ASEAN+3 BOND MARKET GUIDE

REPUBLIC OF KOREA

MAY 2018

ASIAN DEVELOPMENT BANK

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ADB recognizes "Korea" as the Republic of Korea.

In this report, international standards for naming conventions—International Organization for Standardization (ISO) 3166 for country codes and ISO 4217 for currency codes—are used to reflect the discussions of the ASEAN+3 Bond Market Forum to promote and support implementation of international standards in financial transactions in the region. ASEAN+3 comprises the Association of Southeast Asian Nations (ASEAN) plus the People's Republic of China, Japan, and the Republic of Korea.

The economies of ASEAN+3 as defined in ISO 3166 include Brunei Darussalam (BN; BRN); Cambodia (KH; KHM); the People's Republic of China (CH; CHN); Hong Kong, China (HK; HKG); Indonesia (ID; IDN); Japan (JP; JPN); the Republic of Korea (KR; KOR); the Lao People's Democratic Republic (LA; LAO); Malaysia (MY; MYS); Myanmar (MM; MMR); the Philippines (PH; PHL); Singapore (SG; SGP); Thailand (TH; THA); and Viet Nam (VN; VNM). The currencies of ASEAN+3 as defined in ISO 4217 include the Brunei dollar (BND), Cambodian riel (KHR), Chinese renminbi (CNY), Hong Kong dollar (HKD), Indonesian rupiah (IDR), Japanese yen (JPY), Korean won (KRW), Lao kip (LAK), Malaysian ringgit (MYR), Myanmar kyat (MMK), Philippine peso (PHP), Singapore dollar (SGD), Thai baht (THB), and Vietnamese dong (VND).

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Foreword

The Asian Development Bank (ADB) is working closely with the Association of Southeast Asian Nations (ASEAN) and the People's Republic of China, Japan, and the Republic of Korea—collectively known as ASEAN+3—to develop local currency bond markets and facilitate regional bond market integration under the Asian Bond Markets Initiative to strengthen the resilience of the region's financial systems.

Thanks to the efforts of member governments, local currency bond markets in ASEAN, the People's Republic of China, and the Republic of Korea have grown rapidly, with the total outstanding amount of bonds reaching more than USD10 trillion in 2016. Despite this remarkable development, intraregional investment in bond markets has remained subdued. As ADB has estimated that developing Asia will need to invest USD26 trillion from 2016 to 2030 (or USD1.7 trillion per year) in infrastructure for its continued growth, it is critical to mobilize the region's vast savings for the enormous investment needs. As an essential platform for such resource mobilization, the financial markets in ASEAN+3 need to be more harmonized and integrated. Also, the regional efforts should support developing member countries at early stages of market development.

The ASEAN+3 Bond Market Forum (ABMF) was established with the endorsement of the ASEAN+3 Finance Ministers in 2010 as a common platform to foster the standardization of market practices and harmonization of regulations relating to cross-border bond transactions in the region. As an initial step, ABMF published the ASEAN+3 Bond Market Guide in 2012, which was welcomed as the first official information source offering a comprehensive explanation of the region's bond markets.

Since publication of the ASEAN+3 Bond Market Guide, bond markets in the region have continued to develop. ABMF recognizes the need for revisions to the guide to reflect these changes, though it is never an easy task to keep up with rapid changes in the markets. This report is an outcome of the strong support and kind contributions of ABMF members and experts, particularly from the Republic of Korea. The report should be recognized as a collective good to support bond market development among ASEAN+3 members. It is our hope that the revised ASEAN+3 Bond Market Guide will facilitate further development of the region's bond markets, contribute to increased intraregional bond transactions, and promote efficient allocation of capital within the region.

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Economic Research and Regional Cooperation Department

Acknowledgments

The Korea Bond Market Guide was first published in 2012 as the initial output of Phase 1 of the ASEAN+3 Bond Market Forum (ABMF).[1] Across the region, domestic bond markets, including the Korean bond market, have experienced tremendous development over the past 5 years. Now in Phase 3, ABMF would like to share, in the public domain, information on these developments by publishing an update to the Korea Bond Market Guide.

The ABMF Sub-Forum 1 team—comprising Satoru Yamadera (Principal Financial Sector Specialist, Asian Development Bank, Economic Research and Regional Cooperation Department); Kosintr Puongsophol (Financial Sector Specialist, Asian Development Bank, Economic Research and Regional Cooperation Department); and Asian Development Bank consultants Shigehito Inukai and Matthias Schmidt—would like to stress the significance and magnitude of the contributions made by ABMF national members and experts for the Republic of Korea, including the Financial Services Commission and Financial Supervisory Service, the Korea Capital Market Institute, Korea Exchange, the Korea Financial Investment Association, as well as the Korea Securities Depository. These policy bodies, regulatory authorities, and market institutions generously gave their time for market visit meetings, discussions, and follow-up. They have also reviewed and provided inputs on the draft Korea Bond Market Guide over the course of ABMF Phase 3.

The Korea Bond Market Guide could not have been completed without the support of the ASEAN+3 Bond Market Forum Korea, a group comprising the above members as well as other market experts and volunteer supporters, who on numerous occasions made a significant effort toward the completion of this Bond Market Guide.

No part of this report represents the official views or opinions of any institution that participated in this activity as an ABMF member, observer, or expert. The ABMF Sub-Forum 1 team bears sole responsibility for the contents of this report.

May 2018

ASEAN+3 Bond Market Forum

[1] ASEAN+3 refers to the 10 members of the Association of Southeast Asian Nations (ASEAN) plus the People's Republic of China, Japan, and the Republic of Korea.

Abbreviations

ABCP	asset-backed commercial paper
ABMF	ASEAN+3 Bond Market Forum
ABS	asset-backed securities
ADB	Asian Development Bank
AMBIF	ASEAN+3 Multi-Currency Bond Issuance Framework
ASEAN	Association of Southeast Asian Nations
ASEAN+3	Association of Southeast Asian Nations plus the People's Republic of China, Japan, and the Republic of Korea
BOK	Bank of Korea
BQS	Bond Quotation System
CRA	credit rating agency
CRPA	Corporate Restructuring Promotion Act
ETF	exchange-traded fund
FB	FreeBond (system)
FSC	Financial Services Commission
FSCMA	Financial Investment Services and Capital Markets Act
FSS	Financial Supervisory Service
ICSD	international central securities depository
IDM	inter-dealer market
IOSCO	International Organization of Securities Commissions
KDB	Korea Development Bank
KOFIA	Korea Financial Investment Association
KONEX	Korea New Exchange
KRW	Korean won (ISO code)
KRX	Korea Exchange
KSD	Korea Securities Depository
KSFC	Korea Securities Finance Corporation
KTB	Korea Treasury Bond
LPB	License and Permit Bonds
MOSF	Ministry of Strategy and Finance
MSB	Monetary Stabilization Bond
MTM	mark-to-market
MTN	medium-term note
NHB	National Housing Bond
OTC	over-the-counter
QIB	Qualified Institutional Buyer
SF1	Sub-Forum 1 of ABMF
SMEs	small and medium-sized enterprises
SPC	special purpose company
SRO	self-regulatory organization
SRS	Securities Registration Statement
SSF	Single Submission Form
USD	United States dollar

USD1 = KRW1,071.00 as of 28 February 2018[2]
(Official foreign exchange reference rate by Seoul Money Brokerage Services)

[2] For current foreign exchange rates, please see http://www.smbs.biz/Eng/ExRate/TodayExRate.jsp

I

Overview

A. Formation and Early Development of Bond Market in the Republic of Korea

The Government of the Republic of Korea issued its first bond, a National Foundation Bond, in 1950 to promote economic growth and finance post-war reconstruction. As market and economic conditions have changed over time, the bond market has intermittently seen dominance by either corporate bonds or government bonds such as Grain Bonds, Monetary Stabilization Bonds (MSBs), and Korea Treasury Bonds (KTBs), among others.

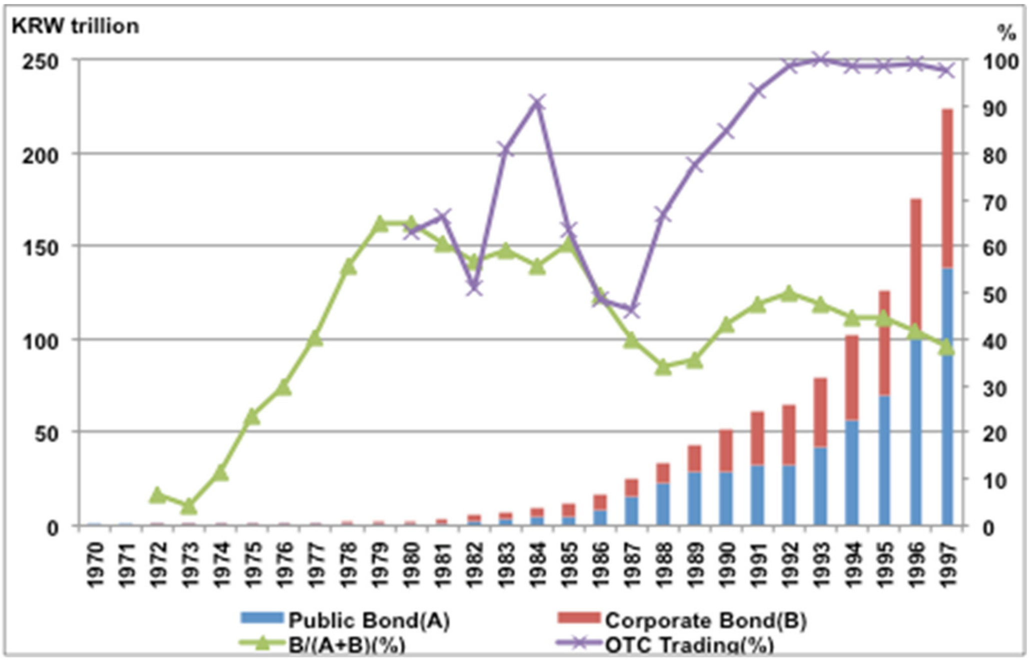
The issuance of National Foundation Bonds, which had led the bond market in the early 1950s, was subsequently suspended due to growth in the national debt and fiscal soundness concerns. In the late 1960s, government agencies and public institutions that had been established under special laws started to issue special bonds in their place.

The government, which was trying to raise private sector funds for economic development, put forward a capital market development plan at the same time. The Capital Market Promotion Act was enacted in November 1968, setting up a base for the formation and development of a market for publicly offered corporate bonds. The publicly offered corporate bond market, which was established in 1972, grew rapidly on the basis of (i) institutional support, including firm commitments, payment guarantees from financial institutions, and mandatory listing on a securities exchange; and (ii) policy measures for spurring demand such as the establishment of investment trust companies. Publicly offered corporate bonds dominated the bond market in the Republic of Korea until the mid-1980s.

As a result, corporate bond issuance, as measured by bonds listed on the securities exchange, rose from nearly KRW4.7 billion during the first year after its inception to KRW1,001.4 billion in 1979, accounting for 65% of total listed bonds outstanding at that time. Figure 1.1 shows the outstanding amount by bonds by type (public and corporate bonds), the proportion of corporate bonds, as well as the proportion of over-the-counter (OTC) trading in the market since the inception of the corporate bond market up until the 1997/98 Asian financial crisis.

A corresponding change also occurred in the secondary bond market. With the securities market at a nascent stage, the government strived to concentrate securities transactions on the exchange. OTC bond trading was prohibited by the Securities and Exchange Act of 1962. However, bonds were allowed to be traded in the OTC market in the 1970s when the rise in corporate bond issuance led to the introduction of repurchase agreements (repos) as a means of using corporate bonds as collateral to obtain financing. As not only repos but also bonds were actively traded in the OTC market, OTC trading became widespread practice. From the second half of the 1980s onward, OTC transactions were predominant in the secondary bond market.

Figure 1.1: Korean Bond Market Expansion Prior to the 1997/98 Asian Financial Crisis



Sources: Korea Exchange, Korea Financial Investment Association.

In the mid-1980s, concerns arose over inflation due to a pick-up in foreign capital inflows, which resulted from growth in the current account surplus and a subsequent increase in market liquidity. MSBs, which are short-term bonds designed to protect against inflation, showed a huge increase, reaching 69.4% of new government bond issues and 45.6% of total listed bonds and notes in 1998. MSBs effectively changed the structure of the bond market, which had been dominated by corporate bonds, and came to dominate the market.

However, as the current account surplus declined in the 1990s, the bond market again focused on corporate bonds. Guaranteed bonds continued to prevail in the corporate bond market, but guarantee providers were more diverse than before. Concurrently, Korean firms' growth, supported by the domestic economic expansion and their improved financial structure, led to an increase in the issuance of non-guaranteed corporate bonds. Furthermore, the bond market became more diverse with increased issuance of bonds with embedded options such as convertible bonds.

In the mid-1990s, 7-year and 10-year National Debt Management Fund Bonds were issued to lengthen the maturity of government debt. More than 90% of corporate bonds, which still dominated the market at that time, had a 3-year maturity.

On the infrastructure side, the Bank of Korea (BOK) launched BOK Wire in December 1994, a real-time gross settlement system for high-value payments typical in the bond market. BOK Wire introduced a guarantee of settlement finality and effectively eliminated settlement risk. Also, with the establishment of the Korea Securities Depository (KSD) in 1994, the use of KSD became mandatory for bond settlement. The efforts to modernize the payment and settlement systems laid the foundation for the emergence and growth of the repurchase (repo) and securities lending markets within the next few years.

The Government of the Republic of Korea had initially allowed nonresidents to invest directly in the bond market, starting with bonds issued by small and medium-sized enterprises (SMEs) in 1994, and planned to gradually expand the scope of eligible bonds. However, such plans were accelerated with the full opening of the Korean bond market to foreign investment following the 1997/98 Asian financial crisis as almost all restrictions on foreign investment in bonds were lifted under measures designated by the International Monetary Fund.

B. After the 1997/1998 Asian Financial Crisis

In the aftermath of the 1997/98 Asian financial crisis, the bond market underwent dramatic changes and emerged structurally different in the post-crisis period. First, the market shifted its focus from corporate bonds to government bonds, centered on KTBs. Second, corporate bonds accounted for a decreasing portion of the bond market, while non-guaranteed bonds replaced the previously dominant guaranteed bonds in the corporate bond market. Third, the bond market became more diverse with the advent of asset-backed securities (ABS) and structured securities whose underlying assets consisted of bonds. A rise in the share of foreign investment in the bond market also resulted from increased market diversity.

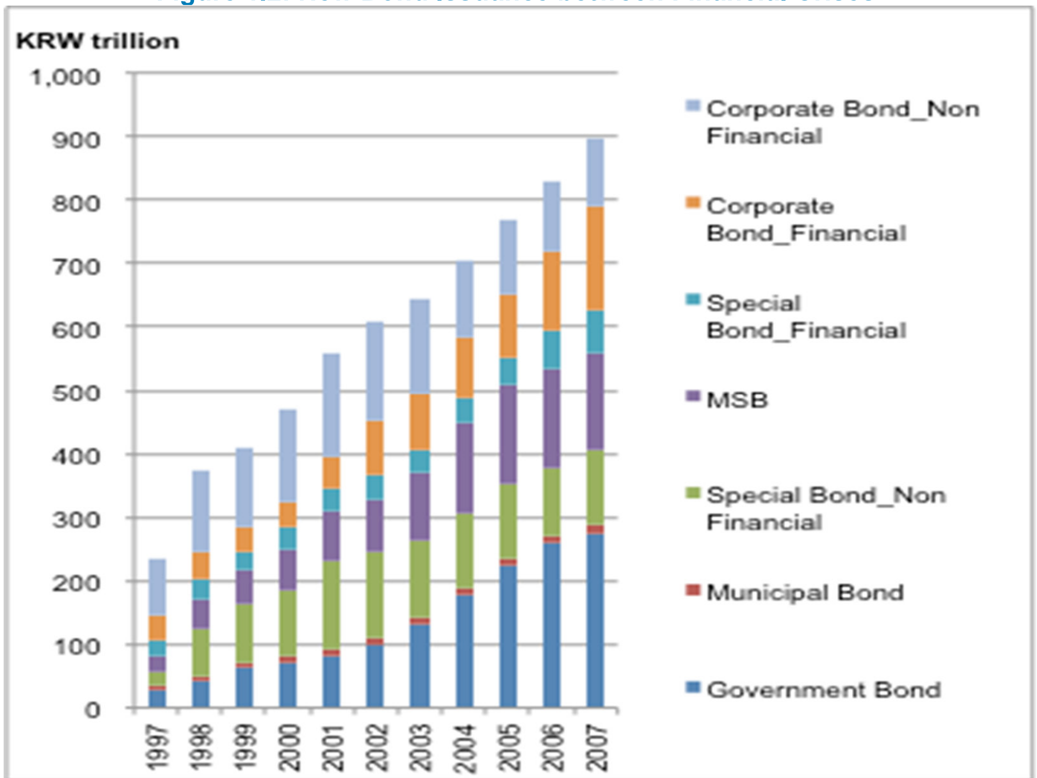
Such changes were attributed to the implementation of diverse policies and the efforts of market participants to address the causes of the 1997/98 Asian financial crisis. The Republic of Korea's financial crisis seemingly stemmed from the sudden depletion of the country’s foreign reserves, but institutional flaws in financial markets amplified the crisis.

A variety of policies were put in place to improve and deepen the shallow and narrow bond market, which was the result of market’s small size and limited number of participants, a lack of market transparency, and the inconsistent application of international standards.

Most noteworthy were the introduction of the Primary Dealer system and the launch of the KRX KTB, an inter-dealer market for KTBs established on KRX in 1999. The Primary Dealer system, in particular, enabled government bonds to be sold through competitive bids, unlike the previous practice in which major government bonds had been issued and sold through planned allocations to financial institutions. As guarantee providers refrained from issuing guarantees for corporate bonds in the wake of the 1997/98 Asian financial crisis, the corporate bond market dwindled; guaranteed corporate bonds as a proportion of total new bond issuances plunged below 5% in the 2000s. From the mid-2000s onward, guaranteed bonds almost disappeared from the corporate bond market. By contrast, government bond issuance was on the rise, owing to the government’s policy to nurture the KTB market. Figures 1.2 and 1.3 track new bond issuances and outstanding amounts, respectively, between the 1997/98 Asian financial crisis and the global financial crisis.

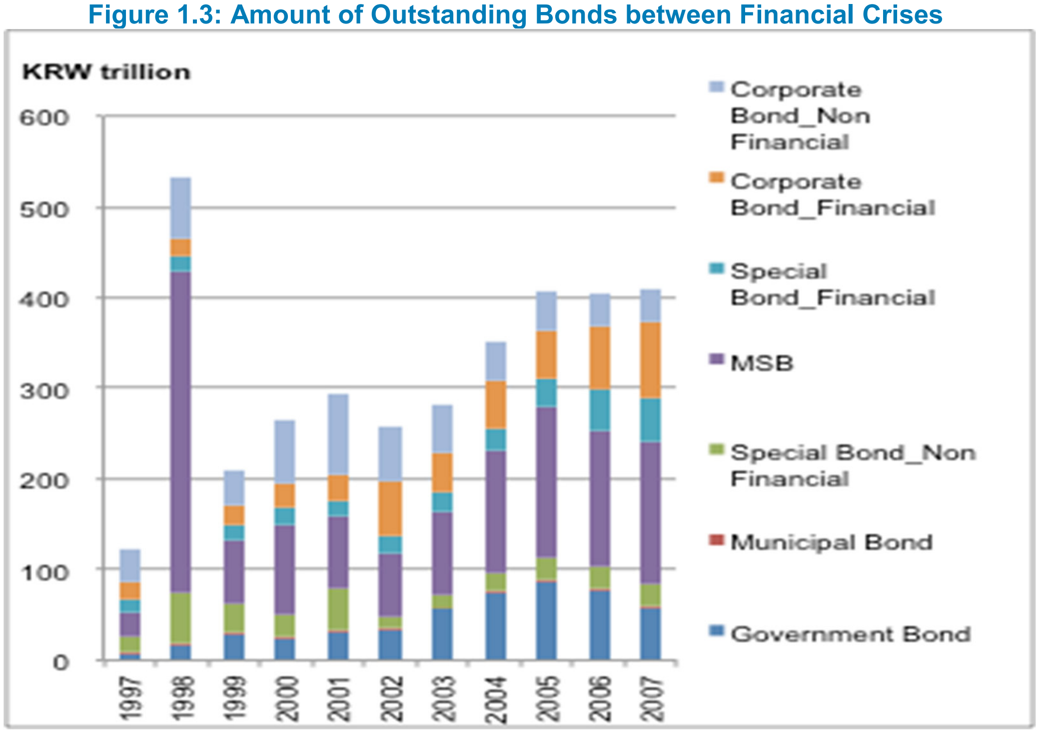
Because information about transactions on the exchange is disclosed in real time to market participants, the growth in government bond transactions in the KRX KTB brought about improvements in the transparency of the secondary bond market. Grain Bonds and National Debt Management Fund Bonds were integrated into KTBs in 2000 and 2003, respectively, in order to expand the liquidity base for government bonds. And the fungible issue system, in which new KTBs issued within a specified period are regarded as the same KTB issue, was introduced in 2000.

Figure 1.2: New Bond Issuance between Financial Crises



MSB = Monetary Stabilization Bond.
Source: Koscom.

Figure 1.3: Amount of Outstanding Bonds between Financial Crises



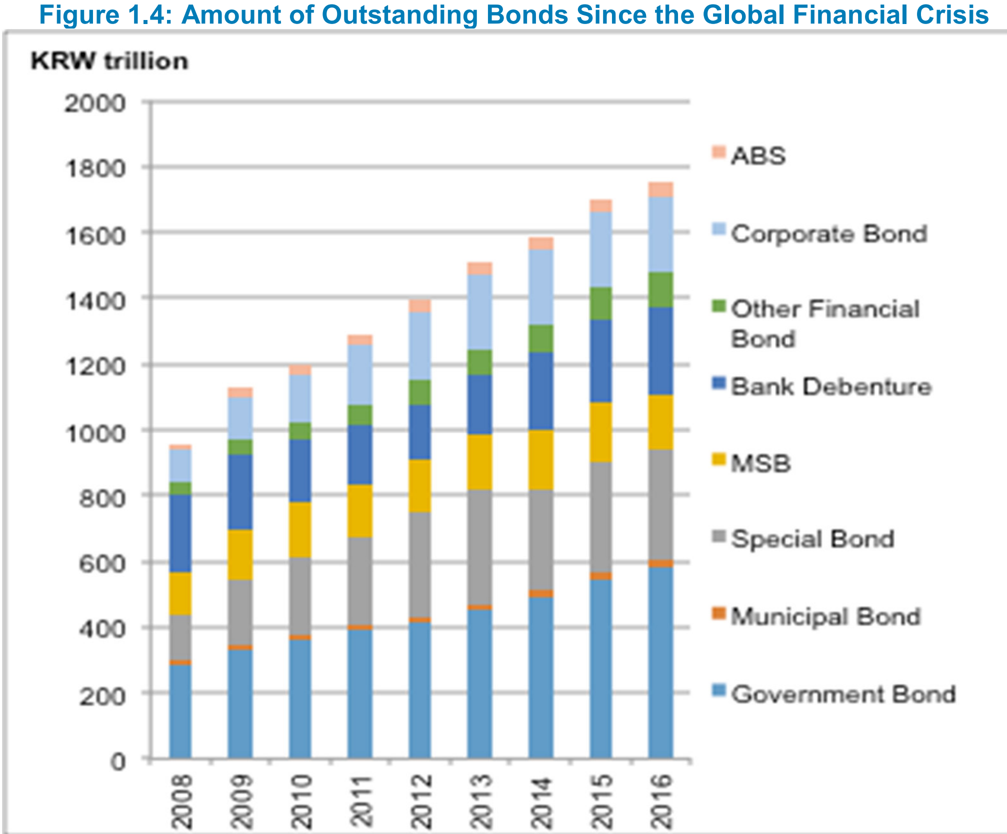
MSB = Monetary Stabilization Bond.
Source: Koscom.

The fungibility of KTBs was initially set to a 3-month basis, but the fungible issue period was extended to 6 months as KTB maturities were lengthened. The Republic of Korea started to issue 10-year KTBs in 2000, 20-year KTBs in 2006, 30-year KTBs in 2012, and 50-year KTBs in 2016.

Over time, a number of measures were introduced to make the OTC market more transparent. For example, the "15-minute rule" was introduced in 2000 and the Bond Quotation System (BQS) in 2007. Under the pre- and post-trade transparency regime for the OTC market, the online bond trading system FreeBond was launched in 2010 to organize the OTC market and facilitate OTC transactions. FreeBond was recently upgraded to K-Bond (see also Chapter IV).

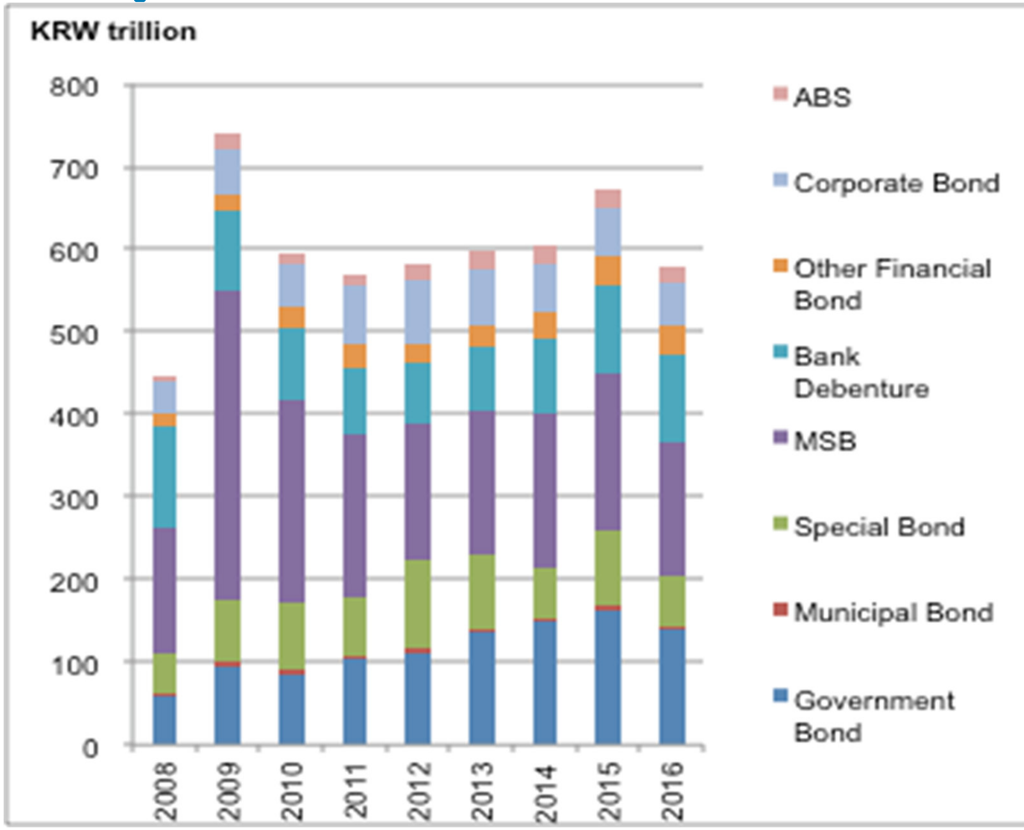
Based on its experience in overcoming the 1997/98 Asian financial crisis, the Republic of Korea continued along a stable growth path with relatively less exposure to the effects of the global financial crisis that began in late 2007. Despite the global financial crisis, the volume of outstanding bonds, which had stood at about KRW890 trillion at the end of 2007, surpassed KRW1,000 trillion in 2009 and increased to KRW1,750 trillion at the end of 2016 (Figure 1.4). In the case of MSBs, however, new issues in 2009 were large enough to account for 50% of aggregate new bond issues, but their portion in total outstanding bonds only amounted to around 13% in 2009 because the majority of MSBs at the time were short-term notes. Recently, the proportion of MSBs among outstanding amounts dropped to below 10% (Figure 1.5).

