

Avoiding Foreign Exchange Law Bottlenecks and Pitfalls in Your Korean Investments

Investing in a startup should be as simple as conducting due diligence, signing the investment contracts, and wiring the investment funds at the closing. Although this may be true in the U.S. and other jurisdictions, this is not true for cross-border investments in Korea.

Foreign investors seeking to invest in Korea for the first time would likely not be aware of Korean foreign exchange laws or the delays that may be caused from failing to make the necessary preparations to comply with the laws' requirements. It is important for foreign investors to at least have a basic understanding of Korean foreign exchange law requirements given that timing is often a crucial factor in startup investments due to companies' needs for prompt access to funding.

This article seeks to provide foreign investors looking to invest in Korea with a brief overview of Korean foreign exchange law requirements and what they can prepare in advance to help their investments proceed in an efficient manner.

Rule of Thumb

Under Korean foreign exchange laws, the general rule of thumb regarding investments into Korea is that any non-Korean resident acquiring equity in a Korean entity will need to file a report with the relevant bank in Korea before acquiring such equity. The type of report may differ depending on the investment amount, how much equity is acquired, the type of securities acquired, and the type of entity into which the investment is made, but for the purposes of this article, we will focus on the acquisition of shares or convertible bonds of a Korean joint-stock company (as these are most common in the startup context). The relevant thresholds for these investments are as follows:

1. If a non-Korean resident is acquiring unlisted/unregistered shares or equity in a Korean entity and is acquiring:
 - (i) less than 10% equity ownership in such entity, or
 - (ii) 10% or more equity ownership in such entity with an investment amount less than KRW 100 million,

then such person must file a securities acquisition report with a foreign exchange bank after execution of the investment contract but prior to closing.

2. If a foreigner is investing at least KRW 100 million in a Korean entity and either:
 - (i) acquires at least 10% of the voting equity of the Korean entity, or
 - (ii) obtains the right to appoint a director of the Korean company,then such person must file a foreign investment report with a foreign exchange bank after execution of the investment contract but prior to closing.

3. A non-Korean resident acquiring convertible bonds issued by a Korean entity must file a securities acquisition report with the Bank of Korea before execution of the convertible bond subscription agreement.

For convenience, we will refer to securities acquisition reports and foreign investment reports simply as “f/x reports”.

Potential Bottlenecks and Pitfalls

As discussed above, f/x reports must be filed prior to acquiring shares issued by a Korean company (and in the case of a convertible bond, prior to signing). As a practical matter, the banks also monitor incoming funds, so if there is an attempt to remit investments funds without filing an f/x report, the bank will likely discover the transaction and suspend it until the f/x report is properly filed. In other words, failure to promptly file the proper f/x report with the relevant bank will cause delays in the closing of the investment.

Also, as Korean foreign exchange laws are known to be rather complex, foreign investors should retain local counsel to help determine the appropriate f/x report to file and to prepare and submit the f/x report with the appropriate bank.

Even after retaining local counsel, however, a potential bottleneck may still arise relating to the documents required to be submitted with the f/x report, including a power of attorney, which the banks generally require be notarized and apostilled (or legalized by a Korean embassy/consulate), and other KYC (or “know-your-customer”) documents. In our experience, the notarization and apostille of a power of attorney is the most time-consuming aspect of f/x report preparation, especially in recent years, given

that government institutions performing the apostille may shut down or not be at full capacity due to COVID-19 infections. As such, it would be prudent for investors to have local counsel assist with f/x report preparation early in the investment process (e.g., in the term sheet phase) to ensure that the f/x report is ready to be submitted on our around signing.

Conclusion

If a foreign investor acquires equity in a Korean company without filing the appropriate f/x report, this could raise issues later in an exit event, as the bank will require submission of the f/x report when the equity is sold or otherwise liquidated. If it is discovered that no f/x report (or an improper f/x report) was filed, the bank will refuse to process the transaction for the sale/liquidation and the investor will not be able to receive the proceeds until it has undergone a remedial procedure, which involves submission of a report detailing the violation of foreign exchange laws (and the reason for the violation) that will be reviewed by the bank as well as the Ministry of Economy and Finance—a process that can take months. The violations may also be subject to administrative fines (although first-time offenders are typically only issued warnings). This highlights the importance of retaining local counsel experienced in foreign exchange law matters to ensure the proper f/x reports are filed.

We hope the foregoing is helpful in providing a basic understanding of foreign exchange law requirements for Korean investments and expediting your future Korean investments.

If you require assistance in foreign exchange law or other matters, please do not hesitate to contact SEUM Law

본 자료에 게재된 내용 및 의견은 일반적인 정보제공만을 목적으로 발행된 것이며, 법무법인 세움의 공식적인 견해나 어떤 구체적 사안에 대한 법률적 의견을 드리는 것이 아님을 알려 드립니다. Copyright ©2021 SEUM Law.

다니엘 정 외국변호사

Associate

daniel.chong@seumlaw.com