the two parties to a transaction (i.e. between seller and buyer), have been invalidated because such settlements were not executed through the settlement mechanism of the KSE. The KSE must be the intermediate party of each transaction for such a settlement to be valid.

Under the SEA, members are required to deposit with the KSE a specified ratio of their respective trading value as a joint compensation fund to compensate for losses incurred by the default of a member.⁷⁴ The fund is managed by the KSE and used to make up losses if a member defaults, and the losses are later billed to the defaulting member. The amount of the deposit for the fund is determined by the KSE depending on the type of traded securities, up to an amount equal to 1/100,000 of sales value per transaction. In addition, the KSE has the highest priority for any receivables from a member to any other creditors. Clients are also entitled to priority over other unsecured creditors in cases where the receivables arise from the default of the member concerned. However, such clients are not entitled to priority over secured creditors whose debts are by rental rights or pledge rights (mortgage rights).

B. *Off Exchange Trading (OTC Trading)*⁷⁵

According to the 1976 revision of the SEA, the SEC provides regulations on methods of trading, settlement and other matters for OTC trading.⁷⁶ OTC Trading in Korea is conducted through a securities company called KOSDAQ, a subsidiary of the Korean Securities Dealers Association. Trading and transfer of market data such as current and offered prices are conveyed over computer networks.

72. Settlements of trading made on in the KSE market are executed through the KSD acting under contract as the settlement organ. The concept of settlements includes both clearing and settlement procedures.

73. SEA, *supra* note 7, art. 94.

74. *Id.* art. 95. *See also* SEA, *supra* note 7, art. 97; Enforcement Decree, *supra* note 21, arts. 48-51, 55-56.

75. Off Exchange Trading (OTC Trading) in Korea is equivalent to over-the-counter trading in the United States.

76. SEA, *supra* note 7, art. 194.

C. *Stock Index Futures Trading*

To prepare for the regulation of the stock index futures trading introduced in 1996 by the KSE, the SEA was revised in 1994 to include the securities indices and securities index futures transactions under the category of securities and securities transactions, respectively.⁷⁷ In addition, provisions on the licensing of futures businesses and futures advisory businesses, the futures trading reserve, and the deposit of a joint compensation fund for futures trading were added in the SEA.

In November 1995, the Futures Trading Act (FTA)⁷⁸ was enacted to regulate all kinds of futures trading on commodities and financial products. However, in order to avoid the incongruity of two different laws regulating futures trading on stocks and stock indices, the FTA exempts these from regulation until such exemption is removed by presidential decree. Furthermore, there was a jurisdictional dispute in Korea concerning futures trading similar to the dispute between the SEC and the Commodity Futures Trading Commission in the United States. The exemption can be seen as a result of the compromise between competing bodies.

VI. REGULATIONS ON UNFAIR TRANSACTIONS

A. *Insider Trading*

Insiders, including officers, employees or major shareholders of listed or registered corporations must comply with strict restrictions when trading in shares of their corporation. Insiders are largely subject to three kinds of regulations on trading securities issued by their corporations: prohibitions on capitalizing on insider information, restitution of profits from short-term trading, and prohibitions on short selling.

The purpose of regulating insider trading is not to prohibit insiders from trading securities but to protect public investors and to secure an effective corporate disclosure system. This policy enables common investors to trade in the securities market with equitable access to information by forcing insiders to disclose inside information. In the United States, the principle of "disclose or abstain" was created by its case law. Korea has neither law nor precedent which clearly formulates a

77. *Id.* art. 2-2, inserted by Law No. 4701, Jan. 1, 1994.

78. Futures Trading Act, Resolution of Standing Session of the National Assembly, (Dec. 1995).

similar legal principle, but the general purpose sought by the U.S. principle underlies all Korean regulations on insider trading.

The concept of "insider" pertains not only to officers, employees and major shareholders of a registered or a listed corporation but also to quasi-insiders and tippees such as officers and employees of regulatory organizations, CPAs, or lawyers. Quasi-insiders are defined as those who have access to inside information of the corporation by means of contracts, agency relations, or by nature of their position, etc.⁷⁹ This concept appears to be equivalent to the concept of a "constructive insider" under U.S. corporation laws. Under the SEA, insiders are defined as follows:

- (1) officers, employees and agents of the corporation;
- (2) major stockholders⁸⁰ of the corporation;
- (3) persons who are authorized to grant any permission or approval, to give any direction or any control or other competence, with respect to the corporation;
- (4) persons who have entered into contracts with the corporation; and
- (5) agents and other employees of a person falling under any of items (2) to (4) above.

1. Prohibition on Capitalizing Inside Information

Any insider who is informed of important information⁸¹ affecting a corporation not available to the public in the course of performing his/her duties is prohibited from using that information or allowing any other person to use that information in trading securities issued by the affected corporation.⁸² If the insider violates this restriction, she or he shall be imprisoned for not more than three years or fined not more than twenty million won; provided, however, that if the amount equivalent to three times the profit gained or the loss evaded by the offense exceeds twenty

79. SEA, *supra* note 7, art. 188-2.

80. A "major shareholder" is any person who beneficially owns more than 10 percent of the total issues of the corporation. *Id.* art. 188(1).

81. "Important information" refers to information which may affect an investor's decision to invest, including things such as the new issuance of equity, default, planned mergers or acquisitions, and natural disasters. *Id.* art. 188-2(2).

