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## Press Release

December 30, 2008

### **Review of Indemnification Provisions for Financial Institution & its Officers**

#### **Background**

The government took a decisive step against the current financial difficulties by provisionally indemnifying financial institution and its officers after convening the Economy and Finance Policy Meeting earlier today. This measure will allow financial institutions to extend greater support to firms and others suffering from the credit freeze.

#### **Summary of Current Provisions**

##### **Sanctioning Authority**

The FSC has the authority to both suggest the dismissal of directors and executives from office and suspend their business duties while the FSS governor has the authority to issue warnings and caveats.

##### **Current Indemnification Provisions**

The 'Regulation on Examination and Sanctions against Financial Institution and its Officers' either suspends or renders a lighter sentence on financial institution and its officers in cases where extraneous circumstances outside of its control are recognized, including when loans become distressed as a result.

Regulation on Examination and Sanctions against Financial Institution and its Officers  
Article 23: Imposition of Lighter Sanctions against Financial Institution and its Officers

A financial institution and its officers may be subject to a lighter sanction or discharged from a sanction against the occurrence of bad loans, etc. in cases of the following items and other inevitable circumstances.

1. Case that it was caused by general financial and economic environment's regression;
2. Case recognized as in accordance to the necessities of the national industrial policy;
3. Case that it was recognized that adequate credit analysis and sufficient review of the business plan were performed in advance;
4. Case that it was caused by the change of the asset classification standards;
5. Case that the overall rating of evaluation for the management status is raised by more than one grade in comparison with the preceding period with outstanding management; or
6. Case found to have been caused by inevitable internal or external circumstances.



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## **Lapses in the Current Indemnification Provisions**

The main provisions of the current indemnification, including Clause 1 and Clause 2 of Article 23 above, are open to broad interpretation and severe in sanctions against financial institutions and its officers, limiting the inducement on financial institutions to be active and voluntary in extending capital support. Neither do the main provisions specify the indemnitee with precedents, which renders clear indemnification judgment difficult in times of examination and sanctions. The current system also triggers mandatory sanctions with even the slightest breach in protocol.

## **Provisional Indemnification of Financial Institutions & Its Officers**

Indemnification, on a provisional basis, will have reviewed the existing indemnification provisions given the unprecedented nature of the global economic crisis with “caused by general financial and economic environment’s regression” (Article 23 Clause 1) being interpreted as 1) adding liquidity to SMEs that are on the Fast Track program, 2) aiding joint efforts of the Council of Creditor Financial Institutions and others at corporate restructuring, and 3) support extended independently by financial institutions to SMEs that have been otherwise sound except for a temporary shortage in liquidity, among others.

In regards to the “cases recognized as in accordance to the necessities of the national industrial policy” (Art. 23 Clause 2), specification of the indemnification provisions will include cases of capital support for “national industrial policy,” such as economic policy direction in 2009.

During the course of conducting examinations, only those financial institution and its officers not liable for clear intentional misconduct, gross negligence, embezzlement, and fraud, among others will be indemnified.

A thorough review, from initial examination to sanctioning review and decision, will either grant or withhold indemnification to a director or executive. If the key provisions are determined to have been met during an examination, the head examiner will use his/her discretion in indemnifying the potential indemnitee without preamble.

During the sanction review and decision, the indemnitee will be indemnified and held harmless from claims by instituting and making the filing the ‘Indemnification Application Form’ and the ‘Examiner’s Opinion’ both mandatory. The Indemnification Application Form, which is submitted by a director or executive of a financial institution, offers an opportunity to claim indemnification or give deposition before either the Sanctioning Review Committee or the FSC. On the other hand, the Examiner’s Opinion will be a means for an examiner to refute an applicant’s claim for indemnification by submitting findings.



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To prevent moral hazard in financial institutions, the provisional indemnification will stay in force until December 31, 2009 although indemnification will continue to be in effect during examinations that commence after the sunset date. Its extension will be reviewed if the worsening economic conditions are continuing at the time.

### **Future Plans**

The FSC/FSS will presently make available the 'Indemnification Guidelines' and notify financial institutions of the review while encouraging them to devise their own guidelines. A director and executive level seminar will be held to disseminate the indemnity provisions to working level employees. The seminar will seek the support of financial institution and its officers and encourage the use of the Guidelines to raise its effectiveness in the field.

#### Contact Persons:

Song Byung Kwan  
Deputy Director  
Financial Policy Division  
Financial Services Commission  
(02) 2156-9716

Hwang Seung Soo  
Associate Director  
Enforcement Review Office  
Financial Supervisory Service  
(02) 3786-7802

Lee Bum-Yoal  
Associate Director  
International Cooperation Department  
Financial Supervisory Service  
(02) 3786-7910