Enhancement of Audit Committee Requirements and Statutory Audit System

I. Enhancement of Audit Committee Requirements for Listed Companies

A. Audit committee under the current KCC

Under the current Korean Commercial Code ("KCC"), an audit committee is classified into two categories: (i) an audit committee that is required to be established ("Mandatory Audit Committee") for a listed company with total assets of KRW 2 trillion or more ("Large Listed Companies") and (ii) an audit committee established in lieu of a statutory auditor in accordance with a company's articles of incorporation ("General Audit Committee"). With respect to the composition of a Mandatory Audit Committee, the so-called "3 percent rule" applies (a rule established to prevent a shareholder holding more than 3% of the voting shares from exercising its voting rights -- that arises from voting shares which exceed 3% of voting shares -- in respect of decisions relating to the appointment of a member of an audit committee). With respect to the composition of a General Audit Committee, the "3 percent rule" does not apply.

Meanwhile, under the current KCC, although a listed company with total assets of KRW100 billion or more but less than KRW2 trillion ("Small Listed Company") is required to appoint one or more statutory auditors, an exception exists "in the case an audit committee is established pursuant to the KCC or other applicable laws." Based on the interpretation of the foregoing statutory provision, as Small Listed Companies are exempt from the legal requirement to appoint a statutory auditor by establishing either a Mandatory Audit Committee or a General Audit Committee, Small Listed Companies have avoided the requirement to appoint a statutory auditor by establishing a General Audit Committee which is exempt from the application of the "3 percent rule".

B. Amendments to the KCC

The legislative intent of the amendments to the KCC is to limit the application of the exception to the legal requirement to appoint a statutory auditor only to the case where "establishment of a Mandatory Audit Committee or the establishment of an audit committee pursuant to other laws." Consequently, the establishment of a General Audit Committee (in lieu of an auditor) for the purpose of avoiding the "3 percent rule" is prohibited. The provisions of the amended KCC relating to audit committees will become effective on April 15, 2012. As such, once the amended KCC takes effect, Small Listed Companies must either (i) appoint a statutory auditor or (ii) in lieu of a statutory auditor, establish a Mandatory Audit Committee, and the application of the "3 percent rule" will be unavoidable.

II. Enhancement of Statutory Audit System

To promote the faithful execution of the duties of the statutory auditor, the amended KCC has new provisions that permit the statutory auditor to obtain assistance from expert advisors at the expense of the company. However, as the KCC does not specify details of such allowance, such as the scope of expert advisors or the limitation on costs and expenses, in case of a conflict between the interest of the statutory auditor and the company, a dispute may possibly arise.

* Correction Notice: Please note that we correct the following from the August 12, 2011 Legal Update Newsletter (Introduction of Additional Company Entities: Hapja Johap and Yuhan Chaekim Hoesa). We replace "In addition, the LLC is allowed to issue corporate bonds, which are not applicable to a yuhan hoesa (limited company)" with "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."

If there is any question regarding the above, please contact us as set out below.

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