82. *Id.* art. 188-2.

million won, the insider shall be punished by a fine not exceeding an amount equivalent to three times the amount of profit or loss.⁸³

Furthermore, the insider shall be liable civilly for the damage suffered by his/her counterpart as a result of such transaction.⁸⁴ On the other hand, if the alleged offender can prove that he did not gain any profits by using confidential information acquired through the insider's work or position, then he cannot be held liable. No other defense principles which could be used by alleged offenders have been developed. There have been significant difficulties in criminally prosecuting insider traders because of the difficulties in proving violations of such laws. Recently, however, the number of prosecutions of insider trading have gradually increased due to investigations conducted by the KSE and the SSB.

2. Restitution of profits from short-term trading

If any officer, employee or major shareholder of a listed or registered corporation profits from selling or purchasing shares of the corporation within six months after purchasing or selling the shares, the corporation or the SEC may demand the tendering of those profits to the corporation.⁸⁵ The SEC and the corporation have standing to bring a claim for restitution of profits from the trading within two years from the date on which such profits were realized. Restitution goes directly to the corporation rather than to individual shareholders, so that in this way all the shareholders of the corporation will profit.

Practically speaking, there have been no attempts to find people who have been damaged by short-swing trading in Korea, since it is almost impossible to find them in the Korean securities market situation. Under Korean laws, claimants must prove that insiders made profits by using inside information. However, U.S. laws do not ask whether, once insiders have profited from short-swing trading, the trading was done on the basis of inside information or not. If the corporation does not exercise its claim against short swing trading, other shareholders can exercise the claim on behalf of the corporation.

3. Prohibition on short selling

83. *Id.* art. 208.

84. *Id.* art. 188-3.

85. *Id.* art. 188(2).

No officer, employee or major shareholder of a listed or registered corporation may sell stocks, convertible bonds, or bonds with stock purchase warrants of the corporation without owning those securities.⁸⁶ Offenders may be confined to penal servitude for up to two years, or fined up to ten million won.⁸⁷

B. Manipulation of Prices and Trading Volume

Manipulation of price and trading volume to gain profit is considered a crime because it undermines the fairness and the trading rules of the securities market. Price pegging by underwriters in issuing new shares is, however, regarded as an exception. Price pegging is conceptually similar to price stabilization. Under Korean laws, price pegging is an illegal activity, but price stabilization is legal to the extent that it is intended to assist in the process of issuing and selling securities for a certain period of time. The SEA stipulates that no person shall engage in the following acts to create a false or misleading appearance of active transactions or cause any other person to make false judgments with respect to transactions of listed securities:⁸⁸

- (1) making a purchase or sale by prior arrangement with another person for that person to purchase or to sell the securities concerned at the same time and the same price of his purchase or sale;
- (2) effecting any wash sale without intent to transfer ownership of securities;
- (3) effecting, entrusting or being entrusted with, alone or in conspiracy with other persons, transactions of securities which create a false or misleading appearance of active trading or which cause the fluctuation of securities prices;
- (4) circulating a rumor to the effect that the price of securities will fluctuate as a result of manipulation by himself or by other persons;
- (5) making false or misleading representations intentionally with respect to any material fact regarding transactions in the securities concerned;

86. *Id.* art. 188(1).

87. *Id.* art. 209.

88. *Id.* art. 105.

- (6) intentionally circulating false price quotations or facts or other rumors, or deceiving for the purpose of obtaining unjust benefits;
- (7) acquiring money or other benefits with property value by causing others to misunderstand by means of a document containing false representations of material facts or omitting material facts; or
- (8) making use of any non-public information on specific securities obtained through his duties or position, or making that information available to others.

Any person who manipulates the price of securities shall be confined to penal servitude for not more than three years or fined not more than twenty million won⁸⁹ and be liable to compensate for the damages suffered by a person due to the manipulated price.⁹⁰ However, a claimant must prove that 1) price pegging activities took place; 2) the prices of securities were affected by price pegging activities; 3) trading took place on the basis of the affected price; and 4) the claimant was damaged by the trade.⁹¹ Most price pegging is achieved when several people (or sometimes several branch offices of a company) conspire to submit purchase orders for securities to an extent that such orders have a heavy impact on the market price of such securities, or with the occurrence of a concentrated purchase of securities vulnerable to price manipulation because of the relatively small volume of such listed securities.

C. *Mutual Shareholding*

The Commercial Code prohibits subsidiaries (of which at least 40% of equity is held by the parent company) from holding shares in their parent company in order to keep capital reserves at a satisfactory level and to prevent corporate governance without capital contribution.⁹² The Monopoly Regulation and Fair Trade Act⁹³ permits corporations which are part of conglomerates to hold shares mutually within 40% of their asset value through intermediary corporations. However, the SEA allows listed corporations to hold shares mutually up to 1% of the total outstanding

89. *Id.* art. 208.

90. *Id.* art. 106.

91. MOFE Ministerial Decree.

92. Commercial Code, *supra* note 10, art. 342-2.

93. Law No. 4198, Jan. 13, 1990 (as amended Dec. 32, 1994), *supra* note 18.

shares of other corporations.⁹⁴ The policy rationale behind this restriction is that mutual shareholding is very likely to be used for increasing the concentration of economic power, controlling companies without legitimate assets or capital, improperly distributing unregistered securities to the public through the mechanism of indirect holding, or increasing the possibility that inside information will be appropriated.