Figure 1.4: Amount of Outstanding Bonds Since the Global Financial Crisis



ABS = asset-backed securities, MSB = Monetary Stabilization Bond.
Source: Koscom.

Figure 1.5: New Bond Issuance Since the Global Financial Crisis



ABS = asset-backed securities, MSB = Monetary Stabilization Bond.
Source: Koscom.

The contraction in the corporate bond market, on the other hand, weakened the private sector's financing abilities through the capital market. In particular, bond issuance by SMEs with poor credit quality shrank further. To facilitate SME financing through the bond market, the Qualified Institutional Buyer (QIB) Market was launched in 2012. Privately placed bonds issued by firms with assets less than KRW500 billion can be traded in this market if such issuers meet certain requirements.

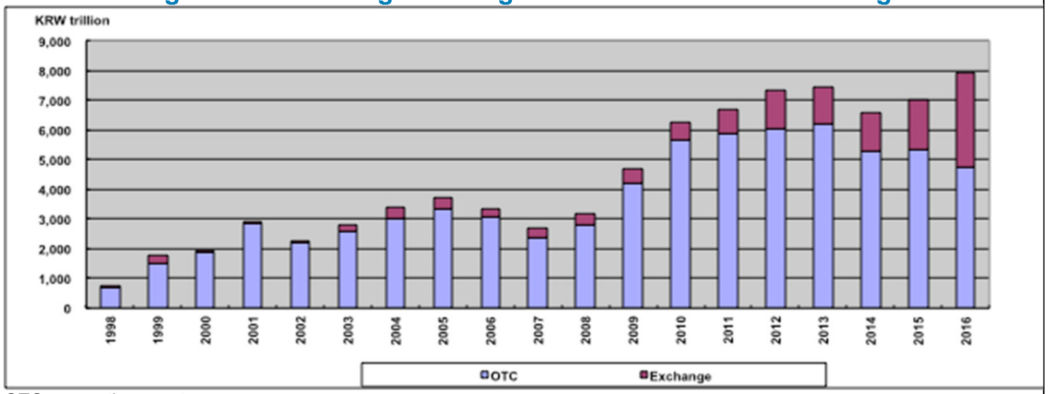
By the end of 2016, as a result of deregulation, the scope of eligible issuers was expanded to include all companies with assets less than KRW2 trillion. Regardless of their asset size, foreign companies were allowed to issue bonds in the QIB Market, which paved the way for nonresidents to secure an easy route to issue bonds.

In addition, a due diligence and book-building system for publicly offered non-guaranteed corporate bonds was introduced to improve transparency in the primary market. Similar to an auction system, it was aimed at capturing effective demand from institutional investors and determining a reasonable offer rate for a target bond issue. Since its introduction in April 2012, the system has undergone additional institutional improvements, becoming a fundamental part of the corporate bond issuance process.

The increased bond issuance volume and the improved institutional framework in the primary market have led to a rise in the volume of bond transactions in the secondary market. Particularly, the Financial Investment Services and Capital Market Act (FSCMA), enacted in 2009 and further revised in 2011, contained the fundamentals for the institutional structure of the Korean capital market.

As shown in Figure 1.6, bond transactions have increased significantly from only about KRW700 trillion in 1998 to about KRW8,000 trillion in 2016. Except for declines, notably in OTC trades, during the global financial crisis in 2007–2008 and again in 2014, the growth has been steady. In a separate development from the increased trading volume, the proportion of bonds traded on the exchange, most of which were KTB trades, has climbed gradually to about 40% of total bond trades in 2016.

Figure 1.6: Exchange Trading vs. Over-the-Counter Trading



OTC = over-the-counter.
Note: OTC trading volume is calculated as the sum of the traded amount for the buy and sell side (so-called "double counting"). Meanwhile, the exchange trading volume is calculated as the actual traded amount (so-called "single counting").
Sources: Korea Exchange, Korea Financial Investment Association.

An increase in the trading of bonds as an underlying asset made possible the growth of the market for derivatives linked to bonds. Following the introduction of 3-year KTB futures in 1999, 5-year and 10-year KTB futures were introduced in 2003 and 2008, respectively, and have been traded actively. Structured products such as KTB exchange-traded funds (ETFs) have also been introduced, which helped increase overall bond market diversity.

In line with the bond market's development, the repo market expanded and bond borrowing and lending transactions increased, adding liquidity to the bond market and strengthening the diversity of bond portfolio management. The repo market was launched in the mid-1970s to cater mainly to retail investors. In late 1999, KSD began to provide a triparty repo service. In 2002, KRX launched the repo market for institutional investors on its trading platform. These developments became drivers for structural change in the bond market.

Active utilization of the securities borrowing and lending facility provided by KSD from 1996 onward also contributed to increased liquidity in the bond market. The Korea Securities Finance Corporation (KSFC) started to provide bond borrowing and lending services in 2000, expanding its repo-linked borrowing and lending. KSFC has also participated as an intermediary in the OTC institutional repo market since 2011.

The quantitative growth and qualitative changes in the bond market heightened the need for investor protection. Subsequently, an indenture trustee system was adopted in 2012 to replace the existing bond trustee system, which was believed to be favoring issuers who were paying the service fees to bond trustees.

C. Challenges and Future Direction

In spite of its multifaceted development, the Korean bond market faces various challenges. Most notable is the recent stagnation of private sector financing through the capital market, which may be a result of the corporate bond market's contraction owing to crowding-out effects from the government bond market. Another challenge is the polarization of issuance by issuers with different credit ratings.

1. Stagnation in Private Sector Financing Through the Capital Market

The proportion of nonfinancial corporate bonds among total listed bonds reached a record high of 65% in the mid-1980s and hovered around 40% before the 1997/98 Asian financial crisis. However, the proportion of nonfinancial corporate bonds started to decline sharply in the wake of the 1997/98 Asian financial crisis. In recent times, corporate bonds have accounted for only around 10% of total bonds outstanding.

Traditionally, corporate bond issuance via public offering has been an important source of corporate financing. However, issuance volume and bonds' proportion of total corporate financing have shown little improvement while exhibiting high volatility. As Table 1.1 indicates, the proportion of corporate bonds to the total amount of corporate financing was 87.7% in 2005; this share dipped sharply in 2007 with the onset of the global financial crisis, but bond issuance recovered and bonds' share of corporate financing was largely stable in 2008–2011 before rising as high as 98.2% in 2012. In 2016, however, bonds accounted for 91.5% of corporate financing, illustrating the subsequent decline and stagnation of corporate bond issuance volumes.

Table 1.1: Corporate Financing Through Public Offering of Corporate Bonds
(KRW billion, %)

Year	Corporate Bonds		Total Amount (Stocks + Bonds)
	Issued Amount	Share of Total	
2005	48,103	87.7%	54,866
2006	41,678	86.5%	48,178
2007	45,160	72.4%	62,417
2008	74,116	93.6%	79,196
2009	114,940	91.8%	126,556
2010	112,919	93.8%	123,259
2011	130,492	91.0%	143,385
2012	128,693	98.2%	131,056
2013	116,295	95.7%	121,497
2014	116,172	95.3%	121,838
2015	123,102	93.9%	131,114
2016	109,858	91.5%	120,116

Source: Financial Supervisory Service.

2. Polarization of Issuance by Issuers with Different Credit Ratings

Issuance polarization among nonfinancial corporate bonds has become more severe because credit ratings are overly concentrated in a particular, higher-rated category. As of 2016, about 96% of nonfinancial corporate bonds were rated A or above. As a result, it has become difficult even for BBB-rated (investment grade) companies to issue bonds.

The stagnation in corporate bonds as a proportion of the bond market in the aftermath of the two financial crises was due in part to the improved capital structures of Korean firms. Given little change in the bond proportion of total debt held by domestic companies before and after the financial crises, the decreased proportion of corporate bond issuance resulted from corporates' debt reduction. The debt-to-equity ratio of large firms, which at one point had exceeded more than 1,000% (10 times) in the mid-1990s, plunged in the wake of the 1997/98 Asian financial crisis. It fell further to less than 100% in the wake of the global financial crisis in 2007–2008.

However, bonds issued by SMEs, which had reached nearly 28% of the volume of issuance by large firms in the early 1990s, dropped drastically in the aftermath of the two crises and stood at only about 1% after the global financial crisis. This well illustrates the polarization of the Korean bond market.

Hence, the financial authorities needed to take policy measures to facilitate the issuance of bonds by SMEs that carry a higher credit risk and are subject to asymmetric information problems. One of the policy measures was the launch of the QIB Market in 2012 (see section B), which is the bond market for professional investors.

3. Imbalance between Bond Investment and Issuance by Nonresidents

One of the challenges facing the Korean bond market is the deepening imbalance between bond investment and issuance by nonresidents. Underpinned by the growth of the bond market, foreign investment in domestic bonds has steadily increased since the mid-2000s. While foreign investors held merely KRW1 trillion worth of Korean bonds in the early 2000s, their investments exceeded KRW100 trillion in 2015. Bond investment by foreign investors tends to be concentrated in specific types of bonds, mainly KTBs and MSBs.

On the other hand, the volume of bonds issued by nonresidents in the Republic of Korea is still insignificant. As of 2016, the volume of outstanding bonds issued by nonresidents through public and private placements stood at KRW320 billion and KRW440 billion, respectively, together representing only 0.04% of total outstanding bonds in the Korean bond market.

4. Professional Market as a Driver of Bond Market Development

A market for professional investors can be characterized by lowered entry barriers for securities issuers through a loosening of the full disclosure requirements (i.e., the introduction of concise disclosure), the participation of qualified investors who possess sophisticated information gathering capabilities and large amounts of capital to invest, and free trading only among qualified investors without resale restrictions.

The capital market in the Republic of Korea has developed as market infrastructure has been established for professional investors. On the other hand, the markets for professional investors have gradually opened their doors to foreign issuers. The deregulation of the QIB Market, which came into force in 2016, widened the range of SME issuers and expanded the issuer scope beyond SMEs, allowing foreign issuers to raise capital in the domestic QIB Market.

5. Importance of Joining the ASEAN+3 Multi-Currency Bond Issuance Framework

The ASEAN+3 Multi-Currency Bond Issuance Framework (AMBIF), which represents bond and note issuance to professional investors only, can provide opportunities for Koreans to invest in bonds issued by foreign issuers and give Korean firms easier access to capital in the region. Moreover, Korean investors can contribute to regional financial integration by participating in other ASEAN+3 bond markets. In turn, it would help strengthen regional cooperation and play a part in regional co-development.

II

Legal and Regulatory Framework

A. Legal Tradition

The Republic of Korea has a civil law tradition. To some extent, it has also been influenced by neighboring and international laws including British Common Law, European Union law, and United States law.

B. English Translation

As far as the translation of the laws and regulations in the Republic of Korea are concerned, the Ministry of Government Legislation hosts a database of translated Korean laws.[3] All of the translations contained in this system are unofficial. Only the original Korean texts of the laws and regulations have legal effect, and the translations are to be used solely as reference materials to aid in the understanding of Korean laws and regulations.

The Government of the Republic of Korea is not responsible for the accuracy, reliability, or currency of the legislative materials provided, or for any consequences resulting from use of the information on the website hosted by the Ministry of Government Legislation.

For purposes of interpreting and applying a law to any legal issue, users should consult the original Korean text published in the Official Gazette. Furthermore, any translation in which the title of a law indicates it to be a tentative translation has not yet been proofread or corrected by a native English speaker or legal translation expert; these translations may be revised in the future.

C. Legislative Structure

The Republic of Korea features a multitiered legislative structure to govern the financial and capital markets, guided by the Constitution of the Republic of Korea as the supreme law.

[1st tier] Constitution of the Republic of Korea
- [2nd tier] Statutes and acts (fundamental and key legislation for the market and market participants)
  - [3rd tier] Subordinate legislation (e.g., Presidential or Enforcement Decree and Enforcement Rule of the Prime Minister or Regulation of a Ministry)
    - [4th tier] Self-regulatory organization (SRO) rules (e.g., from Korea Financial Investment Association [KOFIA] or KRX)

[3] Government of the Republic of Korea, Ministry of Government Legislation. Korean Law Translation Database System. http://www.law.go.kr/main.html

Table 2.1 illustrates the legislative structure mentioned above by giving significant examples of relevant securities market legislation for each of the individual tiers.

Table 2.1: Examples of Securities Market Legislation by Legislative Tier

Legislative Tier	Content or Significant Examples
Constitution of the Republic of Korea (1988)	Principles, Rights, and Obligations
Statutes and acts (fundamental and key legislation for the market and market participants)	• Act on the Establishment, etc. of the Financial Services Commission (28 May 2014) • The Bank of Korea Act (29 May 2016) • Banking Act (13 August 2013) • Commercial Act (23 May 2011) • Financial Investment Services and Capital Markets Act (28 January 2014) • Act on Issuance and Distribution of Short-Term Electronic Bonds, etc. (14 July 2011) • Secured Bond Trust Act (17 May 2010)
Subordinate legislation (Presidential Decree or Enforcement Rule of the Prime Minister or Ministry)	• Enforcement Decree of the Banking Act (20 April 2005) • Enforcement Decree of the Financial Investment Services and Capital Markets Act (30 December 2013) • Enforcement Rule of the Financial Investment Services and Capital Markets Act (29 August 2013) • Enforcement Decree of the Act on Issuance and Distribution of Short-Term Electronic Bonds, etc. (4 December 2012) • Enforcement Decree of the Secured Bond Trust Act (29 February 2008) • Enforcement Rule of the Secured Bond Trust Act (3 March 2008) • FSC Regulation on Financial Investment Business (31 December 2013) • FSC Regulation on Issuance, Public Disclosure, etc. of Securities (28 June 2016) • FSS Detailed Rules of the Regulation on Financial Investment Business (30 March 2015) • FSS Detailed Regulations on Issuance, Public Disclosure, etc. of Securities (16 July 2014)
SRO rules (e.g., from KOFIA or KRX, and their enforcement rules)	• KOFIA Regulations on Business Conduct and Services of Financial Investment Companies (21 June 2016) • KOFIA Regulations on Securities Underwriting Business, etc. (21 April 2016) • KOFIA Standard Working Rules on Ethics for Financial Investment Companies (26 October 2012) • KOFIA Regulations on Registration and Management, etc. of Securities for Qualified Institutional Buyers (21 June 2016) • KRX-KOSPI Market Business Regulation (31 January 2018) • KRX-KOSPI Market Disclosure Regulation (28 December 2016) • KRX-KOSPI Market Listing Regulation (31 January 2018) • KSD Regulation on Settlement Service for Securities (28 December 2012) • KSD Regulation on Deposit Service for Securities (28 December 2012) • KSD Regulation on Bond Registration Business (28 December 2012) • KSD Securities Lending and Borrowing Regulation (29 May 2014)

FSC = Financial Services Commission, FSS = Financial Supervisory Service, KOFIA = Korea Financial Investment Association, KRX = Korea Exchange, KSD = Korea Securities Depository.
Source: ADB consultants for SF1.

1. Fundamental and Key Legislation (Statutes and Acts)

Fundamental legislation establishes the key stakeholders of the financial and capital markets in the Republic of Korea, including central bank and regulatory authorities. Statutes and acts, in the context of the bond market, refer to legislation specifically aimed at the securities market or capital market. These laws and acts establish and govern securities markets or market segments, including the bond market, and related institutions and participants, and define instruments and their basic issuance requirements. These laws and acts are passed by the National Assembly of Korea (Parliament). Laws generally state in their text when they take effect.

Among the fundamental legislation is the Banking Act, which regulates the activities that banks and other financial institutions may carry out, including in the bond market. On 15 January 2018, the Financial Services Commission (FSC) proposed amendments to the Banking Act to relax certain compliance and capital requirements, and remove investment limits on certain classes of debt securities. Key provisions include the following: (1) banks are to be exempt from ex-ante reporting for concurrent businesses that are registered, approved, or authorized pursuant to legislation other than the Banking Act; (2) the investment limit on low-risk debt securities such as municipal bonds is to be removed; and (3) banks are to accumulate at least 10% of their cash dividend as an “earned surplus reserve” until the aggregate reserve amount reaches half of the capital as they are required under the Commercial Act. The public comment period for the proposed amendments ended on 25 February 2018.

The FSCMA effectively represents the key legislation relevant for the Korean bond market. The FSCMA is the fundamental law governing the domestic financial and capital markets in the Republic of Korea, as well as securities and other financial instruments, their issuance, and trading.

Public sector bonds are issued based on the relevant laws. Government bonds are issued under Article 5 in the State Bond Act. According to this article, government bonds are issued by the Minister of the Ministry of Strategy and Finance (MOSF), and the issuing method and other necessary matters are determined by a corresponding ordinance of the Minister. The legal basis for municipal bonds issuance includes the Local Autonomy Act and the Local Public Enterprises Act.

Special bonds are also issued based on the acts under which the issuer was established. MSB, a representative special bond, is based on Article 69 of the Bank of Korea Act. BOK can issue and buy back bonds in the open market, as prescribed by the act and the Monetary Policy Committee. Acts for other financial special bonds include the Korea Development Bank Act, Export and Import Bank of Korea Act, and Industrial Bank of Korea Act. The acts for nonfinancial special bonds include the Korea Railroad Corporation Act, Korea Land and Housing Corporation Act, Korea Water Resource Corporation Act, and Korea Expressway Corporation Act. These public banks and corporations can generally issue bonds up to the limit not exceeding a prescribed amount based on capital and reserves, as stipulated in the respective acts.

2. Subordinate Legislation (Decrees or Enforcement Rules)

Subordinate legislation is issued in the form of Enforcement Decrees of the President or Enforcement Rules of the Prime Minister, or Regulations or Detailed Regulations of the FSC as the government body administering the legislation for the financial and capital markets in the Republic of Korea. This subordinate legislation renders statutes and acts effective, and interprets aspects from key legislation for practical application in the markets.

3. Self-Regulatory Organization Rules

In turn, the rules and enforcement rules of the SROs, which have been charged with governing their respective markets and their participants on a day-to-day basis, play a very important part in defining the roles and responsibilities of market institutions and their participants, and the actions they may take. These rules contain descriptions on how regulations should be applied and specific market activities carried out.

D. Korean Bond Market Regulatory Structure

The capital market and various aspects of the bond market in the Republic of Korea are governed by regulations issued and enforced by BOK, the FSC, the Financial Supervisory Service (FSS), and MOSF. In addition, the bond market is administered by two SROs, KOFIA and KRX, which organize their own membership and market participation, and issue rules for market conduct and practices.

Market regulatory authorities involved in the bond and note issuance approval processes—in effect for corporate bonds, notes, and commercial paper—include the FSC, the FSS, KOFIA, and KRX.

1. Ministry of Strategy and Finance

MOSF is committed to developing a strong economy and building growth engines through the concerted efforts of its offices and bureaus. MOSF works to ensure macroeconomic and financial stability, effective policy coordination, efficient allocation of national resources, fiscal soundness, rational tax policies, and robust international cooperation.

MOSF is responsible for (i) implementing mid- to long-term national growth strategies; (ii) economic and fiscal policy coordination; (iii) budget planning and the monitoring of budget implementation; (iv) efficiently managing fiscal resources such as tax revenue and public funds, while working on government accounting and lottery policies; (v) overseeing the management of public institutions; (vi) establishing policies regarding international financial markets and financial cooperation; and (vii) strengthening economic cooperation with both emerging and advanced economies.

For attaining these goals, the main source of government income is tax revenue. However, depending on the social and economic conditions, the income from tax may not be sufficient to cover the required fiscal expenditures. In such cases, the issuance of government bonds is an important fiscal means, so MOSF plays a key role in the government bond market.

Within the limit approved by the National Assembly, MOSF determines the issuance amount of government bonds, which affects the primary market of all Korean bond markets. MOSF also influences the secondary government bond market by appointing the Primary Dealers, who are the major participants in the bond market.

2. Financial Services Commission

As a government organization, the FSC is a board-style administrative organization under the Prime Minister’s Office. But unlike other governmental organizations whose authorities are designated by the Government Organization Act, the FSC’s authority is designated by the Act on the Establishment, etc. of the Financial Service Commission, the enforcement decree of the act, and other acts and decrees on financial supervision.

The FSC conducts matters regarding financial policies and institutions, including inspections and placing restrictions on financial organizations; licensing and authorizing the establishment of financial organizations; the management, supervision, and surveillance of the capital market; legal and regulatory enactment; and the revision of financial policies and systems. The FSC also manages the business activities, operation, and management of the FSS, and reviews and determines the FSS's budget and account settlement, along with the revision of the FSS rules and regulations.

3. Financial Supervisory Service

The FSS is a special legal entity that has no capital base. It is independent from the central and local governments, conducting public affairs as a public corporation. By law, the FSS is not a government institution, but an independent public corporation, as it aims to carry out politically neutral and financially specialized supervisory functions over the Korean financial market.

With guidance from the FSC, the FSS is responsible for the inspection and supervision of financial institutions. It reports the results to the FSC, as well as any follow-up recommendations of the inspections. The FSC can require the FSS to make necessary changes to ensure effective monitoring and guidance over the FSS. The FSC can also enact general or partial suspension orders to actions taken by the FSS when those actions are deemed to be legally inappropriate or to go against the public benefit, such as investor or depositor protection.

The bond market supervision activities of FSS are conducted as a part of its capital market supervision to ensure that the capital market is effective. These activities are generally grouped into four distinct areas: corporate disclosure, securities market, investigation of securities violations, and accounting. The FSS supervises corporate disclosure to make sure companies and bond issuers that are required by law to publicly disclose certain operating and financial information comply with the law. The FSS also oversees trading activities in the bond market and enforces fair and orderly conduct to protect investors and preserve the integrity of the market.

4. Bank of Korea

BOK decides and implements monetary policy with the aim of maintaining price stability. In implementing monetary policy, BOK influences the volume of money and interest rates through its operational instruments, including money market operations such as buying and selling MSBs, for the purpose of currency and monetary controls.

To contribute to the maintenance of the financial system's stability, BOK conducts on-site examinations and off-site monitoring of the institutions under its purview, and acts as the lender of last resort to provide liquidity as necessary. BOK is responsible for the entire operation of Government of the Republic of Korea securities, including issuance, registration, interest payment, and redemption.

5. Korea Financial Investment Association

KOFIA, the SRO of the primary and secondary bond markets, manages and oversees the OTC market and discloses its trading information pursuant to Article 307 of the Enforcement Decree of the FSCMA.

In the primary bond market, KOFIA issues and maintains regulations for, among others, the QIB Market, as well as regulations on securities underwriting. KOFIA is also charged with ensuring market transparency in the secondary bond market; all quotes and transaction records of bonds traded in the OTC market are required to be reported to KOFIA for the purpose of easy dissemination.

KOFIA monitors the book-building process, the underwriting activities of the primary market including that of the managing companies, as well as transaction details of the secondary market and the reporting of price quotes. When a KOFIA member company violates the regulations, KOFIA can impose restrictions through the Self-Regulation Committee and impose a penalty on the member company, its executives, or its employees.

6. Korea Exchange

KRX operates the KOSPI market, KOSDAQ market, derivatives market, and Korea New Exchange (KONEX) market. Debt securities, including bonds and notes, are traded on the KOSPI market.

The responsibilities of KRX include the establishment and operation of its markets; transaction of securities and exchange-traded derivatives; transaction confirmation; debt acquisition; confirmation of settlement securities, settlement items, and settlement amounts; settlement execution guarantees; follow-up measures on settlement failure and settlement instruction as a result of transactions on the securities market and the derivatives market; reporting and disclosure of listed corporations; and self-resolution of disputes arising from transactions on its markets.

KRX conducts self-regulatory activities—such as market surveillance, investigations into abnormal trading activities, member inspections, and inter-market surveillance—and carries out disciplinary actions against members (and their officers and employees), as well as preventative activities for unfair trading, under the FSCMA.

7. Korea Securities Depository

KSD is the central securities depository of the Republic of Korea, providing a wide range of post-trade services for the Korean securities market. KSD was established in 1974 as a special public corporation, the Korea Securities Settlement Corporation, and designated as KSD in its current form in 1994. There are several mechanisms to ensure the fairness and transparency of its activities; KSD is supervised by regulatory bodies such as the FSC and FSS.

KSD regulates activities within the bond market by setting forth settlement regulations to be observed by all parties. All settlement processes are carried out according to the regulations. The regulations also establish eligibility criteria that anyone who wishes to participate in settlement processes as a member must fulfill beforehand. In addition, KSD sets rules for, and monitors activities in, securities borrowing and lending, and repo transactions, through its platform.

In the professional bond market, KSD sets systematic restrictions to ensure QIB securities are traded only among QIBs registered with KOFIA. Payment and settlement of QIB securities may only be conducted via financial investment companies, and financial investment companies may do so only on a QIB's proprietary account at KSD.

E. Regulatory Framework for Debt Securities

1. General Regulatory Framework

The regulatory framework for debt securities in the Korean market largely depends on the nature of bonds, especially in the primary market. In case of public bonds (government bonds, municipal bonds, and special bonds), the issuance is made by the issuer according to the acts under which the issuers have been established.

In contrast, the regulatory framework for debt securities issuance in the private sector depends on the prescribed disclosure level—for either a public offering or private placement—rather than on the characteristics of the issuer, even though specific provisions on the obligations of the issuer may be stated in, among others, the Commercial Act, Banking Act, or Specialized Credit Finance Business Act.

In the case of a public offering of debt securities, a registration of the proposed issuance with the FSC is required. In contrast, private placements other than those offerings in the QIB Market (see next section) are issued in the market through negotiation between the issuer and underwriters. Once the debt securities are issued, applicable regulations are largely dependent on whether the securities are traded on the exchange or in the OTC market. The exchange trading is regulated by the FSS and KRX rules; only publicly offered bonds can be listed on the exchange. Trading in the OTC market, which is possible for both publicly offered and privately placed bonds and notes, is regulated by the FSC and subject to KOFIA rules.

2. Framework for the Qualified Institutional Buyer Market

QIB bonds are issued based on Article 2-2 (2) of the Regulation on Issuance, Public Disclosure, etc. of Securities issued by FSC. In addition, the Regulations on Registration and Management, etc. of Securities for Qualified Institutional Buyers, issued by KOFIA as the SRO presiding over the QIB Market, prescribe the conditions under which specific private placement bonds and notes can be regarded as QIB bonds and notes, if the bonds and notes are traded only among QIBs. KOFIA regulations stipulate the registration and cancellation practices for QIB and QIB bonds and notes, and the notification and request for document submission, among other provisions. The original requirement for QIB bonds to be traded on K-Bond in the KOFIA rules was amended to allow any type of OTC trading. Nevertheless, QIB transactions remain under the oversight of KOFIA, since KOFIA manages the OTC market and its constituents, and facilitates OTC trading of debt securities in the Republic of Korea.

F. Debt Securities Issuance Regulatory Processes

Public offers of debt securities require (i) registration with the FSC and (ii) the publication of a prospectus. A listing is optional and would attract separate listing eligibility screening and listing approval from KRX as the single listing place in the Republic of Korea.

Privately placed corporate bonds can be issued without registering with the FSC. Private placements aimed at QIBs—a separate category within private placements—that are issued to and traded among QIBs only require registration with KOFIA as the QIB market registration authority.

All debt securities issued are to be admitted to and settled at KSD as the single central securities depository in the Korean bond market.

1. Regulatory Processes by Issuer Type

The regulatory processes for the issuance of debt securities in the Republic of Korea differ depending on issuer type and method of issuance. Financial institutions under the purview of BOK require additional approval, depending on their purpose of issuance. Nonresident issuers may issue bonds and notes in the Korean bond market, though specific registration and reporting requirements may apply depending on the method of issuance.

