VI. Liability of Promoters

57. Playing the central role in the incorporation process, promoters may be subject to liability on various occasions. Although not formally a promoter, one who has allowed his/her name to be used to show his/her support in an offering document like a prospectus shall be subject to the same liability as the actual promoters (Article 327).

A. *Regarding Completed Incorporation*

1. Liability for Unsubscribed or Unpaid Shares

58. Promoters may still be held liable even where the corporation is successfully incorporated. Where any shares are found to remain unsubscribed after the incorporation, or where their subscription is later cancelled, the promoters are deemed to have jointly and severally subscribed to those shares (Article 321(1)). Where any shares remain unpaid for after the incorporation, the promoters must pay for them jointly and severally (Article 321(2)). In establishing these statutorily imposed liabilities, the claimant does not have to prove negligence on the part of the promoters.

2. Liability for Damages to the Corporation

59. Where the promoters neglect their duty and cause loss to the corporation, they will be jointly and severally liable to the corporation for any damages (Article 322(1)). If the corporation fails to pursue the promoters' liability, any shareholder(s) with 1% or more of the shares may demand that the corporation file a lawsuit. If the corporation fails to comply with such demand, the shareholders may themselves bring a derivative suit against the promoters (Articles 324, 403–406).

3. Liability to Third Parties

60. When promoters neglect their duty with intention or gross negligence, they will be jointly and severally liable to a third party for any damages (Article 322(2)). Third parties to whom the promoters may be liable include any persons other than the corporation.

B. *Regarding Incomplete Incorporation*

61. Promoters' efforts for incorporation may sometimes fail midway. In that case, the promoters will be personally responsible for all incorporation-related activities jointly and severally. They also have to pay for costs incurred during the incorporation process (Article 326(2)).

VII. Liability of Directors and Statutory Auditors

62. Although not a central player in the incorporation process, directors or statutory auditors may in some cases be subject to liability. Under the KCC, directors and statutory auditors are required to examine the incorporation process to see if there is any violation of law or the articles of incorporation (Article 313). If they neglect this duty, they may be liable to the corporation and third parties for any damages (Article 323). If the promoters are also liable, all the responsible parties will be held jointly and severally liable for the same damages.

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§2. Corporate Personality

63. Once incorporated, a stock corporation is regarded under the law as an independent person separate and distinct from its shareholders (Article 169). It is the same even if a single person owns or controls all of the issued shares of the corporation.

I. Corporate Personality and the *Ultra Vires* Doctrine

64. Although a corporation is granted capacity as a legal person, according to the courts, its capacity is confined to objects stipulated in the articles of incorporation (Civil Code, Article 34). The relevant case law is almost unanimously criticized by commentators. The courts, however, still maintain the *ultra vires* doctrine but dilute its harmful effects by broadly interpreting the objects of the corporation concerned. The courts hold that acts within the scope of the corporate objects encompass acts needed, directly and indirectly, for achieving such objects (Supreme Court, 8 October 1999, 98*Da*2488).

II. Lifting the Corporate Veil

65. Although a corporation is a legal person, its personality may be disregarded in exceptional cases. The court has recognized this doctrine in several cases in order to prevent deliberate attempts to evade corporate obligations. Commentators divide into two categories those cases where the personality of a corporation may be disregarded. The first category, which may be called the 'Nominal Personality Category', relates to cases where a corporation's separate legal personality is in name

only. The second category, which may be called the 'Abusing Personality Category', relates to cases where the legal personality is abused with the intention of avoiding liability.

For the cases falling under the Nominal Personality Category, commentators enumerate various factors which may lead the court to recognize the nominal nature of the corporation concerned. A prime example of such factors is a commingling of funds between the controlling shareholder and the corporation concerned. It is difficult, however, to find a case where the court pierced the corporate veil only on the basis of such factors. The Supreme Court held that a parent company is not responsible for the debt of a subsidiary even when the subsidiary's capital is inadequate for its size of business (Supreme Court, 25 August 2006, 2004*Da*26119).

The court seems more likely to disregard corporate personality in cases falling under the Abusing Personality Category. A common example of such cases is where a controlling shareholder of an insolvent firm opens up a new corporation which is functionally identical to the old firm in terms of shareholders, employees, type of business, and business assets, with the intention to avoid the liability of the old firm (Supreme Court, 12 November 2004, 2002Da66892). In other words, functional similarity between the old and the new firms and the intention to avoid the liability of the old firm are two key elements in the cases of the Abusing Personality Category. The court is not likely to hold the new firm responsible for the debts of the old firm when the new firm paid a fair price for the business assets (Supreme Court, 21 August 2008, 2006*Da*24438; Supreme Court, 11 September 2008, 2007*Da*90982).