Under the SEA, except in cases otherwise prescribed by the Enforcement Decree, listed corporations shall not cause, pursuant to an agreement, any other listed corporation to own shares issued by itself while the listed corporation owns shares of such other listed corporations.⁹⁵ Mutual shareholdings between unlisted corporations or between a listed corporation and an unlisted corporation are not subject to this restriction. Mutual shareholding is permitted in cases where financial institutions, such as securities companies and banks that engage in securities business, acquire shares of other listed corporations for transaction purposes or in cases where the amount of shares held in mutual ownership is not more than one percent of the total outstanding shares.⁹⁶

Any person who violates the prohibitions on mutual shareholding may be confined to penal servitude for up to two years, or fined up to ten million won.⁹⁷

VII. MANAGEMENT PROTECTION OF LISTED CORPORATIONS

A. *Reporting on Block Ownership of Shares ('Five Percent' Rule)*

Reporting requirements for block shareholdings are designed to improve market transparency by disclosing both large shareholdings and changes of share ownership. Under the SEA, when a person⁹³ in conjunction with other shareholders owns through a special relationship⁹⁹ more than five percent of the total outstanding voting shares of a listed corporation, or when the aggregate shareholding ratio changes by one

94. SEA, *supra* note 7, art. 189; Enforcement Decree, *supra* note 21, art. 84.

95. SEA, *supra* note 7, art. 189.

96. Enforcement Decree, *supra* note 21, art. 84.

97. SEA, *supra* note 7, art. 190.

98. Under the SEA, a "person" includes not only a natural person but also an incorporated entity.

99. "Special relationships" include relations with spouses, immediate family members, corporations for which 35% or more of its shares are owned by the person, corporations which own 35% or more shares of the person, and corporations belonging to conglomerates as defined by the Monopoly Regulation and Fair Trade Act. Enforcement Decree, *supra* note 21, art. 86-2.

percent or more, that person must report the contents of the acquisition or change to the SEC and the KSE within five days after such event occurs.¹⁰⁰

Exemptions apply to this reporting requirement in cases where: 1) the ratio changes without a change in the number of shares, 2) the share ownership changes through an acquisition of shares through an exercise of shareholders' rights, and 3) the SEC deems it unnecessary to disclose the contents of changes in shareholding.¹⁰¹ The third case above usually arises when non-voting preferred stocks are entitled to voting rights because the surrounding circumstances make it impossible to distribute dividends to such preferred stock owners.

If a person holding five percent or more of voting shares fails to fulfill the reporting requirement, the offender is subject to imprisonment of one year or less or a fine of five million won.¹⁰²

B. Tender Offers

Tender offers rarely occur in Korea because they are regarded to be outside the norms of social and cultural tradition. There have been only five tender offers since 1994, despite the introduction of the tender offer provision in the 1976 revision of the SEA that permits this practice.¹⁰³ Tender offers were not allowed before 1977 because the public had a negative image of tender offers. Additionally, the founder-owners of Korean corporations were regarded highly with respect to their establishment and management of corporations, to such an extent that the public did not want these corporations to be taken over by others. After 1977, the government started allowing tender offers because they recognized the efficiencies of tender offers in foreign markets and started regarding the tender offer mechanism as a tool to motivate South Korean corporations to manage themselves more effectively.

In order to buy securities through an offer to purchase or through a solicitation of an offer to sell securities outside the securities market as against many and unspecified persons, an effective tender offer registration statement must be filed with the SEC.¹⁰⁴ Stock certificates, warrants, and

100. SEA, *supra* note 7, art. 200-2. A less stringent deadline is applied to financial institutions, designated institutional investors, similar institutions recognized by MOFE, and corporations belonging to a conglomerate. They must report shareholding statements by the tenth of each month. Enforcement Decree, *supra* note 21, art. 86-7.

101. *Id.* art. 86-5.

102. SEA, *supra* note 7, art. 210.

103. *Id.* art. 21.

104. *Id.* art. 21(1).

convertible bonds issued by listed corporations or registered corporations are subject to tender offer registration requirements.¹⁰⁵

A person who intends to purchase securities through a tender offer must file a tender offer registration statement with the SEC through a securities company acting as an agent.¹⁰⁶ The registration takes effect ten days after the receipt of the statement by the SEC.¹⁰⁷

A tender offeror must send a copy of the tender offer statement to the issuer of the securities before the statement is to take effect.¹⁰⁸ When a tender offer statement has taken effect, the tender offeror must, without delay, give public notification to at least two daily newspapers.¹⁰⁹ If the securities concerned have been listed on the KSE market, the tender offeror must submit a copy of the statement to the KSE.¹¹⁰ Any tender offeror must prepare a written explanation regarding the tender offer.¹¹¹

A person making a tender offer without filing the registration statement or buying the securities other than by the tender offer during a tender offer period may be punished by imprisonment for not more than two years or a fine not exceeding ten million won.¹¹² Any tender offeror who presents a material misstatement¹¹³ in the registration may be punished by imprisonment for not more than one year or a fine not exceeding five million won.¹¹⁴

C. Restrictions on Proxy Solicitation

The Commercial Code allows shareholders to exercise their voting power through proxy.¹¹⁵ The SEA incorporated detailed regulations on the proxy solicitation for better disclosure of corporate actions in 1976.¹¹⁶ A proxy is mostly used by the corporations for the purpose of meeting quorum requirements for general meetings of shareholders. Proxy solicitation for public corporations designated by Enforcement Decree can

105. Enforcement Decree, *supra* note 21, art. 10.

106. *Id.* art. 11.

107. SEA, *supra* note 7, art. 21(3).

108. *Id.* art. 22(1).

109. *Id.* art. 22(2).

110. *Id.*

111. *Id.* art. 24.

112. *Id.* art. 209.

113. In this context, a "material misstatement" refers to falsely stated information which may significantly influence the decision-making of the investors concerned.