The issuance of bonds and notes denominated in foreign currencies by nonresident issuers is possible. But it should be reported to the Minister of MOSF with an issuance plan, including information on the use of proceeds.

Table 2.2 provides an overview of these regulatory processes by corporate issuer type and identifies which regulatory authority or market institution will be involved. In order to make the issuance process by issuer type more comparable across markets in the Association of Southeast Asian Nations plus the People's Republic of China, Japan, and the Republic of Korea—collectively known as ASEAN+3—the table features common issuer type distinctions that are evident in regional markets. Not all markets will distinguish all such issuer types or prescribe approvals. Sovereign issuers are typically exempt from corporate issuance approvals but, at the same time, may be subject to different regulatory processes.

Table 2.2: Authorities Involved in Regulatory Processes by Issuer Type

<table>
<tr><th>Type of Issuer</th><th>FSC</th><th>MOSF</th><th>KOFIA</th><th>KRX</th></tr>
<tr><td>Resident issuer</td><td rowspan="8">Submission of Securities Registration Statement (for public offers only)</td><td rowspan="4"></td><td rowspan="8">Registration of Placements (for QIB Market-eligible securities only)</td><td rowspan="8">Listing eligibility and actual listing subject to approval and criteria in the KRX Listing Rules</td></tr>
<tr><td>Resident nonfinancial institution</td></tr>
<tr><td>Resident financial institution</td></tr>
<tr><td>Resident issuing FCY-denominated bonds and notes</td></tr>
<tr><td>Nonresident issuer</td><td rowspan="4">File a report with the Minister of MOSF (Nonresident issuers only)</td></tr>
<tr><td>Nonresident nonfinancial institution</td></tr>
<tr><td>Nonresident financial institution</td></tr>
<tr><td>Nonresident issuing FCY-denominated bonds and notes</td></tr>
</table>

BOK = Bank of Korea, FCY = foreign currency, FSC = Financial Services Commission, KOFIA = Korea Financial Investment Association, KRX = Korea Exchange, MOSF = Ministry of Strategy and Finance.
Source: ADB consultants for SF1.

The regulatory processes for all types of issuances are further explained in subsequent sections.

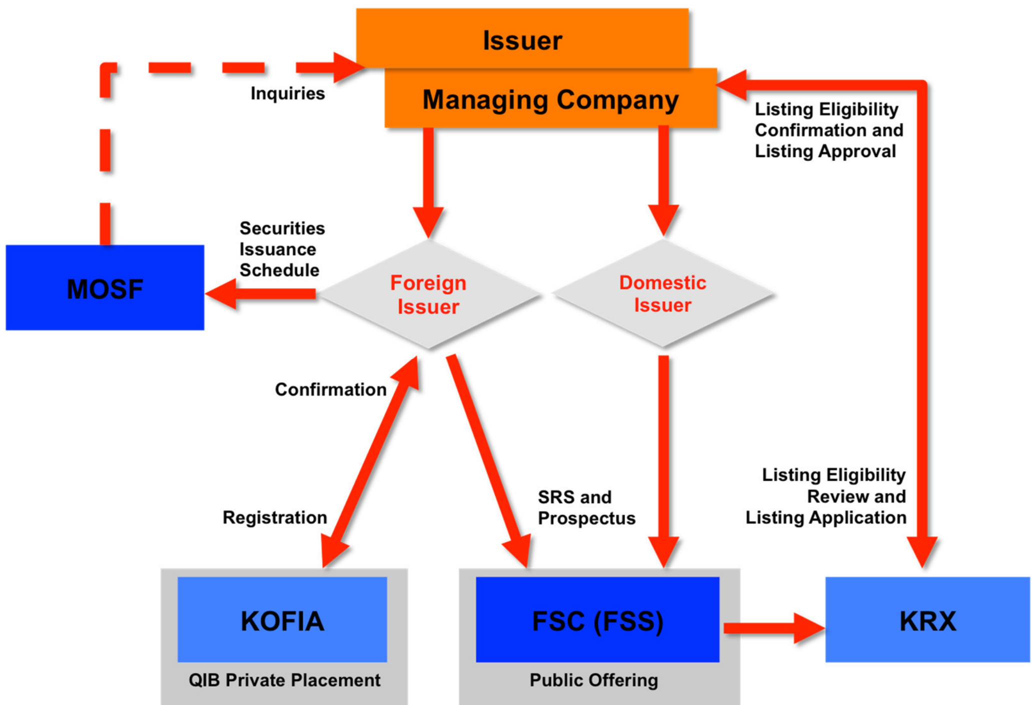
2. Regulatory Process Overview

The issuance of bonds and notes in the Korean market can be made by public offering or private placement, including private placements to QIBs (QIB offering). A public offering represents an invitation to at least 50 investors to acquire newly issued securities. Meanwhile, private placement means an invitation to acquire newly issued securities without placing them for public offering.

For bonds and notes to be publicly offered or sold, a Securities Registration Statement (SRS) needs to be filed by the issuer in connection with the public offering or sale of the securities with the FSC, and should be accepted by the FSC.

Public sector bonds are usually exempted from the registration requirement. These bonds and notes include government bonds, local government bonds, special bonds, or other securities deemed to be those where investors are properly protected through sufficient public disclosure pursuant to the relevant acts governing the issuer.

Figure 2.1: Regulatory Process Map—Bond and Note Issuance in the Republic of Korea



FSC = Financial Services Commission, FSS = Financial Supervisory Service, KOFIA = Korea Financial Investment Association, KRX = Korea Exchange, MOSF = Ministry of Strategy and Finance, QIB = Qualified Institutional Buyer, SRS = Securities Registration Statement.
Source: ADB consultants for SF1.

In the Korean bond market, there is no explicit rule that governs the appointment of a lead manager(s) or lead arranger(s), termed a "managing company" in domestic market practice.[4] However, the appointment of a managing company is mandatory for a public offer. In practice, the appointment is common in the public offering of non-guaranteed bonds, which represent most of the corporate bond market in the Republic of Korea. On the other hand, the appointment of a managing company is optional in private placements. Naturally, it is also optional for a placement of debt securities

[4] The term "managing company" used in the Korean bond market is the equivalent of the lead manager, arranger, or lead underwriter commonly seen in other bond markets.

registered in the QIB market. At the same time, the use of one or more managing companies may be practical to reach the intended investor universe.

A managing company must be licensed by the FSC. The managing company may appoint additional underwriter(s) upon request of the issuer or on its own accord. The managing company is also expected to support the compilation of issuance documentation for either a public offer or a private placement, and aid in the submission of said documentation and disclosure information to the respective regulatory authorities, as the case may be.

The listing of debt securities is optional in the Republic of Korea. Listing debt securities does not require a listing sponsor; however, it is established market practice that the managing company would look after the listing process as well.

The regulatory process map shown in Figure 2.1 may help with the navigation of the applicable regulatory processes to be applied to a proposed bond or note issuance in the Korean bond market.

Table 2.3: Matrix on Corporate Bond Offering or Sale in the Republic of Korea

<table>
<tr><th colspan="2"></th><th>(1). Newly Issued Securities</th><th>(2). Already-Issued Securities</th></tr>
<tr><td colspan="2">1. Public offering (an invitation to at least 50 investors to acquire newly issued securities) and sale</td><td>1-(1). Public offering (gathering 50 or more investors within the past 6 months)</td><td>1-(2). Public sale (gathering 50 or more investors)</td></tr>
<tr><td rowspan="2">A. Duty of submission of an SRS to FSC
B. Certain obligation to report to FSC</td><td>Offering or sale of KRW1 billion or more</td><td>A. Yes; B. Yes</td><td>A. Yes; B. Yes</td></tr>
<tr><td>Offering or sale of less than KRW1 billion</td><td>A. No; B. Yes or No</td><td>A. No; B. Yes or No</td></tr>
<tr><td colspan="2">2. Private placement (an invitation to acquire newly issued securities without placing them for public offering) and sale</td><td>2-(1). Private placement (issued directly to certain demand-side parties) (gathering less than 50 investors within the past 6 months)</td><td>2-(2). Private sale (sold directly to certain demand-side parties) (gathering less than 50 investors)</td></tr>
<tr><td colspan="2">A. Duty of submission of an SRS to FSC
B. Certain obligation to report to FSC</td><td>A. No; B. No
(but if the securities can be issued to 50 or more persons within 1 year of issuance and meet certain requirements, it is deemed a public offering)</td><td>A. No; B. No
(but if the securities can be transferred to 50 or more persons within 1 year of issuance and meet certain requirements, it is deemed a public offering)</td></tr>
<tr><td colspan="2">3. Private placement and sale offered to QIBs in QIB Market</td><td>3-(1). Private placement offered to QIBs in QIB Market (only for QIBs)</td><td>3-(2). Private placement sale for QIBs in QIB Market (only for QIBs)</td></tr>
<tr><td colspan="2">A. Duty of submission of an SRS to FSC
B. Certain obligation to report to FSC or MOSF</td><td>A. No; B. Yes or No</td><td>A. No; B. Yes or No</td></tr>
</table>

FSC = Financial Services Commission, MOSF = Ministry of Strategy and Finance, QIB = Qualified Institutional Buyer, SRS = Securities Registration Statement.
Source: ADB consultants for ABMF SF1.

In the Republic of Korea, the issuance approval processes and underlying requirements differ between a public offer and issuances of debt securities aimed at QIBs (see Chapter III.N.2).

The issuer may issue QIB Market-eligible securities using a shelf-registration with KOFIA. A shelf- or program registration is valid for 1 year and may be renewed (see Chapter II.F.7).

The following sections provide detailed descriptions of the individual regulatory processes required for each instance. In the Korean corporate bond market, the FSCMA distinguishes between a public offering or sale of securities and a private placement or sale of securities, irrespective of whether those securities are issued domestically or outside the Republic of Korea. For easy reference, Table 2.3 contains a matrix of these offerings and secondary distribution methods of corporate bonds in relation to the specific provision of the FSCMA and supplementary regulations.

3. Regulatory Process in Case of a Nonresident Issuer

Nonresident issuers can issue debt securities in the Korean bond market. Since the FSCMA regulates matters for securities issued not only by domestic issuers but also foreign issuers, the issuance by foreign issuers is also regulated by FSCMA and other related regulations.

According to Article 118 of the FSCMA, the provisions for an SRS in the act are not applied to government bonds, local government bonds, special bonds, or other securities deemed to be those for which investors are properly protected through sufficient public disclosure pursuant to other acts, or as specified by Presidential Decree. According to Article 119 (2) 4 of the Presidential Decree of the FSCMA, the securities of nonresident issuers for which SRS provisions are not applied are those issued by an international financial institution under Article 2 (1) of the Act on the Measures for the Admission to International Financial Institutions, with approval from the Minister of MOSF, and following prior consultation with the FSC.

In consequence, other than the cases mentioned above, the provisions for an SRS apply to public offerings by every nonresident issuer, including foreign governments. However, the FSC may, if it is deemed necessary for protecting investors, prescribe and publicly notify different rules on the descriptions for an SRS and accompanying documents, taking into consideration the characteristics of the issuers, such as foreign enterprises, and the categories, types, and other factors of the securities (Article 129 of the Presidential Decree of the FSCMA).

The Provisions of Regulations on Issuance, Public Disclosure, etc. of Securities distinguish the contents of an SRS, depending on whether the issuer is a foreign enterprise or a foreign corporation that is not a foreign enterprise. Provision 2-11 (1) 1 of the regulation states that, in case of a foreign enterprise, the SRS shall contain

i. signatures of the representative director and director under Article 119 (5) of the FSCMA regarding the matters under subparagraphs of the article of the decree;
ii. details about the public offering or sale (7 items);
iii. details about the issuer (18 items); and
iv. where a foreign enterprise prepares, as its main financial statement, consolidated financial statements in accordance with International Financial Reporting Standards or other standards the issuer applies, the matters of some items in iii. shall be described based on such consolidated financial statements, including the financial statements of the foreign enterprise, and

the auditor's opinions shall contain an opinion on such consolidated financial statements and the financial statement of the foreign enterprise.

If a foreign issuer is not a foreign enterprise, Provision 2-11 (1) 2 of the regulation requires the SRS to contain the abovementioned signatures as well as the following items:

i. details about the issuance,
ii. details about the issuer,
iii. the current status of any alliance or investment in the Republic of Korea,
iv. the purpose of the use of funds raised by the issuance,
v. details on the underwriting and sale, and
vi. other matters necessary for the protection of investors.

The SRS requirements for the foreign corporation that is not a foreign enterprise are simplified compared with the requirements for a foreign enterprise.

Private placement issuance by foreign issuers is not restricted by SRS provisions. Instead, the issues are subject to the same regulations that apply to domestic issuers of private placements, including applicable resale restrictions. At the same time, private placements in the QIB Market, which is part of the overall private placement market, are free from resale restrictions because all transactions are only possible among QIBs as professional investors. Companies contemplating the issuance of QIB Market-eligible securities are required to register their bonds or notes with KOFIA (see section 6).

As is the case for public offerings by nonresident issuers, an issuance in the QIB Market by nonresident issuers is also subject to the Foreign Exchange Transactions Regulation, which contains obligations on the issuer such as reporting to MOSF.

Following an admission of a nonresident issuer to the QIB Market, there are no remaining substantive distinctions between types or domicile of issuers for the purpose of issuing debt securities. As such, the regulatory process for the issuance of debt securities by a nonresident issuer and related reporting obligations principally follow the processes outlined for placements in the QIB Market, in sections F.6 and G.2, respectively.

Nonresident issuers may also list their debt securities on KRX. For a complete description of the listing process, please refer to Chapter III.I.1.

4. Regulatory Process for a Public Offer and Sale

Unlike professional investors, ordinary investors may not have sufficient ability to assess the risks associated with an investment in debt securities and may not be well informed about such instruments. As such, bonds and notes issued to ordinary investors should be provided with a certain level of information. Therefore, except for the bonds that are considered to already ensure investor protection, as provided in Article 118 of the FSCMA, sufficient disclosure for the protection of ordinary investors should be ensured in the case of debt securities, which are publicly offered. To this end, Chapter 3 of the FSCMA prescribes the issuance of securities including the registration of a public offering and sale.

An offer of securities to the public in the Korean bond market requires the registration of the offer with the FSC. For that, the issuer or their appointed managing companies, which is the term used in the Korean bond market for the lead manager and other underwriters, will need to submit an SRS. The issuer is legally responsible for the submission.

Pursuant to the Regulation on Issuance, Public Disclosure, etc. of Securities as well as the Standard Instructions on Due Diligence for Non-Guaranteed Bond Issuance issued by the FSC, the issuer must sign a contract with a managing company or lead manager, which must include information concerning due diligence and intended book-building. Such lead management contracts shall be signed at least 10 business days before submission of the SRS and the contract must be reported to KOFIA within 5 business days of the contract signing date. The managing company or lead manager of the bond or note issuance will need to include in the SRS specific information on the conclusions from the mandatory due diligence on the issuer and the information to be provided on the issuance to the public.

In addition to the appointment of managing companies, the appointment of a paying agent and an indenture trustee is required for the offer of debt securities to the public; please see Chapter III.M.4. for a description of the functions of these market participants.

The regulatory process does not involve a formal approval from the FSC as such. Instead, the SRS has an effective date (see steps below) by which the FSC will have to raise an objection that would prevent the issuer and lead managing company from going ahead with the planned issuance.

The issuance of securities to the public also requires a prospectus; however, the prospectus only serves as the key disclosure document to the investors and need not be filed with the FSC together with the SRS.

The following steps describe the actions to be undertaken by the parties involved in the regulatory process to be able to issue debt securities via a public offer.

In the event that a bond or note, or a bond or note issuance program, offered to the public is intended to be listed on KRX, a listing approval will need to be obtained from KRX. The application and disclosure requirements will follow the provisions in the KRX Listing Rules. The listing approval process is further described in Chapter III.I.

Step 1—Submission of Securities Registration Statement to the Financial Services Commission

The issuer or its appointed managing company or companies (lead manager[s]) needs to submit an SRS to the FSC. According to Article 119 (5) of the FSCMA, senior representatives of the issuer will need to state in the signed SRS that no false statement or representation of a material fact, nor omission of a material fact, is contained in the descriptions in the SRS.

To the SRS, the issuer or its appointed managing company will need to attach the required specific supporting documents, which include a lead management agreement, a subscription agreement, indenture trustee agreement, paying agency agreement, and other relevant documentation.

KOFIA's Regulations on Securities Underwriting Business, etc. have been revised to prescribe a contract between a managing company and an issuer for corporate bond issuance, which must include due diligence details, such as information on business performance of the issuer, its financial status, and a review of comments regarding information provided in the SRS and other such reports.[5] The lead management contract typically used in the Korean bond market is based on a standard agreement proposed by KOFIA.

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[5] See http://eng.kofia.or.kr/brd/m_15/down.do?seq=166&file_seq=1&data_tp=A

The prospectus for the proposed bond or note issuance need not be filed with the FSC at the time of the submission of the SRS; instead, the prospectus will need to be filed with the FSC once the SRS becomes effective (see Step 3).

Pursuant to Article 119 (3) of the FSCMA, an issuer may make a so-called "forward-looking statement" concerning predictions or projections for the financial status of the issuer, its future business performance, and other such statements in the SRS filed with the FSC, such as

i. predictions and projections for the issuer's sales performance, including sales volume, size of income, and other business performance indicators;
ii. predictions and projections for the issuer's financial status, including size of capital and cash flow;
iii. information on the issuer's business performance in connection with the occurrence of a specific event or the establishment of a specific plan, or the targeted level at a certain point in time; and
iv. other information prescribed by Presidential Decree as those concerning future predictions and projections for the issuer.

Article 125 in the Presidential Decree of the FSCMA contains information on the mandatory descriptions in an SRS and its accompanying documents, including

i. the articles of incorporation or any other similar document that stipulates the operation of organizations, and rights and obligations of investors;
ii. a copy of the minutes of the general meeting of shareholders or directors' meeting at which a resolution was passed to issue securities or any other document evidencing a resolution to issue securities;
iii. a document substantiating the incorporation, equivalent to a corporation registration certificate;
iv. a document substantiating that permission, authorization, or approval has been granted where such permission, authorization, or approval from an administrative agency is required with respect to the issuance of securities;
v. a copy of a contract for the underwriting of securities, if such contract has been executed;
vi. a document containing the results of a preliminary listing examination by an exchange if the bonds are intended to be listed;
vii. a preliminary investment prospectus;
viii. a short-form investment prospectus; and
ix. other documents prescribed and publicly notified by the FSC as necessary for the protection of investors.

In the event an issuer would like to issue debt securities under a program, the issuer or its appointed managing company (or companies) will only need to file an SRS and lodge the prospectus for the entire program prior to the first issuance, pursuant to Article 119 (2) of the FSCMA.

Article 120 of FSCMA prescribes that the submitted SRS shall be effective on the day after the expiration of the time period prescribed by its Enforcement Rule (Article 12 of the Enforcement Rule of the FSCMA), considering, for example, the type of securities or the characteristics of the transaction. The time period shall begin on the next business day following the day on which the SRS is submitted and accepted by the FSC. A registration of debt securities for a public offering or public sale becomes effective from the day on which 7 days elapse after the acceptance date of the SRS. However, the period is reduced to 5 days in cases of secured bonds, guaranteed bonds, ABS, and debt securities publicly offered or sold in accordance with a universal shelf-registration statement.

The FSC shall not refuse to approve an SRS unless it is not prepared in conformity with the prescribed form, there is any false description or representation concerning a material fact, or there is any description or representation of a material fact is omitted.

Step 2—Book-Building by the Managing Companies

The managing companies (lead manager[s]) of the proposed bond or note issuance may engage in a book-building exercise on behalf of the issuer to determine the potential interest rate, and to capture potential investor demand for the purchasing price, interest rate, and investment amounts, to ensure a realistic picture for the chances to place the bond or note issuance in the market.

The issuer shall file an investment prospectus and a short-form investment prospectus with the FSC on the day on which the relevant SRS becomes effective. If a party intends to solicit an offer for a public offering of bonds and notes before the SRS becomes effective, the party may use (i) the preliminary investment prospectus prepared by the issuer; or (ii) use a short-form investment prospectus prepared by the issuer—through an advertisement, a notice, or a leaflet via newspapers, broadcasting, magazines, or an electronic transmission medium—after the relevant SRS is accepted.

Step 3—Publication of Prospectus (effective date of Securities Registration Statement) and Actual Issuance (including listing on KRX, if so intended)

The SRS will become effective 7 business days (for a non-guaranteed corporate bond) or 5 business days (for guaranteed bonds, collateral bonds, and ABS) after its submission to the FSC (Article 12 in the Enforcement Rule of FSCMA). On the effective date, the issuer may distribute and disclose the prospectus at its head office, the FSC, and financial firms that will accept applications for the proposed bond or note issuance.

The prospectus requirements are based on Article 123 of the FSCMA (Preparation and Public Notice of Investment Prospectus). The prospectus is to be prepared in accordance with Article 131 in the Presidential Decree of the FSCMA.

The investment prospectus needs to be composed of two separate sections, which are the title and the main text. The title of an investment prospectus contains the following information:

i. the effective date of the SRS filed;
ii. the price of the securities publicly offered or sold;
iii. the subscription period;
iv. the payment period;
v. the place at which a copy of the SRS and the investment prospectus are available for inspection;
vi. a statement that manipulation for stabilization or market creation may be attempted in the securities market, when the manipulation for stabilization or the marker creation is intended;
vii. a statement that some of the descriptions in the SRS are subject to change until the day immediately before the subscription date;
viii. a statement that the government does not confirm that the descriptions in the SRS are true or accurate, nor guarantee or approve the value of the relevant securities; and
ix. other matters prescribed and publicly announced by the FSC as necessary for the protection of investors.

The main text of an investment prospectus for bond or note issuance is required to have the following contents:

i. signatures of the representative director and the director responsible for filing the SRS;
ii. the following details concerning the public offering or sale:
    a. general matters concerning the public offering or sale;
    b. details of rights to the securities publicly offered or sold;
    c. investment risks ensuing from the acquisition of the securities publicly offered or sold;
    d. the underwriter's opinion on the securities publicly offered or sold, applicable only where there is an underwriter;
    e. the purposes for which the funds are used; and
    f. other matters prescribed and publicly announced by the FSC as necessary for the protection of investors;
iii. the following details concerning the issuer:
    a. an overview of the company;
    b. details of its business;
    c. information on its financial standing;
    d. an auditor's opinion;
    e. information on the organizational structure of the company, such as the board of directors, and its affiliated companies;
    f. information on shareholders;
    g. information on executive officers and/or employees;
    h. details of transactions with interested parties; and
    i. other matters prescribed and publicly announced by the FSC as necessary for the protection of investors.

The issuance of the bonds or notes is made on the day that the prospectus is published. The issuance of publicly offered bonds, payment by bondholders who buy bonds through a public offering, remittance of proceeds by the underwriter(s) to the issuer, and listing of bonds on KRX (if so intended) take place simultaneously on the issuance date. Listing is optional. For a comprehensive description of the listing process for bonds on KRX, please see Chapter III.I.

There is no post-issuance reporting obligation on KRX. If a bond is listed on KRX, the issuer will be subject to the applicable continuous disclosure obligations. Details may be found in section G.

5. Regulatory Process for Offers to Qualified Institutional Buyers

The issuance of debt securities in the QIB Market, or the OTC bond market segment for private placements of bonds or notes aimed at QIBs (see also Chapter III.N.2. for a detailed explanation), requires the registration of QIB Market-eligible securities with KOFIA as the administrator and SRO for the QIB Market.

There is no separate approval required from the FSC or FSS, and no SRS will need to be submitted. The issuer does not need to compile and publish a prospectus. The appointment of a managing company or an underwriter is not required for securities offered to QIBs, but in reality securities for QIBs can be registered by underwriters if they so have been appointed by the issuer. The issuer will need to appoint a paying agent. The agreements with the underwriter (if so appointed) and paying agent form part of the documentation to be submitted to KOFIA in support of the registration of QIB Market-eligible securities.

Issuers to be registered with KOFIA for the QIB Market may be (i) Korean companies with assets of less than KRW2 trillion as of the end of the previous financial year at the time of issuance, or (ii) foreign companies without any limit on the size of their assets.

An issuer of QIB Market-eligible securities is required to make public, through KOFIA's website, certain minimal information as required under the Detailed QIB Regulations, such as type of securities, name of the issuer, issuance amount, issuance date, maturity date, nominal interest rate, currency, name of dealers and/or brokers (if any), and other necessary items. A foreign issuer is also required to submit its annual report to KOFIA and make it public within 120 days after the end of each financial year.

QIB Market-eligible securities refer to debt securities, including corporate bonds, equity-related bonds such as convertible bonds, bonds with warrants, and ABS. For ABS, more than 80% of their underlying assets should be QIB Market-eligible debt securities. The issuer is required to designate KSD as the depository of the QIB Market-eligible securities and register the securities' details with KSD.

Due to the specific nature of the QIB Market and its requirements, a listing of QIB Market-eligible securities on KRX is presently not possible.

Step 1—Submit Registration Application for QIB Market Debt Securities to KOFIA

The issuer will need to register debt securities intended to be issued in and traded on the QIB Market with KOFIA. Pursuant to the Detailed QIB Regulations of KOFIA, the Application Form for Registration of QIB Market-eligible securities needs to contain

i. general information relating to the issuance, such as
   a. major rights of the securities;
   b. profile of the issuer (in the case of ABS, also profiles of the asset owner, details on the ABS, and details on the asset securitization plan);
   c. financial statements; and
   d. a legal opinion (in the case of a foreign company);
ii. minutes of the Board of Directors meetings;
iii. an excerpt from the corporate registry or equivalent document(s);
iv. a credit rating report (in any);
v. the subscription agreement and/or the arrangement agreement;
vi. the agency agreement for payment of principal and interest;
vii. the permit, approval, or application required by the Foreign Exchange Transactions Act or other regulations; and
viii. other agreements executed with related authorities in relation to the securities issuance.

The registration application will need to indicate if a shelf- or program registration is intended, including the total planned issuance amount and the terms of planned multiple issuances, but the supporting documents are similar to those for a normal registration.

If a foreign issuer intends to issue QIB Market-eligible securities under its existing international medium-term note (MTN) program, such as a euro MTN or a global MTN program, the issuer would need to file an application for a shelf-registration of QIB Market-eligible securities with KOFIA, and disclose all information relating to such an MTN program, as amended and supplemented, as required by KOFIA.

The aforementioned documents may be submitted in English. Foreign corporations need to receive a legal opinion on the issuance procedure for QIB registration, legitimacy of the relevant contracts, and integrity of the submitted document, among other subjects. In such cases, a legal opinion from a law firm based in the Republic of Korea needs to be attached.

Obtaining a credit rating is not mandatory for QIB Market-eligible securities to be issued.

Step 2—Registration of QIB Market Debt Securities by KOFIA

KOFIA reviews the registration application form and the submitted documents and will list QIB Market-eligible debt securities on the registry within 2 business days from the date when the registration application was received, or will reject the application if it has determined that the securities are not qualified. KOFIA will notify the applicant and KSD of the decision and related information.[6]

From a practical perspective, it is advisable to submit the application to KOFIA on an unofficial basis for an informal review approximately 5 days in advance to gain time for adjustments, as may be necessary.

6. Obligations after Approval and after Issuance

In the case of a public offer, issuers shall submit a report on the result of an issuance of securities to the FSC (FSS) without delay once a bond or note offering or distribution is completed. In contrast, no post-issuance reporting obligations exist for a placement in the QIB Market.

a. Public Offers

After the issuance of a bond or note to the public, the issuer or its appointed managing company will have to submit specific reports to the FSS as well as to KOFIA.

