

MEASURES TO IMPROVE PROTECTIONS FOR GENERAL SHAREHOLDERS IN IPO OF SPLIT OFF SUBSIDIARY

The FSC introduced a plan to improve the rights and interests of general shareholders in IPOs of split off subsidiaries in order to help restore fairness and trust in the capital markets and strengthen investor protections.

BACKGROUND

With some companies recently deciding to split off rapidly growing portions of their business and went ahead with IPO of split off subsidiaries within a short period of time, the issue of general shareholders incurring losses has become problematic as their shareholder rights are stripped away and stock prices for the parent company tend to decline. Unlike in a spin off, shareholders of the parent company in a split off are not allocated with stocks of a split off subsidiary and therefore they have no shareholder rights over the split off company. There is also a study suggesting that the valuation of the high growth split off business section is not necessarily reflected in the valuation of parent company stocks.¹

Especially, the fact that the rights of general investors who have been opposed to the split off decision are not adequately protected has presented an ongoing problem which has also been closely related to the so-called Korea discount phenomenon. As an equity interest, a stock's worth largely consists of a right to participate in the decision making process and a right to make a claim on present and future profits. However, in a capital market where these two principles are not properly observed, it will be difficult for investors to have high levels of confidence.

Therefore, as one of the key policy tasks of the new administration for restoring fairness and trust in capital markets, the financial authorities have prepared the following measures to improve the rights and interests of general shareholders in IPO of split off subsidiaries after months of engaging in discussions with experts and relevant stakeholders.

KEY DETAILS

I. STRENGTHEN DISCLOSURE

Companies planning to carry out a split off of their business should disclose specific purpose of split off (e.g. business restructuring, sale, listing, etc.) and investor

¹ Korea Capital Market Institute, Apr. 2022.

protection measures through their material information report (within three days after board decision for split off). In particular, if there are plans for a post-split off IPO of a subsidiary, disclosure should be made on expected schedule, etc. and if there are any changes to the IPO plan, a corrective disclosure should be filed.

II. INTRODUCE THE RIGHT TO REQUEST STOCK PURCHASE

Shareholders of listed companies who have been opposed to the company's split off decision will have the right to request that the company purchase his/her shares. Shareholders who voted against the split off decision at a general meeting for deciding the prospects of a split off can sell their shares at a price² determined prior to the split off set in motion.

III. BOLSTER LISTING REVIEW PROCESS

When companies plan to list their subsidiaries within five years after the split off, the Korea Exchange (KRX) will review the parent company's efforts at protecting general investors, and an IPO will be restricted if the parent company's efforts are found to be insufficient. This enhanced listing review process will also apply to companies that have completed a split off of a subsidiary within five years even before the revision to the KRX listing standards takes place. In addition, there will be detailed suggestions about specific shareholder protection measures³ that companies can choose as well as examples of insufficient cases⁴ on the KRX's listing guidebook, thereby increasing predictability for companies and ensuring implementation of effective shareholder protection measures.

EXPECTATION

The three-levels of safeguards are expected to form the basis upon which businesses give an adequate consideration for the rights and interests of general shareholders in the process of pursuing a split off of a subsidiary.

(FOR BUSINESS) Through disclosure and communication with shareholders, businesses should actively explain that their split off plan will help improve the value of the company and are aligned with the rights and interests of general shareholders. In the case that companies cannot obtain support and agreement

² Under the article 165(5)-3 of the Capital Markets Act, when exercising the right to request a purchase of stocks of a listed company, purchasing price is determined through an agreement between the shareholder and the company. → If no agreement is reached, market price (an arithmetic mean of the weighted average price of stock for two months, one month and one week each prior to the day before the board decision for split off) will be applied according to the Article 176(7)-3 of the Enforcement Decree of the Capital Markets Act. → If there is still no agreement on this, a petition can be filed to the court for determining a purchasing price.

³ e.g. (a) Offering dividends-in-kind (with parent company's holding of subsidiary stocks) to shareholders of parent company or providing opportunities to exchange parent company's stocks with subsidiary's stocks and (b) distributing growth profits to general shareholders of parent company through increased dividends and buybacks (apart from these, a variety of other shareholder protection measures can be considered through communication with shareholders.)

⁴ e.g. (a) When no disclosure has been made regarding the split off plan, purpose and shareholder protection measures through corporate governance structure report, etc. related to the split off or IPO, (b) when there is a failure to comply with the shareholder protection measures that had been indicated in disclosure through corporate governance structure report, etc. related to the split off or IPO and (c) when there is a failure to consider the problem that had been raised in the process of communicating with general shareholders without a reasonable cause.

from general shareholders, pursuing a split off of a subsidiary may in effect become difficult.⁵

(FOR GENERAL SHAREHOLDER) General shareholders will be provided with sufficient information about what led to the company management's decision on its split off plan as well as the expected effects of the business split off and use this information for decision making at a general meeting of shareholders, etc. When there is a split off decision against investors' own decisions, general shareholders can actively seek loss recovery by exercising the right to request stock purchase.

(POST-SPLIT OFF IPO PROCESS) In addition, the KRX will work to ensure the effectiveness of investor protections in the process of post-split off IPO of subsidiaries by seeking a comprehensive review on whether companies have diligently carried out relevant investor protection measures and whether they have properly handled investor protection issues that may have arisen during the IPO process.

FURTHER PLAN

The financial authorities will immediately carry out follow-up measures to ensure prompt implementation of the plan which aims to restore trust in capital markets and protect investors. Authorities will work to complete revisions to the corporate disclosure form and the KRX listing standards until October this year. Regarding the introduction of the right to request stock purchase, authorities aim to finish making regulatory improvements within this year as the revised bill for the Enforcement Decree of the Capital Markets Act becomes available for public comment starting from today (September 5).

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For press inquiry, please contact Foreign Media Relations at fsc_media@korea.kr.

⁵ When a majority of general shareholders are opposed to the split off plan and the split off results in a drop in company valuation (stock price), general shareholders may exercise their right to request stock purchase at a large scale.