

SOUTH KOREA

'Double derivative suits' by shareholders

By Hun Mook Lee

The Justice Ministry announced in February 2007 that it was planning to amend the Commercial Act to adopt a 'double derivative suit' system allowing shareholders of a parent company to file a law suit against directors of its subsidiaries for the purpose of strengthening shareholders rights and improving corporate governance. Currently the bill is a hotly disputed issue with businesses in harsh opposition to the amendment. The corporate sector has opposed the plan because more lawsuits will raise the financial burden on them.

Derivative suits by shareholders

Directors of a company who deliberately or through negligence cause harm to the company in violation of laws or article of incorporation shall be jointly and severally liable for the damages to the company. Any shareholder who owns no less than 1/100 of the total outstanding shares may demand in writing that the company file a suit against the directors to enforce their liability. If the company refuses or fails to file such a suit within 30 days from the date of the receipt of the demand, the shareholder who demanded the suit against the directors may immediately file such a suit on behalf of the company.

This derivative suit by shareholders was rarely used prior to the IMF financial crisis in Korea because most minor shareholders were unaware of the derivative suit and were not interested in legality of their company's business operation. However, as a many companies went into bankruptcy during the IMF financial crisis and, as a result, the value of their shares plunged or became valueless, minor shareholders have been seeking methods to recover damages caused by directors' misconduct and filed suits against directors who made up financial accounts.

Any shareholder who owns no less than 1/100 of the total outstanding shares may demand in writing that the company file a suit against the directors to enforce their liability. If the company refuses or fails to file such a suit within 30 days from the date of the receipt of the demand, the shareholder who demanded the suit against the directors may immediately file such a suit on behalf of the company

A Supreme Court case

In a case in which shareholders of a company brought a suit against directors of its subsidiary company, the Supreme Court (Supreme Court 2004. 9. 23. held 2003da49221) held that the double derivative suit allowing shareholders of a parent company to file a suit against directors of its subsidiary

company is not permitted in that a parent company and its subsidiary are independent and separate legal entities and shareholders who may file a suit against directors are limited to shareholders of the company to which the directors against whom a suit is brought belong, notwithstanding that the parent company holds all or a greater part of the outstanding shares of its subsidiary and the subsidiary incurred damages from its directors' misconduct.

Requirements for the double derivative suit

The Justice Ministry set up an adjustment committee in December 2006 including a number of corporate leaders as members to sooth the business sector. Under the committee's adjustments, a shareholder who owns no less than one percent of a parent company would be allowed to bring a suit against directors of a subsidiary for misconduct, but only if the parent company holds no less than 50/100 of the total outstanding shares.

The National Assembly is expected to review the above bill around May 2007.

Law Firm Pureun

28/F Samil Building
 Gwanchul-Dong 10-2
 Jongro-Gu, Seoul, Korea

Tel: (82) 2 775 1560

Fax: (82) 2 319 3900

Email: pureun@pureunlaw.com

hmlee@pureunlaw.com

www.pureunlaw.com