Article 128 of the FSCMA stipulates that an issuer or its appointed managing company should submit an issuance report, referred to as the "post-issuance report," to the FSS in the manner prescribed, and that it be publicly announced by the FSC. The report should be submitted without delay when a public offering or sale is complete.

Details that should be contained in the report are described in Article 2-19 (Report on Results of Issuance of Securities) of the Regulation on Issuance, Public Disclosure, etc. of Securities. The FSC shall make the post-issuance report available to the public for inspection at a specified place for 3 years, together with the SRS and the investment prospectus, and shall disclose them to the public through its website and other means, as applicable. Details of formats and methods of preparation of the post-issuance report are to be determined by the FSS Governor.

In addition, the managing companies (lead underwriter and other underwriters, if so appointed) will each have to send KOFIA an issuance report that reviews their respective underwriting performance within 5 business days of the issuance date. The reports are submitted electronically via the KOFIA website.

b. Placements in the Qualified Institutional Buyer Market

KOFIA, as the administrator of the QIB Market, imposes no specific requirements for post-issuance reporting on the issuers of QIB Market-eligible

[6] The KSD shall operate the system in a manner that only allows for the distribution of QIB Market debt securities among the QIBs registered with KOFIA.

securities. No report immediately following an issuance is required to be submitted. There is also no reporting requirement to FSS.

As part of the prescribed continuous disclosure (see also section G), the issuer will need to make available its annual reports, via the KOFIA website, within 120 days from the end of the respective financial year. This requirement is also applicable to foreign issuers.

7. Issuance Process Specific for a Domestic Financial Institution

The bonds issued by domestic financial institutions in the Republic of Korea are categorized into special bonds issued by public financial corporations and bank debentures or corporate bonds issued by financial institutions. The legal basis for bond issuance comprises the provisions in the laws under which the financial institutions have been established. A notable distinction is that special bonds do not require an SRS submission when the bonds are publicly offered, whereas the other bonds offered by financial institutions are subject to SRS regulations.

The issuance of bonds and notes by domestic financial institutions is determined by the financial institutions themselves and do not require approval from BOK.

8. Regulatory Process for Foreign-Currency-Denominated Debt Instruments

The Korean bond market does not have any limitation or restriction with regard to foreign-currency-denominated bonds or notes. Bonds and notes denominated in offshore Chinese renminbi, Japanese yen, and US dollars can be issued, traded, and settled in the Korean bond market.

As a result, there are no separate approvals or regulatory processes required to be observed for the issuance of foreign-currency-denominated bonds and notes. Thus, in principle, the regulatory process for foreign-currency-denominated debt instruments follows the processes described in the sections for public offers or the other applicable sections above.

However, a nonresident issuer of foreign-currency-denominated bonds and notes will need to file a proposed debt securities issuance schedule with MOSF before embarking on the listing process and before issuance. Proceeds raised by the issuance of such securities should be used for the specified purposes described at the time that the issuance was filed with MOSF.

G. Continuous Disclosure Requirements in the Korean Bond Market

The requirements for the continuous disclosure pursuant to bond or note issuance in the Korean market depend on the method of issuance.

1. Public Offers

The disclosure requirements for bonds and notes issued in the Korean bond market via a public offering are prescribed in the FSCMA and further detailed in the Ordinance of the Prime Minister. Distinctions are made in the regulations between the initial disclosure—in the form of the SRS (see section F)—and the continuous disclosure requirements during the lifetime of the bond or note, as well as the disclosure requirements for foreign issuers.

Articles 159, 160, and 161 in the FSCMA stipulate that "a corporation subject to business reporting" shall submit its business reports to the FSC. Pursuant to Article 167 in the Enforcement Decree of the act, the issuer that has publicly offered or sold non-guaranteed bonds, along with other securities, is included among those corporations subject to business reporting.

2. QIB Market-Eligible Debt Securities Placed in the QIB Market

KOFIA announced the relevant operating regulations with effect from 1 August 2016, including the duty of disclosure for issuers of QIB Market-eligible securities and the need for data submission and reporting.

Foreign corporations shall submit a business report or a document equivalent to a business report within 120 days after the end of each business year after issuing securities aimed at QIBs.

3. Debt Securities Listed on Korea Exchange

a. Companies Subject to Disclosure Regulations

A bond listing corporation is a company that has listed bonds and contingent convertible bonds on the KOSPI market of KRX. The corporation should fulfill obligations of regular disclosure and timely disclosure in compliance with the FSCMA and the KOSPI Market Disclosure Rules. The duration of the obligations stretches from the listing date to the de-listing date of the bonds.

b. Regular Disclosure

A bond listing corporation should submit an annual report to the FSC and KRX within 90 days after the end of the fiscal year. The annual report should cover overall conditions of the corporation, management performance, financial status, and audit opinions of an auditor, among other subjects. A corporation required to submit an annual report has to hand in an annual report (semi-annual report) within 6 months from the beginning of the fiscal year and an annual report (quarterly report) within 3 months and 9 months from the beginning of the fiscal year to the FSC and KRX within 45 days after each period elapses.

c. Timely Disclosure

When a material fact of the present or future regarding management of a bond listing corporation arises or there is a change in the rights of the bonds, and such fact or change cannot be provided by regular disclosure, KRX requires the corporation to make timely disclosure so that investors can be informed in a timely manner. If an issue required to be disclosed according to the KOSPI Market Disclosure Regulation occurs, the corporation should report it to KRX on the day it occurs (Article 57. [1]) or the following day (Article 57. [2]).

The major management issues to be reported are

i. where a bill or check issued by the corporation is dishonored or its current account transactions with a bank are suspended or banned;
ii. where its business activities are completely suspended, or a substantial part thereof is partially suspended (including the case where a decision on such suspensions was made);
iii. where it falls under any of the following, pursuant to the Debtor Rehabilitation and Bankruptcy Act:

   a. where an application for commencement, conclusion, or discontinuation of rehabilitation procedures is filed, and where it is notified of the court rulings on the commencement, conclusion, or discontinuation of rehabilitation procedures, the dismissal of the application for commencement of rehabilitation procedures, the cancellation of the decision on commencement of rehabilitation procedures, and the approval or disapproval of the rehabilitation plan, etc.; or
   b. where an application for bankruptcy is filed, and where it is notified of the court rulings on declaration of bankruptcy or dismissal of the application for bankruptcy;

iv. where a ground for dissolution provided for in the Commercial Act or other acts occurs;

v. where an event prescribed in articles of division and merger of the Commercial Act occurs;

vi. where a lawsuit that will have a significant influence on the listed bonds is filed;

vii. where, according to the audit report submitted by the certified public accountant auditor pursuant to the Act on External Audit, a fact falling under any of the following is found:
   a. where the certified public accountant auditor's opinion is adverse, disclaimer of opinion or qualified due to the limit placed on the scope of audit; or
   b. where the capital is completely impaired in the latest fiscal year;

viii. where, according to the semiannual review report, the auditor's review opinion is adverse or disclaimer of opinion;

ix. where it falls under any of the following in relation to the violation of accounting standards:
   a. where it is confirmed that the concerned corporation is informed or referred to the persecutor's office pursuant to the Regulation on External Audit and Accounting, etc. by the Securities and Futures Commission and the outcome thereafter is confirmed; or
   b. where the concerned corporation is indicted by the persecutor for the reasons of violating the accounting standards or the outcome thereafter is confirmed; however, this provision shall not apply to the case where a report was filed pursuant to the provisions of subparagraph (a); and

x. where a trigger event for conversion of contingent capital securities into stocks occurs, or a trigger event for mitigation of or exemption from the obligation to redeem the contingent capital securities and pay interest thereon occurs.

However, for convenience, if the corporation has listed its equities on the KOSPI or KOSDAQ market, and it makes disclosure on the issue to KRX on the day the issue arises, KRX shall deem that the corporation fulfills the reporting obligation as a bond listing corporation.

d. Electronic Bond Disclosure System

KRX has established an Electronic Bond Disclosure System to help bond listing corporations submit documents electronically rather than in person or by postal service or fax. The system consists of the disclosure submitting system and disclosure distributing system.[7] The disclosure submitting system is part of the KRX's disclosure system for bond listing corporations to register persons in charge of disclosure and inform investors of their management status through

[7] For the disclosure submitting system, see http://filing.krx.co.kr; for the disclosure distributing system, see http://kind.krx.co.kr

electronic documents. The disclosure distributing system is for the general public to access and search for disclosure documents submitted by bond listing corporations.

H. Self-Regulatory Organizations in the Korean Bond Market

The participation and daily business activities in the bond market in the Republic of Korea are organized, governed, and administered by the three SROs described in detail in this section.

1. Korea Financial Investment Association

KOFIA was created through the merger of the Korea Securities Dealers Association, Korea Futures Association, and Asset Management Association of Korea in February 2009, as set forth by the FSCMA.

KOFIA offers three different types of memberships: regular, associate, and special. Regular members consist of licensed financial investment services companies. Associate members are registered financial investment firms and concurrently run financial investment business entities. Special members include financial investment-related institutions, general administrative service companies, fund and bond pricing companies, and credit rating agencies. As of December 2017, KOFIA had 162 regular members, 116 associate members, and 23 special members.

The next two sections explain the key roles and functions of KOFIA in the financial investment sector in the Republic of Korea.

a. Establishment and Enforcement of Self-Regulatory Measures

KOFIA introduces and implements self-regulatory measures that foster a culture of investor protection and fair business practices in financial trading.

The revision of the Securities and Exchange Act in 2002 created the legal basis for enhancing KOFIA's self-regulatory function, while the passage of the FSCMA in 2009 broadened KOFIA's role as a self-regulatory body of the Korean capital market, by granting it the authority to oversee the financial investment industry.

Furthermore, the FSCMA stipulates how conflicts of interest between the association's key roles—its membership services and self-regulatory functions—are to be avoided. The act also defines KOFIA's powers of investigation and sanction, as well as its obligation to submit documentation to the relevant authorities and report on the status of its member firms' legal and regulatory compliance.

With the enactment of the FSCMA, the establishment of KOFIA's Self-Regulation Committee went from being optional to a mandatory requirement, designed to prevent any possible conflicts of interest between its member services function and the self-regulatory process.

The role of the committee is to protect investors while conducting self-regulation activities such as the enactment and deliberation of regulations; enactment and revision of regulations related to the business conduct of member companies; and administration of disciplinary measures to member companies, corporate executives, and employees failing to comply with the regulations.

Credit rating and bond assessment working groups under KOFIA also regularly monitor the rating track record of credit rating agencies and the bond valuation prices provided by bond pricing agencies.

b. Over-the-Counter Market Management

KOFIA also manages and administers the OTC bond market.

To enhance the transparency of OTC bond trading, KOFIA provides market participants with essential information, such as bond trading details, mark-to-market (MTM) yields, representative bond yields, and final quotation yields for different bond types through its website.[8]

As part of its mandate to achieve transparency, KOFIA prescribes a report of transaction details by counterparties to KOFIA within 15 minutes of the trade being concluded; KOFIA then discloses this information via the KOFIA Bond Information website.[9]

KOFIA also provides and maintains the BQS, which collects information on quotes and executed prices of bonds traded in the OTC market.

FreeBond, the trading support system that enables financial investment firms and market participants to discover quotes and supports trade negotiations was introduced in 2010, and was updated to K-Bond in 2017.

KOFIA also operates the QIB Market, which enables domestic and foreign companies to issue bonds to professional investors without an SRS. Please see Chapter II.F.5 for a detailed description of the QIB Market and its processes.

2. Korea Exchange

KRX operates a number of financial instrument exchange markets, including a bond market. KRX issues rules and regulations that are authorized by the FSC and applied to members and market participants' business activities.

KRX standardizes trading terms and conditions in its listed bond market to increase market efficiency and to operate a stable exchange market. In addition, it issues specialized rules for each market segment. In its KRX trading rules, KRX stipulates matters necessary for the trading of securities in the KRX bond market. Further details about trading on the KRX bond market can be found in Chapter IV.

In addition to trading regulations, KRX also promulgates listing rules. Listed bonds have been examined by KRX listing services on their suitability for the KRX bond market. In its listing rules, KRX stipulates the need to review the securities to be listed on the KRX bond market and the process to administer listed corporations and securities.

As part of its SRO role, KRX sets and enforces disclosure obligations by listed companies and the issuers of listed securities, including timely disclosure of events, as further described in section G. In its disclosure rules, KRX stipulates details of reporting, disclosure obligations, and the managing of corporate information in the KRX bond market.

The KRX Market Oversight Committee issues market oversight regulations to examine market fairness. Under the market oversight regulations, KRX stipulates matters

[8] See www.kofia.or.kr
[9] See www.kofiabond.or.kr

necessary for market surveillance, investigation into abnormal trading activities, member inspection, inter-market surveillance, and the disciplinary actions taken against members and their officers and employees for unfair trading.

3. Korea Securities Depository

KSD was established on 25 April 1994, as a special public organization with a diversified ownership structure, to function as a single, common, and reliable central securities depository for all eligible types of securities. KSD's roles and functions—inherited from its predecessor organization, the Korea Securities Settlement Corporation—were also enhanced to include international services for investors.

At the end of 2017, KSD held deposit securities valued at KRW3,997 trillion (USD3.8 trillion at the time). KSD handles the settlement of securities traded on KRX as well as the settlement of equity and bonds traded in the OTC market, currently processing a daily settlement volume of KRW22.1 trillion.

At the end of 2017, KSD participants totaled 1,244, comprising financial institutions, including securities companies, banks, and insurance companies, as well as foreign investors. Participants must be a depositor under the Regulation on Deposit Service of Securities; meet financial soundness standards as set forth in the Detailed Rules of KSD; and have sufficient human resources, computer systems, and other tangible facilities to perform the work as a settlement member.

As an SRO, KSD sets rules for its operation and participants. Changes to KSD rules require approval from the FSC. This ensures the enactment of fair and reliable regulations, and promotes stability and predictability when enforcing market practices as prescribed by the rules.

The detailed functions and a complete description of the role of KSD in the Korean securities market at large and its post-trade services can be found in the Phase 2 Report of the ABMF Sub-Forum 2 (SF2), *Information on Transaction Flows and Settlement Infrastructures*, dated 13 June 2014.[10]

I. Rules Related to Licensing and Trading Conventions

This section refers to the regulatory framework for licensing and trading conventions. For information on the actual trading of debt securities in the Korean bond market, please see Chapter IV.

1. Rules Related to Licensing

KRX, KSD, and KOFIA are bond market infrastructure institutions based on the provisions of the FSCMA. Most of the other participants in the bond market are financial investment business entities that must be authorized by the FSC to carry out their activities in the capital market, pursuant to provisions in the FSCMA. In the Korean bond market, the term "authorized" by FSC is largely similar to licensing found in other markets. The FSCMA distinguishes between authorization for which permission by the FSC is required, and registration, which does not require FSC permission.

Entities acting in the primary bond market must be authorized for investment trading business. Investment trading business under the act comprises selling and purchasing financial investment instruments, issuing and underwriting securities, inviting offers,

[10] See http://www.adb.org/publications/asean3-information-transaction-flows-and-settlement-infrastructures

offering, and accepting offers for securities on one's own account or in the name of another party.

Participants in the secondary bond market conduct investment brokerage business and should be authorized for participation by the FSC. Investment brokerage business comprises selling and purchasing financial investment instruments.

The procedures for authorization and registration of financial investment businesses, including the aforementioned businesses, are given in Chapter 1 of Part II of the FSCMA. For an investment advisory business or investment trust business in the Korean bond market, a registration is required in accordance with the procedure prescribed in section 2 of the chapter.

As a participant in the capital market, a single business unit can be defined through the combination of factors such as the types of financial investment business, the scope of financial investment products, and classes of investors. An entity that wishes to operate a registered financial investment business shall create a single business unit by combining the aforementioned three factors and select all or part of the business units for registration with the FSC as a financial investment business.

Based on the Enforcement Decree of the FSCMA, if a financial investment company launches an investment trading service that handles debt securities, equity securities, beneficiary securities, derivatives-combined securities, and securities depository receipts, the company should have minimum net assets of KRW50 billion. However, if it is only managing debt securities, the net asset requirement is KRW20 billion. For an investment brokerage business, the minimum net asset requirement is KRW1 billion, with the amount halved to KRW500 million if the company only targets professional investors who require relatively lower levels of protection.

2. Rules Related to Trading Conventions

KOFIA specifies the trading conventions for the OTC market in the K-OTC Market Regulations and in additional regulations, rules, and guidelines for specific products and activities. According to Article 5-4 in Part V of the Regulations on Financial Investment Business, payment for OTC traded bonds shall be settled within 30 business days from the day immediately after the date on which a seller and a buyer enter into a trading contract, which is concluded through negotiation. It also infers that OTC bond trading is carried out by negotiation conducted by phone or messenger. See the next section for details and the list of KOFIA regulations and rules in Appendix 3.

Trading conventions for the exchange market segments on KRX are contained in the KOSPI Market Business Regulations, including for repo transactions. Article 46 (Principles for Trading of Debt Securities) stipulates that debt securities shall be traded by way of an individual auction, which shall be classified into a period call auction and a continuous auction. The execution of bond trades in the major bond market segments of KRX is carried out through these auction methods.

Nevertheless, the regulations also acknowledge special cases. Article 53-2 stipulates that KRX may execute a trade at a price or repurchase rate which is determined by negotiation between a party who requests for a quotation and the other party who places a quotation in response to the quotation request during the regular trading session. See next section and Chapter IV.H for more details on repo. Chapter IV of the Market Business Regulations contains provisions on the trading of debt securities.

J. Rules Related to Bond Listing or Registration, Trading, and Disclosure

KOFIA and KRX, being SROs for the OTC and exchange markets, respectively, set rules for their constituents and trading participants. These rules include provisions for the listing or registration of debt securities, trading of debt instruments in their respective markets, and prescribed disclosure at the time of issuance and throughout the lifecycle of such debt instruments. The rules are approved by the FSC.

1. OTC Market Rules issued by KOFIA

In addition to its Articles of Association and general regulations on business conduct, the regulations and rules published by KOFIA are often specific by the product or activities of its participants. As an example, KOFIA has issued a number of separate regulations on the OTC market and the QIB Market, respectively. Chapter III of the Market Business Regulations contains provisions on the OTC Trading of Bonds. A list of relevant KOFIA regulations and rules is available in Appendix 3.

2. Rules of Korea Exchange

KRX issues market listing, disclosure, and business regulations for its KOSPI market, which includes the bond market platform.

a. KOSPI Market Business Regulations

KRX stipulates matters regarding the trading of securities (including bonds) in the KOSPI market in the KOSPI Market Business Regulation, pursuant to Article 393 of the FSCMA.

Article 393 (Business Regulations) (1) contains provisions with respect to transactions on the securities market and requires the exchange to issue Securities Market Business Regulations. Such regulations are expected to contain prescriptions on

i. the type of transactions and the consignment thereof;
ii. the opening, closing, suspension, or temporary closing of the securities market;
iii. the methods of conclusion of transaction contracts and settlement thereof, provided that delivery of securities and payment shall be excluded;
iv. the regulation of transactions such as payment of margin; and
v. other subjects relevant for securities transactions.

Detailed information on trading regulations is provided in Chapter IV of the KOSPI Market Business Regulation.[11]

b. KOSPI Market Listing Regulations

KRX reviews securities (including bonds) to be listed on the KOSPI market in compliance with Article 390 of the FSCMA. It stipulates matters required for controlling listed corporations and securities in the KOSPI Market Listing Regulations.

Under Article 390 (Listing Regulations), KRX shall prescribe Listing Regulations for Securities (Listing Regulations) for reviewing the securities to be listed and

[11] See http://global.krx.co.kr

for managing listed securities. Listing Regulations shall include the following subjects:

i. listing standards and listing review of securities;
ii. de-listing and de-listing standards for securities;
iii. suspension of transactions of securities and its revocation; and
vi. other subjects necessary for the management of listed corporations and listed securities.

Details on bond listing provisions are provided in Part III of the KOSPI Market Listing Regulation, which is available on the KRX website.[12]

c. KOSPI Market Disclosure Regulations

KRX has issued Disclosure Regulations, which include necessary prescriptions for the reporting, disclosure, and management of information regarding listed corporations, pursuant to Article 391 of the FSCMA.

According to Article 391, disclosure regulations shall include details on the following matters:

i. on which a stock-listed corporation is required to make a report;
ii. on the methods and procedures that a stock-listed corporation is required to follow in making a report or disclosure;
iii. on the requests made by the KRX to report or confirm as to whether a rumor and news concerning the listed corporation of stock certificates, for example, is true or not and as to the cause of remarkable changes in the price or trading volumes of securities issued by the listed corporation of stock certificates;
iv. excluded from the disclosure or report taking into account the protection of investors and confidentiality in management of the stock-listed corporation;
v. on the disclosure of details reported by the stock-listed corporation;
vi. as to the standards to decide whether a stock-listed corporation has committed a violation or what type of violation has been committed under subparagraphs i. through iv. as well as the measures taken in response to the violation;
vii. on the management of the stock-listed corporation such as the suspension of transactions;
viii. on the compliance with supervision over the report obligation of the stock-listed corporation; and
ix. other necessary matters on the report or disclosure by the stock-listed corporation.

Detailed information is provided in Part II of the KOSPI Market Disclosure Regulations, available on the KRX website.

K. Market Entry Requirements (Nonresidents)

1. Nonresident Issuers

There are no restrictions or limitations for nonresident issuers, but some specific reporting requirements or conditions will apply when issuing bonds or notes in the Korean bond market.

[12] Footnote 11.

If a foreign company raises funds through the issuance of bonds or notes denominated in Korean won or a foreign currency, the foreign company is required to register with MOSF under provisions in the Foreign Exchange Transactions Act.

When a nonresident issuer intends to list foreign bonds (bonds issued by a foreign corporation) on KRX, stricter listing review requirements are applied compared to those applied to bonds issued by Korean corporations. KRX limits foreign corporations eligible for listing their foreign bonds to international financial organizations, foreign governments, corporations that have listed stocks on foreign exchanges, and corporations that have listed foreign stocks on KRX. An eligible foreign corporation is required to hold equity capital worth KRW10 billion or more, the credit rating of the bond to be listed should be at least BBB (a domestic bond listing carries no minimum credit rating), and the corporation should appoint a domestic listing agent who represents the issuer or acts as a proxy on behalf of the issuer for all interactions with KRX.

2. Foreign Investors

Foreign investors wishing to access the Korean bond market will need to obtain an Investment Registration Certificate (IRC) before investing, regardless of whether they wish to access the OTC market or trade securities in the exchange market. The IRC concept and the process of obtaining an IRC are explained in section M.

Foreign investors wishing to participate in the QIB Market will need to register with KOFIA as a QIB prior to investing. The registration criteria are further explained in Chapter III.H and N.

L. Market Exit Requirements (Nonresidents)

1. Nonresident Issuers

There are no market exit requirements for nonresident issuers.

2. Foreign Investors

There are no market exit requirements for foreign investors. Foreign investors may repatriate their capital investment and interest free of restrictions. At the same time, if the proceeds from disposal of securities or interest are received in Korean won, the foreign investors will need to convert the amount into a foreign currency before remitting the funds abroad.

M. Regulations and Limitations Relevant for Nonresidents

1. Foreign Investor Registration

Foreign investors who wish to acquire or dispose of securities listed on the securities market, or securities offered or sold with the intention of a listing, must register with the FSS.

Foreign investors who wish to buy and sell bonds and notes listed on KRX, or bonds and notes that will be listed on KRX, such as bonds and notes publicly offered or sold in order to be listed on the exchange for the first time, also must be registered with the FSS.

The documents required by the FSS should be submitted in person or through a local agent so that an IRC can be issued. After submitting an IRC, a licensed local investment dealer or investment broker may open an account for securities trading for these foreign investors.

The foreign investor registration aims to manage foreign investment limits and other related issues. Through the system, statistics on foreign investment including foreign holdings are able to be compiled. Furthermore, the IRC is used to authenticate the real name of an investor when opening an account, easing the burden placed on the investor of submitting other identification documents to individual financial investment companies or other intermediaries.

2. Investors Subject to Registration

Generally, an individual of foreign nationality who has not maintained residence in the Republic of Korea for more than 6 months will be subject to registration if he or she intends to invest in listed securities. This means that a Korean citizen residing outside the country need not register for an IRC, given his or her Korean nationality.

The same applies to corporations. Any corporation that does not have an office in the Republic of Korea and was established according to foreign laws must register in order to invest in listed securities in the Republic of Korea. However, local subsidiaries of foreign corporations established by Korean nationals are viewed as foreign entities; therefore, they must register with the FSS for an IRC.

In addition, the main office and branch offices (except branch offices established within the Republic of Korea) of a foreign corporation are viewed as a single foreign entity and are only required to have one IRC issued.

In the case of investment funds, however, a master fund and sub-fund cannot be registered together, according to Article 6-10 (2) of the Regulation on Financial Investment Business, in order to ensure the effectiveness of the investment registration. If they are registered together, a single beneficiary owner may eventually have more than two certificates. However, when a master fund is not registered, each sub-fund is able to register individually since these sub-funds are considered separate beneficiary owners.

3. Exemptions from Registration

Foreign nationals, foreign-incorporated entities, or local branches of a foreign corporation engaging in business activities in the Republic of Korea that qualify for “foreigner under national treatment” status shall be exempt from registration upon submitting documents verifying their status.

Registration will also be exempted in the case of acquiring or disposing of stocks on the OTC market for the purpose of “direct investment,” but the details of the relevant transactions must be reported promptly to the FSS.

Exemption from registration will also apply to cases where government bonds and MSBs are acquired and sold using an omnibus account at an international central securities depository (ICSD).

4. Specific Registration Provisions

When registering as an investor, one IRC is issued per beneficiary owner. There are certain exceptions however to make investing more convenient for foreign investors.

Overseas branches or business offices of a domestic investment dealer or investment broker can register separately under the name of the financial institution concerned when it is necessary to arrange the outsourcing of transactions in the securities market.

And a foreign financial institution can register separately under its own company name when it needs to manage its own assets and customers' assets separately.

An investment dealer or an investment broker can also separately file for registration of an investment under its own name when it is necessary to process entire orders for an investor group and allocate purchased securities to them. A foreign investor group can submit orders by using the same IRC.

Here, foreign investors eligible for submitting orders are those where the investment manager of the investor group has reported details to the relevant investment dealer or investment broker before engaging in trading. Investment dealers and brokers have an obligation to keep a record of orders, order execution, and order distribution.

5. Specific Registration Provisions

According to the Detailed Rules of the Regulation on Financial Investment Business, foreign investors, or corporations and institutions engaged in securities trading for foreigners, have an obligation to report. The reporting is normally done by the investor's custodian on behalf of the investor as part of service provision as the standing proxy. The reporting includes transactions by nonresidents as well as transactions involving foreign currency.

N. Regulations on Credit Rating Agencies

This section covers the regulations and requirements applicable to credit rating agencies operating in the Republic of Korea and their business. For the actual credit rating requirements in the Korean bond market, and the application of such credit ratings in the issuance process for bonds and notes, please refer to Chapter III.N.

Article 9-26 of the FSCMA stipulates that credit rating business means the business of credit assessment on, for example, financial investment instruments, enterprises, collective investment scheme, and assigning a credit rating represented by symbols or numbers, and providing such credit ratings to the issuer, underwriter, investors, and other interested persons, or allowing them to inspect such credit ratings.

In order to conduct credit rating business, an eligible entity must be authorized by the FSC, pursuant to Article 335 of the FSCMA. Any entity that wishes to obtain authorization shall file an application for authorization with the FSC. The authorization procedure and other details on the authorization are prescribed in Chapter III-2 of Part IV of the FSCMA. An entity that wishes to obtain authorization before final authorization may file an application for preliminary authorization with the FSC. Each credit rating agency shall continue to meet the requirements for authorization, while engaging in credit rating with proper authorization. A credit rating company may conduct concurrent and incidental businesses, such as business as a bond rating company.

