

# PANORAMIC

# VENTURE CAPITAL 2024

Contributing Editor

Curtis L. Mo

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 LEXOLOGY

# Venture Capital 2024

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Quick reference guide enabling side-by-side comparison of local insights, including into the general role of venture capital and market conditions; parties and deal structures; process; due diligence; financial terms; control rights; public offerings and listings; sale transactions; disputes; foreign investment considerations; and recent trends.

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## MARKET AND PURPOSE

### General role and purpose

- 1 | How would you describe the role of venture capital in the financing markets in your jurisdiction?

Venture capital has been undoubtedly a primary driving force for start-up funding, with private equity funds gradually increasing for start-ups. Venture capital investors are actively investing in companies at pre-Series A or Series A and later stages prior to the pre-IPO financing stage.

Law stated - 24 February 2023

### Market conditions

- 2 | How would you describe the current market conditions for venture capital in your jurisdiction?

According to [market statistics](#) published by the Korean Venture Capital Association (KVCA), venture investment in Korea's start-up ecosystem increased consistently until the first half of 2022. In 2021, in particular, when the market was flushed with liquidity, the total amount of venture investment reached up to 7.68 trillion won, showing a massive 78.4 per cent increase compared to 2020. Venture investment in the first half of 2022 was 4.61 trillion won, showing a 24.3 per cent increase compared with the same period in the preceding year.

However, since the third quarter of 2022, investors' confidence has substantially declined due to the post-covid interest rate hike and currency fluctuations, which inevitably caused a sharp drop in venture capital investment. According to the KVCA data report, the amount of venture capital investment during 2022 was 12.61 trillion won, showing a 21.6 per cent decrease compared to 2021.

This downward trend continued through the first half year of 2023: according to the data report published by KVCA, the total amount of venture investment during the foregoing period was 4.44 trillion won, showing a 42 per cent decrease compared with the same period in 2022 and a 32 per cent decrease compared with the same period in 2021. However, there has been a meaningful recovery of the venture capital investment market in Korea during the latter half of 2023. While the data for the fourth quarter of 2024 is yet to be published, 3.24 trillion won (in total) of venture investments were made during the third quarter of 2024, presenting a substantial increase from 2.57 trillion won of venture investments made during the same period in the preceding year while falling short of 4.29 trillion won of venture investments made during the third quarter of 2021, which was the peak of the Korea venture capital market.

A large portion of venture capital investors in Korea are structured as investment funds. According to the KVCA's latest market statistics, venture investors underlying such funds in the cumulative first three quarters of 2023 consisted of general corporate entities (21.4 per cent), pension funds and mutual aid associations (5.1 per cent), government-contributed

funds of funds (13.8 per cent), individuals (10.9 per cent), other entities or associations and foreign investors (2.6 per cent), financial institutions (34.5 per cent), venture capital (11.8 per cent) and state-owned entities (13.8 per cent).

Law stated - 24 February 2023

## PARTIES AND DEAL STRUCTURES

### Issuers – typical profile

3 | How would you describe the types of companies, and their different stages of development, that typically receive venture capital investment in your jurisdiction?

Target companies in Korea's venture capital investment market are mostly 'stock companies' as defined under the Korean Commercial Code (KCC) because:

- a corporate entity that wishes to undergo an IPO in Korea is required to be a stock company as defined under the KCC; and
- this type of entity is much preferred in most M&A transactions.

While venture capital funds in Korea have different investment preferences in terms of target companies' stages of development, we have frequently seen their investments in pre-Series A or Series A and later rounds prior to the pre-IPO financing.

Law stated - 24 February 2023

### Issuers – domicile and company structures

4 | Are there any preferred or required legal domicile or company structures for issuers in venture capital transactions?

Many start-ups and early-stage companies in Korea prefer being located in Seoul or the Seoul Metropolitan Area (eg, Pangyo) due to ease of transportation, accessibility to investors and talent attraction, but some are domiciled in regional metropolitan cities such as Busan, Daejeon and Daegu. Legal domicile is not required under Korean laws, and there is no preferred or required company structure for issuers in venture capital transactions.

Law stated - 24 February 2023

### Investors – typical profile

5 | How would you describe the types of investors that make venture capital investments, including by stage of company development, in your jurisdiction?