114. SEA, *supra* note 7, art. 210.

115. Commercial Code, *supra* note 10, art. 368(3).

116. SEA, *supra* note 7, art. 199.

only be carried out by the public corporation concerned, and its solicitees must be shareholders with voting rights.¹¹⁷

Solicitors must make solicitations through a letter of commission, copies of which must be filed with the SSB, on which solicitees can respond by approving or disapproving each item of the agenda of a general meeting of shareholders, and provide reference materials designated by the SEC for solicitees.¹¹⁸ For example, management or shareholders who want to proceed with proxy solicitations are obligated to use proxy statements where other shareholder solicitees can indicate “yes” or “no” to all issues of the general meeting. In addition, they should provide relevant materials required by the SEC. The proxy statements and relevant materials should be filed with the SEC. Misstatements, ambiguous statements, and omission of material information in such documents are not allowed. These examples could constitute violations of relevant laws or regulations which prohibit any “material misstatement or omission” in the proxy solicitation process. If a proxy solicitation is made in violation of relevant regulations, the responsible person may be punished with imprisonment for up to two years or a fine of ten million won.¹¹⁹

D. Restrictions on Acquisition of Treasury Stock

With a few exceptions, the Commercial Code prohibits corporations from purchasing their own shares.¹²⁰ The SEA, however, allows listed corporations to reacquire their stocks to protect themselves from hostile takeovers.¹²¹ Listed corporations may reacquire their own shares under their own names and accounts through the stock exchange market. The reacquisition must be made for less than ten percent of the total outstanding shares or within certain balance sheet tests calculated by methods set by the SEC, whichever is less.¹²² When the ratio of treasury shares exceeds ten percent due to a reduction of capital or other reasons, the shares beyond the limit must be disposed of within three years.¹²³

Where a resolution or a decision is made on the acquisition or disposal of treasury shares by the board of directors, the president, or other person designated by the Enforcement Decree, the corporation must,

117. *Id.* art. 199(2).

118. Enforcement Decree, *supra* note 21, art. 85.

119. SEA, *supra* note 7, art. 209.

120. Commercial Code, *supra* note 10, art. 341.

121. SEA, *supra* note 7, art. 189-2.

122. *Id.* art. 189-2(1).

123. *Id.* art. 189-2(3).

without delay, notify the SEC and the KSE of the fact thereof.¹²⁴ Any person violating such rules may be punished by imprisonment for not more than two years, or a fine not exceeding ten million won.¹²⁵

E. Restrictions on Block Ownership of Shares

In order to protect the founder's interest of a corporation, the SEA provides that no one shall own, beneficially under any name, shares issued by a listed corporation or a designated public corporation in excess of the ratio prescribed by law.¹²⁶ This provision was introduced to develop the securities market at the initial stage by encouraging founders of corporations to sell their shares to the public without the risk of losing control of their corporations. After January 1, 1997, however, the provision will no longer be applied to listed corporations.¹²⁷

The shareholding limit is applied only to shares with voting rights of listed corporations and designated public corporations.¹²⁸ The limits applied to listed corporations are: 1) the ratio of major shareholders' holdings at the time of listing, and 2) ten percent for all other shareholders. In cases where a major shareholder transfers part of his share holdings, the reduced ratio is thereby applied for him. For a corporation designated by MOFE as a "public corporation," the limits are 1) the ratio of major shareholders' holdings at the time of registration, and 2) the ratio, within three percent, for others prescribed in the public corporation's articles of incorporation.

Shareholdings exceeding the above limits are legal if they are the result of a tender offer, a direct purchase from a major shareholder, a purchase from the government, a government controlled corporation, or a foreigner, or any other purchases approved by the SEC.¹²⁹

Shareholders owning shares in excess of the limit determined by law may not exercise voting rights on the shares over the limit, and the SEC may order such shareholders to sell their shares so as to comply with the

124. *Id.* art. 189-2(2).

125. *Id.* art. 209.

126. *Id.* art. 200.

127. This decision was made according to a government policy that major shareholders should protect the company's management and that the management should be carried out so that the interests of the founding shareholders (who typically are the major shareholders), general shareholders, and the company should be in harmony.

128. SEA, *supra* note 7, art. 200(1).

129. *Id.* art. 200(2).

limit.¹³⁰ Shareholders who violate this limit are subject to a fine of up to five million won, and in cases of noncompliance with SEC orders, penalties are imprisonment for up to two years or up to a ten million won fine.¹³¹

VIII. INTERNATIONALIZATION OF KOREAN SECURITIES MARKET

Foreign portfolio investment is regulated by two laws, the SEA and the Foreign Exchange Management Act ("FEMA").¹³² The SEA provisions deal with the licensing of foreign securities firms that operate in Korea and set limits on securities investment by foreign investors. The FEMA stipulates matters and procedures related to inflow and outflow of foreign exchange.

In order to cope with the rapidly changing global financial environment, the Korean government has continuously pursued the opening of the securities market since the early 1980s. In opening the market, the government took a gradual, step-by-step approach to minimize the possible adverse effects of the liberalization policy on the economy and securities market. The gradual implementation of the liberalization plans resulted in a more open and transparent securities market with improved efficiency and stability of securities market transactions. Encouraged by these developments, the government is now accelerating the pace of financial reforms to develop Korea's securities market as a fully-open and self-regulated market.

A. *Foreign Investment in Korean Securities Markets*

1. Foreign Entry into the Securities Industry

Foreign securities companies can take part in the Korean securities industry by establishing a branch, a joint venture, or a local subsidiary in Korea. Under the SEA, foreign securities companies must be licensed by MOFE if they intend to engage in securities business in Korea.¹³³ If a foreign securities firm plans to establish a representative office to enter the

130. *Id.* art. 200(3).

131. *Id.* arts. 209, 210.