Under its mandate on improving the transparency of the bond market, KOFIA regularly monitors the rating track record of credit rating agencies and their performance through its credit rating working group. KOFIA officially announces those results once a year via the KOFIA Bond Information website. The working group consists of seven members, including experts from related fields such as finance, law, and accounting.

III

Characteristics of the Korean Bond Market

Since the Korea Bond Market Guide was first issued in 2012, substantial changes to the regulatory environment as well as to market features have occurred. The purpose of this chapter is to give an updated, comprehensive view of the specific characteristics of the Korean bond market.

A. Definition of Debt Securities

Article 4 (3) of the FSCMA defines debt securities in the following manner:

> The term "debt securities" in this Act means state (government) bonds, local government bonds, special bonds (referring to bonds issued by a corporation established by direct operation of an Act; hereinafter the same shall apply), corporate bonds, corporate commercial papers (referring to promissory notes issued by a company for raising the funds required for its business, which shall meet the requirements prescribed by Presidential Decree; hereinafter the same shall apply), and other similar instruments, which bear the indication of a right to claim the payment.[13]

B. Types of Bonds and Notes

In the Korean bond market, bonds are classified by several criteria (e.g., the type of issuer, method of interest payment, options embedded with the bond, and redemption period, among others).

The Korean bond market does not have any limitations or restrictions on the choice of currencies of denomination of debt instruments. KRW-denominated bonds issued by nonresident are called Arirang bonds, whereas foreign-currency-denominated bonds issued by nonresidents are called Kimchi bond. In practice, the settlement of bonds and notes denominated in Korean won, Japanese yen, offshore Chinese renminbi, and US dollars is supported. Bonds denominated in these currencies can also be deposited with KSD.

The individual features of bonds and notes issued in the Korean market are further explained in the subsequent sections.

[13] See http://www.law.go.kr/eng/engLsSc.do?menuId=1&query=financial+services+and&x=28&y=27#liBgcolor12

1. Bonds and Notes Categorized by Type of Issuer

Bonds and notes issued in the Korean market may be best distinguished by the type of issuer. While the market is dominated by government bonds, it also features government-like bonds and corporate bonds.

a. Government Bonds

Currently issued government bonds include KTBs, National Housing Bonds (NHBs) Types 1 and 2, and Foreign Exchange Equalization Fund Bonds, which are denominated in a foreign currency.

Among these government bonds, KTBs are issued in the largest volume and trading is active. Accordingly, the on-the-run KTB market yields serve as a benchmark yield. There are currently six types of KTBs issued, according to maturity; these are 3-year, 5-year, 10-year, 20-year, 30-year, and 50-year KTBs. These KTBs fall into fixed-interest type bonds (3-year, 5-year, 10-year, 20-year, 30-year, and 50-year issuances) and inflation-linked KTBs (limited to the 10-year maturity). Inflation-linked KTBs link the principal and coupon rate of the KTB to a consumer price index.

KTBs are fungible issues, meaning that the issuing conditions, including maturity and coupon rates, are the same for bonds issued within a certain period of time. Currently, 3-year KTBs and 10-year KTBs are issued on 10 June and 10 December each year, 5-year KTBs are issued on 10 March and 10 September, 20-year KTBs are issued on 10 September, and 30-year KTBs are issued on 10 March. The coupon rates of KTBs are set to multiples of 0.125%.

For details on the issuance methods of KTBs, please refer to Chapter III.E.

There are two ways to redeem KTBs: (i) redemption at maturity, and (ii) redemption before maturity. Through the redemption at maturity, the principal is redeemed in a lump sum upon maturity of the bond, while the interest is paid every 6 months from the issuing date. If the date of the redemption of principal falls on a public holiday, the principal is due on the following business day. If it does not coincide with a public holiday, then it is due on the prior business day. The amount paid corresponds to the amount designated for the original maturity date, regardless of whether it is a public holiday.

Redemption before maturity may be carried out via KTB reverse biddings held for Primary Dealers and are purchased directly from KTB holders when MOSF deems it necessary. There is no bidding limit for Primary Dealers, and the minimum amount for each issue is KRW1 billion (par value), with incremental increases in multiples of KRW1 billion.

The winning bid from a Primary Dealer is decided consecutively from interest rates that have been bid for each issue, spanning from the highest interest rate down.

The purchased amount is derived by applying the lowest rates from each of the interest rate groups, which are grouped in intervals of 2 basis points from the lowest bid upward. BOK handles the redemption at maturity, as well as any redemption before maturity and interest payments for KTBs. For that purpose, BOK makes deposits to KSD’s current deposit account, and KSD transfers principal and interest to the deposit account of the institution that holds the KTBs.

b. Municipal Bonds

Municipal bonds are issued by local governments, which comprise regional development bonds and urban railway bonds.

Regional development bonds are issued by local governments under the Local Autonomy Act. Currently, 18 municipalities issue the bond with 5-year maturity. Urban railroad bonds are issued under the Urban Railway Act to finance subway construction in major cities. The issuing entities are not the local subway corporations but the local governments. Urban rail bonds are issued by five municipalities, including Seoul.

c. Special (Purpose) Bonds

Special (purpose) bonds are issued based on the laws on which the issuers are established. Since these issuers are government agents, the bonds may be regarded as government agent bonds, similar to the practice in other countries.

This type of bond consists of the issues from financial institutions such as BOK, the Korean Development Bank (KDB), and the Export–Import Bank of Korea, and issues by nonfinancial public corporations such as Korea Land & Housing Corporation and Korea Rail Network.

For example, the Korea Development Bank Act provides for the issuance of industrial finance bonds. Article 23 of the act stipulates that (i) KDB may secure funds necessary for performing business operations by issuing industrial finance bonds; (ii) industrial finance bonds shall be issued exclusively by KDB; and (iii) the aggregate of the amount of industrial finance bonds issued, the outstanding balance of bonds and debts guaranteed, and the outstanding balance of debts guaranteed or accepted by KDB shall not exceed 30 times the aggregate of the paid-in capital of KDB and its reserve funds.

Among special bonds, MSBs, which are issued by BOK (see also section C), represent a substantial portion of the overall bond market. As such, statistics on the issuance of MSBs are, in practice, managed separately from the statistics for other special bonds.

d. Private Sector Bonds (Corporate Bonds)

Private sector bonds can be categorized into (traditional) corporate bonds issued by traditional (usually manufacturing) business firms and corporate bonds issued by financial business firms such as commercial banks and specialized credit finance business firms. The bonds issued by financial institutions, such as commercial banks and credit specialized financial business companies (e.g., credit card companies and leasing companies), have long been regarded as special bonds.

For the issuance of bank debentures, Article 33 of the Banking Act stipulates that a bank may issue debentures within the limit specified by Presidential Decree by up to five times its equity capital. A bank can issue bank debentures with a resolution by the board of directors or a general meeting of stockholders.

Corporate bonds can be classified further into guaranteed bonds, collateral bonds, and non-guaranteed bonds.

i. Guaranteed Bonds

Guaranteed corporate bonds refer to corporate bonds where a financial institution guarantees the redemption of the principal and payment of interest. Such guarantees of the principal and interest payments are provided by banks, the Korea Credit Guarantee Fund, the Korea Technology Finance Corporation, merchant banks, financial investment companies, and surety insurance companies. The issuing company pays a guarantee fee to the guaranteeing company.

ii. Collateral Bonds

Collateral bonds are secured by physically guaranteeing the redemption of the principal and payment of interest. They are issued in accordance with the Secured Bond Trust Act.

iii. Non-Guaranteed Bonds

Non-guaranteed bonds are issued based on the issuer's credit without a guarantee provided by a financial institution or collateral provided by the issuer for the repayment of the principal. Most Korean corporate bonds are issued as debentures. The underwriters of the bonds are required to undergo a credit assessment of the debentures from two or more credit rating agencies.

Corporate bond issuances also can be divided into direct issuances and indirect issuances depending on who bears the issuing risk. Please see section E for more information on these methods of issuance.

2. Bonds Categorized by Interest Payment

Bonds can also be categorized by their interest payment as either coupon bonds, discount bonds, or compound bonds. Coupon bonds refer to corporate bonds with coupons denoting the payment of interest at a regular schedule. Discount bonds are bonds where the principal and interest rate are stated at par value and the interest is discounted from par value upon purchase. Compound bonds involve the computation of compound interest for the interest cycle. Thereafter, the principal and interest are paid in a lump sum on the date of maturity.

Every KTB and most corporate bonds are coupon bonds. Short-term MSBs and special bonds issued by financial corporations are discount bonds. NHB Type 1 is a representative compound bond.

In addition, there are fixed-rate bonds and floating-rate notes. A fixed-income bond involves the payment of fixed periodic returns, and a floating-rate note has a variable interest rate that is linked to the benchmark interest rate.

3. Bonds Categorized by Redemption Period

Depending on the redemption period, bonds can be divided into short-term bonds, medium-term bonds, and long-term bonds. Generally, short-term bonds have redemption periods under 1 year; medium-term bonds, between 1 year and 10 years; and long-term bonds, over 10 years.

MSBs comprise notes with maturities as short as 14 days and bonds with maturities up to 2 years. KTBs are issued with medium- to long-term maturities (see also section 1.a).

4. Bonds Categorized by Embedded Option

Bonds can be categorized by an embedded option as convertible bonds, bonds with warrant, exchangeable bonds, participating bonds, or bonds with a call or put option. Convertible bonds can be converted to the issuing company's equity on certain conditions. Meanwhile, bonds with warrants entitle the holder to purchase a certain quantity of any future issue of the company's stocks at a fixed price after a set period has passed.

Exchangeable bonds permit the holders to exchange their bond holding for the listed shares of a company under previously agreed conditions within a set timeframe. Participating bonds entitle the holder to receive dividends. Bonds with a call option allow the issuer to redeem all or part of the bond before it reaches its maturity date, whereas bonds with a put option allow the holder of the bond the right to demand the issuer to repay the principal on the bond.

5. Issuance Programs

The issuance of bonds or notes by issuers using an issuance program is possible in the Republic of Korea. To create an issuance program, a so-called "universal shelf-registration statement," instead of a standard SRS, needs to be filed with and accepted by the FSC.

6. Bonds Issued by Nonresidents

Nonresidents may issue bonds and notes in the Republic of Korea (see Chapter II.K for details on any specific provisions). KRW-denominated bonds issued by nonresidents are called Arirang bonds, whereas foreign-currency-denominated bonds issued by nonresidents are called Kimchi bonds. Offshore Chinese renminbi bonds issued in the Republic of Korea are considered to be a type of Kimchi bond. As of the end of 2017, four Arirang bonds amounting to KRW170 billion and 12 Kimchi bonds with a combined face value of KRW840 million were listed on KRX.

7. Asset Backed Securities

The issuance of ABS, which are common in the Korean bond market, is based on the provisions of the Asset-Backed Securitization Act enacted in 1998. For more information on ABS, please refer to section P in this chapter.

C. Money Market Instruments

Money market instruments are short-term financial products. In the Republic of Korea, representative instruments that are actively issued and traded include certificates of deposit issued by banks, and commercial paper and short-term electronic bonds issued by corporations.

1. Instruments Issued by the Bank of Korea

BOK issues MSBs to help absorb liquidity in support of its monetary policy. The issuance is subject to the ceiling on total outstanding volume set every 3 months by the Monetary Policy Committee. MSBs are discount and coupon instruments issued in 13 standardized tenors ranging from 14 days to 2 years, which explains their significant issuance size and turnover in the market. As such, MSBs can be considered both money market instruments and bond market issuances.

Short-term MSBs, which have a maturity of less than 28 days, are issued at irregular intervals depending on market conditions, while the bidding date for MSBs with a maturity of 28 days or longer is pre-fixed every month.[14]

2. Instruments Issued by Corporates

Corporations and other businesses operating in the Republic of Korea issue a number of money market-type instruments, such as commercial paper and short-term electronic bonds. These short-term financial instruments are transacted in the debt market along with short-term bonds. They compete in terms of yields as well as market share.

a. Commercial Paper

Commercial paper is a promissory note issued by a company for the raising of funds required for its business operation. It is a financial instrument typically acquired by a bank (commercial bank or special purpose bank) and is prescribed in Article 4 of the Enforcement Decree of the FSCMA; the bank typically makes a payment on behalf of a company under a commission agreement with the company, who then issues the commercial paper. The commercial paper should be produced in the form of a bill with the words "corporate commercial paper" printed on it.

b. Electronic Short-Term Bonds

Electronic short-term bonds are issued based on the Act on Issuance and Trading of Electronic Short-Term Bonds, which was enacted in January 2013, to enable a market for a registered form of short-term financial instruments, as an alternative to commercial paper. Electronic short-term bonds are issued at a discount and may be traded in multiples of KRW100 million.

The electronic short-term bonds system was adopted to develop the short-term financial market and lay the foundation for the introduction of electronic securities. Under this system, the issuance, circulation, and exercise of rights of short-term bonds (issued with maturities of 1 year or less for short-term corporate financing) are processed electronically through an electronic registrar.

KSD registers and manages the details of issued electronic short-term bonds through the issuer account book and the account manager's proprietary and client management account books.[15]

D. Segmentation of the Market

To provide a better illustration of the segmentation of the different types of debt securities issued in the Korean bond market, Table 3.1 gives an overview of the outstanding amounts by type of instrument as detailed in Section B.

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[14] Information adapted in part from Bank for International Settlements. 2012. Public Debt and Monetary Policy in Korea. *BIS Paper.* No. 67. https://www.bis.org/publ/bppdf/bispap67p.pdf

[15] Specific information on electronic short-term bonds is available from the KSD website at https://www.ksd.or.kr/eng/static/EB1504000000.home?menuNo=117

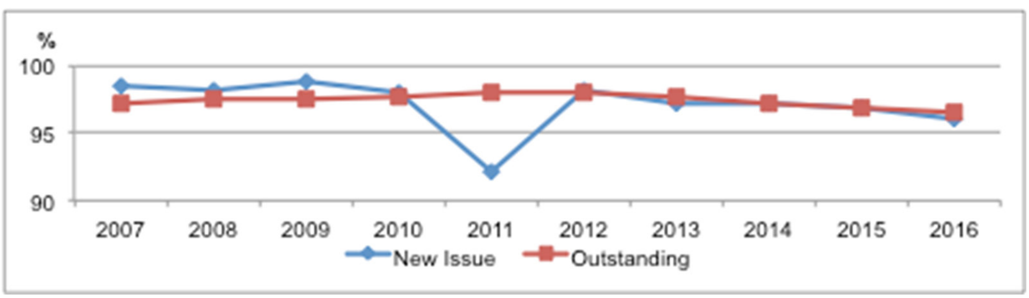
Table 3.1: Segmentation of the Market—Outstanding Value of Korean Won Debt Securities in the Republic of Korea by Type
(as of 31 December 2016)

Sector	Type of Bond	Outstanding Amount (KRW trillion)	% of Total
Public	Government Bond	581.3	33.2
	Municipal Bond	21.2	1.2
	Special Bond	336.6	19.2
	MSB	168.4	9.6
Private	Bank Debenture	267.2	15.3
	Other Financial Bond	107.1	6.1
	Corporate Bond	225.6	12.9
	ABS	43.3	2.5
	Total	1,750.6	100.0

ABS = asset-backed securities, MSB = monetary stabilization bond.
Source: Korea Financial Investment Association. http://www.kofiabond.or.kr/

As a further distinction in the bond market in the Republic of Korea, the proportion of issuance of bonds or notes via private placement has generally been less than 4% of the overall bond issuance volume (Figure 3.1).

Figure 3.1: Proportion of Publicly Offered Bonds in the Republic of Korea



Source: Infomax. http://yonhap.einfomax.co.kr/newinfomax/

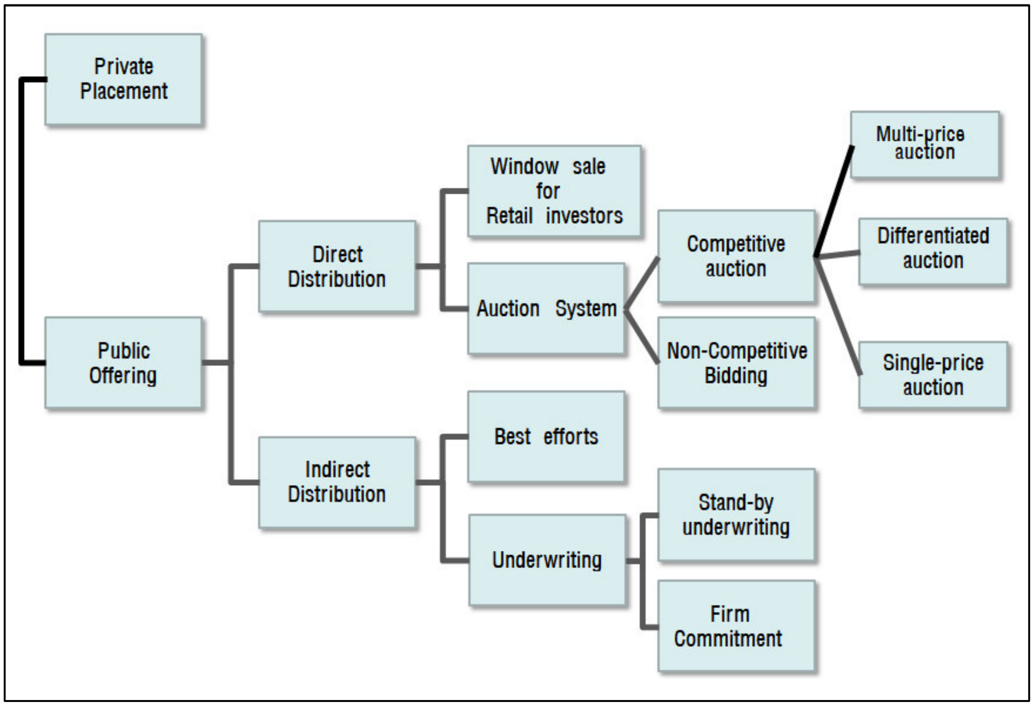
E. Methods of Issuing Bonds and Notes (Primary Market)

The Korean bond market offers a number of issuance methods for bonds and notes, often depending on the individual types of bonds and notes, and as prescribed in regulations or by the respective SRO, or as evolved in market practice.

1. Overview of Issuance Methods

In the Republic of Korea, bonds and notes are issued by either public offering or private placement. These issuance methods are divided into direct distribution and indirect distribution depending on the involvement of a financial institution, which acts as a managing company during the issuance process (Figure 3.2).

Figure 3.2: Overview of Bond Issuance Methods in the Republic of Korea



Source: Korea Financial Investment Association.

Debt securities issued by the public sector, such as government bonds and bonds issued by public corporations, are issued via the direct distribution method. KTBs are issued regularly to Primary Dealers and Preliminary Primary Dealers through the electronic auction system that is part of BOK Wire+. In these cases, competitive auction is the usual issuance method, in particular when involving institutional investors. KTB and MSB issuances are the representative examples of competitive auction.

The institutional investors who want to invest large amount of bonds need to participate in the auction. Investors interested in smaller investment sizes may participate in issuances via the window sale or noncompetitive bidding methods.

2. Issuance Methods by Issuer Type

Issuance methods in the Korean bond market may differ by the type of debt securities as well as the issuer of the debt securities. This section will focus on the different methods used in each case.

a. Government Securities

Government bonds, such as KTBs and MSBs, are issued via auction. There are two main types of auction: multiple price auction and uniform price auction.

i. Multiple Price Auction

In a multiple price auction, an issuer orders bids by price (yield) in descending (ascending) order and accepts the higher (lower) bids until the issue is exhausted. Each successful bidder pays the price they bid.

However, the auction tends to shift the demand curve down and to the left for a given quantity, for bidders bid more cautiously in the auction. Bidders who paid higher prices may face larger capital losses if the trading in these securities occurs below the price the bidder paid at the auction. This method was used before August 2000.

ii. Uniform Price Auction

In uniform price auctions, an issuer, just like in multiple price auction, orders bids in descending order and accepts those that allow full absorption of the amount up for issue. However, all winning bidders pay the price of the lowest successful bid in the uniform price auction.

iii. Differential Auction

A differentiated auction is a mixture of the two main methods. In this method, the accepted bid yield is determined by categorizing all bid yields into groups at intervals of 2 basis points in descending order, and by selecting the highest bid yield in each group (Figure 3.3).

iv. Noncompetitive Bidding

Noncompetitive bidding is classified into three categories; (i) noncompetitive bidding for general investors (e.g., individuals and corporations) who are not qualified to participate in competitive bidding; (ii) noncompetitive bidding which is given as an option to the KTB Primary Dealers participating in competitive bidding; and (iii) noncompetitive bidding of the STRIPS dealers who are required to perform the stripping (separating the coupon from the bond itself) of the KTBs.

Figure 3.3: Method of Determining Successful Bidding Yield

- The highest cut-off yield : 5.055% of primary dealer G
- Grouping : (5.055~5.040%), (5.035~5.020%), (5.015%~5.000%)
- Cut-off yields

<table>
<tr><th rowspan="2">PD</th><th rowspan="2">Bid yield</th><th colspan="3">Cut-off yield</th></tr>
<tr><th>Differential Pricing Auction Method</th><th>Dutch</th><th>Conventional</th></tr>
<tr><td>A</td><td>5.005%</td><td rowspan="2">A,B : 5.015%</td><td rowspan="7">All 5.055%</td><td>A : 5.005%</td></tr>
<tr><td>B</td><td>5.010%</td><td>B : 5.010%</td></tr>
<tr><td>C</td><td>5.025%</td><td rowspan="2">C,D : 5.035%</td><td>C : 5.025%</td></tr>
<tr><td>D</td><td>5.030%</td><td>D : 5.030%</td></tr>
<tr><td>E</td><td>5.040%</td><td rowspan="3">E,F,G : 5.055%</td><td>E : 5.040%</td></tr>
<tr><td>F</td><td>5.050%</td><td>F : 5.050%</td></tr>
<tr><td>G</td><td>5.055%</td><td>G : 5.055%</td></tr>
</table>

Source: Ministry of Strategy and Finance. https://ktb.mosf.go.kr/eng/

Before August 2000, KTB issuance was conducted by multi-price auction. Since then, the single-price auction has been used for the issuance of KTBs. Non-financial special purpose bonds also tend to be issued in this manner. The differentiated auction method was introduced in September 2009 to fix the problems inherent to the multi-price auction method, as well as those using single-price auction.

b. Corporate Bonds and Notes

For corporate bond issuances in the Republic of Korea, financial institutions, such as financial investment companies and KDB, play key roles as managing companies. A managing company carries out the administrative process for issuance and pricing the new issue. In addition, the company assigns parts of the new issue to the other underwriters.

i. Underwriting

Most corporate bonds are issued by firm commitment in the Republic of Korea, which means that the issuance of a corporate bond is mostly made through an indirect issuance method where the managing company also bears the issuing risk. In firm commitment underwriting, the managing company or underwriter guarantees to purchase all the securities being offered for sale by the issuer, regardless of whether they can sell them to investors.

In best-effort underwriting, however, the managing company or underwriter will do their best to sell all the securities that are being offered by the issuer. Nevertheless, there is no obligation for the managing company or underwriter to purchase the securities for their own account. Any bonds in a best-effort underwriting that have not been sold will be returned to the issuer.

The stand-by underwriting method is the mixture of the two methods. The managing company that enters into a stand-by underwriting agreement will purchase any securities that are not sold to the public. The stand-by underwriter will then resell the securities to the public.

The issuance of financial corporate bonds tends to be dependent on the use of shelf-registration. Large financial institutions using shelf-registration, such as commercial banks, tend to formally issue their bonds through the firm commitment underwriting of a lead managing company. However, the firm commitment by the lead managing company is made after bids from other managing companies and securities firms for their own or on behalf of institutional investors have been received.

At the same time, financial corporate bonds by smaller-sized financial institutions, with smaller issuance amounts and lower issuance frequency tend to be issued through individual underwriting contracts with a small number of managing companies.

ii. Book-building

Book-building is an integral part of the offer or sale of debt securities in the Korean market. KOFIA has stipulated rules for mandatory book-building in offers for all its constituents.

Conducting a book-building process is mandatory when offering non-guaranteed corporate bonds to the public. The lead managing company is required to perform such book-building process in order to determine at which price or yield an IPO is to be offered. This process is included as an obligation under the lead managing company's contract with the issuer. The lead managing company is also mandated to record details regarding its pricing decisions based on the outcome of the book-building process; these details are to be included in the securities registration process.

iii. Direct Sale

Special purpose bonds are usually issued to institutional investors by way of auction. At the same time, these bonds are also issued to general investors who want to invest for savings purposes. In that case, the bonds are sold directly to the investors at the counters of issuers who are mostly special purpose banks, and issuance terms such as maturity and coupon rate are predetermined. However, this type of issuance is very small in comparison to other issuance methods and, hence, has little significance in the overall issuance volume.

3. Issuance Methods by Disclosure Type

The major issuance methods for debt securities in the Korean bond market also differ in the type and amount of disclosure that the issuer is required to provide, whether to the regulatory authorities, an indenture trustee, a listing place, or directly to investors. The most common methods distinguished by disclosure are public offers and private placements. In addition, issuers or intermediaries may decide to issue debt securities via a window sale (e.g., a bank counter) or directly to investors.

a. Public Offer

In practice, issuers with large issuance volumes, such as financial institutions, tend to use a universal shelf-registration statement, which states the total amount of securities to be publicly offered en bloc over a certain period. If the statement is accepted by the FSC, such securities may be publicly offered or sold without submitting a securities registration statement each time the securities are publicly offered or sold during the period. Please also see Chapter II.F for a complete description of the regulatory process for issuance of debt securities via public offering.

b. Private Placement

Issuance via private placement is assumed to be deficient of information on the bond and the issuer compared to publicly offered issues. For that reason, privately placed issues have a 1-year resale restriction from the date of issuance. The restriction tends to make it difficult for SMEs to issue corporate bonds in the Republic of Korea. Thus, institutional improvements were made to promote issuance of corporate bonds by SMEs.

F. Governing Law and Jurisdiction (Bond and Note Issuance)

Governing law and the jurisdiction for specific service provisions in relation to a bond or note issuance may have relevance since potential issuers may consider issuing under the laws or jurisdiction of a market other than the place of issuance. The choice of governing law or the contractual preferences of stakeholders can affect the accessibility to a specific investor universe that may otherwise not be accessible if a bond or note were issued under the laws of the place of issuance.

The provisions for the use of governing law for the issuance of debt securities in the Korean market depend on the nature of the offerings, as described below.

In any case, the actual use of governing laws or jurisdictions other than those of the Republic of Korea may be subject to clarification or legal advice from a qualified law firm, as may be necessary.

1. Public Offers

When issuing a bond or note to the public in the Republic of Korea, the choice of governing law and jurisdiction is limited to the laws of the Republic of Korea and Korean courts, respectively.

2. Offers Registered on the QIB Market

The governing law and jurisdiction, with respect to the terms and conditions of the bonds or notes, may be agreed among the contracting parties, subject to relevant provisions in applicable laws and regulations.

Provisions for QIB Market-eligible debt securities to be registered with KOFIA may be determined with elements of intraregional bond markets or practices, as well as general international capital market agreements.

The provisions for and registration on the QIB Market are based on the applicable regulations for the Korean capital market, such as the Regulations on Issuance, Public Disclosure, etc. of Securities and the Enforcement Rules and Decrees of the FSCMA.

3. Arirang Bonds Issued by Nonresidents

An Arirang bond is a KRW-denominated bond issued by a foreign entity in the Republic of Korea. Similar to domestic issuers, the issuance of Arirang bonds by nonresident issuers is also governed by Korean law since they are considered domestic bonds.