Accelerators are actively engaging in venture investments from seed to pre-Series A round, using their own capital or through funds. Following pre-Series A funding, venture capital



funds are major players in start-up investments, and thereafter private equity or securities firms invest in companies at the pre-IPO stage.

On the other hand, we are recently witnessing a growing trend of financial institutions (eg, banks) participating in venture capital investment. In addition, funds formed by state-owned entities for the purpose of assisting small and medium enterprises (SMEs), such as the Korean Credit Guarantee Fund and the Korea Technology Finance Corporation, are making investments through extending loans to start-ups typically at Series B or earlier rounds. In January 2023, Korea's Ministry of SMEs and Startups announced that funds of funds with a total size of 280 billion won will be formed to make venture investments in less popular industries and market segments.

Over the past few years, strategic investors are increasing their investment in start-ups. Such investors primarily target start-ups relevant to their business goals and broadly participate in early-stage financing (eg, Series A) to pre-IPO fundraising.

Law stated - 24 February 2023

### Investors – structures

6 | How are venture capital investors usually structured and does their structure affect their investment approach or terms?

A large portion of venture capital investors in Korea are structured as investment funds. Since such funds are generally subject to certain periods of maturity, their venture capital transactions typically include terms allowing a secondary sale of their interest in target companies to a third party, and assignment of contractual rights and obligations to such potential purchaser.

Law stated - 24 February 2023

### Seed financings

7 | What structures and types of investments are typically used for seed-stage investments in your jurisdiction?

When making seed-stage investments, venture capital investors in Korea tend to relatively prefer investing through the acquisition of common shares of a target company (as opposed to the acquisition of preferred shares for later round investments). In many seed-stage transactions, contractual terms tend to be more issuer-friendly than those commonly used by venture capital funds.

Law stated - 24 February 2023

### Early-stage and later investments

8 |

What structures and types of investments are typically used for early-stage and later investments, following seed-stage investments, in your jurisdiction?

For early-stage and later investments, venture capital investors generally prefer investing through the acquisition of redeemable convertible preference shares (RCPSs) than common shares. This structure provides investors with several exit protections; for example, although a redemption right is seemingly of less importance because, under the KCC, a company can only technically redeem its shares if it has profits available for dividends, investors can still circumnavigate this requirement by requesting the company to convert its paid-in capital in excess of par into the 'profits available for dividend' and thereafter having a general meeting of shareholders to approve the conversion. Moreover, investors in most cases require the inclusion of anti-dilution protection or conversion price re-fixing (linked to per share price at an IPO) in their RCPS investment terms for the purpose of safeguarding the value of their investments.

Another type of early-stage investment, a simple agreement for future equity (SAFE), was introduced in the venture capital investment market in 2020 and has been increasingly used by venture capital investors. According to the statistics published by the Ministry of SMEs and Startups, there were 53 cases of SAFE investment transactions in the first half of 2022, a significant increase from 23 cases in the first half of 2021.

Law stated - 24 February 2023

## PROCESS

### Term sheets

9 | Do parties normally use term sheets? If so, what is normally covered in such term sheets?

Yes. Term sheets used in venture capital transactions in Korea generally include the following items:

- type of stock;
- investment amount;
- issue price (per share) and pre-money valuation;
- shareholder rights:
  - redemption yield;
  - redemption period;
  - preferred return;
  - duration of preference share (before conversion to common share);
  - voting right;
  - conversion right and conditions (including refixing);
  - liquidation preference;

- penalty upon contractual breach (ie, indemnification or put option);
- use of proceeds;
- employee stock ownership plan pool;
- allocation of expenses incurred for investment; and
- exclusivity.

Law stated - 24 February 2023

## Documentation

- 10 | What are the standard documents for a venture capital transaction, and who prepares them? Are there popular forms for such documentation in your jurisdiction?

Parties generally enter into a share subscription agreement that contains most of the terms included in a shareholders' agreement for a typical equity investment transaction. The share subscription agreement is normally prepared by the lead investor, but in some cases an issuer proposes an initial draft. In most cases, parties negotiate based on a standard contract form frequently used by venture capital funds.

Law stated - 24 February 2023

## Key steps and timing

- 11 | What is the normal process and timing of venture capital investments in your jurisdiction?

Venture capital investments in Korea are generally initiated through two routes:

- start-ups circulate investor relations materials for venture capital investors' review; or
- venture capital funds approach a certain target company to propose investment.

