Financial regulatory changes in Korea

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Leakages of personal data and sales of defective financial products have led to various measures being adopted to strengthen the protection of personal information. We have seen the introduction of consumer protection regulations and the lowering of the ceiling on interest rates. In addition, significant amendments were introduced to the Financial Services and Capital Markets Act on August 29 2013 and the levels of interest in covered bonds finally saw the enactment of the Covered Bonds Act of Korea on April 15 2014. A summary of the relevant measures and legislation follows.

Personal data protection in the financial sector

The Korean government announced measures to fight personal data leakage after the financial regulators confirmed that over 20 million users were affected by massive data leaks. These measures, mainly enforced against financial institutions, include the following:

a) Financial companies are permitted to only collect the necessary minimum personal information and store it for up to five years.

b) Resident registration numbers will be required only once in the first financial transaction and stored in an encrypted form.

c) Financial institutions will introduce a 'do-not-call' system under which registered customers can deny marketing calls. Customers will also be able to check whether their personal information is being used or shared legitimately by financial institutions.

d) The financial institutions' responsibility regarding data protection and security are to be raised. Punitive sanctions against those who fail to safeguard customer information are to be significantly strengthened.

e) All unnecessary personal information provided by financial institutions and information shared with their affiliates must be immediately deleted. Financial institutions will be required to establish a contingency plan for future data leak accidents.

Legislative bill on Financial Consumer Protection Act

Increasing adverse effects on consumers in the financial sector caused by information asymmetry and conflicts of interest between financial institutions and consumers have triggered the initiative by the Financial Service Commission (the 'FSC') to submit a bill for the Financial Consumer Protection Act to the National Assembly. The Financial Consumer Protection Act aims to protect financial consumers, expand both ex-ante and ex-post protective measures and adopt a 'functional regulation' approach whereby similar business types, rather than institutions, will be supervised by the same regulating bodies. The Financial Consumer Protection Act categorises financial products by their characteristics into (a) deposit-type products, (b) investment-type products, (c) guaranteed-type products and (d) loan-type products and classifies financial institutions into (a) direct sales institutions, (b) sales agents, and (c) advisory agencies. Relevantly, the FSC is currently contemplating the establishment of a new financial consumer protection authority, which is expected to deal with all matters relating to financial consumer protection.

Limitation on interest rates

There are two general laws that restrict the maximum lending interest rates: the Act on Registration of Credit Business, etc. and Protection of Finance Users (the "Credit Business Act") and the Interest Limitation Act. The amendments to these Acts took effect on April 2 2014 and July 15 2014 respectively.

The lending interest rate of the finance companies regulated by the amended Credit Business Act cannot be higher than 34.9% per annum, whereas the lending interest rate of individual lenders or finance companies not registered under the Credit Business Act cannot be higher than 25.0% per annum. Any interest rate, which is higher than the relevant cap will be null and void under the relevant Acts and the violators can be subject to criminal penalties.

The Financial Investment Services and Capital Markets Act

The amendment to the Financial Investment Services and Capital Markets Act (the 'Capital Markets Act') took effect on August 29 2013, introducing alternative trading systems and investment banking businesses and also revising provisions relating to sectors such as private equity funds, collective investment vehicles, public disclosures, unfair transactions and other special provisions on listing companies. Key changes are as follows.

For investment banking businesses, a securities firm must now hold equity capital worth W3 trillion or more and have a risk management system as well as an internal control system. Investment banking businesses can provide prime brokerage services to financial companies, pension funds, and hedge funds (both Korean and foreign). Further, investment banking businesses can also provide loans and payment guarantee.

For private equity funds, a general partner that wishes to establish a private equity fund must register with the FSC and satisfy certain registration requirements. Private equity funds and special purpose companies that are registered with the FSC must report to the FSC on the status of any borrowings and guarantees of debt.

As to special provisions relating to listed companies, a listed company can now give a range of estimated values of a merger rather than fixing such value without a range. Further, a listed company that wishes to issue stock, convertible bonds or bonds with warrants must first cancel the issuance of any unsubscribed portions. It cannot issue bonds with warrants if such warrants can be detached.

The Covered Bonds Act of Korea

The newly enacted Covered Bonds Act of Korea is expected to improve the housing loan market by providing financial institutions with a long-term stable funding source and fixed rate loans.

Covered bonds are debt securities backed by cash-flow generating pool of assets (a 'Cover Pool') provided by an issuer to the covered bondholders, such as mortgage loans, loan receivables secured by ships or aircrafts or public-sector loan receivables. Financial institutions with equity capital of at least W100 billion and a BIS ratio of greater than 10% are eligible as "qualified issuers" and can issue covered bonds.

For mortgage loans to be included in a Cover Pool, the loan-to-value ratio of each mortgage loan must not exceed 70%. Further, each mortgage loan must be secured by first priority residential mortgages and 30% of such mortgage loan must be fixed-interest rate loans. The total asset value of the Cover Pool should exceed 105% of the total outstanding amount of the covered bond.

A covered bond issuer must register the issuance plan and details of the proposed Cover Pool with the FSC. After registration, the issuer may issue covered bonds of up to the principal amount not exceeding 4% of the issuer's total assets at the end of the previous fiscal year.