Issuance and Trading of Electronic Short-Term Bonds

The Act on Issuance and Trading of Electronic Short-Term Bonds and the Enforcement Decree thereunder (together, the "Act") come into force on January 15th, 2013. The objective is to implement the scope, registration methods and procedures for issuance and trading of electronic short-term bonds, together with other more detailed matters required for enforcement of the Act.

The Act was enacted to introduce the electronic short-term bond as a new financial instrument to take the place of commercial paper (CP) in the hopes of improving upon the inefficiencies of physical issuance and lack of information transparency associated with CP issuances. Electronically issued short-term bonds, which can be denominated in minimum units of KRW100 million (unlike their CP predecessors, which could not be divided into integral multiples) are expected to revitalize the capital market through freer tradeability.

Electronic short-term bonds do not have equity-related rights and must be issued in units of KRW 100 million or more, with maturities of not more than 1 year and must be unsecured. They are simplified forms of bonds with rights and obligations similar to CP, and are not subject to the Commercial Code requirements for maintenance of a bond register or convening of bondholders meetings due to their short-term nature. The representative director of a company may also be delegated the authority to issue electronic short-term bonds within an amount falling within the aggregate issuance ceiling determined by the company's board.

Electronic short-term bonds must be registered with the Korea Securities Depository (the "KSD"). No physical certificates are issued, and all issuances, transfers, pledges, entrustments or other dealings in the bonds can only be conducted and given effect by means of book-entry method; further, registrations are cancelled upon redemption of any principal and interest amounts. Purchasers may be entitled to rely on the KSD's register as evidence of bona fide acquisition, as the KSD is required to publish on its homepage the type, class, amount, terms of issuance and other information on matters relating to the electronic short-term bonds registered with the KSD.

To promote the smooth implementation of the new electronic short-term bond system, the Financial Services Commission (the "FSC") is considering an exemption of electronic short-term bonds with maturities of not more than 3 months from securities registration requirements through a partial amendment to its Regulations on Issuances and Disclosures of Securities; there is also some talk of extending such securities registration exemption to apply to electronic short-term bonds with longer maturities (e.g., 9 months).

A proposal to exempt withholding taxes on a significant portion of interest income earned on holdings of electronic short-term bonds has also been raised for consideration as a means to promote energetic trading of electronic short-term bonds.

It is anticipated that once electronic short-term bond trading systems are built into financial institutions and transactions between issuers and the institutional investors who provide capital funding are running smoothly, such systems will become a means to supplement secondary market call and repurchase transactions.

The enforcement of the Act through the Enforcement Decree signifies another important development in the implementation of systems for electronic or paperless securities in line with the 2004 amendments made to the Act on Issuance and Trading of Electronic Notes and the 2011 amendments to the Commercial Code to provide for an electronic securities registration system.

Nonetheless, due to difficulties in interpreting inconsistencies between the Act with the current securities law framework and systems regarding matters such as transfers, creation of security interests, registration requirements (for amounts in excess of exemption limits) and consolidations and splits of electronic securities, it is recommended that legal advice be sought.

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