§3. Organizational Structure of Corporations

I. Introduction

66. In the past, the KCC provided for three main organs in a corporation: (1) shareholders and the GMS; (2) directors, representative directors, and the board of directors; and (3) statutory auditors. The KCC now allows a corporation to deviate from this standard organizational structure. A corporation is now authorized to appoint statutory officers instead of representative directors (Article 408-2) and to establish an audit committee instead of a statutory auditor (Article 415-2). A corporation with assets not amounting to KRW 1 billion is allowed to dispense with the board of directors (Article 383(1)(4)). The KCC requires a listed firm with the assets amounting to KRW 2 trillion or more to establish an audit committee (Article 542-11(1)). In addition, certain corporations including firms with assets amounting to KRW 10 billion or more are subject to external audit by certified public accountants (AEA, Article 2).

These organs are supposed to check and balance each other. If each organ performs its assigned function properly, agency problems will diminish. In the following sections, we will look at the basic allocation of powers among various organs, how these company organs act, and how they affect each other in the context of corporate governance.

II. General Meeting of Shareholders

A. *Introduction*

67. As in most other countries, small shareholders in Korea have little interest in attending the GMS. Many of them are speculators rather than investors, interested in short-term capital gains. Even when small shareholders attend meetings, their impact, in most cases, is insignificant because a substantial block of shares are securely placed in the hands of a few controlling shareholders. Consequently, despite the statutory illusion of management accountability to shareholders, the reality is that top managers tend to pursue the interests of controlling shareholders, sometimes even at the expense of small shareholders.

The situation is now a little different in large listed firms because of the presence of foreign investors. In terms of market value, foreign shareholders held 33.6% of the total market capital of the Korean stock market as of the end of 2017. Another important factor causing a change in the GMS is the National Pension Service (NPS). National Pension Plan is the nationwide mandatory pension plan of Korea, and the NPS is the entity in charge of managing the assets of the National Pension Plan. As of May 2018, the NPS owns approximately 8% of the total market capital of the Korean stock market, and its holdings are expected to grow further with the increase in its size.

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B. *Powers of the GMS*

68. As the KCC adopts the board system, the GMS is given only a limited scope of powers. Under Article 361 of the KCC, the power of shareholders at the GMS is limited to such matters as are provided for in the KCC or in the articles of incorporation.

1. Matters Set Out in the KCC

69. The matters specifically reserved for the GMS under the KCC may be classified into three categories, depending on the kind of resolution required: (1) matters requiring an ordinary resolution; (2) matters requiring a special resolution; and (3) matters requiring unanimous approval.

Matters requiring an ordinary resolution include the following items:

- election of directors and statutory auditors (Articles 382(1), 409(1));
- approval of financial statements (balance sheets, income statements, and profit and loss disposal statements) (Article 449); and
- decision on the compensation of directors and statutory auditors (Articles 388, 415).

Matters requiring a special resolution and a unanimous approval are found at D.4 below.

2. Powers Set Out in the Articles of Incorporation

70. Although the power of the GMS is limited in principle to the above matters, this power can be expanded to cover other matters if the articles of incorporation so stipulate. Indeed, the KCC makes it clear in some provisions that the GMS, rather than the board, may determine if the articles of incorporation so provides. For example, although issuance of new shares is up to the board of directors, the articles of incorporation may empower the GMS to decide on whether to issue new shares (Article 416).

A question may arise where the KCC does not explicitly authorize the expansion of the GMS' power in the articles of incorporation: is it still possible to expand the GMS' power to include such matters? For example, unlike issuance of shares, Article 469, which deals with the issuance of bonds, does not contain any language that suggests such possibility. Can the articles of incorporation provide that the GMS, rather than the board, has the power to decide on the issuance of bonds? As yet, there is no relevant court decision on this issue. Although there are different views among commentators, it is the prevailing view that the power of the GMS may be expanded to cover any matters.

3. Delegation by the General Meeting

71. According to the prevailing view, the GMS in principle may not delegate any of its power to the board or a representative director. An obvious example may be the delegation to the board of the power to appoint directors (Article 382(1)). In some cases, however, delegation may and does take place. A prime example is directors' compensation. Although the GMS is supposed to determine the compensation of directors (Article 388), the widespread corporate practice is that the GMS determines only the maximum limit on the total amount of directors' compensation, delegating to the board or representative director the power to determine the compensation of individual directors.