Investors then commence a due diligence exercise based on more comprehensive materials about the company and propose a term sheet in accordance with their due diligence findings. After the term sheet is negotiated and finalised, venture capital funds go through their internal approval process. If the investment committee approves the investment, parties execute a share subscription agreement and the deal closes after certain conditions are satisfied. The entire process of venture capital investment generally takes two to three months, but it could take shorter or longer depending on the specifics of the investment.

Law stated - 24 February 2023

## Closing conditions

## 12 | What closing conditions are common in venture capital transactions?

While more specific closing conditions may be included in accordance with the findings of investors' due diligence exercise, the following conditions are frequently found in typical venture capital transactions in Korea:

- compliance with pre-closing covenants and undertakings;
- truth and accuracy of representations and warranties;
- no proceedings, laws or governmental order prohibiting or restricting the closing;
- acquisition of relevant regulatory approvals (if applicable);
- acquisition of third-party approvals required for the transaction (if applicable);
- completion of any requisite corporate procedures for the issuance of new shares (eg, amendment of the articles of incorporation, board resolution and so on); and
- no material adverse change.

Law stated - 24 February 2023

### Multiple closings

## 13 | Are venture capital transactions ever divided into multiple closings? If so, how and why?

An issuer often has multiple closings with several investors in the same round of financing. In some cases, this results from differences in the time incurred by each investor for its internal approval process. Issuers sometimes prefer completing the first closing if certain target amount of investment commitment is achieved and afterwards explore additional investments. In a multi-closing round, if required, a shareholders' agreement is entered into among initial investors first, and then subsequent investors enter the agreement by executing a joinder. However, a shareholders' agreement is in fact not generally entered into between investors in most venture capital transactions in Korea. Rather, shareholders' rights are typically stipulated in a share subscription agreement, which often contains terms harmonising rights (eg, tag-along, first refusal or director appointment) of different investors.

In rare cases, multiple closings take place for one investor's venture capital. One example is an investment urgently required by an issuer while running out of cash for its operation. In this case, the investor often requests certain milestones to be achieved by the issuer before additional funding is made.

Law stated - 24 February 2023

## DUE DILIGENCE

### Legal due diligence

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## 14 | What legal due diligence is typically undertaken for venture capital transactions, and what specialists are typically involved?

Parties often do not hire an external legal adviser for small-size venture capital transactions. In such cases, investors' in-house legal counsel review investment documents with existing shareholders, material business contracts, any legal proceedings involving an issuer or any other important materials. Investors nonetheless may request an external legal adviser's opinion on certain specific issues.

In larger venture capital investments, parties tend to seek relatively more assistance from external legal advisers. When external legal advisers conduct due diligence, the scope of due diligence includes the aforementioned materials as well as permits and authorisations relating to the target's business, labour and HR issues and assets and liabilities.

Law stated - 24 February 2023

### Critical due diligence areas

## 15 | What are normally critical areas of due diligence focus or red flags in venture capital transactions?

In our experience, a common issue that often arises relates to the terms and conditions of existing shareholders' investment. For example, we have seen several cases in which the conversion price adjustment or other anti-dilution protection for existing shareholders has already been triggered without the issuer being aware, resulting in the new investor's anticipated shareholding (on a fully diluted basis) being different from the actual shareholding.

Moreover, start-ups often face regulatory issues, including obtaining requisite permits and authorisations, as they generally attempt to differentiate their business model or products and services from those of existing players. While these regulatory issues are hardly noticed in very early stages of business development, they can become critical once companies step into growth stages, so investors are recommended to conduct a close review of them.

Law stated - 24 February 2023

### Other due diligence

## 16 | What other types of due diligence are commonly undertaken in venture capital transactions?

Venture capital investors often conduct financial due diligence together with legal due diligence. In addition, they carry out interviews with potential customers targeted by an issuer to review and analyse whether its business has sufficient value. Such feasibility analysis is directly conducted by venture capital investors, rather than through external counsel.

Law stated - 24 February 2023

## ECONOMIC TERMS

### Valuation and pricing

- 17 | How is the company valuation and investors' purchase price usually determined in venture capital transactions?

If a target company's business has already entered the growth stage, investors usually refer to valuation of similar companies on a public exchange or under private M&A transactions in determining the target company's valuation. However, for early-stage companies, investors put more importance on founders' experience. For example, a start-up established by a serial entrepreneur tends to be valued relatively highly by venture capital investors.

