SOUTH KOREA

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Sale and purchase of equity and inter-company loan of foreign invested company

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The Foreign Investment Promotion Act (FIPA) was enacted in Korea in 1998 for the purpose of increasing foreign direct investment (FDI). Common forms of FDI include the acquisition of shares of a domestic company or a long-term loan to a foreign invested company. For an acquisition of shares by a foreign investor of a domestic company to qualify as FDI, the amount of investment should be at least KRW 100,000,000 and the foreign investor must own at least 10 percent of either the total equity ownership or the total number of voting shares. A long-term loan (maturity of five years or more) to a foreign invested company by a foreign parent company would also qualify as FDI. A loan with a maturity of less than five years from the foreign parent company or a loan from a non-related entity would not qualify as FDI.

A foreign investor must file a Foreign Investment Report with Invest Korea (KOTRA), Korea Business Centers of KOTRA, headquarters and branches of domestic foreign exchange banks, or branches of delegated foreign banks and obtain a certificate of completion of foreign investment report for the FDI.

Case study

In 2008, an overseas foreign investor establishes a 100 percent owned Korean subsidiary company (Korean Sub) by investing US$12,000,000 and obtains a certificate of completion of foreign investment report. In 2009, Korean Sub learns that to obtain a financial incentive benefit for seven years from a certain Korean public corporation, Korean Sub needs to have at least US$20,000,000 in FDI. Thus, in order for Korean Sub to qualify for the financial incentive benefit, in 2009, Korean Sub's foreign parent company makes a five year loan in the amount of US$8,000,000 to Korean Sub and obtains a certificate of completion of foreign investment report. After receiving the loan, Korean Sub receives the financial incentive benefit from the Korean public corporation for seven years (from 2009 to 2016).

In 2011, the overseas foreign investor decides to sell 100 percent of its shares in Korean Sub for US$9,000,000 (the fair market value) and its loan to Korean Sub for US$8,000,000. If the buyer is a foreigner, when it purchases the shares of Korean Sub and the loan to Korean Sub for US$17,000,000, the foreign buyer will be able to keep the seven year financial incentive benefit that Korean Sub received until 2016. When the foreign buyer acquires 100 percent of the shares of Korean Sub for US$9,000,000, it will be able to take over and assume Korean Sub's FDI amount of US$12,000,000, the amount that the foreign parent company invested in Korean Sub in 2008.

As a cautionary measure, it would be advisable for the foreign buyer to obtain a written confirmation from the Korean public corporation that the new foreign owner of Korean Sub would be able to keep the seven year financial incentive benefit after the purchase.

Conclusion

In order for the new foreign investor to maintain the same level of FDI of the Korean Sub it is acquiring, the foreign investor should acquire 100 percent of the Korean Sub and any long-term loan with a maturity of five years or more that the Korean company received from its foreign parent company. A purchase of any loan with a maturity of less than five years from the foreign parent company or a loan from a non-related entity would not qualify as FDI.

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