C. Convening of the General Meeting

1. Power to Convene

72. Unless otherwise provided in the KCC, the board of directors determines whether to convene the GMS (Article 362). Shareholders with 3% or more of the total outstanding shares may request that the board call an extraordinary GMS (Article 366(1)). In a listed firm, the shareholding threshold is lowered to 1.5%, although a six-month holding period is required (Article 542-6(1)). The shareholders must submit to the board a written statement on the agenda of and reasons for the GMS. If the board fails to take steps for convening the GMS immediately, the shareholders may on their own convene the GMS with the approval of the court (Article 366(2)). An extraordinary GMS may be convened by a statutory auditor as well (Article 412-3(1)). Like the 3% shareholders, the statutory auditor is required

to submit a written request to the board first. If the board fails to take necessary actions immediately, the statutory auditor may on his/her own convene the GMS with court approval (Articles 412-3(2), 366(2)).

If the court finds it necessary to hold the GMS based on the report by an inspector on the corporation's operation or financial condition, the court may order the representative director to do so (Article 467).

2. Ordinary and Extraordinary General Meeting

73. Every corporation must hold a GMS once a year on a predetermined date (Article 365(1)). If the fiscal year of a corporation is shorter than one calendar year, the meeting must be held once every fiscal year (Article 365(2)). This is called an ordinary GMS. In addition to the ordinary GMS, the board may call a GMS from time to time whenever necessary, which is usually called an extraordinary GMS (Article 365(3)). No difference exists between the two kinds of meetings.

3. Notice of the General Meeting

a. General

74. In order to hold a GMS, notice must be given to the shareholders. Shareholders with no voting power are not entitled to receive such notice (Article 363(7)). Thus, the corporation need not give notice to holders of non-voting shares.

b. Methods of Notice

75. The notice should be given in writing to individual registered shareholders at least two weeks before the date of the meeting (Article 363(1)). A listed corporation may satisfy the notice requirement by publishing the notice twice in a daily newspaper or by posting the notice through the electronic disclosure system of the Financial Supervisory Service ('FSS') or Korea Exchange (Article 542-4(1)).

c. Contents of the Notice

76. The KCC requires the corporation to state the agenda of the meeting in the written notice (Article 363(2)). Generally, corporations tend to mention the agenda only briefly in the notice. In a few cases, such as amendment of the articles of incorporation, merger, and the reduction of capital, the corporation is required to provide an outline of the proposal (Articles 433(2), 438(2), 522(2)). When the corporation plans to amend the articles of incorporation, it must indicate both the original provision in question and the proposed new provision. In the case of merger, however, the extent of disclosure that the firm must make is not clear. In practice, corporations have not been particularly eager to provide their shareholders with adequate and sufficient information. A listed firm is subject to stricter disclosure requirements.

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financial statements, the creditor may file a claim against the director based on Article 401 (Supreme Court, 11 September 2008, 2007*Da*31518). It does not mean that the director owes any duty directly to the creditors. Rather, a creditor of the company who incurred damages due to the director's breach of duties to the company may directly sue the directors – what is breached here is the director's duty to the company, not to the creditor.

As is the case in liabilities to the company, if more than one director is involved, the directors shall be liable jointly and severally. In order to claim a director's liability to a third party, however, the third party plaintiff faces a higher burden of proof: he/she has to prove at least gross negligence on the part of the director.

2. Scope of Third Party's Damage

158. Several issues exist as to the scope of this liability. No one doubts that a creditor of the company constitutes a third party. However, commentators take different view among themselves as to whether the firm's shareholders may be regarded as third parties. The prevailing view answers this question in the affirmative.

Commentators are also in dispute as to whether this liability extends to 'indirect' as well as 'direct' damage. Indirect damage refers to damage incurred by a third party as a consequence of damage inflicted on the company. For example, if the company's value decreases due to a director's misconduct, the company's shareholders would suffer indirect damage as a result of a declining share price. The court has held that the shareholders are not able to claim damages for indirect damage against a wrongdoing director under Article 401 (Supreme Court, 26 January 1993, 91*Da*36093). In such cases, a shareholder will have to rely on a shareholders' derivative suit (Article 403) to recover damage inflicted on the company.

It is not always easy to distinguish between the direct and indirect damage. In a recent case, shareholders of a listed company filed a lawsuit against its director (who was actually managing the company) based on Article 401. The facts can be summarized as follows: (i) the plaintiff purchased shares on the exchange (Tranche 1); (ii) the defendant embezzled corporate assets and made false disclosures of the company's financial status without reflecting such embezzlement, and as such, the stock price of the company was much higher than what it would have been if correct disclosures had been made; (iii) the plaintiff purchased additional shares (Tranche 2) on the exchange without knowing about the embezzlement and false disclosures; and (iv) later the misconduct was known to the market and the stock price plummeted. The Supreme Court held that the damage related to Tranche 2 was 'direct damage' payable under Article 401 because the plaintiff was defrauded to pay higher price than fair price, while most of the damage related to Tranche 1 was simply 'indirect damage' not claimable under Article 401 because this is just a reflection of the damage incurred by the company (which can be claimed by the company itself or through a derivative action) (Supreme Court, 13 December 2012, 2010*Da*77743).

