

## FSC REFORMS LARGE SHAREHOLDING REPORTING RULES

The FSC plans to amend large shareholding reporting requirements under the so-called 'the 5% rule' in an effort to support institutional investors' shareholder activities.

### **BACKGROUND**

The 5% rule is intended to ensure fairness and transparency in the securities market by disclosing information about concentration of shareholdings in listed companies. Under the 5% rule<sup>1</sup>, a person who holds 5% or more of the equity securities of a listed company or who thereafter changes its holdings by 1% or more in the company must file a report with the FSC and the KRX within five days from the date of such changes. The reporting deadline is extended for institutional investors whose shareholding purpose is not intended to exercise influence over the company's management. They are also allowed to submit a simple report.

As institutional investors increasingly engage in shareholder activities with the adoption of the stewardship code<sup>2</sup>, there are calls for reforms to the 5% rule. Growing shareholder activism in regard with a company's dividend policy or corporate governance makes it difficult to draw a clear line between activities with the purpose of 'exercising influence over the management' and those without such purpose. Institutional investors are concerned that their shareholder activities might be led to unintended violation of the 5% rule, as the scope of "exercising influence over the management" under the current rule is defined broadly and ambiguously.

Against this backdrop, amendments are intended to clarify the scope of shareholder activities to "exercise influence over the management" and apply differential reporting requirements according to shareholding purpose.

### **AMENDMENT PROPOSAL**

#### **1. CLARIFICATION ON THE SCOPE OF EXERCISING INFLUENCE OVER THE MANAGEMENT**

The scope of shareholder activities intended to exercise influence over the management, subject to the requirement of a detailed report within five days, is to be clarified and narrowed. Followings are to be exempted from such strict requirement as they are deemed with no intention to exercise influence over the management:

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<sup>1</sup> Article 147 of the Financial Investment Services and Capital Markets Act (FSCMA)

<sup>2</sup> As of end-July 2019, 100 institutions adopted the stewardship code.

- Exercise of shareholder rights against unlawful acts by a company or its executives under the Commercial Act (e.g. the right to injunction against unlawful acts or the right to demand dismissal of an executive officer, etc.)
- Shareholder activities by public pension funds to change the articles of incorporation in accordance with pre-released principles to improve corporate governance
- Shareholder activities in regard with a company's dividend policy.
- Expression of shareholders' opinion or intention

Exercising *de-facto* influence over the management (e.g. dismissal of an executive officer, shareholders' proposal for M&A) is regarded as "activities to exercise influence over the management," still subject to the requirement of detailed reporting within five days.

## **2. DIFFERENTIATION OF REPORTING REQUIREMENT BY SHAREHOLDING PURPOSE**

Shareholder activities without the purpose of exercising influence over the management, currently allowed to file a simple report, will be subdivided into two categories: 'simple investment' and 'general investment' activities. They will be subject to differential reporting requirements.

- **Simple investment** activities are limited to cases in which shareholders exercise their rights guaranteed regardless of shareholding ratio. They will be subject to a minimum level of reporting requirements.
- **General investment** activities are cases in which shareholders do not intend to exercise influence over the management but actively engage in shareholder activities – e.g. changing dividend policy or strengthening qualification for auditors. Compared to 'simple investment' activities, stricter reporting requirements will apply to 'general investment' activities.

## **3. SPECIAL EXEMPTIONS TO PUBLIC PENSION FUNDS**

Reporting requirements are to be eased to public pension funds, given that in they are subject to eased reporting requirements under the current rule in the case of shareholdings not intended to exercise influence over the management.

## **SCHEDULE**

The FSC proposed amendments to the Enforcement Decree of the Financial Investment Services and Capital Markets Act, open for public comments from September 6 to October 16. The amended 5% rule is expected to take effect in the first quarter of 2020.

## HOW THE 5% RULE WILL BE AMENDED

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<Current >

Shareholding purpose	Intention to exercising influence over the management	No intention of exercising influence over the management
Shareholder activities	- activities to exercise 'de-facto' influence over the management (e.g. shareholder proposals to appoint or dismiss executive officers)	- Other activities
Reporting Requirements	- 5-day deadline - detailed reporting	- (general investors) monthly, simple reporting - (public pension funds) quarterly, simple reporting



<Amended >

Shareholding purpose	Intention to exercising influence over the management	No intention of exercising influence over the management	
		'General' investment	'Simple' investment
Shareholder activities	- activities to exercise 'de-facto' influence over the management (e.g. shareholder proposals to appoint or dismiss executive officers)  - <b>exemption: activities in regard with dividend policy and corporate governance</b>	- active shareholder activities with 'NO' intention of exercising influence over the management (e.g. shareholder proposals in regard with executive pay, dividend payout )	- shareholder's right guaranteed regardless of shareholding ratio (e.g. voting right, preemptive rights to acquire new shares issued by a company)
Reporting Requirements	- (general investors) 5 day-deadline, detailed reporting - (public pension funds) 5 day-deadline, simple reporting	- (general investors) 10 days, simple reporting - (public pension funds) monthly, simple reporting	- (general investors) monthly, simple reporting - (public pension funds) quarterly, simple reporting

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