132. Foreign Exchange Management Act of Dec. 31, 1961, Law No. 933 (as wholly amended by Law No. 4447, Dec. 27, 1991).

133. SEA, *supra* note 1, art. 28 (1)-(2).

Korean securities market during the preparatory stage, it should report to MOFE in advance.

Once a foreign securities company's application for local securities business has been filed, MOFE examines the application according to such criteria as international credibility, capital requirements¹³⁴ and reciprocity.¹³⁵ MOFE then may issue a license which authorizes the line of securities business. Once a foreign securities company is granted a license for business, it is subject to the same regulations that govern Korean securities companies. Aside from these regulations, foreign securities companies¹³⁶ are subject to additional regulations which require them to maintain assets within Korea equivalent to its working capital needs plus debt, and to make up any shortfall which occurs.¹³⁷

The SEA provides that a foreign branch or other business office that goes bankrupt must use its local assets primarily to pay any liabilities generated by its securities transactions with domestic counterparts.¹³⁸ If a foreign securities company is deemed unfit to do business for violating local or foreign laws, it can be punished through various measures, including the cancellation of its securities business license or suspension of business.¹³⁹

2. Investment Ceilings for Foreigners With Respect to Stocks and Bonds

The Enforcement Decree provides the definition of foreigners or foreign corporations which are subject to a limitation on securities purchases as follows:¹⁴⁰

134. In determining whether to grant a license to a foreign securities company to engage in the securities business, MOFE will consider the applicant's financial condition and profitability, the composition of the company, and the status of securities trading and other economic conditions of the area. *Id.* art. 32.

135. Enforcement Decree, *supra* note 21, art. 17-2.

136. The number of foreign securities firm branches is 19 and the number of other business offices is 18 (as of July, 1996). The number of foreign investors registered is 4,691. Among them, the number of individual investors is 1,655 and that of institutional investors is 3,036 (as of May 1996). As for the inflow and outflow of foreign investment money (per million dollars unit, between 1992 and May 1996), the inflow is 35,422, outflow is 20,699 and the net flow is 14,723.

137. The SEA regulates securities companies' asset management by setting maximum debt-net asset ratios and maximum reserve requirements in proportion to the trading volume of securities. SEA, *supra* note 7, art. 39-40.

138. *Id.* art. 28-2(3).

139. *Id.* art. 57(1).

140. Enforcement Decree, *supra* note 21, art. 87-2.

- (i) individuals of a foreign nationality;
- (ii) corporations established by foreign law;
- (iii) international organizations designated by the SEC;
- (iv) persons designated by the SEC who are similar to those described in items (i) to (iii); and
- (v) corporations established under Korean law and virtually controlled by, or with more than half of its shares owned by persons described in items (i) to (iv).

Resident foreigners¹⁴¹ or foreign corporations that meet the criteria set by the SEC are treated the same as Korean nationals.¹⁴² The SEC is authorized by the SEA to regulate investment ceilings, investment procedure, and trading methods by establishing regulations for securities trading by foreigners.¹⁴³

With respect to trading in securities, foreigners are allowed to buy only KSE-listed shares, and trading must take place on the exchange except in exceptional cases stipulated by SEC rules. Foreign investors who have bought shares in excess of the ceiling cannot exercise voting rights for the excess shares and are required to sell the excess amount within three months of the purchase date.¹⁴⁴

Up through 1991, foreign investment in domestic securities could be made indirectly in the form of beneficiary certificates ("BCs") established for foreigners and country funds such as Korea Funds. In January 1992, foreigners were allowed within established levels to make direct investments in the Korean stock market. Initially, foreign investment was permitted in listed domestic stocks, subject to an aggregate ceiling of 10 percent of the total outstanding shares of the corporation and a ceiling of 3 percent for each individual foreign investor. Since the opening of the stock market in 1992, more than 4,000 foreigners from 55 countries have invested in Korean stocks, and net capital inflow of foreign investment was recorded at over US\$15.1 billion by the end of June 1996.

141. The term "resident" means any individual having his/her domicile or residence in the Republic of Korea, or a legal entity the principal office of which is located in the Republic of Korea. Foreign Exchange Management Act, *supra* note 133, art. 3(1), item 12.

142. SEA, *supra* note 7, arts. 17-2(1)(2), 33-34.

143. *Id.* art. 118(1).

144. *Id.* art. 203; Enforcement Decree, *supra* note 21, art. 87-2.

In order to accelerate the opening of the stock market, the government raised the aggregate foreign investment ceiling¹⁴⁵ to 12 percent in December 1994, and again to 15 percent in July 1995. The investment ceiling was further raised on April 1, 1996.¹⁴⁶ The aggregate foreign share ownership for corporations was raised to 18 percent, and 12 percent for designated public corporations. The individual ceiling of 3 percent was raised to 4 percent. By the end of 1996, those ceilings were to be further raised from 18 percent to 20 percent for general corporations, 12 percent to 15 percent for designated corporations, and 4 percent to 5 percent for individual ceilings. In 1999, the individual ceiling will be raised to 10%. The aggregate foreign investment ceiling will be raised to 23%, 26% and 29% during 1997, 1998 and 1999, respectively. And the aggregate ceiling is being reviewed for further increase or abolishment by 2000.¹⁴⁷

The government will allow foreign investment in unlisted stocks during 1996 by permitting country funds to include it in their portfolios. The limit on issuance of BCs for foreign investment funds will be raised in 1996 and deregulated in 1997-98. The "foreigner-only beneficiary certificate"¹⁴⁸ is a type of international investment trust which operates essentially the same as a domestic BC. Domestic investment trust companies take charge of operating the BCs and foreign investors get the investment profit. In other words, the "foreigner-only BC" is a means of indirect investment through the use of BCs as opposed to directly investing in domestic stocks and bonds.¹⁴⁹ Matching funds are facilitated by selling BCs to domestic and foreign investors, with the right of repurchase being restricted for a period of time. The investment coverage of the fund includes domestically listed stocks and overseas listed stocks, and bonds.¹⁵⁰

Regarding "bond investments," foreign investors may purchase convertible bonds ("CBs") issued by small or medium-sized companies and public bonds with low interest and long-term maturity designated by the

145. The limit of domestic securities foreign investors may acquire shall be as prescribed in the Securities Exchange Act and its regulations. Foreign Exchange Management Regulations of MOFE, regulation No. 94-9, May 20, 1994, art. 10-61(1).