IV. Statutory Auditors and Audit Committee

A. General

159. The KCC contemplates two kinds of supervisory organs within the company: a statutory auditor (a.k.a. an internal auditor) and an audit committee. Until the concept of the audit committee was first introduced to Korean law in the late-1990s under the influence of US law, every Korean corporation had to have at least one statutory auditor regardless of the size of the company. Based on the belief that an audit committee may be in a better position to play an independent supervisory role than statutory auditors, the KCC was amended a few times to boost the utilization of the audit committee.

As a result of the frequent amendments to the KCC, related provisions are quite complex. First, a non-listed corporation whose legal capital is KRW 1 billion or more and a listed company whose total assets are less than KRW 100 billion must have at least one statutory auditor or establish an audit committee composed of at least three directors, with at least two-thirds of the members being outside directors (Articles 409(1)(4), 415-2(1)(2)). Second, a listed corporation whose total assets are between 100 billion and KRW 2 trillion must have at least one full-time statutory auditor or establish a 'qualified' audit committee (Article 542-10(1)). Third, a listed corporation whose total assets are KRW 2 trillion or more must establish a 'qualified' audit committee (Article 542-11(1)). For difference between a 'normal' and a 'qualified' audit committee, *see infra* 171.

B. Statutory Auditor

1. Election

160. A statutory auditor is elected at the GMS (Article 409(1)). In electing a statutory auditor, any shareholder with more than 3% of the total outstanding voting shares may not vote the excess shares (Article 409(2)). Such a rule (the so-called 3% rule) intends to limit the influence of large shareholders over the election of the statutory auditor and secure the neutrality and independence of the statutory auditor. In reality, however, independence of the statutory auditor has been frequently questioned.

The statutory auditor may not serve concurrently as a director, a general manager, or as any other employee of the corporation (Article 411). Other than that, there is no qualification for becoming a statutory auditor under the KCC. The term of the statutory auditor's office normally runs for three years and expires at the time of closure of the third ordinary GMS in his/her term (Article 410).

2. Removal

161. A statutory auditor may be removed by the resolution of the GMS. The '3% rule' applicable to the election does not apply to the removal in case of the non-listed corporations but does apply to the removal in case of the listed corporations (Article 542-12(3)). The statutory auditor may attend the GMS and express his/her opinion when his/her removal became an agenda at the meeting (Article 409-2).

In calculating the 3% for purposes of the '3% rule' to elect or remove statutory auditors of a listed corporation, shares held by 'specially related persons' of the largest shareholder as defined under the KCC are counted together as if they are one single shareholder (Article 542-12(3)). Note that such consolidation only applies to the largest shareholders of a listed corporation.

3. Powers

a. Supervision of Accounting and Operational Matters

162. The statutory auditor supervises operational as well as accounting matters of the company (Article 412(1)). In performing his/her supervisory role, a statutory auditor may exercise any of the following powers:

- to call on the directors at any time for a report on the business and to investigate corporate affairs and financial status (Article 412(2));
- to call on a subsidiary of the firm for a report on the business, and in certain circumstances, to investigate the subsidiary's affairs and financial status (Article 412-5);
- to review the directors' proposals and documents to be submitted at the GMS and to comment on their compliance with the law and the articles of incorporation (Article 413);
- to receive notice of the board meeting (Article 390(3)) and to attend any board meeting and express his/her opinions (Article 391-2(1));
- to report to the board of directors if he/she finds that a director has violated, or is likely to violate, the law or the articles of incorporation (Article 391-2(2)); and
- to submit an audit report to the directors (Article 447-4).

b. Power to Convene a GMS

163. A statutory auditor may have the board of directors call an extraordinary GMS by submitting to the board of directors a written request including the agenda of the meeting and the reasons for calling the meeting (Article 412-3(1)). If the board, upon receiving the request, fails to take necessary steps immediately, the statutory auditor himself/herself may call a GMS with the approval of a court (Article 412-3(2)).

c. Power to Seek Injunction

164. Where a director is likely to commit an act in violation of the laws or of the articles of incorporation, and the act might cause irrecoverable damage to the firm, a statutory auditor as well as minority shareholders are authorized to request the relevant director to abstain from the act in question (Article 402). Together with the request, the statutory auditor may apply to the court for a preliminary injunctive order.

d. Power to File Various Suits

165. The KCC lists several occasions in which a statutory auditor is empowered to initiate a corporate legal proceeding. Such suits include the following:

- suit for nullifying the firm's incorporation (Article 328);
- suit for revocation of a resolution of the GMS (Article 376(1));
- suit for nullifying issuance of new shares (Article 429);
- suit for nullifying reduction of the legal capital (Article 445); and
- suit for nullifying a merger (Article 529).

