



INTRODUCTION OF ADDITIONAL COMPANY ENTITIES: *HAPJA JOHAP* AND *YUHAN CHAEKIM HOESA*

I. BACKGROUND

The Korean Commercial Code (KCC) is the main body of laws in Korea relating to business and business enterprises in Korea. The recent amendments to the KCC include the addition of two new types of business entities: *hapja johap* (literally translated as “partnership association”) and *yuhan chaekim hoesa* (literally translated as “limited liability company”) to meet the increasing demands of investors and dynamics in Korea’s economy. The additional business entities were created to provide greater flexibility in the formation, operation and dissolution of a business enterprise to promote commerce while providing limited liability protection to investors. With the additional legal entities, the business entities that will be recognized under the amended KCC will be as follows: (i) *johap* (association), (ii) *hapmyung hoesa* (general partnership), (iii) *hapja hoesa* (limited partnership), (iv) *yuhan hoesa* (limited company), (v) *chusik hoesa* (joint stock company), (vi) *hapja johap* and (vii) *yuhan chaekim hoesa*. The main features of a *hapja johap* and *yuhan chaekim hoesa* are summarized below.

II. *HAPJA JOHAP*

A *hapja johap* is a business entity similar to a limited partnership recognized in the United States. The main features of a *hapja johap* are as follows:

- A. A *hapja johap* can be established upon an agreement among (i) one or more managing partners who agree to bear unlimited liability in the partnership and (ii) one or more limited partners, whose liability is limited to their capital contribution in the partnership to make joint capital contributions to conduct business together. A *hapja johap* is not a separate legal entity per se and, instead, is recognized as an “association” authorized by law to engage in business (similar to *johap*).
- B. The major matters required to be included in the limited partnership agreement are as follows: (i) the purposes of the partnership, (ii) the name of the partnership, (iii) the individual names of the partners, (iv) the contribution amounts of each partner, (v) ratio allocation of profits and losses of

the partnership among its members, (vi) matters regarding assignment of limited partners' interests in the partnership and (vii) matters relating to the distribution of residual assets among its partners. Once a *hapja johap* is established, certain information stipulated in the KCC (e.g., above items (i) to (iv)) must be registered with the court having jurisdiction over the *hapja johap*.

- C. The managing partner has a fiduciary duty to the other partners to manage and represent the partnership with care and loyalty. However, the managing partner may not sell, assign or transfer of her interest in the partnership to a third party without the unanimous consent from all partners.
- D. Unless otherwise permitted in the partnership agreement, a limited partner must refrain from managing or representing the partnership and making capital contributions in the form of credit or labor services. A limited partner is largely a passive investor with a right to review the management of the partnership and its financial matters. A limited partner may sell, assign or transfer her interest in the partnership to a third party in accordance with the limited partnership agreement. Further, the outgoing partner's right and obligations in the partnership will bind the incoming partner.
- E. Tax issues for a *hapja johap* are not settled under the current tax law; however, many believe double taxation should not arise as a *hapja johap* is legally treated as an association and, thus, should allow pass-through tax treatment.

III. YUHAN CHAEKIM HOESA

A *yuhan chaekim hoesa* is viewed to be similar to a limited liability company in the United States or akin to a *godo kaisha* in Japan. This entity was intended to provide flexibility in the composition of the organization and recovery of investments while providing limited liability protection against creditors of the company up to their invested amounts. Summarized below are the main characteristics of a *yuhan chaekim hoesa* ("LLC").

- A. The LLC can be established upon a capital investment by one or more persons and registration of its incorporation. Capital contributions can be made in any form, such as cash or other tangible assets except those that are difficult to determine the reasonable market value (e.g., services or credit). In case of an LLC, although it is not subject to Article 600 of the KCC which is the basis of prohibition of issuance of corporate bonds for *yuhan hoesa*, whether the LLC can issue bonds is still up for debate as it continues to be subject to Article 604 Section 1 of the KCC, which states that a joint stock company (i.e., *chusik hoesa*) shall not change the company form to *yuhan hoesa* unless the redemption of bonds has been completed..
- B. There is no minimum capital requirement to establish an LLC. While a manager is required (may be a person or a legal entity), there is no mandate to have directors or an auditor. The LLC may also

change its legal business status to a *chusik hoesa* (joint stock company) with the unanimous consent of all of the members.

- C. A member is allowed to transfer her interests in the LLC to a third party with the consent of other members or if permitted in the LLC's Articles of Association. Unless otherwise stated in the Articles of Association, a member may obtain a refund of her investment in the LLC by exiting at the end of the LLC's fiscal year after the member has given at least six (6) months' prior notice to the LLC. Thus, if the company's fiscal year is the calendar year, the member must submit notice to the company by June and leave by December. However, if the amount refunded to the exiting member exceeds the capital surplus of the LLC, the LLC must provide notice to its creditors informing them that objections may be submitted to the member's exit and must also provide the objecting creditors adequate security if there is a possibility that the refund may damage such creditor.
- D. Tax issues pertaining to a *yuhan chaekim hoesa* have not been determined yet; however, many believe the LLC will be treated similarly to a *chusik hoesa* (corporation), including double tax.

IV. EXPECTED EFFECT

Hapja johap and *yuhan chaekim hoesa* offer additional options for investors to conduct their business in Korea as they provide flexibility in corporate organization and operation while limiting liability to the investors' capital contribution. While *chusik hoesa* (corporation) and *yuhan hoesa* (limited company) will likely remain the popular choice for larger companies, a *hapja johap* and *yuhan chaekim hoesa* will likely appeal to small-sized companies or investors with limited objectives. The utilization of the new company vehicles, however, will depend much on their tax treatment.

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