



## CRIMINAL LAW

# Avoiding bae-im

Non-Korean companies acting in the country must protect themselves against criminal breach of duty



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Criminal breach of duty, or bae-im in Korean, is a typical crime on which owners, directors, officers or managers of corporations and businesses in Korea are frequently indicted. A person commits bae-im when he, in dealing with the affairs of another person, breaches his duty and obtains, or enables a third person to obtain, a pecuniary advantage through such breach, thereby causing a loss to the person to whom the duty is owed.

## Examples

While owners, directors and officers of Korean companies have been the subjects of most bae-im prosecutions, foreign companies doing business in Korea are not immune from being charged. Recent cases include the following:

- A chairman of a Korean conglomerate was indicted on the charge of bae-im for providing the conglomerate's buildings as security and instructing the conglomerate to provide joint and several guarantee for the purchase of a building for his own account; and
- A chairman of a Korean conglomerate was prosecuted for bae-im for paying too high a price when investing in a venture company and for investing in a venture company without proper consideration of the business and financial risks.

Acquisition of a company through a leveraged buyout (LBO) can give rise to bae-im in Korea. In a landmark case, a person established a special purpose company to acquire a target company, and the target company's real estate and other assets were provided as collateral for the loan taken out to finance the acquisition of the target company. The Korean Supreme Court ruled that the target company's director committed bae-im since no consideration was paid or provided by the acquirer to the target company for the use of the target company's assets as collateral for the loan. The court found that the target company suffered losses by providing the collateral without receiving an adequate quid pro quo, because it exposed itself to the risk of losing its assets upon default of the loan. In a series of rulings following the seminal case, the court has taken a position that not all LBO transactions utilising a target company's assets for acquisition financing constitute bae-im and facts should be analysed on a case-by-case basis.

## Legal definition of Bae-im

Bae-im is codified in Articles 355(2) and 356 of the Korean Criminal Code.

The elements of bae-im are: (i) a person owing a duty to another person or an entity or in a position within an entity to administer the business of the entity (ii) gains, or enables a third party to gain, a pecuniary advantage, which results in a loss to the entity to whom the duty was owed, (iii) in breach of his duty.

The court has interpreted the Criminal Code provisions in core precedents, giving clarity in their application. Among other things, according to the court, a person can be prosecuted for bae-im only if he or she is under a duty to administer the affairs of another person or corporate entity. In addition, the court held that the duties owed and the good-faith administration of those duties must be both typical and essential for the protection and management of the other person or corporate entity. As to the violation of duty, the court has taken an aggressive approach by holding that inaction or omission to act as well as action can constitute violation of duty. Further, the court made it clear that not only actual loss but also the risk of loss can fall within the definition of "loss" as it pertains to bae-im.

## Business judgment rule and bae-im

The crime of bae-im is typically committed in cases where (i) a company, without justification, extends a loan to or provides a guarantee in favour of its affiliate or another person without receiving sufficient security, (ii) a company acquires another company at an unjustifiably high price, (iii) a company sells at a low price or purchases at a high price material assets without justification, or (iv) a company makes an investment without fully considering the risk.

The Korean courts have applied the 'business judgment rule' as a defence to the charge of bae-im. Thus, a business manager would be found not guilty of bae-im if he can demonstrate that he (i) acted in good faith without any intention of obtaining personal advantage, (ii) made an informed decision, (iii) believed that his decision was in the interest of the company concerned, and (iv) made a decision in a prudent manner.

## Conclusion

Given the far-reaching implications of bae-im, it is advisable to obtain the advice of experienced Korean legal counsel before making an important business decision. Also, it is important to employ and follow best practices to benefit from the 'business judgment rule' defence.

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