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e. Power to Represent the Firm in a Suit Against a Director

166. The power to represent a corporation normally vests in the representative director. In a lawsuit between the company and any director, however, the statutory auditor has the power to represent the company (Article 394). A statutory auditor represents the firm both when a director files a suit against the firm and when the firm files a suit against a director. It is the statutory auditor who has power over the decision to bring a suit. So when a shareholder makes a demand on the company to bring suit against a director, the demand must be directed at the statutory auditor.

4. Duties and Liabilities

a. Duties of Statutory Auditors

167. When a statutory auditor finds that any director violates (or is likely to violate) the laws or the articles of incorporation, he/she should report it to the board of directors (Article 391-2(2)). Also, the statutory auditor is required to examine the agenda and related materials to be submitted by the directors to the GMS and to express at the GMS his/her opinion on whether they are in violation of the law or the articles of incorporation or manifestly unfair (Article 413). The statutory auditor must keep minutes of all audit work (Article 413-2(1)). The minutes must include the summary and results of the audit (Article 413-2(2)). Prior to the ordinary GMS, the statutory auditor must perform the audit and submit an audit report to the directors (Article 447-4).

b. Liabilities of Statutory Auditors

168. A statutory auditor may be held liable to the company for his/her intentional or negligent breach of any duty (Article 414(1)). A shareholder may file a derivative suit to pursue the liability of a statutory auditor (Articles 415, 403). If the statutory auditor is grossly negligent, he/she may be held liable to a third party as well (Article 414(2)). Where any director is also responsible for the damages, the director and the statutory auditor are jointly and severally liable (Article 414(3)).

5. Securing the Independence of Statutory Auditors

169. Although legislators attempted to strengthen the role of statutory auditors, statutory auditors in reality merely acted as a 'rubber stamp' in many cases. This discrepancy between law and reality resulted from the lack of independence of statutory auditors. The KCC does not entirely ignore the importance of the independence of statutory auditors. First of all, the KCC explicitly prohibits a statutory auditor from serving concurrently as a director, a general manager, or any other employee of the corporation, but no more is required. Thus, as long as he/she does not presently maintain any of those positions, any person may qualify as statutory auditor, however obvious and strong his/her ties are to management.

One may argue that prohibiting a shareholder with more than 3% of the total outstanding voting shares from voting the excess shares may substantially diminish the influence of the controlling shareholder on the election of the statutory auditors (Article 409(2)). But this 3% limit does not seem to play a significant role in reality. In most shareholders' meetings, decisions are passed unanimously without actually counting the votes. In these cases, the chairman of the meeting need not pay any attention to this limit. Combined with the inertia and disorganization of small shareholders, this procedural approach is not highly likely to enhance the neutrality of statutory auditors.

C. Audit Committee

1. General

170. In lieu of having a statutory auditor, a corporation may establish an audit committee as a subcommittee of the board of directors (Article 415-2(1)). If a corporation establishes an audit committee, it may not have a statutory auditor (Article 415-2(1)). An audit committee is composed of at least three directors, with at least two-thirds of the members being outside directors (Article 415-2(2)).

2. Composition of the Committee

a. Election and Removal of Audit Committee Members

171. As discussed above, a listed corporation whose total assets are more than KRW 100 billion and not more than KRW 2 trillion must have at least one full-time

statutory auditor or establish a 'qualified' audit committee (Article 542-10(1)), and a listed corporation whose total assets are KRW 2 trillion or more must establish a 'qualified' audit committee (Article 542-11(1)). The most significant distinction between a 'normal' and 'qualified' audit committee lies in the way the members are elected. In case of a 'normal' audit committee, the audit committee members are elected by the board of directors among the board members. On the contrary, members of a 'qualified' audit committee are elected by the shareholders at the GMS, among those who were elected as directors at the same meeting.