For instance, in the case of nonresident-issued Arirang bonds, the considerations for investor protection in the domestic Korean market as the place of issuance and sale dictate Korean law as the governing law, and jurisdiction rests with Korean courts. From this point of view, for bonds and notes settled in the Republic of Korea (Korean domestic bonds), KSD requires that the terms and conditions of the notes shall be governed by Korean law.

G. Language of Documentation and Disclosure Items

The language of documentation for bond and note issuance, as well as the related initial and continuous disclosure items, is a significant factor of consideration for issuers.

English is the preferred language for most issuers, simply because it allows the issuers to reuse documentation already issued in international markets. However, each domestic bond market in ASEAN+3 may require the submission of approval-related information in their prescribed format and in the local language, particularly in the case of offers to the public or retail investors.

1. Public Offers

If bonds or notes are intended to be offered to the public in the Republic of Korea, issuers or their agents are required to produce the relevant documentation and disclosure items in Korean.

At the same time, the possibility exists for the issuer or their agents to produce documentation in English, for example, in the form of a summary of the disclosure information, such as the short-form investment prospectus. English documentation and disclosure items may also be submitted via the Data Analysis, Retrieval, and Transfer System, or DART, the filing system for SRS for public offerings of bonds and notes. Users can enquire on English documents in the system, as they are marked as such.

2. Private Placements

In the case of a private placement of bonds or notes in the Republic of Korea, issuers or their agents may provide documentation in Korean or English, or a combination of both languages. The key driver for the language of documentation is likely to be the targeted investor universe for the private placement.

3. Bonds Registered on the Qualified Institutional Buyer Market

KOFIA launched the QIB Market debt securities registration and disclosure platform on 1 August 2016. Documentation and disclosure items in English are now accepted by KOFIA. For foreign issuers, the submission of documentation and disclosure information in English became available for the first time in the Republic of Korea.

4. Bonds Listed on Korea Exchange

When a Korean corporation makes continuous disclosure for listed bonds to KRX, it is required to disclose such information in Korean and, if necessary, may disclose the same in English within 1 week. A foreign corporation is required to make timely disclosure in Korean as well. However, if inevitable (e.g., in a case where KRX deems that the issuer cannot make disclosure in Korean in a timely manner), the issuer is required to disclose in English first and then in Korean without delay (i.e., as soon as possible).

H. Registration of Debt Securities

A registration of securities in a given market is typically carried out with the objective of introducing newly issued securities to the market, achieving issuance approval, facilitating information disclosure, or establishing proof of ownership. This section explains the registration concepts evident in the Korean bond market.

The term registration for debt securities in the Korean market is used in two forms, each having a particular purpose in the context of the bond market or securities market at large. Debt securities must be registered with KSD to be eligible for settlement in the Korean market and to be able to track ownership. On the other hand, specific QIB-Market eligible debt securities may be registered with KOFIA to be traded in the OTC market, and to fulfill the intended market information and disclosure obligations of the issuers.

The term registration is not used for debt securities traded on KRX since the listing process fulfills the underlying requirements for disclosure and market transparency.

The term registration is also used in the context of an issuance application to the FSC for debt securities to be offered to the public, via a securities registration statement. This registration and approval process is described in great detail in Chapter II.F.

1. Registration of Debt Securities at Korea Securities Depository

Debt securities issued in the Korean market must be registered at KSD to be eligible for settlement in the bond market, regardless whether such debt securities are to be traded in the OTC market or on the exchange.

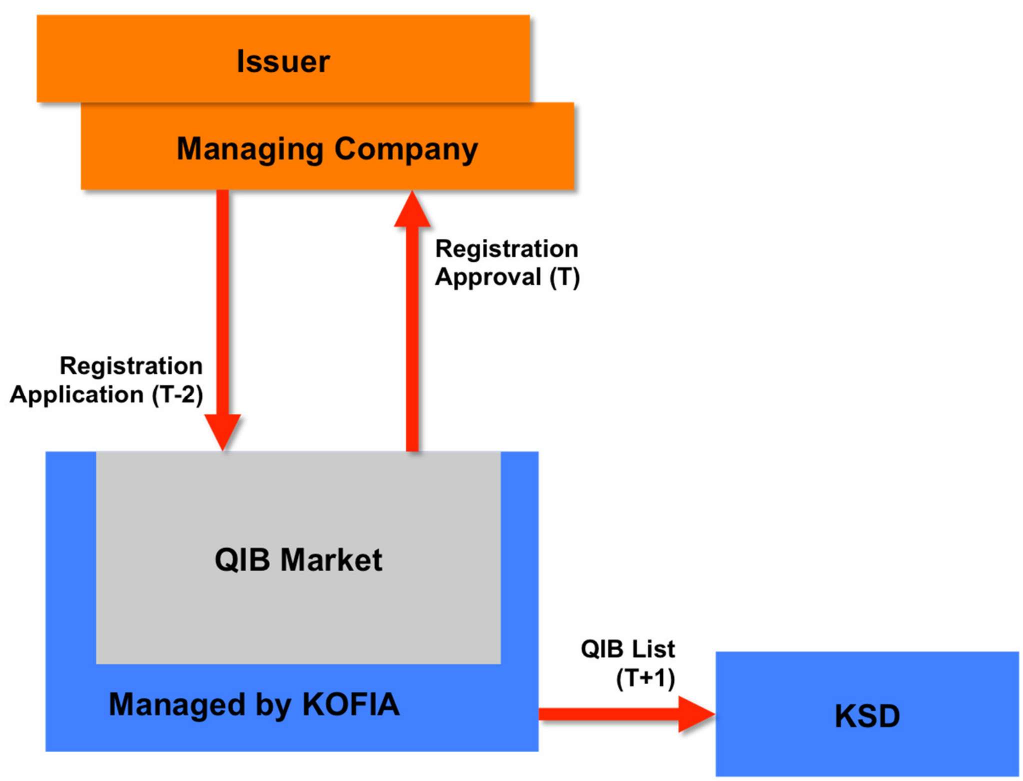
The registration is required since KSD creates and maintains the book-entry records of holdings and ownership of the debt securities—in fact, all securities—in the accounts of its participants and their underlying clients. Transactions in the participant accounts of KSD's book-entry system enjoy settlement finality and constitute the legal ownership records of the investors (see also section L in this chapter).

KSD also sets systematic restrictions to ensure QIB securities are traded only among QIBs registered with KOFIA (see also next section). To be able to ensure compliance, KOFIA sends a list of QIBs and their KSD account numbers to KSD on a daily basis.

2. Registration of Debt Securities in the QIB Market

KOFIA, as the administrator of the QIB Market, is responsible for the registration and management of QIB securities, as well as the actual investment participants of the market, the QIBs (see Chapter III.N.2 for more information on QIBs). The QIB Market is the bond market segment for professional investors and represents a subset of the OTC market in the Republic of Korea. At present, QIB securities are not able to list on KRX.

Figure 3.4: QIB Securities Registration Process



KOFIA = Korea Financial Investment Association, KSD = Korea Securities Depository, QIB = Qualified Institutional Buyer, T = trade date.
Source: Korea Financial Investment Association.

Debt securities intended to be traded among QIBs must be registered with KOFIA, subject to the provisions for QIB-eligible securities. The same debt securities must also be registered with KSD to be eligible for settlement (see previous section).

KOFIA requires the issuer or the appointed managing company to submit a registration form, together with the relevant supporting documents. The registration may be done electronically, via KOFIA's online registration platform. As a separate step, KOFIA provides a list of QIBs to KSD to ensure that trades in QIB securities may only be settled among QIB accounts (Figure 3.4).

If an issuer registers an issuance limit for QIB securities (based on the unredeemed balance) with KOFIA in advance, issuance will be allowed at any time with streamlined documentation. The approach is similar to issuance under an MTN program or a note issuance program.

I. Listing of Debt Securities

If an issuer wishes to list its debt securities in the Korean market, a listing is available on KRX. The listing process is divided into two distinct parts: (i) the review of listing eligibility of both the issuer and the debt securities to be issued, and (ii) the actual listing application and approval. The listing process on KRX is subject to the KRX Listing Rules (official name: KOSPI Market Listing Regulation).

Listing is not mandatory for debt securities in the Korean market, including in the case of a public offer, but debt securities must be listed on KRX to be tradeable on the exchange markets. In 2017, 92% of publicly offered bonds were listed on KRX. A listing application should be made only once the SRS has been accepted by the FSC.

Nonresident issuers may also list their debt securities on KRX, but will have to fulfil additional requirements compared to the bond listing requirements for a Korean domestic issuer. As per domestic issuance requirements for KRW-denominated bonds and notes, a foreign bond issuer should also submit an SRS to the FSC.[16] However, the nonresident issuer will need to obtain the prior consent of MOSF. And after its issuance, the foreign issuer should submit a securities issuance report, which contains details of the foreign bonds, issuance cost, and the amounts acquired by each of the appointed underwriters. Bonds issued by a foreign corporation in the Korean bond market are typically referred to as Arirang bonds.

1. Regulatory Process for Listing of Corporate Bonds and Notes

Bonds and notes listed on KRX can be traded in the KRX bond market, which has four segments: (i) KRX KTB, which is an interdealer market specializing in KTB trading; (ii) KRX BondsAll, which is an open market for all market participants including individual investors; (iii) KRX Repo, and (iv) KRX LPB, which is a License and Permit Bond market for individual investors. For detailed explanations of these market segments, please refer to Chapter IV.

The listing of debt securities on KRX is subject to the provisions of Part III in the KRX Listing Rules and a prior assessment based on eligibility criteria.[17]

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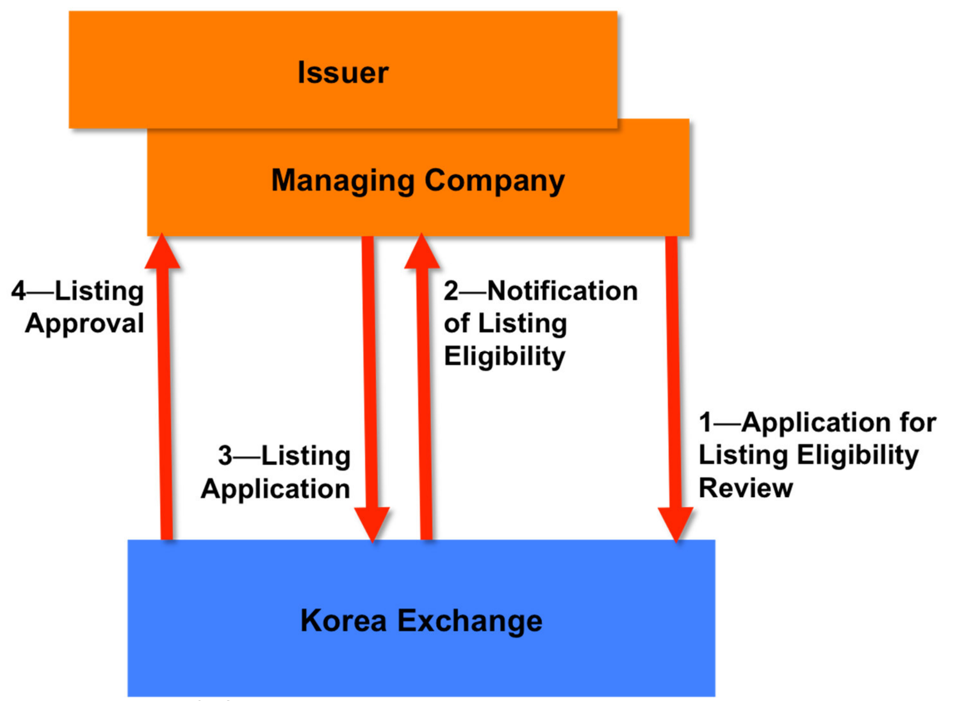
[16] KRX limits foreign corporations eligible for listing their bonds to international financial organizations, foreign governments, corporations that have listed stocks on foreign exchanges, and corporations that have listed foreign stocks on KRX.
[17] Korea Exchange. KOSPI Market Listing Regulation. http://global.krx.co.kr

To be eligible for an initial listing of non-guaranteed debt securities on the KRX bond market, the following requirements should be satisfied: (i) the issuer's equity should be more than KRW500 million, (ii) the bonds should be issued through a public offering, and (iii) the face value of the bonds or notes should be higher than KRW3 million.

For an initial listing of debt securities by foreign issuers, there are additional requirements: (i) the firm's equity should be more than KRW10 billion; (ii) the bonds should be registered with KSD; (iii) the face value of the bonds or notes should be higher than KRW10 billion; (iv) the issuer should have its stock listed on a foreign or Korean exchange, or should have issued its stock through a public offering; and (v) the bonds should carry an investment grade rating (BBB or above).

Figure 3.5: Debt Securities Listing Process on Korea Exchange



Source: ADB consultants for SF1.

Figure 3.5 displays an overview of the individual steps to be taken by issuers. These steps are further detailed in the subsequent text.

A nonresident issuer will need to file a proposed debt securities issuance schedule with MOSF before embarking on the listing process and before issuance.

Step 1—Listing Eligibility Review by Korea Exchange

KRX expects every prospective foreign issuer of to-be-listed debt securities to consult with KRX for a listing eligibility review as a first step. The issuer will be informed of the required listing documents and disclosure items by KRX (see specific eligibility criteria for foreign issuers in the earlier part of this section).

After consultation, the foreign issuer will submit the listing documents to KRX. KRX does not charge for the listing eligibility consultation for foreign issuers.

Step 2—Initial Listing Application to Korea Exchange

Equipped with a confirmation of listing eligibility, the issuer may file an application for initial listing. KRX expects the issuer to make use of its online bond listing system.[18] All listing proceedings are conducted via KRX's bond listing website.

There are no qualitative requirements for a bond listing. There are only quantitative requirements such as an issuer's minimum equity and a bond's minimum face value. KRX may also request additional information to aid it in the decision-making process. Supplementary documents may be submitted in physical form or by fax, or when the SRS is uploaded to the bond listing system.

The listing application procedure allows for a prospective issuer to designate a bond's listing date, except for on the day of the application submission itself.

Since most of the relevant information has already been submitted to KRX as part of the listing eligibility review, the listing application is straightforward and the review timeframe is short.

Step 3— Review of Application and Listing Approval

Provided that the initial listing application is complete and all necessary requirements set out in the KRX (KOSPI Market) Listing Rules have been complied with, KRX will be able to review the application and communicate the listing approval within 1 business day.

A listing approval email will be sent to the applicant, which at present is only available in Korean.[19] The listing approval information will also be sent to information vendors and can be found on the KRX website on the day of approval.

KRX charges a listing fee and annual dues. For details of listing-related fees, please refer to Chapter VI or the KRX website.[20]

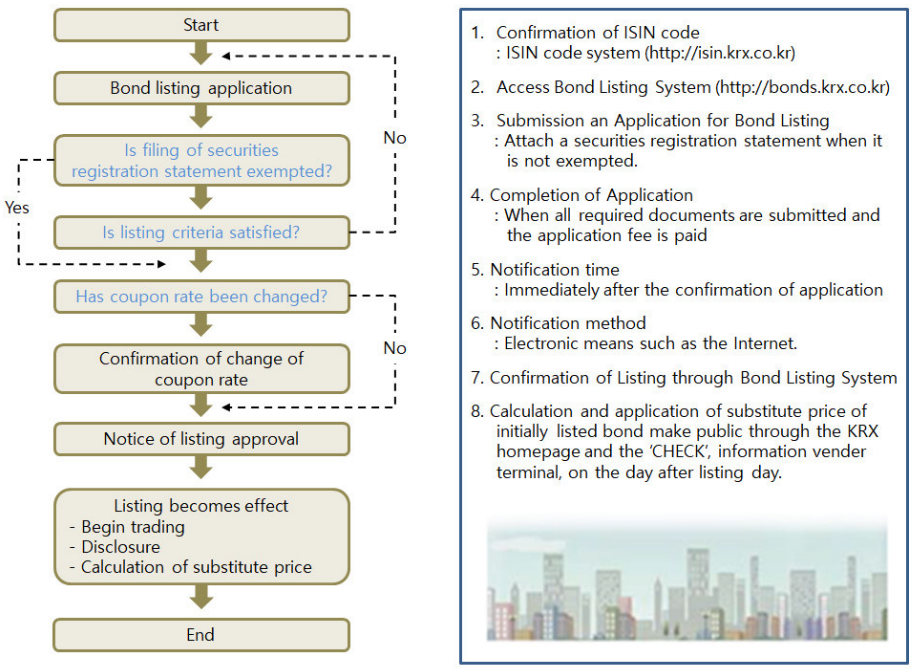
Step 4—Actual Listing and Trading

The actual listing is effective upon the listing date indicated in the approval from KRX and trading may commence on the day of listing, following an official announcement on the KRX website. There is no defined cooling-off period between listing approval and actual listing.

Some of the detailed information and steps to be completed in the bond listing system are shown in the schematic in Figure 3.6.

[18] See http://bonds.krx.co.kr/main/main.do
[19] See http://bonds.krx.co.kr/main/main.do
[20] See https://global.krx.co.kr/contents/GLB/03/0305/0305010000/GLB0305010000.jsp

Figure 3.6: Bond Listing System



ISIN = International Securities Identification Number, KRX = Korea Exchange.
Source: KRX.

2. Other Listing Activities on Korea Exchange

In addition to the listing of debt securities described above, there are also other types of listing activities on KRX.

a. Shelf-Listing of Debt Securities

NHBs and some municipal bonds (e.g., provincial development bonds and metropolitan city subway bonds) are shelf-listed. Shelf-listing is applied to the listing of government bonds, municipal bonds, and special bonds that were issued on a certain day of each month and then distributed throughout the year. The issuance schedule of these types of bonds for the following year will be determined at the end of each year. The listing of NHBs and shelf-listed municipal bonds is handled by KRX. On the first day of each month, KRX lists NHBs and shelf-listing municipal bonds, and adjusts listing amounts every day upon receiving the notices of issuance amounts. The documents required for a shelf-listing are an application for a shelf-listing, a confirmed issuance schedule, and a report on the result of the issuance. The listing application and attached documents for shelf-listing can be submitted online, via the KRX bond listing system.

b. Re-Listing

A bond or note de-listed for a valid reason may be re-listed on the KRX bond market. To be re-listed, the face value of such bonds or notes should be more than KRW300 million and a bond or note and its issuer should no longer satisfy the de-listing conditions at the time of applying for a re-listing. The issuer should submit an application for re-listing, an approved recent audit report, and documents proving that the de-listing conditions no longer exist.

c. Supplementary Listing

If an issuer of a listed bond or note intends to issue bonds or notes of the same class as the bond or note already listed, the issuer should submit to KRX an application for supplementary listing and attach relevant documents in a bid to increase the amounts of the bonds and notes already listed. All bond issuance terms will remain unchanged except the listed face amount.

d. Listing Change

If an issuer of listed debt securities decides to change its name, the issuer should submit to KRX an application for a listing change and attach relevant documents to substantiate the change of its name and the designation of its bonds or notes.

e. De-Listing

KRX may de-list a bond or note that may no longer be eligible for listing on the KRX bond market in cases such as (i) where an issuer's equity falls below KRW500 million; (ii) where, in the most recent annual report, the auditor's audit opinion comes under any of the Disclaimer, Adverse, or Qualified categories, depending on the limitations on the scope of audit; (iii) bankruptcy of the issuer; and (iv) a court has made a decision to turn down the application for commencement of rehabilitation procedure of the issuer.

3. Listing of Government Bonds

Government bonds are listed upon receipt of the listing application without a listing examination. Of the government bonds issued presently, Treasury bonds and foreign exchange stabilization bonds are listed on the issuing day according to the regulations governing the shelf-listing of bonds; NHB Types 1 and 2 are listed on the first day of each month.

The listing of Treasury bonds and foreign exchange stabilization bonds is facilitated by BOK, as the issuing agent, over the Internet. The listing of NHB Types 1 and 2 is based on the application for shelf-listing for bonds scheduled to be issued during the following year at the end of each year. KRX lists the scheduled quantity on the first day of each month and adjusts the listing value upon receiving the notices of issuance value following confirmation of such bond issuance for the current month.

4. Listing of Municipal Bonds

Similar to government bonds, municipal bonds are listed without listing examination, taking into account their public benefits. The listing of shelf-listed municipal bonds (i.e., provincial development bonds and local subway bonds) is handled by KRX in the same manner as described for NHBs above and the listing of bonds issued through a public offering is handled in the same manner as the listing of corporate bonds.

The documents required for a listing application for provincial development bonds and subway bonds are an application for a shelf-listing and a report on the result of the issuance. The documents required for a listing of municipal bonds issued through a public offering include an application for listing, a trust deed, the underwriting agreement or sales contract, and a copy of an agreement on the offering on commitment, in cases where the bonds are issued through an indirect offering. As for corporate bonds, the listing application for municipal bonds can be submitted online via the KRX bond listing website.

5. Listing of Debt Issuance Programs

The listing of debt issuance programs follows a process similar to the one described for shelf-listing above.

J. Methods of Trading Bonds and Notes (Secondary Market)

Bonds and notes issued in the Korean bond market may be traded OTC or on the exchange. Similar to other bond markets, the OTC market represents the dominant volume of bond and note trading. However, in the Republic of Korea, bond trading on the KRX has maintained a significant portion of overall trading, accounting for 40% of the overall trading volume in 2016 (please also see Chapters I and IV for details).

The individual methods are briefly described in the sections below and are further detailed in the applicable sections of Chapter IV. All debt securities traded in the Korean bond market are settled through KSD.

1. Trading in the Over-the-Counter Market

The OTC market is administered by KOFIA and populated by institutional investors only. The OTC market is, in effect, divided in the normal OTC market and the QIB Market, which only trades QIB Market-eligible securities (see also Chapter II.F).

Participants in the OTC market trade using the K-Bond trading platform and other trading tools. Almost all OTC trading in the Korean bond market is conducted on K-Bond, where trading is made by negotiation among the market participants.

The bonds traded on K-Bond are mostly publicly offered bonds and notes listed on the exchange, such as government bonds, special bonds, and large-issue sized corporate bonds.

QIB Market participants must be QIBs themselves and register as such with KOFIA to be able to be traded on the QIB Market.

2. Trading on Korea Exchange

Investors can also trade bonds on KRX, in one of its four market segments. Bonds traded on KRX should meet certain requirements for listing that KRX imposes; key among them is the requirement to have been issued via a public offering.

Bond trading is carried out through the electronic trading system in the KRX bond market. The electronic trading system collects all quotations and displays them on trading screens in real time; trades are executed electronically. The KRX bond market offers straight-through processing from quotation searching to trade execution to downstream functions like clearing and settlement. KRX also acts as central counterparty for each trade.

The actual trading of debt securities on KRX occurs on KRK KTB and KRX BondsAll. KRX KTB is not limited to exchange members and is populated by institutional participants, such as banks and investment companies, and includes the Primary Dealers. KRX BondsAll caters to ordinary investors who must use exchange members (i.e., brokerage companies) to trade debt securities. KRX BondsAll transactions are traded in smaller denominations, in line with the investor profile.

The bond market segments on KRX are further explained in Chapter IV.

K. Bond and Note Pricing

Following the 1997/98 Asian financial crisis, the Government of the Republic of Korea introduced MTM valuation in November 1998 to improve transparency in trust asset management, secure investor confidence, and enhance the asset quality of financial institutions.

1. Bond Pricing Agencies

The Korean market features a number of dedicated bond pricing agencies, in addition to KOFIA and KRX, who provide bond pricing information for instruments and transactions on their respective platforms. KIS Pricing, KBP, and NICE Pricing Service provide pricing services on the back of their original function as credit rating agencies (Table 3.2). In April 2012, Fn Pricing began to provide MTM base yields as well.

Table 3.2: Bond Pricing Agencies in the Republic of Korea

Name	KAP	KIS Pricing	NICE P&I	Fn Pricing
Capital	KRW5.3 billion	KRW3.0 billion	KRW3.0 billion	KRW5.0 billion
Largest Shareholder	TWOSUN PEF1	KIS	NICE	Fn Guide

KRW = Korean won.
Note: Company names are reflected as used in the market.
Source: ADB consultants for SF1.

2. Korea Financial Investment Association

KOFIA does not serve as a bond pricing agency itself, but monitors the relevance and accuracy of the prices calculated by the bond pricing agencies. In addition, KOFIA announces a daily MTM benchmark yield table that provides the standard for the appraised prices calculated by the bond pricing agencies for each type, maturity, and day.

KOFIA calculates such MTM prices for each type of bond based on two or more bond yields provided by the three domestic bond-rating companies—KIS Pricing, KBP, and NICE Pricing Service—who also provide pricing services (see also Chapter IV.G).

Furthermore, KOFIA monitors the validity of the valuation price provided by each bond rating company, as per the Regulations on Business Conduct and Services of Financial Investment Companies. The results are reported to each company and the FSS and posted on KOFIA's Bond Information Service website every quarter.[21]

3. Korea Exchange

KRX provides information on average yields and prices of bonds rated by the three major bond credit rating agencies to help bond investors make decisions. Information on all bonds listed on the KRX market is provided and, particularly, conversion prices and current prices of the underlying equity for equity-related bonds. KRX also discloses credit ratings, credit rating methodologies, and substitution prices of bonds,

[21] See www.kofiabond.or.kr

among other information. For more details on the bond-related information provided by KRX, please see Chapter IV.

KRX also features market-maker programs to help determine interest rates in the secondary market. On KRX KTB, 17 Primary Dealers and 4 pre-Primary Dealers are engaged in the market-maker program for 6 on-the-run KTB issues and over 40 off-the-run KTB issues. On KRX BondsAll, 24 market makers are engaged in market-making for over 15 listed bonds daily, regardless of the type of bond.

L. Transfers of Interests in Bonds and Notes

All debt securities to be settled in the Korean bond market will have to be registered at KSD (see also section H in this chapter), regardless whether the debt securities are intended to be traded OTC or on the exchange. Since the Korean market is immobilized, any physical certificates will need to be deposited into KSD to be eligible for settlement.

In its book-entry system, KSD keeps the electronic records of ownership of the bonds and notes deposited according to the account names maintained by its participants on behalf of the underlying investors. Foreign investors must keep securities accounts with their custodian and corresponding accounts at KSD in a name that matches their IRC (see also Chapter II.M).

1. Settlement of Transactions and Finality

The settlement of a transaction results in the transfer of (debt) securities in the KSD book-entry system from the account of the KSD participant acting for the seller to the account of the KSD participants acting for the buyer, with a corresponding transfer of the resulting cash amount in reverse for a delivery-versus-payment transaction. KSD guarantees the finality of the settlement once the corresponding account entries have been effected.

Settlement from trades originating from the exchange bond market are seamlessly transmitted to KSD by KRX, while OTC trades require the separate capture of settlement instructions into the KSD system by the settlement agents for the trade counterparties.

2. Other Transfers

Transfers between participant accounts at KSD, and corresponding changes in the interests in or beneficial ownership of debt securities, may also occur as a result of other transaction types, such as repo, securities borrowing and lending, or margin transactions. Details on repo and securities lending transactions are explained in Chapter IV.

Other transfers may include a transfer of ownership between related parties, if not so prohibited (see next section), or as the result of a gift, bequest, or inheritance.

3. Transfer Restrictions

Restrictions on the book-entry transfer of securities are listed in Article 24 of KSD's Regulation on Deposit Service for Securities. These include securities yet to be available for transfer, those due for redemption, or those pledged by the account holder for other purposes.

M. Market Participants

Bond market participants in the Republic of Korea consist of a number of significant types of issuers and investors. Bond market investors are typically institutional investors, whether domestic or from overseas.

In addition, the market features a number of market institutions and infrastructure for the issuance, trading, and settlement of bonds.