Law stated - 24 February 2023

### Option pool

- 18 | What do investors typically require for option pools or equity incentive arrangements in connection with venture capital transactions?

Under the Korean laws, an issuer that is qualified as a 'venture company' can grant its employees stock options to purchase up to 50 per cent of the total issued and outstanding shares (this threshold is however limited to 10 per cent for a non-venture company). However, as investors want to limit an option pool, for early-stage companies the option pool generally ranges from 10 per cent to 20 per cent of the total issued and outstanding shares following the applicable investment. Later stage companies are often required to maintain an even lower threshold.

In some cases, investors prohibit an issuer from granting stock options or any other equity incentives with per share prices lower than that of the shares issued to such investors. On the contrary, in other cases, a start-up might request investors to allow it to grant options at a discounted per share price, as stock options are substantially important incentives to hire or maintain key talents for the company.

Law stated - 24 February 2023

### Dividends, distributions and redemptions

- 19 | What are the normal provisions governing dividends, distributions, redemptions or other profit distributions in venture capital transactions? Are there any legal limits thereon in your jurisdiction?

Preferred shareholders are normally entitled to preferential dividends based on a certain fixed percentage of par value or issue price of their shares. If the dividend rate applicable to common shares exceeds that applicable to preferred shares, shareholders holding

'participating' preferred shares will receive the same amount of dividends payable to common shares. On the other hand, dividend-related terms are not usually specified for common shares. Despite the foregoing, under many venture capital transactions in Korea, companies are rarely required to pay out a certain amount of annual dividends.

Under article 462 of the Korean Commercial Code (KCC), dividends can be payable within the limit of a company's profits available for this purpose, calculated by the formula set out below. Each item under this formula should be based on the numbers presented in the company's balance sheet for the preceding year.

Profits available for dividend = net asset – total capital – capital reserve – earned surplus reserve – earned surplus reserve that should be accumulated as of the settlements of accounts – unrealised profits

Redemption rights are frequently attached to preferred shares. Investors holding preferred shares are entitled to redeem them at a certain redemption price (eg, issue price of preferred share \* (1 + IRR X per cent per annum)) for which they can guarantee a certain amount of return on their investment. However, since the company bears the redemption obligation only to the extent of profits available for dividend discussed above pursuant to article 345(1) of the KCC, if profits available for dividend are not sufficient at the time of the exercise of the redemption right, investors will not be able to redeem their shares.

In lieu of redemption, the company can acquire its shares from its investors. This is, however, subject to the restrictions under article 341 of the KCC that:

- any consideration payable to investors for such acquisition should be within the limit of profits available for dividend; and
- the company is required to make offers to every shareholder on the same terms and conditions.

Therefore, the aforementioned legal limits may prevent the investors' exits through dividend, redemption or share repurchase, so in consideration of such undesirable situation the investors often request put-option, tag-along or drag-along rights as alternative exit strategies and have interested parties of an issuer (eg, founder or largest shareholder), as well as the issuer, equally bear the same obligations upon the exercise of these rights by the investors.

**Law stated - 24 February 2023**

## Company sales and liquidations

**20** | How are venture capital investments treated in portfolio company sales or liquidations?

Venture capital investors holding preferred shares are given a liquidation preference over shareholders of common stock so that these investors can recover their investment as well as certain preferential return.

In the event of the sale of the target company, as investors are contractually entitled to a tag-along right in most cases of venture capital transactions, they will be able to exit at the same share price with the largest shareholder by exercising the tag-along right.

Law stated - 24 February 2023

### Anti-dilution protection

21 | What anti-dilution protections are typically built into the terms of venture capital securities?

An issuer is generally required to obtain consents from venture capital investors in the event of the issuance of new shares, and investors normally have a pre-emptive right with respect to the issuance of new shares. Further, if venture capital investors subscribe to convertible preferred shares for their investment, they usually request such shares to be subject to a conversion price adjustment so that their conversion prices can be adjusted if the issuer issues new shares to a third party at a per share price lower than the investors' conversion price as at the applicable time. We have seen both full-ratchet and weighted-average anti-dilution protections, but the former appears to be more popular in the Korean venture investment market.