146. Press release of MOFE, March 1995.

147. Press release of MOFE, October 7, 1996.

148. See Foreign Exchange Management Regulations, *supra* note 146, art. 10-69(1)-(3).

149. There are 59 international BCs which are issued in favor of nonresidents (including foreigners) in which the issued fund is operated in Korea. Among them, 25 BCs are operated by Hanguk Investment Trust Company, 19 BCs by Daehan Investment Trust Company, and 15 BCs by Kookmin Investment Trust Company.

150. Currently there are three matching funds issued in favor of residents and nonresidents in which the issuing fund is operated in Korea and overseas, operated by the companies listed in note 149 *supra*. Issuance is US\$ 100 million per matching fund.

SEC. In the case of listed bonds, foreigners may only trade these on the stock market. In July 1994, the bond market was opened to foreigners through CBs issued by small and medium-sized companies. Each foreign investor may purchase up to 5 percent of each issue of CBs. The aggregate foreign ownership for such CBs is limited to 30 percent. Foreign investors who hold bonds in excess of the ceiling must sell the excess amount within three months from the purchase date.¹⁵¹ Foreigners are also allowed to subscribe to government and public bonds in the primary market with interest rates comparable to international rates.

Since May 1995, foreigners have been able to invest indirectly in domestic bonds by purchasing foreigner-only BCs issued by domestic investment trust companies. In April 1996, the issuance limit on foreigner-only BCs for bond investments was raised. The foreign investment limit on CBs issued by small and medium-sized firms was increased from thirty percent to fifty percent of aggregate investment amount, and from five percent to ten percent for individual investors. In addition, small and medium-sized firms may issue non-guaranteed bonds strictly for foreigners.

In 1997, foreigners will be allowed to invest directly in all non-guaranteed long-term bonds issued by small and medium-sized firms. The issuance limit on the foreigner-only BCs for bond investments will be raised further or liberalized after 1997.¹⁵² In December 1997, non-guaranteed long-term bonds over five years issued by small and medium-sized firms will be liberalized and in December 1998, non-guaranteed long-term CBs issued by large firms will be deregulated. Finally, in December 1999, non-guaranteed long-term bonds over five years issued by large firms will also be deregulated.

According to SEC rules, foreigners must register under their real names in order to invest in the Korean securities market. While the rules do not require foreigners to designate a standing proxy, non-resident foreigners are strongly recommended to have a standing proxy to ensure that their investment related activities are carried out in a timely manner. Foreign investors must appoint a custodian because securities certificates are required to be kept in the custody of an eligible custodian in Korea. Only foreign exchange banks, securities firms, and the Korea Securities Depository are eligible to be custodians for the safekeeping of shares for foreigners. The SEC rules provide that foreigners must trade stocks through

151. SEA, *supra* note 7, art. 203(3); Enforcement Decree, *supra* note 21, art. 61(2).

152. Press release of the MOFE, March 1996.

the KSE market; although, in the case of odd lot trading, inheritances, gifts, and exercise of warrants, OTC trading is permitted.

B. Offerings and Sales of Foreign Securities in Korea

According to Korea's plan for the liberalization of capital markets, the issuance of domestic bonds by foreigners has already been achieved. As of May 1, 1995, the issuance of domestic won-denominated bonds by international institutions was permitted, and the Asian Development Bank (ADB) issued the first won-denominated bond worth US\$ 100 million (roughly 80 billion won) on September 1, 1995. The Korean government has announced that public offerings of shares issued by foreign corporations will be allowed from 1996. Because of the high level of domestic interest rates¹⁵³ and some restrictions on the use of money procured in the domestic market, no foreign companies may offer and sell its stocks in the Korean domestic market at this time.

The formation of a secondary market for foreign bonds will contribute to the internationalization and advancement of the Korean domestic bond market. The encouragement of capital outflow will neutralize the capital inflow stemming from the opening of the stock market. The issuance of won-denominated bonds by foreigners will also upgrade the worldwide reputation of the won currency and will allow the internationalization of the won currency to proceed.

From July 1, 1996, the issuance of won-denominated bonds by foreigners was deregulated.¹⁵⁴ The class of issuers, which had been limited to international institutions, was expanded to include foreign governments, public institutions, financial institutions, companies, and international institutions. The requirements for a credit rating was lowered from an "above A" ranking to an "above BBB" ranking. The leading managing securities companies now sell won-denominated bonds issued by foreigners to domestic and foreign investors at different prices. Portions for

153. The interest rates in the Korean financial market for 1994 and 1995 were as follows:
Call Rate 12.3% (as of the end of 1994)
 12.5% (as of June 1995)

Corporate bonds 12.9% (as of the end of 1994)
 14.7% (as of June 1995)

Han'guk Kyôngje [Korean Economy], 1996, at 22.

154. Press release of MOFE, May 31, 1996.

overseas sales will be autonomously decided by the leading managing companies within 50% of the issued amount.

