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## Press Release

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September 27, 2011

### REVISION OF ENFORCEMENT DECREE OF FSCMA APPROVED AT CABINET MEETING

#### **BACKGROUND**

The proposed revision of *the Enforcement Decree of the Financial Investment Services and Capital Markets Act* (FSCMA), aimed at introducing home-grown hedge funds (tentatively named “specialized private equity funds”) to Korea’s capital markets, was approved at the Cabinet meeting on Tuesday, September 27, 2011.

#### **KEY CONTENTS OF THE REVISION**

##### **I. Creation of Hedge Funds**

1. The scope of hedge fund investors will be extended to individuals with risk-taking capability. (Article 271-2①)

Currently, investments in private equity funds are allowed only to a limited number of “qualified investors” such as financial firms and pension funds. However, in order to provide more diverse investment opportunities, the revision will allow individuals who can invest KRW 500 million or more to join a hedge fund.

2. The revision will bring about greater autonomy and creativity in asset management. (Article 271-2①②, Article 80⑥)

(1) The requirement that private equity funds should invest more than 50% of their investments into companies under restructuring programs will be abolished so that hedge funds can invest in a wider range of assets such as securities, derivatives, and commodities.

(2) Restrictions on leverage\* and derivatives trading\*\* will be eased so that hedge funds can employ more diverse investment strategies such as short selling and leverage.

\* Limits on leverage will be eased from 300% of fund assets to 400%.

\*\*Investments in derivatives, currently limited to 100% of fund assets in estimated maximum losses, will be allowed up to 400%, equivalent to restrictions currently applied to general private equity funds.

3. A new category, “hybrid asset funds,” will be created for approval of hedge fund operations. Asset managers, securities firms and investment advisory firms that meet requirements\* in equity capital, track record and expert fund managers will be given approval for hedge fund operations.



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(i) Hedge funds under the category of “hybrid asset funds” (3-14-1)

- (Scope of investment products) “hybrid asset funds” with virtually no restrictions on investment products
- (Minimum equity capital) KRW 6 billion

(ii) Track record

- asset managers with funds and assets under management more than KRW 10 trillion, securities firms of which equity capital is more than KRW 1 trillion, investment advisory firms with trusted assets more than KRW 500 billion

\* Further detailed requirements will be specified in regulations on financial investment business

(iii) Expert human resource

- More than three fund managers with experience in hedge fund operations home and abroad

4. Supervision and surveillance on fund operations will be strengthened. (Article 271-2④⑤⑥)

In line with global discussions on strengthened financial regulations, hedge fund operators will be required to meet strengthened reporting obligations corresponding to their enhanced autonomy in operations.

\* Fund operators will be required to report to authorities on operational strategies, types of assets in investment, and leverage and derivative trading positions on a quarterly basis.

## II. Revision of Regulations on Prime Brokers

1. Regulations on Chinese Walls (Article 50① i, ii, iv)

Prime brokers will be allowed to deal with both trading and brokerage business and trust business within one department. However, in principle, prime brokerage service unit should be separated from other business units within a securities firm in order to avoid conflicts of interest.

2. Prime brokers will be allowed to extend (i) credit loans and (ii) securities-collateralized loans to hedge funds. (Article 69②③)

3. Regulations on prime brokers' custody and management businesses of fund assets (Articles 54ii(f), 85v)

(1) In order for prime brokers serving hedge funds to engage in other prime brokerage



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services such as securities lending, transactions between hedge fund assets under their custody and management and their own assets will be exceptionally allowed.

- (2) It will be allowed for prime brokers to entrust part of their custody and management businesses to other trust business providers such as banks and securities finance companies.

### **FUTURE PLAN**

The FSC will ensure regulatory reforms as planned so that we can see the first Korean hedge fund within this year.

The revision of the Enforcement Decree of FSCMA will be enforced immediately after public announcement, expected to be made in early October.

Also, the revision bill on the FSCMA which we already made a legislative notice on July 27, will be submitted for parliamentary approval in the upcoming regular session of the National Assembly.

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