Likewise, members of a 'normal' audit committee are removed by the resolution of the board of directors which requires affirmative votes of at least two-thirds of the incumbent directors (Article 415-2(3)), while members of the 'qualified' audit committee are removed by the resolution of the GMS.

b. Restriction of Voting Right Exceeding 3%

172. Application of the '3% rule' to the audit committee members is quite complex. To begin with, such a rule is irrelevant for a 'normal' audit committee because the members are elected by the board. For a 'qualified' audit committee: (i) for members who are outside directors, the '3% rule' applies to all the shareholders holding more than 3% of the voting stock, on a non-consolidated basis (i.e., not counting together the shares held by the specially related persons), only in case of election (not removal) (Article 542-12(4)); while (ii) for members who are non-outside directors, the '3% rule' applies only to the largest shareholders (i.e., other shareholders are not subject to the 3% limit), on a consolidated basis (i.e., counting together the shares held by the specially related persons), both to the election and removal of the audit committee members (Article 542-12(3)).

It may seem quite draconian to apply the '3% rule' to the election of the audit committee members (thus, limiting the large shareholders' voting rights) considering that they are directors as well. However, since the audit committee members are elected among those who were already elected as directors, the voices of minority shareholders are not powerfully reflected in the election of the audit committee members. They can at best veto the audit committee member candidates who were already elected as directors under the influence of the controlling shareholder.

c. Representative of the Audit Committee

173. Once an audit committee is composed, the members elect a representative of the audit committee (Article 415-2(4)). It is also possible to elect multiple representatives who jointly represent the audit committee.

3. Powers, Duties, and Liabilities

174. Most of the provisions of the KCC regarding powers, duties, and liabilities of a statutory auditor are applied *mutatis mutandis* to the audit committee (Article 415-2(7)). Therefore, most of the powers, duties, and liabilities discussed above in relation to the statutory auditor are also applicable to the audit committee. Unlike

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f. Protection of Creditors

293. Where a divided company has decided to split the liabilities of the newly formed, acquiring, and/or divided companies, the divided company should implement creditor protection procedures as discussed in *supra* 265 in relation to a capital reduction and *supra* 278 in relation to a merger (Articles 530-9(4), 527-5). Such procedures also apply to a division-merger (Articles 530-11(2), 527-5). If a certain creditor of the divided company, who is known to that company, did not receive individual notice pursuant to such creditor protection procedures, then the newly formed, acquiring, and/or divided companies are subject to joint and several liability since the split of liability is allowed only to the extent that creditor protection procedures are completed in good order (Supreme Court, 30 August 2004, 2003*Da*25973).

g. Registration of Division, Merger, and Incorporation

294. Division or division-merger ends with its registration in the company registry. Where the divided company ceases to exist as a result of the division or division-merger, the company is required to register its dissolution. If a new company is formed as a result of the division or division-merger, registration of its incorporation is required. However, the acquiring and divided companies (to the extent they still exist) only have to amend their registered items reflecting the changes caused by the division or division-merger (Articles 530-11(1), 528).

3. Effect of Division or Division-Merger

295. Upon registration of the division or division-merger, newly formed companies and acquiring companies, by operation of law, succeed to the rights and obligations of the divided company in accordance with the division plan or division-merger agreement (Article 530-10). Unlike a merger, the 'universal succession' of rights and obligations takes place only for those stipulated in the division plan.

IV. Takeover

A. General

296. Similar consequences of corporate restructuring may result from a takeover. Takeover here implies the acquisition of a controlling stake in a target. The most common way of executing a takeover is by acquisition through a privately negotiated transaction with controlling shareholders. The controlling shareholders may receive a control premium generated from this type of takeover. The prevalence of this method is due to the fact that the acquirer, by dealing directly with the owners of the targets, can easily and rapidly complete the transaction without bothering to obtain any approval from the shareholders or board of the target. Typical

conditions in a privately negotiated transaction include obtaining regulatory approval, accuracy of representations and warranties, and compliance with customary pre-closing covenants.

A takeover may also be executed through a tender offer. Even in a privately negotiated transaction, a tender offer by a successful acquirer often follows if he/she wants to make the target company private. A tender offer is the process by which one party ('offeror') suggests a general offer to buy the voting shares or voting-related securities (collectively 'voting securities') in a target company. Unlike the US or the United Kingdom, tender offers in Korea are mostly used for purposes of delisting or during the process of reshuffling corporate groups into a holding company structure. The procedures for tender offers are regulated by the CMA.

B. *Procedures for Tender Offer*

1. Public Notice of Tender Offer and Submission of Tender Offer Statement

297. Anyone who intends to make a tender offer shall provide public notice that indicates the offeror, the target company, the purpose of the tender offer, the class and number of stocks subject to the offer, and terms and conditions of the offer (CMA, Article 134(1)). On the date of the public notice, the offeror shall submit a tender offer statement to the FSC and the Korea Exchange (CMA, Article 134(2)) and send a copy of the statement to the target company (CMA, Article 135). In practice, tender offer statements are publicly accessible on the FSS website (http://dart.fss.or.kr/).