However, reciprocal trade of domestic and foreign sales issues still is not permitted. Since Korea allows the purchase of issues for domestic sales by foreigners, reciprocal sales might cause a full-scale opening of the bond market in which bonds circulate on the basis of market interest rates. The bonds for foreign sales can be traded and settled through accounts of the Korea Securities Depository in foreign custodial institutions and international settlement institutions.¹⁵⁵ The procedures for bond issuances by domestic companies applies to the issuance of won-denominated bonds by foreigners, but taking into account the non-residential status of foreigners, the issuing and listing procedures have been simplified.¹⁵⁶

With respect to post management, the funds raised through bond issuance by foreigners should be principally used overseas. However, domestic use is allowed within permitted boundaries of domestic operations. Won/foreign currency swapping for the carrying of funds out of Korea between issuers and domestic foreign exchange banks is also permitted.¹⁵⁷ Taxation on the interest income of domestic investors from their investment in won-denominated bonds issued by foreigners is deemed equal to that applied to the income from domestic bonds.¹⁵⁸

C. *Overseas Securities Investment by Korean Residents*

The government has encouraged domestic investors to make overseas investments in securities so as to diversify their portfolios. The resulting

155. FEMA Regulation of the MOFE, *supra* note 145, art. 10-63, 10-64.

156. Notification of securities issued by foreigners becomes effective 20 days after the date that the notification letter is accepted. Taking into account international differences in securities issuance systems and customs, mentioned items, and the forms of attached papers, Korean issuing and listing procedures will be adjusted to suit foreign characteristics. For example, for foreign governments, the submission of annual reports replaces the more complicated submission of articles of association and financial reports. External audits have been simplified. For foreign companies and foreign financial institutions, audit reports prepared by foreign auditors based on the laws of their home countries will be approved. As for foreign governments and public institutions, external audits will be exempted and replaced by internal auditing materials. Any single credit rating by a Korean or worldwide credit rating institution is acceptable. The listing procedure has also been simplified. Foreign governments and public institutions will be exempted from the review of listings, and the documents for submission in these institutions will be simplified. Other procedural aspects related to issue amounts, issue terms, issue methods, and participants will follow the procedures for international financial institutions.

157. The detailed terms for swaps will be determined on the commercial basis between foreigners and swapping banks.

158. Press release of MOFE, April 1996.

capital outflows will help prevent any excessive imbalance in capital accounts due to the inflow of foreign investment in domestic securities. Overseas investments by institutional investors were fully deregulated in February 1994. In July 1994, Korean investors (i.e. Korean corporations and individuals) were allowed to invest directly in foreign securities, including stocks, bonds, and mutual funds listed on the foreign exchanges designated by the SEC. Since February 1995, individual investors have been allowed to invest up to 100 million won in overseas securities markets, while corporations have been allowed to invest up to one billion won.¹⁵⁹

On April 1, 1996, the investment limit on overseas securities of general investors was abolished. With the abolition of the designated stock exchange system, general investors are now able to trade securities in stock exchanges throughout the world.¹⁶⁰

At present, general investors can invest in stocks, bonds, and BCs which are listed or are set to be listed on the designated stock exchanges. As a result of the February 26, 1996 liberalization plan, the government permits general investors to invest in unlisted foreign exchange securities, including stocks, bonds, BCs, commercial paper ("CPs") issued by foreign companies, and CDs issued by foreign financial institutions which are traded on authorized over-the-counter markets, including NASDAQ in the United States, JASDAQ in Japan and AIM in England.

As for post management, in order to effectively manage overseas securities investment by general investors, the government has prepared the following supplementary measures. General investors will be required to designate one securities company through which to invest in foreign securities and repatriate proceeds. The designated securities company must submit trading records of foreign currency-denominated securities to the Securities Supervisory Board every month. Through accounts of the Korean Securities Depository in designated foreign depository institutions, foreign currency-denominated securities will be deposited and settled.

D. Issuance of Domestic Securities on Overseas Securities Markets

Domestic firms may issue securities overseas. Two major Korean companies, Pohang Iron and Steel Company ("POSCO") and the Korea

159. Currently, the SEC has designated 13 foreign exchanges: New York, London, Paris, Frankfurt, Zurich, Tokyo, Luxembourg, Amsterdam, Brussels, Hong Kong, Singapore, Kuala Lumpur, and Thailand.

160. Press release of MOFE, February and March of 1996.

Electric Power Corporation ("KEPCO"), were listed on the New York Stock Exchange in October 1994. Several other blue chip companies have followed suit. In order to increase equity capital by banks, a basis for the issuance of depository receipts ("DRs") by banks will be prepared, and usage restrictions on funds raised through the overseas issuance of stock-related securities will be lowered in line with the ongoing liberalization of administrative regulations.

Taking into account the need for the issuing of DRs by banks, issuing requirements will be eased soon compared to those for general corporations, but minimum issuing requirements are still needed to maintain the credibility of overseas Korean securities.¹⁶¹ After banks begin issuing DRs, the total acquisition of stocks by foreigners will be limited to no more than 30% of total stocks issued, excluding portions of foreign direct investment.

As for the issuing schedule of overseas Korean securities, plans will be presented to the Korea Securities Dealers Association each quarter. The total annual issue amount for funds for domestic foreign currency-denominated loans should be within the banks' mid- and long-term borrowing ceiling. The ceiling will be operated differently from the ceiling for non-financial companies (US\$ 2.5 billion). During 1998-99, issuance of all securities overseas by domestic firms will be deregulated.