Law stated - 24 February 2023

### Future investments

22 | What pre-emptive or pro rata investment rights do venture capital investors usually receive?

Investors are usually entitled to exercise pre-emptive rights to new shares to the extent that they can maintain their shareholding percentage (which are based on either the total issued and outstanding shares or a fully diluted basis) as of the date of the board resolution for the issuance of new shares.

Law stated - 24 February 2023

### Insider sales

23 | What rights do venture capital investors normally have over insider sales of securities of portfolio companies?

Venture capital investors typically have an interest in making sure that founders and other key personnel maintain their shareholding in the target company, given the important role insiders play in the growing portfolio company. As preventative measures, investors often:

- contractually prohibit founders or other interested parties from transferring their shares to a third party without the investors' consent; or



- secure tag-along rights so that investors can exit with the founders or other interested parties.

Law stated - 24 February 2023

## CONTROL RIGHTS

### Voting rights

**24** | What voting rights, including veto or consent rights, do venture capital investors normally have as shareholders of their portfolio companies? Do they typically have special voting or consent rights as shareholders?

Venture capital investors have voting rights to the matters specified under the Korean Commercial Code (KCC) as general shareholders, as well as certain other matters listed below that are normally included in contracts for venture capital transactions:

- amendment of the articles of incorporation;
- change in capital structure, issuance of equity-linked securities or grant of stock options;
- merger, split, transfer of business, acquisition, bankruptcy or rehabilitation petition or liquidation;
- purchase or sale of material assets, loan extension, provision of collateral or borrowing;
- engagement of any business different from what was specified in the business plan proposed to investors at the time of their investment or suspension of material business;
- related party transactions (often subject to 'ordinary course of business' carve out);
- incorporation of a corporate entity;
- dividend distribution;
- appointment or change of an external auditor;
- appointment or removal of a representative director, director, statutory auditor or major officer;
- use of proceeds for purposes other than those that have been agreed between investors and an issuer; and
- IPO.

An investor usually secures a veto right to the foregoing matters, but in some cases the affirmative vote of a certain percentage of all shareholders or each series of shareholders are deemed to constitute approval by all shareholders or the series of shareholders, as applicable.

Law stated - 24 February 2023

## Board rights

**25** | What rights to representation on the board of directors or at meetings of the board of directors of portfolio companies do venture capital investors typically receive?

A venture capital investor is often entitled to appoint one director. If multiple investors are participating in the same round of financing, the lead investor of the round generally receives the right to appoint a director. Further, in later financing rounds, new and existing investors determine which investor is to hold the director appointment right.

Law stated - 24 February 2023

## Board protections

**26** | What fiduciary duties and liability protections normally apply to investor directors in your jurisdiction? Do directors typically have special voting or consent rights?

There is no special treatment granted to investor directors. Investor directors, just as other directors, have fiduciary duties to an issuer. Nonetheless, parties often agree to include contractual provisions that require the company to indemnify and hold harmless investor directors against any losses arising out of their service in office as directors (except for losses arising out of gross negligence or wilful misconduct).

We have seen a few cases where contractual arrangements are incorporated to limit the ability of the board of directors to approve certain matters without the consent of the investor directors. However, such provision is generally viewed as ineffective under the KCC.

Law stated - 24 February 2023

## Financial reports

**27** | What rights to financial reporting or company access do venture capital investors normally receive?

Venture capital investors are entitled to information rights to receive annual, semi-annual and quarterly financial statements and notifications before or after the occurrence of material events relating to an issuer. Further, it is common for investors to request rights to inspect the company's accounting procedures or business operations while the scope, method and cost allocation of such inspection vary case by case. In a few cases, venture capital investors have secured the right to appoint a chief financial officer to improve the financial stability of early-stage companies.

If venture capital investment imposes certain restrictions on the use of proceeds, investors often request their rights to receive a record of the use of proceeds and inspect on the earlier of the date all the investment proceeds were used or a certain period after their investment to determine whether an issuer has adequately used the investment proceeds in accordance with the purposes specified in the contract.

Law stated - 24 February 2023

## PUBLIC OFFERINGS AND LISTINGS

### Securities law requirements

- 28 | What are the securities law requirements in your jurisdiction for venture capital investors to sell their securities in the public markets?