2. Disclosure of Tender Offer Prospectus

298. The offeror has to submit a tender offer prospectus to the FSC and the Korea Exchange on the date of the public notice. The prospectus shall be placed in the FSC, the Korea Exchange, and the office of the broker designated by the offeror so that any investors may review it (CMA, Article 137). In practice, the tender offer prospectuses are publicly accessible on the FSS website (http://dart.fss.or.kr/).

3. Tender Offer Period

299. The tender offer period must be at least twenty days but cannot exceed sixty days (CMA, Article 134(3)). The period may be extended if there is a counter tender offer.

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4. Restrictions on Activities of Offer or Target Company

300. The offeror and his/her specially related persons shall not purchase voting securities in deviation from the tender offer from the date of public notice (CMA, Article 140). The purpose of this regulation is to guarantee equal treatment among shareholders to whom the tender offer is made. Under the old regime, the target company was not allowed to take any measures to affect the voting powers of the existing shareholders. Because such restriction was abolished in 2005, the board of directors of the target company, as an anti-takeover defence, may decide to issues new shares. Such decision is, of course, subject to the directors' fiduciary duty.

5. Price and Consideration

301. The rules do not directly regulate or prescribe a range for tender offer prices but do prohibit the offeror from reducing the tender offer price after a tender offer statement has been submitted (CMA, Article 136(3)). An increase of price is allowed where there is a counter tender offer or the market price of the target company shares has reached 90% of the tender offer price (CMA Presidential Decree, Article 147). Upon increase in price, shareholders who already tendered their shares are also entitled to receive the new higher price. Consideration for the tendered voting securities may take the form of cash and/or other securities.

6. Target Company's Opinion on Tender Offer

302. The target company's board of directors is allowed to manifest its opinion on the tender offer through advertisements or letters to the shareholders or in other ways (CMA, Article 138). For instance, the target's board may support the tender offer and recommend that the shareholders offer their shares, or it may oppose to the tender offer and recommend that the shareholders do not offer their shares. In deciding whether to support or oppose a tender offer, the directors are always subject to their fiduciary duty.

7. Revocation of Tender Offer

303. Once notice of a tender offer is publicly given, the offeror may not revoke the offer except in certain situations such as: (i) where there is a counter tender offer, (ii) where the offeror is dead or dissolved or bankrupt, or (iii) where there is a merger, division, transfer of undertaking, dissolution, bankruptcy, or delisting of the target company (CMA, Article 139).

8. Withdrawal by Shareholders

304. Any shareholder who accepted an offer and tendered shares may withdraw his/her tender at any time during the tender offer period (CMA, Article 139(4)).

9. Purchase of Tendered Shares

305. On the day following the expiry of the tender offer period, the offeror is generally obliged to purchase all tendered shares in accordance with the terms and conditions stated in the tender offer statement. The offeror, however, is able to offer to purchase only a part of the shares (e.g., 40%). If the number of tendered shares is larger (e.g., 80%) than the offered, the offeror may purchase the shares on a pro rata basis from each tendering shareholders provided that the offeror has disclosed such plan. If, however, a smaller number of shares are tendered (e.g., 20%), the offeror must purchase all tendered shares unless the offeror has indicated otherwise (CMA, Article 141).

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C. *Mandatory Tender Offer*

306. If a party makes a solicitation to purchase voting securities of a listed company outside the stock exchange from ten or more sellers within a six-month period, resulting in the acquirer (together with any specially related persons) owning 5% or more of the voting securities of the listed company, the party is obliged to acquire such securities through the takeover procedure (CMA, Article 133(3); CMA Presidential Decree, Article 140).

V. Squeeze-Out and Sell-Out

307. In addition to the cash-out merger, the 2011 revision adopted another strong device known as a squeeze-out. A dominant shareholder who has 95% or more of shares in a company may require the remaining shareholders to transfer their shares provided that 100% ownership is necessary to accomplish the business objective of the company (Article 360-24(1)). The dominant shareholder should present his/her plan at the shareholders' meeting and his/her plan should be approved by the shareholders (Article 360-24(3)(4)). If the dominant shareholder and the minority shareholders cannot reach an agreement on the fair price of the share, the court shall determine a fair price. While the KCC has some mechanisms for protecting minority shareholders such as (i) a business objective requirement and (ii) a shareholders' resolution requirement, this new arrangement enables dominant shareholders to easily squeeze minority shareholders out. For example, obtaining shareholders' resolution seems like a nominal requirement for a shareholder who has 95% or more shares. However, minority shareholders have sell-out rights by which they may demand dominant shareholders with 95% or more shares to purchase their shares (Article 360-25).

creditor bank or the Creditors Commission may require the debtor company to receive an inspection by a special independent institution (CRPA, Article 12).