1. Issuers

Issuers in the Korean bond market are legal entities that can issue bonds and notes, as prescribed in Article 4 (3) of the FSCMA. These entities include the Government of the Republic of Korea, local governments, financial or nonfinancial government agencies, and financial or nonfinancial business corporations.

2. Guarantor

Guarantors for bonds are responsible for the payment of interest and principal. Before the 1997/98 Asian financial crisis, the role of guarantors was important because a substantial part of new issues consisted of corporate bonds guaranteed by financial institutions.

The role of guarantors is still important in the case of ABS, especially in cases where underlying assets are financial instruments issued by SMEs. Guarantors active in the Korean market include the Korea Credit Guarantee Fund, the Korea Technology Credit Fund and commercial banks, as well as financial investment companies. The ability to conduct guarantee business is subject to authorization by the relevant regulator; a financial investment company must be authorized by the FSS.

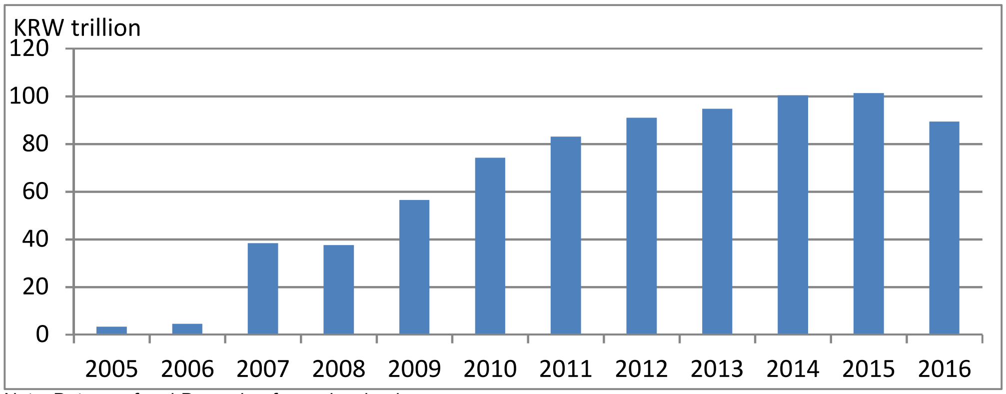
3. Investors

Investors can be categorized into ordinary investors and professional investors. A professional investor means any entity that has an ability to take risks accompanying an investment in light of the expertise held in connection with financial investment instruments and the scale of assets owned. In contrast, ordinary investor means any investor other than a professional investor.

Foreign investors are also an important part of the Korean bond market. Despite some procedural conditions for investment such as the foreign investor registration with the FSS, there is no fundamental distinction between domestic investors and nonresident investors in terms of regulative aspects.

Until the mid-2000s, investment in bonds by foreign investors was not significant. Since then, investment in the bond market has increased rapidly, amounting to KRW101 trillion as of December 2015, which accounted for around 6% of total bonds outstanding at the time (Figure 3.7).

Figure 3.7: Bond Market Investment by Foreign Investors



Note: Data as of end-December for each calendar year.
KRW = Korean won.
Source: Financial Supervisory Service.

4. Parties Involved in Debt Securities Issuance

A number of intermediaries provide services to issuers and investors in the context of the issuance of debt securities in the Korean bond market. The following text provides a brief description of the type of intermediaries and their specific functions.

a. Primary Dealers

The Primary Dealer concept in the Republic of Korea was introduced in 1999 to promote the market for KTBs. Primary Dealers enjoy privileges in the primary market, including exclusive underwriting rights for government bonds and a standing borrowing arrangement. At the same time, Primary Dealers are obliged to fulfill specified duties in the secondary market. At the beginning of October 2016, there were 19 Primary Dealers—10 securities companies and 9 banks.

b. Managing Company

A managing company in the Korean bond market is a financial entity that makes a decision on the terms and conditions of underwriting securities to be publicly offered or sold at the request of the issuer or seller of the securities. The managing company manages all business affairs related to the public offering or sale, including the underwriting of the securities. In cases when there is more than one managing company for a public offering or sale, the issuer or the seller of the securities can appoint a so-called representative managing company. A managing company must be authorized to conduct such business by the FSC, pursuant to provisions prescribed in the FSCMA. The managing company inhabits the role and functions that are typically carried out by an arranger in other markets.

In the past, managing companies (underwriting managers) played a rather minor role in the corporate bond primary market in the Republic of Korea, acting as evaluators of corporate value and risks during the underwriting process. As securities companies focused more on price competition to secure sufficient quantities of bonds rather than the risk assessment or pricing, their capabilities as investment banks were not sufficiently utilized. Moreover, the expansion of the demand base for corporate bonds was impeded as investors gradually lost confidence in the data and prices calculated at the time of bond issuance.

The FSC addressed this problem as part of the Plan to Improve the Primary Market for Corporate Bonds to Promote Investment Banks, announced on 17 October 2011. This plan aimed to strengthen the responsibilities and underwriting capacity of securities companies, and promote the development of the primary market for corporate bonds. The measures mainly focused on two areas: systematic due diligence and mandatory book building. To streamline the due diligence process, the KOFIA Regulations on Securities Underwriting Business were revised at the time.

c. Underwriter(s)

Underwriter refers to an entity that underwrites and bears issuing risk of securities in cases of a public offering, private placement, or public sale of the securities. Underwriters in the Republic of Korea are financial institutions with authorization from the FSC, including some financial investment firms, which are meeting the required business conditions, and KDB. The underwriting business is authorized by the FSC, pursuant to the provisions prescribed in the FSCMA.

d. Paying Agent

For bonds and notes to be issued in the Republic of Korea, an issuer may conclude a paying agency agreement with a designated bank, which will remit funds due from the issuer to KSD for distribution to its participants.

KSD performs the exercise of rights on deposited securities according to Article 314 at the request of its participants (included in the service agreement when opening an account at KSD), and processes the payment of principal and interest through the check clearing system and distributes to its participants.

e. Indenture Trustee

An indenture trustee is a legal entity for investor protection. If appointed, an indenture trustee is entrusted with the administrative affairs for bondholders, such as collecting redemption, preserving bonds, and other administration of bonds. Under Article 26 in the Enforcement Decree of the Commercial Act, institutions eligible as an indenture trustee include commercial banks, special purpose banks, KSD, and the Korea Securities Finance Corporation. Each institution must be authorized by its relevant regulator.

f. Authorized Institution(s) as Depository Participants

Participants are legal entities who open accounts and deposit their securities at KSD for deposit, withdrawal, and transfer of their securities. Those eligible to be participants are securities companies, banks, insurance companies, futures companies, institutional investors, foreign depositories, and other entities deemed appropriate by KSD.

g. Legal Advisers (Legal Counsel)

An attorney-at-law, patent attorney, or tax accountant is able to provide the relevant legal advice to an issuer of debt securities or other market participants in the bond market. The legal adviser should have officially recognized qualifications. Attorneys are licensed by the Ministry of Justice. In addition, they also are required to be registered with the Korean Bar Association.

h. Public Accountants and Auditors

No false statement or representation of a material fact should be made in the documents that are related to the issuance of bonds and notes. These documents may include an SRS, supplements to a universal shelf-registration statement, an investment prospectus, and a business report, among others.

Public accountants and auditors involved in the preparation and review of these documents should be certified persons or entities who are governed by their respective professional bodies. They are authorized by the FSC.

N. Definition of Professional Investors and Related Classification

Among ASEAN+3 markets, the Republic of Korea features one of the most comprehensive definitions of professional investors and its constituent investor types. These definitions are anchored in key legislation and further augmented in FSC regulations. Some market segments are using specific professional investor definitions, such as QIB, while the KRX bond market so far does not make use of such specific definitions.

Investors who are eligible as professional investors may opt out of being considered professional, and can continue as ordinary investors upon a written notification to the financial intermediary with or through which the investors have previously accessed the securities market.

1. General Definition in the Financial Investment Services and Capital Markets Act and Its Enforcement Decree

Article 9 of the FSCMA contains the general definition of professional investor (Section 5) and also defines ordinary investors (Section 6) in the following manner (excerpt below):

(5) The term "professional investor" in this Act means an investor who has an ability to take risks accompanying the investment in light of the expertise that it possesses in connection with financial investment instruments, the scale of assets owned by it, […] and who falls under any of the following subparagraphs: Provided, That a financial investment business entity shall give consent to a professional investor prescribed by Presidential Decree when the investor notifies the financial investment business entity in writing of its willingness to be treated as an ordinary investor, unless there is a justifiable ground otherwise, and such investor shall be treated as an ordinary investor when the financial investment business entity gives such consent:
1. The State;
2. The Bank of Korea;
3. Financial institutions specified by Presidential Decree;
4. Stock-listed corporations: Provided, that trading over-the-counter derivatives with a financial investment business entity shall be limited to cases where an investor notifies the financial investment business entity in writing of its willingness to be treated as a professional investor;
5. Other persons specified by Presidential Decree;

(6) The term "ordinary investor" in this Act means any investor other than professional investors.

Furthermore, Article 10 (Scope of Professional Investors) of the Enforcement Decree of the FSCMA (Presidential Decree No. 24317, 16 January 2013) stipulates the following (excerpt below):

(1) The term “professional investor specified by Presidential Decree” in the proviso to the main body of Article 9 (5) of the Act means a professional investor not falling under any of the following subparagraphs:
1. The State;
2. The Bank of Korea;
3. A person who falls under any provision of [Paragraph 2, 1–17];
4. A person who falls under any provision of [Paragraph 3, 1–11];

(2) The term “financial institutions specified by Presidential Decree” in Article 9 (5) 3 of the Act means any of the following financial institutions:
1. Financial institutions under the Banking Act;
2. The Korea Development Bank under the Korea Development Bank Act;
3. The Industrial Bank of Korea under the Industrial Bank of Korea Act;
4. The Export–Import Bank of Korea under the Export–Import Bank of Korea Act;
5. The National Agricultural Cooperative Federation under the Agricultural Cooperatives Act;
6. The National Federation of Fisheries Cooperatives under the Fisheries Cooperatives Act;
7. Insurance companies under the Insurance Business Act (hereinafter referred to as “insurance companies”);
8. Financial investment business entities [excluding concurrently-run financial investment business entities under Article 22 of the Act (hereinafter referred to as “concurrently-run financial investment business entities”)];
9. Securities finance companies with authorization under Article 324 (1) of the Act (hereinafter referred to as “securities finance companies”);
10. Merchant banks;
11. Financial brokerage companies with authorization under Article 355 (1) of the Act (hereinafter referred to as “financial brokerage companies”);
12. Financial holding companies under the Financial Holding Companies Act;
13. Specialized credit financial business entities under the Specialized Credit Financial Business Act;
14. Mutual savings banks under the Mutual Savings Banks Act and their Central Federation;
15. The Forestry Cooperatives Federation under the Forestry Cooperatives Act;
16. The Korean Federation of Community Credit Cooperatives under the Community Credit Cooperatives Act;
17. The National Credit Union Federation of Korea under the Credit Unions Act;

(3) The term “persons specified by Presidential Decree” in Article 9 (5) 5 of the Act means any of the following persons:
1. The Korea Deposit Insurance Corporation and reorganized financial institutions under the Depositor Protection Act;
2. The Korea Asset Management Corporation under the Act on the Efficient disposition of Non-Performing Assets, etc. of Financial Institutions and the Establishment of Korea Asset Management Corporation;

3. The Korea Housing Finance Corporation under the Korea Housing Finance Corporation Act;
4. The Korea Investment Corporation under the Korea Investment Corporation Act;
5. The Association;
6. The Korea Securities Depository established pursuant to Article 294 of the Act (hereinafter referred to as the “Securities Depository”);
7. The Korea Exchange established pursuant to Article 373 of the Act (hereinafter referred to as the “Exchange”);

8. The Financial Supervisory Service under the Act on the Establishment, etc. of Financial Services Commission (hereinafter referred to as the “Financial Supervisory Service”);
9. Collective investment schemes (excluding those specified and publicly notified by the Financial Services Commission);
10. The Korea Credit Guarantee Fund under the Credit Guarantee Fund Act;
11. The Korea Technology Credit Guarantee Fund under the Technology Credit Guarantee Fund Act;
12. Funds established pursuant to a relevant Act (excluding those under Subparagraphs 10 and 11) and the corporations that manage and operate any of such funds;
13. Corporations that manage any mutual aid business pursuant to a relevant Act.

2. Qualified Institutional Buyer

The QIB concept was introduced by the FSC in May 2012 to define a group of investor types that could make their own investment decisions while supporting the private placement market for SMEs.

QIBs are a subset of professional investors. Professional investors refer to investors who do not need any strong investor protection measures, given their own expertise and experience.

The definition of QIB is stipulated in Article 2-2, Paragraph 4 of the FSC Regulation on Securities Issuance and Disclosures and refers to an expert pursuant to Article 11, Paragraph 1, Items A and B of the Enforcement Decree of the FSCMA; a corporation or organization pursuant to Article 10, Paragraph 3, Subparagraph 16 of the Enforcement Decree of the FSCMA; an SME pursuant to the Small and Medium Enterprises Promotion Act; collective investment schemes established pursuant to Article 6, Paragraph 1, Subparagraphs 5–7 of the FSCMA; and corresponding foreign investors with equivalent credentials.

QIBs include institutional investors such as governments, BOK, pension funds, insurance companies, banks, securities companies, collective investment schemes, and corporations with at least KRW10 billion in capital, but exclude individuals. In addition, corresponding foreign institutions with equivalent credentials can participate in the OTC market as a QIB.

The scope of the QIB concept corresponds closely with the typical scope of professional investors applied to professional bond or note issuance concepts in other markets in the region, such as AMBIF (see also Chapters IX and X).

3. Use of Definition by Korea Exchange

KRX directly applies the concept of professional investors, as stipulated in Article 9 of the FSCMA (see also section 1), for market supervision and surveillance.

KRX is also working on the establishment of an electronic bond trading platform for professional investors only to stimulate and the Korean bond market and create opportunities for a further internationalization of the market.

O. Credit Rating Requirements

Before the 1997/98 Asian financial crisis, most of the corporate bonds issued in the Republic of Korea were guaranteed bonds, so there was little necessity for considering the credit of the corporations issuing new bonds. However, since the crisis, the corporate bond market has become dominated by non-guaranteed bonds, which were solely focused on the credibility of the issuing corporation to service interest payments and redeem the bond upon maturity, thus increasing the importance of credit ratings. Credit ratings are particularly important in the case of a public offering because such an issuance is offered to ordinary investors.

Credit ratings in the Korean market differ by instrument type, as explained further in this section.

1. Public Offers

Section 11 of the Regulations on Securities Underwriting Business issued by KOFIA provides for the credit rating requirements of non-guaranteed bonds.[22]

Chapter III of the regulation states that in the case of an underwriter underwriting non-guaranteed bonds, such bonds shall be rated by at least two credit rating agencies (CRAs) from among those approved for credit rating business pursuant to the provisions of the Act on Use and Protection of Credit Information. One CRA shall suffice in the case of underwriting ABS issued in the form of bonds pursuant to the Act on Asset-Backed Securitization, or in inevitable cases such as the business suspension of a CRA.

Non-guaranteed bonds issued by foreign corporations shall be deemed as rated in accordance with this provision if they are rated by two or more CRAs (referring to international credit rating agencies as prescribed by the Governor of the FSC in the Regulations on Securities Issuance and Disclosure).

2. Corporate Bond Credit Ratings

When a company issues corporate bonds, it is required to obtain a credit rating from a specialized CRA for all non-guaranteed bonds. This is done to ensure fair pricing of bonds based on the creditworthiness of the issuers. Additionally, investors will have access to an independent evaluation and assessment of bonds, which in turn enables them to make informed investment decisions.

There are 10 different credit rating grades for bonds, ranging from AAA to D, depending on how certain the ability of an issuer to pay principal and interest is judged (Table 3.3). Grades ranging from AAA to BBB indicate that principal and interest are deemed to be recoverable, while bonds falling under the BB to C grades are classified as speculative as they are heavily influenced by changes in the investment environment.

[22] KOFIA. Regulation No.146, Chapter III Underwriting Of Non-Guaranteed Bonds, §11. Conclusion of Lead Management Agreement, etc. on Underwriting of Non-Guaranteed Bonds, Regulations On Securities Underwriting Business, etc. (20160421). http://eng.kofia.or.kr/brd/m_15/list.do

Table 3.3: Credit Rating Definitions for Bonds and Notes

Grade	Definition
AAA	Highest ability to repay principal and interest
AA	Excellent ability to repay principal and interest but slightly less than AAA-rated bonds
A	Very good ability to repay principal and interest but vulnerable to economic conditions and environment
BBB	Good ability to repay principal and interest but possibility exists of economic conditions and environment deterioration lowering its ability to repay principal and interest going forward
BB	Although its ability to repay principal and interest is not immediately problematic, the bonds have speculative factors since stability to go forward is not guaranteed
B	Ability to repay principal and interest is lacking; speculative; in a recession, repayment of interest is not certain
CCC	Uncertainties currently exit in its ability to repay principal and interest; highly speculative given the high risk of default
CC	Higher uncertainty factors exit compared with the upper grades
C	High risk of default; lacks ability to repay principal and interest
D	Unable to repay

Note: Bonds rated AA to B are marked with the signs + or – to denote the superior or inferior recoverability of principal and interest.
Source: Korea Investors Service.

3. Commercial Paper Credit Ratings

Companies that seek to obtain short-term financing from merchant banks, securities companies, and commercial banks by issuing commercial paper are required to undergo a credit assessment. The credit rating results are used not only to determine the soundness of the commercial paper, but also as criteria for determining the terms and conditions of issuance.

Accordingly, the government has selected independent CRAs to rate issuing companies and disclose the results, with the aim of developing a commercial paper market and ensuring the financial soundness of asset management, as well as to protect investors.

Credit ratings for commercial paper comprise six grades, ranging from A1 to D (Table 3.4). Among the grades, A1 to A3 are investment grades that recognize the ability of the issuer to repay principal and interest in a timely manner. B and C are speculative grades, indicating that on-time repayment of principal and interest is heavily influenced by changes in the economic environment.

Table 3.4: Credit Rating Definition for Commercial Paper

Grade	Definition
A1	Best ability to repay on time and best stability of repayment ability
A2	Very good ability to repay on time but stability slightly inferior to A1
A3	Good ability to repay on time with good stability but inferior to A2
B	Adequate ability to repay on time but speculative issues exist on its stability depending on short-term changes in conditions
C	Highly speculative issues in ability to repay on time and in its stability
D	Cannot repay

Note: Commercial paper rates A2 to B is marked with + or - to denote the superior or inferior ability to repay principal and interest.
Source: Korea Investors Service.

4. Electronic Short-Term Bond Credit Ratings

Electronic short-term bonds, which are electronically-issued bonds with a maturity of 1 year or less, were introduced on 15 January 2013, pursuant to the Act on Issuance and Trading of Electronic Short-Term Bonds. Their purpose is to complement the shortcomings of commercial paper, such as weak investor protection and slow distribution. These electronic bonds are quickly replacing commercial paper as a major source of short-term financing.

The same credit rating grades and definitions for commercial paper are also applied to electronic short-term bonds. They are used as criteria for determining the terms and conditions of issuance based on the ability of the issuer to repay short-term debt.

5. Asset-Backed Securities Credit Ratings

ABS are given credit ratings in the same manner as non-guaranteed corporate bonds or commercial paper, depending on the type (asset-backed short-term bond or asset-backed commercial paper). The credit rating system and definitions are the same as the system and definitions for non-guaranteed corporate bonds and commercial paper, thereby making it easier to determine the ability of the issuer to repay the principal of and interest on ABS.

6. Credit Rating for Issuance to Qualified Institutional Buyers

Corporate bonds and notes, and note issuance programs registered on the QIB Market, must obtain a credit rating from a CRA recognized internationally and/or by Korean investors. The rating needs to be disclosed, but the level of the rating is not an eligibility criterion for the QIB Market.

Investment by QIBs in QIB Market-eligible securities with a credit rating, and where the issuance-related information is publicly disclosed as required by KOFIA, will result in net capital ratio benefits for eligible QIBs.

Domestic and international CRAs recognized by KOFIA, as the administrator of the QIB Market, include

i. Standard & Poor’s,
ii. Moody’s,

iii. Fitch Ratings,
iv. Korea Rating,
v. KIS Rating, and
vi. NICE Rating.

P. Securitized Products Market

The Korean bond market features substantial issuance of ABS, with a number of distinct instrument types as well as ABS-versions of existing debt instruments such as straight bonds and commercial paper.

The issuance of ABS and representative structured bonds was explosive just after the 1997/1998 Asian financial crisis when the instrument was used for the restructuring of businesses. By 2001, the total issuance amount of ABS had reached KRW36.7 trillion, while the issuance of non-financial corporate bonds stood at KRW87.2 trillion. As the economy recovered, the issuance volume of ABS became smaller. However, the global financial crisis again increased the necessity of the use of ABS. Since 2012, more than KRW30 trillion of ABS have been issued each year.

This section aims to illustrate the securitized products market in greater detail.

1. Basic Structure

To create ABS, an originator typically establishes a special purpose company (SPC) and transfers the assets to the SPC so that it may issue the ABS based on these underlying assets. Once issued, the ABS is managed by an asset management servicer under the supervision of a trustee.

2. Major Participants

Entities involved in ABS issuance include originators, servicers, issuers (SPCs), business trustees, and credit enhancement agencies. Originators are the ultimate beneficiaries of ABS who own the underlying assets.

A servicer manages and maintains the underlying assets and their cash flows. The servicer also plays a significant role in managing the redemption of the ABS. It establishes a separate asset management system to handle claims, redemption, and debt collection. It also collects and provides relevant information, and prepares reports.

An SPC refers to a company that is established to issue ABS and segregate the underlying assets from the originators. Pursuant to the Asset-Backed Securitization Act, an SPC should be a limited company.

The SPC is only allowed to engage in the issuance and redemption of ABS in a way that is described in the ABS plan. Since an SPC is generally a paper company set up exclusively for the purpose of asset securitization, its business is trusted to a business trustee who is responsible for the settlement of accounts, book keeping, and tax affairs of the SPC.

A trustee takes care of ABS payments, management, and reinvestment. The main roles of the trustee are to monitor the overall asset management business on behalf of investors, manage cash and bank accounts related to the redemption of ABS, engage in custodial business activities such as reinvestment as requested by the servicer, and carry out ABS redemption as a proxy.

3. Structure of Asset-Backed Securities

The features of the underlying assets and cash flows are critical factors in determining the structure of an ABS. Collateral for an ABS can be classified as either amortizing or non-amortizing assets.

Amortizing assets are for loans for which the borrower makes regular, periodic payment of principal and interest over the life of said loan. In contrast, non-amortizing assets are for loans that do not have a set schedule for periodic payments by the individual borrower. Amortizing assets include residential mortgage loans, auto loans, corporate loans, and bonds, while credit card receivables and account receivables of corporations are considered non-amortizing assets.

When structuring an ABS, key factors are whether or not there was a true sale, the method of asset segregation and management, the method of wire transfer, and other measures that control the structural risks of securitization. True sales of assets uphold the legal rights of an SPC to the ABS, even when the originator or servicer has declared bankruptcy, by transferring the assets from the originator under a particular transfer structure.

Credit enhancement was introduced to promote the certainty of redemption. There are two primary types of credit enhancement: internal and external. The most common forms of internal credit enhancement are senior and subordinate structures and overcollateralization and excess spreads, while credit lines and credit guarantee are representative of external credit enhancement.

4. Asset-Backed Commercial Paper

Commercial paper is a short-term loan that many companies rely on to supplement their liquidity to pay for immediate expenditures, as they are simple to issue compared to corporate bonds.

Unlike conventional commercial paper, which is issued with credit and no collateral, asset-backed commercial paper (ABCP) is issued to raise capital in consideration of the underlying assets or future cash flows of a corporation or financial institution. In particular, most ABCP is not governed by the Act on Asset-Backed Securitization and is issued by a company that issues commercial paper.

Participants in the ABCP market include issuers, program managers, bill brokerage agencies, liquidity providers, and credit enhancement agencies. ABCP issuers are generally conduits, or SPCs, and raise capital by issuing commercial paper to purchase assets from originators. Program managers are usually commercial banks that manage the overall ABCP program and are responsible for the issuance and redemption of ABCP.

Bill brokerage agencies are mainly securities firms that sell ABCP to investors. Liquidity providers purchase ABCP that are not underwritten in the market to enhance liquidity and maintain the ABCP program, and also engage in approval and supervision activities. And lastly, credit enhancement agencies provide credit guarantees and take other measures to enhance the credit ratings of ABCP.

Q. Market Features for Investor Protection

Investor protection is among the fundamental regulatory objectives for a bond market—any securities market—to work well and develop further. Among different types of investors, professional investors have the ability to take risks in accordance with the investment. As a result, investor protection efforts by policy bodies and regulatory authorities are typically focused on ordinary investors, who are usually retail investors.

The FSCMA and its enforcement decree emphasize investor protection as one of their core purposes through all of the relevant provisions.

The need for investor protection explains why a certain level of information should be provided to the general public when a bond or note is newly issued via a public offering and/or listed on an exchange. In addition, investor protection is required not only in the primary market but also through the activities of ordinary investors in the secondary market.

This section reviews a number of topics that have a bearing on the protection of investors in the Korean bond market, particularly for retail or nonprofessional investors.

1. Investor Complaints

An ordinary investor may file a complaint with the Consumer Complaints Center operated by the FSS, which administrates complaints by consumers of financial products, including bond investors, against financial service firms. Complaints may arise due to alleged market price manipulation, insider or unfair trading, and the use of material nonpublic information, all of which are prohibited under the FSCMA.

For efforts at mediation and the resolution of financial disputes as a result of an investor complaint or petition, the FSS hosts the Financial Disputes Settlement Committee, though its recommendations are not legally binding.

In situations that cannot be mediated and resolved, investors may still choose to seek adjudication on the dispute through the courts. The FSCMA stipulates that a party who causes damage as a result of behavior prohibited by the act should be liable for such damage, and that those who suffered the damage have the right to claim for the damage.

2. Bondholder Rights

A bondholder is entitled to receive interest payments on a periodic basis and receive the repayment of the principal at maturity, in line with the terms and conditions of the bonds. In addition, a bondholder may request from the issuer, at any time during its business hours, to inspect or copy documents, such as the articles of incorporation and minutes of general meetings of shareholders. A bondholder may also raise an objection subject to a capital reduction resolution passed by a meeting of bondholders. An issuing company may designate an indenture trustee that has the power to act on behalf of the bondholders to monitor and enforce bondholder rights.

Information on the meeting of bondholders is provided in section S.

3. Indenture Trustee

In the case of the issuance of debt securities via a public offering, an issuer of non-guaranteed bonds shall appoint an indenture trustee, and both parties shall enter into a standard indenture trustee agreement.

The indenture trustee is entrusted with the bond administrative affairs for bondholders such as collecting redemption, preserving bonds, and other administration of bonds.

The adoption of the indenture trustee concept in 2012 contributes to the protection of ordinary investors, and bondholders overall, and supports the further growth of the corporate bond market. For further information on the nature and function of an indenture trustee, please refer to section R in this chapter.

4. Foreign Investors

The provisions for the protection of investors in the Republic of Korea do not make a distinction between domestic investors and foreign investors. As such, nonresident investors in the bond market have the same rights and obligations as domestic investors.

5. Investor Compensation Fund

The concept of an investor compensation fund, for the purpose of protecting investors in the securities market from financial loss, has been considered by the policy bodies and financial regulatory authorities. However, such a fund concept has not yet been introduced to the market.

R. Indenture Trustee

The revised Commercial Act, which went into effect in April 2012, introduced the indenture trustee system to the Korean market. Under the revised act, terms related to the previous “trustee” were changed to “indenture trustee” and “standard non-guaranteed corporate bond trust indenture agreement.”

