

Announcement of the Draft Enforcement Decree to the Financial Consumer Protection Act

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The Financial Services Commission announced its proposal for the Enforcement Decree to the Financial Consumer Protection Act (the “Draft Enforcement Decree”) on October 28, 2020. The Financial Consumer Protection Act (the “FCPA”), which is scheduled to take effect on March 25, 2021, aims to combine provisions governing the protection of financial consumers that are scattered across different statutes and regulations into a single statute in order to enable the effective administration of the relevant provisions. Overall, the FCPA will apply stricter consumer protection standards than the existing rules and introduce new provisions relating to consumer rights, such as the right of a consumer to terminate contracts that violate the Sales Principles (as defined below) and the shifting of the burden of proof to financial companies in lawsuits concerning a violation of the “duty to explain.”

A large portion of rules that relate to the FCPA will be set out in subordinate legislation, including its Enforcement Decree. We discuss below some of the salient features of the FCPA and the relevant provisions of the Draft Enforcement Decree that were recently announced.

1. Main Provisions of the Draft Enforcement Decree to the Financial Consumer Protection Act

(a) Scope of Application of FCPA

- The FCPA reclassifies financial products and sales channels so that the same regulations apply to the same functions. All financial products listed in the FCPA and the regulations thereunder are reclassified into (i) deposit products, (ii) investment products, (iii) insurance products and (iv) loan products. All sales channels for financial products are reclassified into (i) direct sellers, (ii) sales agents and (iii) financial product advisors.
- The FCPA lists financial products offered by banks, securities companies, asset management companies, insurance companies, savings banks and specialized credit finance companies as being subject to the FCPA. The Draft Enforcement Decree expands the list by including products offered by credit unions, P2P lending companies and registered money lenders, thereby encompassing a large majority of the products offered by financial institutions.

(b) Internal Control Measures for Sellers of Financial Products

- The FCPA requires companies that engage in the sale of financial products to establish internal control standards

for consumer protection. This requirement is separate from the requirement to maintain internal control standards under the Act on Corporate Governance of Financial Companies.

- Specific requirements for internal control measures are now set forth in the Draft Enforcement Decree. The requirements mostly reflect those currently stipulated in the Guidelines for Financial Consumer Protection set forth by the Financial Services Commission. Most notably, such requirements include establishing and maintaining a division and appointing an executive officer dedicated to financial consumer protection, subject to certain exceptions to be set out in subordinate regulations.

(c) Detailed Requirements for Compliance with the Sales Principles

- The FCPA will expand the application of the six sales principles that currently apply to certain financial transactions to most categories of financial products. The six sales principles are (i) the principle of suitability, (ii) the principle of adequacy, (iii) the “duty to explain,” (iv) the prohibition on unfair practices, (v) the prohibition on misleading or unsolicited recommendations and (vi) the prohibition on false or exaggerated advertisements (the “Sales Principles”).
- The Draft Enforcement Decree contains specific guidance regarding the application of the Sales Principles and the obligations that follow. The relevant provisions are mostly consistent with the sales restrictions that were set out in different financial statutes, except for a number of provisions that have been newly introduced for the purpose of imposing stricter consumer protection requirements. For example, Table 4 of the Draft Enforcement Decree sets out detailed standards for determining what constitutes “suitability” and “adequacy” in order to prevent financial companies from conducting customer evaluations in a perfunctory manner, and requires financial companies to prepare evaluation reports based on such suitability and adequacy standards.
- The Draft Enforcement Decree also requires sellers of financial products to provide consumers with documents containing a general description of the product that is being purchased by the consumer, as well as documents setting out the key features of the product, in each case prepared by the seller (Article 14).
- Another obligation imposed on financial companies under the Draft Enforcement Decree is the obligation to notify consumers upon identifying certain events. Financial companies must promptly notify consumers of any violation of applicable laws or regulations or any potential risks that may cause a substantial loss to the consumer’s assets that are discovered through internal audits, complaints or inspections by the Financial Supervisory Service (Article 15(6)).

(d) Withdrawal Rights and Termination Rights

- The FCPA will also strengthen ex post financial consumer protection measures. Such measures include granting consumers withdrawal rights within a certain cooling-off period and termination rights in case of a violation of the Sales Principles.
- Specifically, the FCPA allows customers to withdraw subscription of financial products during a cooling-off period, in which case the sellers would need to make reimbursements to such customers. However, it was difficult to determine how such rules would apply to investment products, which, by their nature, do not guarantee capital

preservation. To address this concern, the Draft Enforcement Decree limits the application of withdrawal rights to highly complex fund products, highly complex discretionary investment agreements and trust agreements, provided, that in the case of monetary trust agreements, withdrawal rights are available only with respect to highly complex monetary trust agreements.

- The FCPA will also grant consumers termination rights pursuant to which the consumers will be able to unilaterally terminate a contract for a financial product if the seller had violated the Sales Principles without a reasonable excuse. The Draft Enforcement Decree provides for such right to be exercisable within the earlier of five (5) years of the date of the relevant financial contract and one (1) year of the date on which the financial consumer becomes aware of the violation. Financial companies are advised to prepare measures to address risks associated with the uncertainty arising from the extended period during which termination rights can be exercised by consumers.

(e) Standards for Penalty Imposition

- The FCPA will impose stricter penalties on non-compliant financial companies by increasing the threshold for administrative fines from KRW 50 million to KRW 100 million and allowing the imposition of penalties of up to 50% of the offender's revenues. In relation to such penalties, the Draft Enforcement Decree specifies what constitutes revenues for purposes of calculating penalties for each category of financial product as follows: (i) for deposit products, amounts received from the financial consumer in accordance with the relevant financial contract, (ii) for loan products, amounts paid to the financial consumer in accordance with the relevant financial contract plus any interest income, (iii) for insurance products, amounts received from the financial consumer as insurance premium and (iv) for investment products, amounts received from the financial consumer in accordance with the relevant financial contract plus profits derived from the management of such funds.

2. Timeline and Implementation

While the Draft Enforcement Decree sets out details that are not fully prescribed by the FCPA, it still delegates certain matters to subordinate regulations. The proposal for the subordinate regulations is expected to be announced in December of 2020. Financial companies should pay close attention to the contents of the FCPA and the subordinate regulations thereunder in order to implement appropriate policies and procedures in their sales and customer support practices.

Shin & Kim's Financial Regulation Group consists of top tier professionals, many of whom are able to draw experience from their tenures at regulatory agencies. Our attorneys are advising numerous leading financial institutions in Korea and will be able to guide you through the process of submitting comments to the Draft Enforcement Decree as well as implementing internal policies that will be required in order to comply with the FCPA.

For further information about the FCPA and related regulations, please contact the professionals listed below.

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