Even after the commencement of joint management, the existing directors and managers of the debtor company continue to operate the company the same as before. During the period of joint management, the debtor company shall submit to the Creditors Commission a restructuring plan, which takes effect upon approval of the Commission (CRPA, Article 13). A restructuring plan contains provisions on credit restructuring (e.g., stays on claim enforcement and debt-to-equity swaps) as well as business restructuring (e.g., reorganization of business departments and adjustment of personnel expenses). If necessary to carry out the restructuring plan, the Creditors Commission may reorganize the credits of financial institutions and extend new credits by its resolution mentioned above (CRPA, Articles 17, 18(1)). New credits extended upon the decision by the Creditors Commission have priority over other financial institutions' credits extended before the joint management (CRPA, Article 18(2)). The main creditor bank shall monitor the performance of the restructuring plan on a quarterly basis and report the result to the Creditors Commission (CRPA, Article 15).

B. *Effect of Restructuring Plan and Termination of Rehabilitation Proceeding*

312. The restructuring plan only binds financial institutions that are members of the Creditors Commission, and therefore, the other creditors may freely exercise their claims. Where the debtor company has fulfilled all obligations under the plan, joint management by the financial institutions would be successfully finished. On the contrary, the Creditors Commission may declare unsuccessful termination of the rehabilitation proceeding where the debtor company has failed to perform major obligations under the plan or has turned out to be financially unviable (CRPA, Article 19). Also, the rehabilitation under the CRPA ends if the court decides to commence the rehabilitation proceedings under the DRBA (CRPA, Article 11(5)).

III. Rehabilitation under the DRBA

313. Rehabilitation proceedings under the DRBA are basically similar to Chapter 11 proceedings under the US Bankruptcy Code. This proceeding affects not only the financial creditors but also transactional creditors, whether secured or unsecured.

A. *Process of Rehabilitation Proceeding*

1. Application for Rehabilitation Proceeding

314. A financially troubled company may apply for rehabilitation under the DRBA if: (i) the company cannot pay its debts as they fall due without a significant impact on business continuity or (ii) there is a fear that the company will enter into

bankruptcy (DRBA, Article 34(1)). Previously, under the Corporate Reorganization Act, only stock corporations were eligible for this court-led rehabilitation, but the DRBA grants eligibility to all forms of companies. The company's shareholders or creditors who meet minimum requirements (i.e., generally those who hold 10% of the aggregate shares or debts) may also apply for the proceeding (DRBA, Article 34(2)). The district court at the location of the company's main office shall have exclusive jurisdiction over the rehabilitation proceeding (DRBA, Article 3(1)).

2. Provisional Order and Temporary Stay Order

315. Upon applying for the rehabilitation proceeding, the court may issue a provisional order which prevents the *debtor* from taking certain actions such as payment of pre-existing debts (DRBA, Article 43). Also, the court may issue an order of ordinary temporary stay which prevents the *creditors* from enforcing their rights (DRBA, Article 44). In addition, the DRBA introduced the concept of a 'comprehensive' temporary stay. While ordinary temporary stay orders are issued against specific enforcement proceedings on a case-by-case basis, a comprehensive temporary stay order covers all enforcement by any creditors whether secured or not. A comprehensive temporary stay will be ordered if the court has reason to believe that an ordinary order will not adequately fulfil the purposes of rehabilitation (DRBA, Article 45). A comprehensive or ordinary temporary stay order as well as a provisional order may be made upon petition by interested persons or on the court's own initiative.

3. Commencement of Proceeding

316. The court will formally approve the commencement of the rehabilitation proceeding if conditions for rehabilitation under the DRBA (e.g., inability to pay its debts) are satisfied. The decision should be made within one month from the date of application (DRBA, Article 49). The court should turn down the application where the rehabilitation proceeding is incompatible with the general interests of creditors or the application is not bona fide (DRBA, Article 42). With the commencement of the rehabilitation proceeding, the court shall appoint an administrator and set a date for the interested parties' first meeting and claim lodging period (DRBA, Article 50).

Upon the commencement of rehabilitation proceedings, both secured and unsecured creditors are prevented from individually enforcing claims that arose prior to the date of commencement (DRBA, Articles 58, 59). Claims arising after the commencement of proceedings are not stayed.

4. Appointment of the Administrator

317. Upon the commencement of the proceeding, the court shall appoint an administrator. Before the appointment, the court shall consult with the Custodial

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