If venture capital investors intend to make a public offering of their securities to 'general' investors, the issuer must file a securities registration report with the Data Analysis, Retrieval and Transfer System operated by the Financial Supervisory Service, whereas an offering to 'institutional' investors is not subject to the foregoing requirement. However, unless the company undertakes an IPO, the former is very rarely seen in the market.

Law stated - 24 February 2023

### Registration and listing rights

- 29 | What registration rights, listing rights or other rights do venture capital investors normally receive?

When investing in early-stage companies, venture capital investors frequently request to include contractual provisions that require an issuer and its founder group to use best efforts to list the company on a stock exchange, and to provide the investors with a put option against the company or the founder group in case the company does not proceed with an IPO even though all listing requirements have been satisfied.

Investments in later stage companies often accompany stronger IPO-related requirements – in addition to the above, the company may be obligated to complete an IPO by a certain date, or the concept of a 'qualified-IPO' may apply to the company's IPO-related obligations.

Law stated - 24 February 2023

### Other resale rights

- 30 | What other resale rights in the public markets do venture capital investors usually receive?

None.

Law stated - 24 February 2023

## COMPANY SALES (M&A)

### Standard sale structures

**31** | What are the standard structures or methods for venture capital portfolio companies to be sold in your jurisdiction?

In most cases, venture capital portfolio companies are sold through private deals, while there are occasionally M&A auction deals for start-ups. In private sales, private equity firms or strategic investors approach a founder to proceed with an M&A transaction, and during the process the founder discusses and negotiates with the existing venture capital investors.

Investors generally sell their existing shares to a potential purchaser in connection with the above-described M&A type of transaction, but we have also seen several cases in which purchasers both purchase the existing shares and subscribe for newly issued shares.

Law stated - 24 February 2023

### Role of investors

**32** | What is the role of venture capital investors in a portfolio company sale? Do they have rights to force or block a company sale?

Venture capital investors in Korea often hold consent rights to a founder's sale of their shares in a portfolio company as well as a tag-along right. That is, upon the sale of the company, investors can either block the sale through their veto rights or require the founder to sell their shares together. Even so, under Korean market practices, it is rare for venture capital investors being entitled to rights to force a company sale.

Law stated - 24 February 2023

### Post-closing protections

**33** | What post-closing matters or protections do venture capital investors typically obtain, for example to address ongoing company sale indemnities or director tail liabilities?

Upon a portfolio company sale, venture capital investors are reluctant to bear any indemnification obligations with respect to representations and warranties relating to the company. Since venture capital investors are structured as investment funds in Korea, following the closing of the portfolio company sale, the proceeds need to be promptly distributed to their underlying investors. Furthermore, such fund-type investors do not usually heavily engage in the business operations of their portfolio company.

Regarding a director's liability, an indemnification clause is usually included in venture capital transactions in Korea, and the clause generally remains effective even following the sale of a portfolio company. Given that legal disputes surrounding directors' actions or non-actions are not relatively common in Korea, we view that director tail liabilities are of low risk. However, as sellers in the sale of their portfolio company, investors occasionally

require adding to a share purchase agreement a provision that a potential purchaser should not initiate a lawsuit against investors in connection with investor directors' liabilities.

Law stated - 24 February 2023

## LEGAL AND REGULATORY CONSIDERATIONS

### Disputes

- 34** | What types of disputes typically arise in venture capital transactions and how are disputes commonly handled? What provisions normally govern disputes, including choice of governing law, choice of forum and alternative dispute resolution mechanisms?

Consent rights held by multiple investors frequently trigger disputes following venture capital investors' investment in a portfolio company. For instance, disputes may arise when a company attempts to push through a transaction or an investment opposed by venture capital investors. However, in cases where other shareholders vote in favour of a transaction, whereas a minority of venture capital investors are against it, the dispute is less likely to develop into legal proceedings because venture capital funds are usually not willing to bear a reputation risk as they are continuously engaging in the start-up financing market.

Other than the foregoing, we have occasionally seen arguments between venture capital investors and founders of their portfolio companies in relation to exit strategies (eg, IPO), but these also rarely develop into legal disputes.

In domestic venture capital transactions, Korean laws are mostly chosen as the governing law and parties prefer resolving disputes through Korean courts. Even in cross-border venture capital investments, foreign investors frequently accept Korean laws as the governing law in consideration that they are better suited to investments targeting Korean companies. For small-size cross-border investments, the Korean courts are still a popular choice for dispute resolution, but foreign investors tend to prefer arbitration at a third country as the size of investment increases.