E. Internationalization of the Korea Securities Industry

In Korea, the securities industry has three major types of companies divided according to their business area: securities companies, securities investment trust companies, and securities investment advisory companies.¹⁶² A firm wishing to conduct each type of securities business should secure the approval of MOFE.¹⁶³

Securities companies have expanded significantly along with the rapid growth of the stock market. By the end of 1995, thirty-two companies were in operation in Korea and their combined capital stock was five billion U.S. dollars, an amount seventeen times greater than in 1984. Securities investment trust companies have been established with the aim of facilitating individual investor investment in securities and to efficiently

161. Detailed requirements were designed by the SEC on May 22, 1996.

162. The beginning of securities investment advisory companies stem from July 1984, when Daewoo Economic Research Center made an investment advisory contract with Scudder, Stevens & Clark regarding the operation of Korea Fund. From 1987, as a result of a boom in the Korean securities market, regulations on the securities investment advisory company business was concretely enacted.

163. SEA, *supra* note 7, art. 28.

mobilize industrial funds in accordance with the Securities Investment Trust Act enacted in 1969.¹⁶⁴ Currently, there are eight such companies. Among them, the three largest, commonly referred to as the "Big Three," are national companies, while the other five are local companies.¹⁶⁵ An amendment to the SEA in 1987 provided a basis for the establishment of securities investment advisory companies.

In 1990, the Ministry of Finance (now MOFE) announced guidelines for the opening of the securities industry. Under these guidelines, foreign securities companies were permitted to set up branch offices and establish joint venture securities companies. The first two branch offices were opened in Seoul by Barings Securities Co. and Jardine Fleming Co. in 1991, and now a total of fourteen branch offices are in operation: four from the United Kingdom, three from the United States, three from Japan, two from the Netherlands, and one each from France and Hong Kong. In 1992, the Ministry of Finance approved the establishment of Dongbang Peregrine Securities Co., which became Korea's first joint-venture securities company. In 1995, the government eased a wide range of regulations regarding the operations of foreign securities companies branches in Korea in line with its financial market liberalization. Foreign securities companies were allowed to establish multiple branches in Korea. The government also eliminated a requirement that a foreign securities company should operate a representative office for over two years before establishing a branch office.

The minimum capital requirement for a branch of a foreign securities company has been drastically eased. The capital requirement for performing the three businesses of underwriting, dealing, and brokering has been lowered to 15 billion won from 20 billion won. The floor limit on capital for branches conducting one or two of the three businesses was lowered to 5 billion won and 10 billion won, respectively, from 10 billion and 15 billion won. In 1995, the government also set forth a liberalization plan for the investment trust and investment advisory business. Under this plan, foreign investment trust companies are allowed to set up branch offices and joint-venture investment trust companies in Korea from 1996. As for investment advisory businesses, foreigners have been allowed to

164. Law No. 2129, Aug. 4, 1969 (as amended); *supra* note 12.

165. The Hanguk Investment Trust Company was established in August 1974. Daehan Investment Trust Company and Kookmin Investment Trust Company were established in February 1977 and June 1982, respectively. In November 1989, five local companies were permitted to be established in Incheon, Taejon, Kwangju, Taegu and Pusan, respectively.

establish branch offices since December 1995 and will be free to set up investment advisory companies after 1997.¹⁶⁶

IX. CONCLUSION

The development of the Korean securities market is remarkable despite its rather short history of only four decades. Such development would have been impossible without the government's will to promote the securities market and without effective securities laws and regulations. There still are many challenges for the Korean securities market to overcome in terms of market size, soundness, internationalization, and international competitiveness. Other issues include: guaranteeing of competitiveness on the basis of full market principles, increasing the size and specialization of financial institutions, advancing the public announcement of financial information, and improving the efficiency of financial intermediation.

For Korea to continue its economic growth in the future, the Korean government must enhance the role of its securities market to effectively mobilize and distribute economic resources. To this end, the Korean securities market has to achieve efficiency and economic equality, while keeping pace with international trends such as securitization, liberalization, and globalization. To reach these goals, the SEA needs to be improved by squaring with the following issues: the development of a disclosure system to facilitate the issuance of securities and protect investors, refinement of the accounting system to enable effective auditing which will secure the credibility of financial information gathered from corporations, enactment of effective regulations on securities fraud and crime, addition of regulations on mergers and acquisitions to maximize the positive functions while minimizing the negative aspects of such corporate restructuring, and the provision of effective mediation for securities-related disputes. Finally, stiffer punishments for violations would be welcome.

The securities regulations need to be flexible enough to change along with a securities business that becomes more complicated day-by-day. Such laws must not become an obstacle to the development of the securities industry. In addition, the SEA has to be compatible with international practices in securities trading as Korea increasingly opens its doors to foreigners to improve the international competitiveness of the Korean securities market.

166. Press release of MOFE, (Dec. 1995).

Korea has accelerated its comprehensive financial liberalization and the opening of its market, and this progress is expected to improve drastically. The process will contribute to the development and globalization of the domestic economy as well as the efficiency of the domestic financial system. With Korea's efforts to liberalize its foreign exchange system, Korea will become more closely integrated into international capital markets and global economic activities. In a rapidly changing world economy that features borderless international trade, Korea's intention is to not remain a passive observer. In that context, the liberalization of Korea's capital markets will contribute to the development of the Korean economy and provide a more favorable environment for foreign businesses.

On October 11, 1996, Korea was admitted as the 29th member of the Organization for Economic Cooperation and Development ("OECD"). With the joining of this international organization, Korea will undoubtedly accelerate its current liberalization and take an active role as a contributor to the improvement of the world economy. By assuming a stronger role, not only in Asia, but in the whole world community, Korea will assume a position commensurate to its enhanced economic status.