Law stated - 24 February 2023

### Regulatory consents and filings

- 35** | What regulatory consents, notifications and filings are required for all investors in venture capital transactions in your jurisdiction? Are there ownership restrictions?

Under article 11 of the Monopoly Regulation and Fair Trade Act, a merger filing must be submitted to and approved by the Korean Fair Trade Commission (KFTC) after the closing of the transaction for an investment resulting in the acquisition of 20 per cent or more (15 per cent or more for a listed company) of the total outstanding shares of a Korean company in which:

-

either an investor or a target company has total assets or annual sales turnover of 300 billion won or greater (including the assets and sales of any affiliates); and

- the other party has total assets or annual sales turnover of 30 billion won or greater (including the assets and sales of any affiliates), as of the most recent fiscal year end.

However, for any such transaction that is subject to the foregoing merger filing requirement, if the total assets or annual sales turnover of an investor or a target company (including those of its respective affiliates) are equal to or exceed 2 trillion won, the merger filing must be made and approved by the KFTC before the closing of the transaction.

On the other hand, where an issuer is a financial institution, investors may be subject to the shareholding cap. Approval by the Financial Services Commission could be required if a transaction results in the change of the major shareholder. Other than these, no other regulatory restrictions are particularly applicable to the shareholding percentage of venture capital investors.

Law stated - 24 February 2023

## Foreign investment

**36** | What foreign investment restrictions and other domestic regulatory issues arise for venture capital investors based outside your jurisdiction?

Foreign venture capital investors are generally required to go through further regulatory procedures. Foreign investors are either required to file a securities acquisition report with a foreign exchange bank prior to their acquisition of shares issued by a Korean company, or they are required to file a foreign direct investment report, pursuant to the Foreign Investment Promotion Act, in case the investors are:

- investing 100 million won or more; and
- acquiring 10 per cent or more of the total issued and outstanding equity securities, or have the right to appoint a director.

Foreign venture capital investors are restricted from investing in a company engaged in [certain categories](#) of business in excess of certain shareholding percentages. However, the scope of such businesses is narrow, only including a few industries such as telecommunications, broadcasting, agriculture and power plants.

Law stated - 24 February 2023

## UPDATE AND TRENDS

### Key developments

**37** |

What are the most noteworthy current trends and recent developments in venture capital transactions in your jurisdiction? What developments are expected in the coming year?

In 2022, an appellate court of Korea made a ruling that it is unlawful to grant specific investors the right to veto major business operational matters of a company. As venture capital investors have been securing these types of consent or veto rights that relate to major business decisions of their portfolio companies, players in the venture capital market paid close attention to this case. In certain transactions, the companies made arguments that they would not include provisions relating to investors' consent or veto right in a share subscription agreement or a shareholders agreement as such provisions are held not to be valid under the foregoing ruling.

However, the above appellate court decision was overturned by the Supreme Court of Korea in July 2023. The Supreme Court concluded that, if there are special circumstances that justify the company's differentiated treatment of shareholders by granting superior rights (eg, consent/veto rights regarding certain operational matters of the company) to certain shareholders, such rights are valid. The Supreme Court also provided the factors that should be considered in deciding whether any such differentiated treatment is permissible, stating that:

consent/veto rights granted to specific shareholders should be acknowledged so long as it (i) was necessary for the company to raise funds, and the grant of such consent/veto rights (ii) is inevitably required to induce investments from such shareholders and (ii) does not cause harm to other shareholders by giving power to such shareholders to check against the management of the company.

In the foregoing case, the Supreme Court nonetheless concluded that indemnification for the company's breach of the consent or veto right granted to certain shareholders should not be excessive, such as allowing such shareholders to recover their investments in the company, while the amount of relevant damages can be agreed upon between the company and the shareholders through a share subscription agreement or a shareholders agreement. The Supreme Court maintained the same position in another case in July 2023, where it upheld that the contractual agreement by which the company is required to return the investor's investment upon a breach of the company's obligations is invalid as such agreement goes against the principle of shareholder equality. These decisions by the Supreme Court reaffirm the existing legal principle under which a penalty put option granted to an investor against the company to which it subscribes new shares is not legally valid, which must be therefore carefully considered by venture capital investors when deciding an investment structure in Korea.

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