The indenture trustee is entrusted with the bond administrative affairs for bondholders such as collecting redemption, preserving bonds, and other administration of bonds.

Article 480 of the Commercial Act and its enforcement decree stipulates that institutions designated to assume the role of indenture trustee are eligible financial institutions such as banks, trust companies, securities companies, KSD, and the Korea Securities Finance Corporation.

The indenture trustee concept ensures objective bond management without any business interests involved between an indenture trustee and issuers. Under the provisions, a company is disqualified as an indenture trustee if there is a potential conflict of interest between the bond issuing company and the indenture trustee, or if the indenture trustee has a special interest in the bond issuing company. In addition, when an indenture trustee acts in violation of the provisions or a resolution by a meeting of bondholders, the indenture trustee shall be jointly and severely liable to the bondholders for compensation for any damage that may result from the violation.

For the issuance of non-guaranteed bonds, an indenture trustee agreement following the standard template specified by KOFIA should be executed between the issuer and the indenture trustee. However, exceptions apply to bonds issued by specialized credit financial companies, merchant banks, commercial banks, and financial investment companies, as well as ABS, as stipulated in Paragraph 11-2 of the Regulation on Securities Underwriting Business.

S. Meeting of Bondholders

Pursuant to Subsection 2 of Section 3 in the Commercial Act, a meeting of bondholders may arrive at resolutions on matters that can affect the interests of bondholders. Such bondholder meetings can be convened by the issuer of the corporate bonds or by an indenture trustee. If at least two classes of bonds have been issued, a meeting of bondholders shall be convened for each class of bonds.

Each bondholder has the right to vote in its proportion to the total of the corresponding class of bonds. A meeting of bondholders may, if deemed necessary, request the issuer to cause its representative to attend the meeting. Any consent or request may be decided upon by a majority vote of the bondholders present. Bondholders not attending the meeting may exercise their right to vote in writing.

To exercise votes in writing, a bondholder shall submit a written application specifying required entries to the convener of the meeting by no later than the day immediately preceding the date set for the meeting of bondholders. The person who has convened the meeting shall request that a court authorize any resolution within 1 week from the date of adoption of such resolution.

A resolution of the meeting of bondholders shall take effect by obtaining authorization by a court. The resolution of the meeting shall be effective vis-à-vis all the bondholders who hold the class of bonds concerned. Any expense incurred in relation to meetings of bondholders shall be borne by the issuer.

T. Bankruptcy and Insolvency Provisions

This section provides a brief history of the evolution of the legal frameworks for bankruptcy and insolvency in the Republic of Korea.

1. Formalization of Workout Arrangement

The principles on bankruptcy in the Republic of Korea were adopted from the German legal system, as introduced by Japan. The principles on rehabilitation were largely modeled on United States federal law, such as Chapter 11 protections.

In June 1998, almost all Korean financial institutions entered into the Financial Institutions Arrangement for Facilitating Corporate Restructuring (known as the Master Workout Arrangement), introducing an informal workout system into the Korean insolvency regime. The Government of the Republic of Korea subsequently enacted the Corporate Restructuring Promotion Act (CRPA), which replaced the Master Workout Arrangement with the aim of facilitating and expediting informal workouts. The act, effective from September 2001 until the end of 2005, was the basic law governing out-of-court, informal corporate rescue procedures.

2. Consolidation of the Legal Frameworks

On 21 March 2005, the Government of the Republic of Korea promulgated the Act on Rehabilitation and Bankruptcy of Debtors, also known as the Unified Insolvency Law, which came into force in April 2006.

The law consolidated the previous Korea Company Reorganization Act, Composition Act, Bankruptcy Act, and Act on Rehabilitation of Individual Debtors in order to establish systematic procedures for the rehabilitation and liquidation of insolvent companies and individuals. In consolidating these statutes, the law abolished the composition procedure and established a rehabilitation procedure which modified and improved the previous reorganization procedure. As a result, the law provided for two corporate insolvency procedures: bankruptcy and rehabilitation. In the application of the Act on Rehabilitation and Bankruptcy of Debtors, nonresidents shall have the same status as that of Korean companies and individuals.

As a response to difficulties in reaching agreement between creditors and a lack of professionalism in the management of insolvent companies, the government introduced the corporate restructuring vehicle in October 2000. The corporate restructuring company was also introduced in May 1999 to promote corporate restructuring of insolvent companies and to address financial institutions' nonperforming loans.

The primary role of the corporate restructuring company is to obtain managerial control of an insolvent company and enhance its corporate value through vigorous restructuring. The insolvent company is eventually sold, within 8 years of the date of acquisition, in order for the corporate restructuring company to realize capital gains.

3. Current Framework and Practices

The latest CRPA, which came into effect on 18 March 2016, is the fifth revised version of the original CRPA enacted in 2001. The subordinate regulations to the new CRPA, the Presidential Decree and the Rules on Supervision of Financial Institutions to Promote Corporate Restructuring, came into effect on 29 April 2016 and 3 May 2016, respectively.

Further details on the restructuring and insolvency frameworks of the Republic of Korea and other economies in Asia and the Pacific can be found in *The Asia-Pacific Restructuring & Insolvency Guide* and *A Guide to Asia-Pacific Restructuring and Insolvency Procedures*.[23]

U. Event of Default

The default of a bond is a failure to meet the legal obligations (or conditions) of the bond issuance. It means that a bond issuer (debtor) has passed the payment deadline on either interest or principal.

In case of default by an issuer on a corporate bond, the indenture trustee has the power under the Commercial Act provisions to carry out on behalf of the bondholders all judicial or extrajudicial activities necessary for the collection of interest and/or redemption payments arising from the bonds or for the preservation of the bond value.

Pursuant to Article 424 of the Commercial Act, the determination on the deferring of a payment with respect to the relevant bond(s), or an exoneration from or settlement of any liability accrued due to the nonperformance of an obligation by the issuer, requires a resolution by a meeting of bondholders.

[23] White & Case LLP. 2016. *Asia Pacific Restructuring & Insolvency Guide; https://www.whitecase.com/publications/alert/asia-pacific-restructuring-insolvency-guide*
Clifford Chance. 2013. *A Guide to Asia-Pacific Restructuring and Insolvency Procedures*. http://financialmarketstoolkit.cliffordchance.com/en/financial-markets-resources/resources-by-type/guides/restructuring-and-insolvency-guide-asia-pacific.html

IV

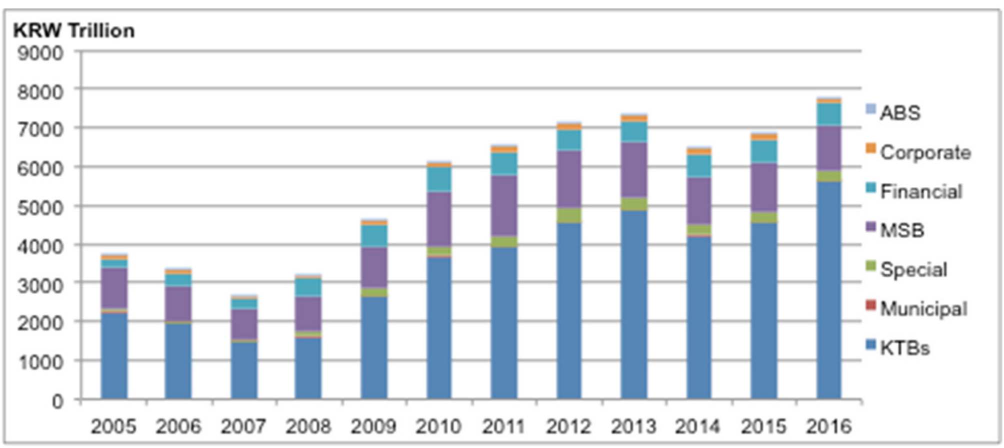
Bond and Note Transactions and Trading Market Infrastructure

A. Trading of Bonds and Notes

The Republic of Korea has a well-functioning secondary bond market. Bonds and notes are actively traded not only on the OTC market but also on the exchange market. Unlike the bond markets in other countries, the proportion of exchange trading in the Republic of Korea is relatively high, accounting for about 55% of all bond market trading.

In the exchange market, only listed bonds that are publicly offered can be traded. There is no restriction in the OTC market on the issuance method. Nevertheless, almost all bonds traded in the OTC market, especially on the K-Bond platform, are also publicly offered bonds.

Figure 4.1: Trading Volumes by Bond Type



ABS = asset-backed securities, KRW = Korean won, KTBs = Korea Treasury Bonds, MSBs = Monetary Stabilization Bonds.
Notes: Data as of end-December for each calendar year. Financial refers to bonds issued by banks and financial institutions.
Source: Korea Financial Investment Association. http://www.kofiabond.or.kr/; Korea Exchange. http://www.krx.co.kr/

In the past, especially before the 1997/98 Asian financial crisis, the trading of corporate bonds dominated the secondary bond market in the Republic of Korea. More recently, public bonds, especially KTBs and MSBs, dominate trading activities in the market. The proportion of the different types of traded bonds has also changed over the years. The proportion of government bonds has grown steadily, accounting for approximately 70% of the total trading volume at the end of 2016, with KTBs the dominant bond type (Figure 4.1).

Aside from KTBs, the other primary drivers of the Korean bond market have been transactions in government and public bonds, which include MSBs, municipal bonds, and special bonds. These bonds collectively make up the largest share of the market's trading volume. The proportion of financial bond and corporate bond transactions (including ABS) has remained steady at around 10% since 2005, recording 9.7% in 2016.

Almost all participants in the Korean bond market are institutional investors such as pension funds, asset management companies, financial investment companies, commercial banks, and insurance companies. Secondary market trading among bond investors is made through investment brokers in both the OTC market and the exchange market.

B. Market Segments and Trading Platforms

In a typical bond market, bonds and notes tend to be traded in the OTC market. In the Korean bond market, however, trading on the exchange platform represents a sizable portion of the overall market trading volume. The OTC trading volume is calculated as the sum of the buy and the sell amounts reported separately by the securities firms (the so-called double-counting). Meanwhile, the exchange trading volume is calculated as the executed amount of the trade (the so-called single-counting). The OTC trading volume is, hence, usually shown as double the amount traded in the OTC market.

The individual markets and their trading platforms are explained in greater detail in this section.

1. Over-the-Counter Market

The traditional OTC market itself is less a trading platform and instead an organized market. Trades in bonds and notes are concluded directly between institutional counterparties via phone or using the services of a voice broker or inter-dealer broker. Individual dealers may also use Bloomberg or similar global trading system providers, and/or an in-house trading system to carry out bond and note trading activities. Trading in the OTC market in the Republic of Korea is divided into this traditional OTC market and the K-Bond system operated by KOFIA, with the majority of OTC transactions executed on K-Bond.

Historically, OTC bond trading had accounted for a high proportion of the entire Korean bond market, about 98%–99% of all bond trading, before the Government of the Republic of Korea made it mandatory in October 2002 for Primary Dealers to deal on the exchange market for the purpose of supporting the development of the KTB market. After adopting the measure, Primary Dealers increased bond dealings on the exchange market, bringing the ratio for OTC to exchange market trading to 60:40.

The main participants in the OTC bond market are institutional investors, including banks, asset management companies, pension funds, and insurance companies. Institutional investors trade bonds through financial investment firms that serve as brokers.

Each institutional investor presents a bid–ask price to the financial investment firm they trade with, while the investment firm matches bid–ask prices to complete the transaction, and can exchange bid–ask prices with other firms to facilitate trading when necessary.

2. K-Bond

The OTC bond market in the Republic of Korea had traditionally used telephone-based voice trading for negotiated transactions.

Based on the Plan for Improving the Secondary Bond Market, which was issued by the FSC in October 2009 to, among others, establish a specialized bond trading system, KOFIA launched FreeBond, an online bond trading system, in April 2010. FreeBond enhanced efficiency in OTC trades by putting together individually scattered OTC trading functions into a single trading platform with messenger and chat room features.

FreeBond was upgraded to K-Bond in August 2017. As of the end of Mar 2018, 312 institutions and 6,622 individuals were registered with K-Bond, of which 226 institutions and 3,199 individuals were active users, based on the daily average trading volume.

K-Bond enables financial investment firms and market participants to discover quotes, and supports trade negotiations. Participants refer to bond trading brokers, dealers, managers, and traders approved by KOFIA, pursuant to its regulations on the registration of financial investment companies, as the SRO for the OTC market in the Republic of Korea.

K-Bond comprises two main components: an instant messenger system and the Trading Board (T-Board). The messenger function provides functions specialized for bond trading negotiations, including chat rooms, which allow participants to discuss 1 to N participants and conclude transactions in private; it also offers the automatic storage of chatting records. T-Board offers various types of bond market data, such as market quote information, 15-minute information, and book-building related information for market analysis.

All financial investment companies engaged in OTC bond trading are required to subscribe to K-bond. Most of the institutional investors that trade bonds in the Republic of Korea—such as pension funds, insurers, credit unions, and banks—are members of K-Bond. K-Bond also distributes bond trading details to the market within 15 minutes (see also section C).

Delivery of the bonds and settlement for OTC trades are carried out simultaneously at KSD, with the settlement date ranging from T+1 to T+30, although most settlements occur on T+1. When foreign investors trade Korean bonds, time differences result in T+3 and T+4 settlements being commonplace. Repo bonds, municipal bonds, and retail bond transactions may all be settled on the same day (T+0).

In December 2007, KOFIA introduced the OTC Bond Quotation System (BQS) in order to boost transparency in the market. The system collects and reports bid–ask prices of all bonds in the OTC market with a par value over KRW5 billion. The collected bid–ask prices are then disclosed to all market participants through the BQS, as well as through information terminals of the CHECK and INFOMAX systems (see section E).[24]

3. Trading on Korea Exchange

On KRX, the bond market and other regular trading markets are grouped under the KOSPI market, which takes its name from the acronym for the Korea Composite Stock Price Index, the representative index from the original stock market on KRX. According to provisions in the FSCMA, the KOSPI market was established for the trading of securities such as equity securities, debt securities, beneficiary securities, investment contract securities, derivative-combined securities, and depositary receipts.

Bond trading on KRX is conducted on an electronic trading platform. Users can access the trading platform through the members-only network and the internet. KRX KTB, in

[24] See www.bqs.or.kr

particular, is a web-based platform; dealers can participate by installing a trading program offered by KRX on their computers.

KRX introduced the Electronic Request for Quote (e-RFQ) concept through screens in March 2016, in addition to the Central Limit Order Book (CLOB), to meet the needs of the market and improve market participants' convenience.

KRX also launched the electronic trading infrastructure Exture+ in March 2014. The Exture+ system is web-compatible as well as being compatible with KRX's Direct Market Access network; therefore, all KRX markets are accessible for global investors, regardless of their domicile and time zone, at no additional charge.

As of February 2018, the KRX bond market comprised four segmented markets: KRX KTB; KRX BondsAll, in which all bonds listed on KRX are traded; KRX LPB; and KRX Repo, which specializes in trading specified bonds.[25] Competitive auction is the basic trading method used on the platforms in KRX bond market segments. Trading hours for all market segments are from 9 a.m. to 3:30 p.m. Table 4.1 displays this and other market segment features in a practical overview.

Table 4.1: Overview of Korea Exchange Bond Market Segments

<table>
<tr><th></th><th>KRX KTB</th><th>KRX Repo</th><th>KRX BondsAll</th><th>KRX LPB</th></tr>
<tr><td>Participants</td><td colspan="2">Banks and Securities Companies</td><td>Securities Companies</td><td>Securities Companies (common account)</td></tr>
<tr><td>Bonds eligible for trading</td><td>KTB, MSB, DIFB</td><td>KTB, MSB, AAA-rated corporate bond</td><td>All bonds listed on the KRX including option embedded bonds</td><td>Type I NHB, Subway Bond, Community Development Bond</td></tr>
<tr><td>Trading hours</td><td colspan="4">9 a.m.–3:30 p.m.</td></tr>
<tr><td>Trading execution method</td><td colspan="2">Continuous auction (individual auction with multiple price)</td><td>- At the market opening: individual auction with single price
- During the session: individual auction with multiple price</td><td>- At the market opening: individual auction with single price
- During the session: individual auction with multiple price
- At the market closing: single price auction with the reported market price</td></tr>
<tr><td rowspan="3">Settlement method</td><td>T+1</td><td colspan="3">T+0</td></tr>
<tr><td colspan="2">DVP: payment through BOK-Wire and securities delivery through KSD</td><td colspan="2">DVP: Payment through Commercial Bank and securities delivery through KSD</td></tr>
<tr><td colspan="4">-Clearing conducted by KRX
-Collective multilateral netting settlement by KSD</td></tr>
</table>

BOK = Bank of Korea, DIFB = Deposit Insurance Fund Bond, DVP = delivery versus payment, KRX = Korea Exchange, KSD = Korea Securities Depository, KTB = Korea Treasury Bond, LPB = Licensed and Permit Bonds, MSB = Monetary Stabilization Bond, NHB = National Housing Board Bond, T = trading day.
Note: AAA denotes a credit rating.
Source: Korea Exchange.

[25] In February 2018, KRX officially renamed the English designations for its bond market segments.

a. KRX KTB

KRX KTB facilitates the inter-dealer market for KTBs and other government bonds. The 1997/98 Asian financial crisis had prompted the Government of the Republic of Korea to announce its Measures to Improve Government Bond Policies and Vitalize the Bond Market. As part of the process to facilitate development of the government bond market, Primary Dealers were introduced in 1999 and KRX KTB was placed on KRX.

On KRX KTB, details of the bid and ask orders presented by each dealer are collected and disclosed, and transactions are carried out between dealers. The tick size varies by remaining time to maturity but stands at KRW1 in case of 10-year benchmark KTB and 10-year inflation-linked bonds. Quotations are based on limit orders.

Eligible market participants are limited to financial investment firms and banks holding licenses for investment dealing of Treasury bonds. Such market participants are classified into two categories: Primary Dealers and preliminary Primary Dealers, who take priority for Treasury bond underwriting in the primary market but have to perform duties as market makers in the secondary market; and Ordinary Dealers, who may participate in the secondary market but not in the primary market. As of October 2017, 17 Primary Dealers, 4 preliminary Primary Dealers, and 41 Ordinary Dealers were participating in KRX KTB.

Tradable bonds are KTBs, MSBs, and Korea Deposit Insurance Corporation Fund Bonds. The trading unit is an integer multiple of a par value of KRW1 billion. Transactions are concluded through individual competitive bidding using multiple prices, based on a principle, which gives priority to the bid–ask quotation with the best price and time. The settlement day was set on T+1 in June 2003 from the original practice of T+0.

b. KRX BondsAll

KRX BondsAll was established in March 1956. All listed bonds—including government bonds, municipal bonds, corporate bonds, and equity-based corporate bonds—are eligible for trading in the market. Convertible bonds should be traded in KRX BondsAll only, not in the OTC market, for the purpose of formation of fair prices and liquidity enhancement. Actual transactions generally involve retail bonds, small-cap government and public bonds, and equity-linked corporate bonds.

In principle, all market participants can trade in KRX BondsAll and non-KRX members can participate in the market indirectly, with ordinary investors being the main participants, by opening entrustment accounts at financial investment firms which hold KRX membership. The trading unit is KRW1,000 and the settlement day is T+0. Transactions are concluded through individual competitive bidding, which are based on the four principles of price, time, brokerage, and quantity.

The market-maker program has been adopted in KRX BondsAll to encourage investors to trade bonds and enhance liquidity. A KRX member that wants to perform as a market maker should submit an application to KRX. Then, on a semiannual basis, the exchange reviews applicant members' financial status, operational personnel, and other details, and determines eligible market makers. The members designated as market makers should fulfill the market-making obligations that KRX imposes. When such members are found to have failed to meet these obligations after KRX has carried out a regular evaluation of their performance, the designation may be revoked. Moreover, trade commission is not charged on market-making quotations, and financial incentives are given to market makers depending on their quarterly market making performance.

c. KRX LPB

When Koreans acquire some license or permits—or purchase houses, real estate, or automobiles—they are required to purchase License and Permit Bonds (LPBs). In the past, certified judicial scriveners or car salespersons often purchased and sold such bonds at low prices on behalf of consumers. KRX established the KRX LPB in October 1995 to promote the trading of LPBs, and such bonds should be traded only on KRX LPB.

A bond purchaser can sell the bonds to a bank (a sales agent). The bank that has purchased the bonds places an ask order in KRX LPB through a financial investment firm with which the bank has signed an agent contract. KRX has established the LPB Membership to process bid orders of the bonds. Members of the system have to submit a certain volume of bid orders on KRX LPB and the reported prices after market closing every day. KRX gathers the reported prices and calculates a new reported market price that serves as a base price for trading or purchase by the banks on the following day.

d. KRX Repo

KRX Repo opened in February 2002 and was designed with market regulations based on the Global Master Repurchase Agreement. The market has adopted the classic repo trading method, which connects the ask (bid) contract on the trading day and the bid (ask) contract on the repurchasing day into one contract.

At the time of compilation of this Bond Market Guide, KRX featured 12,979 listed bonds, of which 159 were traded on a regular basis during the most recent full year. KRX bond trading volume accounted for about 55% of the total bond trading volume in the Korean market; specifically, KTB trading volume in the KRX bond market took up about 70% of the total bond trading volume in the Korean market.

Cash settlement for KRX trades generally takes place via BOK-Wire+, while the bonds are transferred through escrow accounts at KSD. As such, it is similar to and yet slightly different from the OTC market delivery-versus-payment settlement method.

C. Mandatory Trade Reporting

Trading in the OTC market in the Republic of Korea is subject to the regulations set by KOFIA, as an SRO and the administrator of the market. All trades executed in the OTC market—including transactions in the QIB Market as a segment of the OTC market—have to observe the so-called “15-minute rule,” which refers to the requirement that trading information must be reported to KOFIA through an intermediary trading counterparty or a securities broker within 15 minutes after execution, without exception. The rule was established in 2000.

On KRX, trades are quoted, concluded, and executed in the respective electronic trading platforms of the individual bond market segments (see also section B). Quotes and executed trades and their prices are displayed in real time on the screens of trading members and market segment participants. As such, trading members, participants, and KRX are automatically aware of all executed trades and their details, without the need for a separate reporting practice.

D. Market Monitoring and Surveillance in the Secondary Market

Efforts for the monitoring and surveillance of activities in the secondary market and resulting actions depend on the bond market segment in which these activities occur.

Because market monitoring and surveillance in the secondary market is regarded as part of policy implementation for market stability and investor protection by maintaining fairness and securing transparency based by the Act on the Establishment, etc. of the Financial Services Commission, the final responsibility is thought to lie with the FSC. Under the guidance of the FSC, the FSS is responsible for the inspection and supervision of financial institutions.

1. For Trading Activities on Korea Exchange

Based on the Article 403 of the FSCMA, KRX can take necessary actions and measures for market surveillance, investigations into abnormal trading activities, member inspection, inter-market surveillance, and the disciplinary actions taken against members and their officers and employees, as well as preventative activities toward unfair trading, according to Article 1 of the KRX Market Oversight Regulation.

The KRX Market Oversight Commission carries out market surveillance by detecting issues and following up on suspicions of abnormal trading through investigations. The objectives are to identify trades that are likely to violate the regulations governing the business of the exchange, to conduct inspections and, when there is a possibility of abnormal trading, identifying the securities with abnormally soaring prices to prevent any unfair trades.

If there is an unfair or suspicious transaction in the bond market, the KRX Market Oversight Committee will examine that transaction and surveil related market participants. Under the Market Oversight Regulation, the KRX stipulates matters necessary for such market surveillance and investigation into abnormal trading activities, as well as member inspection. Details about the Market Oversight Committee can be found in Chapter II.D of the regulation.

Detection of issues, such as suspicious or abnormal trading activities, takes into consideration the trading type, price fluctuations, and trading volume of securities, the degree of participation in price formation and trading, as well as details of rumors, among other subjects.

2. For Trading Activities in the Over-the-Counter Market

KOFIA monitors the book-building process, the underwriting activities in the primary market including that of the management companies, as well as transaction details in the secondary market and the reporting of price quotes.

When a KOFIA member company violates regulations, KOFIA can impose restrictions through the Self-Regulation Committee and impose a penalty on the member company itself, its executives, or employees. Credit rating and bond assessment working groups under KOFIA also regularly monitor the track record of CRAs in their rating assessments, as well as the bond valuation prices provided by bond pricing agencies. KOFIA officially announces those results or reports them to the FSC.

The Self-Regulation Committee consists of seven members, including the committee chairman, three financial experts, one legal expert, one accounting or finance expert, and the chief executive officer of a regular member company. The working groups mentioned above also consist of seven members including experts from related fields.

E. Publication of Real-Time and Reference Data for Over-the-Counter Bond Trading

One of the focal tasks of KOFIA under its mandate as the SRO and administrator for the OTC market is to ensure market transparency and the distribution of relevant information to all market participants under that goal. This section details some of the reference data that are being collected and distributed by KOFIA through its systems.

1. Publication of OTC Trade Execution Details

After a brokerage house sells a bond in the OTC market, it must report to KOFIA details of the transaction within 15 minutes. KOFIA then publishes this information.

The publication mandate was introduced in 2000 to enhance market transparency and boost the credibility of prices, while the 15-minute rule aimed to improve the accuracy of reporting information on OTC bond transactions. In the same context, KOFIA created the Bond-Trade Report and Information Service (B-TRIS) in 2001, which enables real-time management of data between KOFIA and financial investment companies. B-TRIS is the OTC bond market disclosure system to collect and disclose OTC bond trading information.

Bonds subject to the reporting requirements include government bonds, MSBs, special bonds, and structured securities, among others. The real-time quote information collected through K-Bond, along with execution information provided through B-TRIS, are used as source information for building the bond index and bond ETFs. KOFIA also discloses bond quotes, trading yields, and bond assessment company yields on its website every day. KOFIA also receives trading records on a wide-range of other debt securities such as certificates of deposit, commercial paper, repo, and electronic short-term bonds.

As of March 2015, an average of 3,000–5,000 daily transactions were reported under the 15-minute rule. This rule has not only enhanced market transparency, but also reduced the cost of seeking out price-related information. Furthermore, it expedited the speed of information distribution as information on issues, trading volume, yields, and investor categorization codes is provided in real-time.

2. Publication of OTC Quotation Information

Alongside the 15-minute rule, which promotes post-trade transparency, it was also necessary to introduce a service for enhancing pre-trade transparency. In an effort to improve liquidity and market transparency in general, KOFIA introduced the BQS in 2007.

KOFIA requires financial investment firms, banks, and merchant banks, as well as inter-dealer brokers to report, in real-time, all information on quotes and exercise prices of all bonds traded in the OTC market through K-Bond. This ensures that all OTC quotes can be published, enhancing the price discovery function and increasing transparency as well as liquidity in the OTC market.

3. Publication of OTC Final Quotation Yields

When the market closes, KOFIA posts the final quotation yield for each bond that is represented on the Korean bond market on the BQS website.[26] The information can be used as indicators for economic policies, asset management by financial institutions,

[26] See www.kofiabond.co.kr

and the appraisal of investment performance. Information is collected at 11:30 a.m. and 3 p.m. each working day, and disclosed at 12 noon and 3:30 p.m. the same day.

KOFIA also discloses base yields that are used for daily closings and derives the final settlement price for 3-year, 5-year, and 10-year interest rate futures, and market-making quotation yields for bond-specialized dealers. Furthermore, KOFIA discloses details on commercial paper for transaction information management, yields and indices, certificate of deposit yields and transaction status, customer repo transaction status, and intermediary repo transactions among institutions.

KOFIA has been providing real-time bond indices (see also section G), enabling a real-time assessment of the bond market and the development of new index-linked bond products, including ETFs. The first Korean KTB ETF was listed on KRX in July 2009.

F. Bond Information Services

Investors in the Korean bond market—both professional and ordinary investors—have many opportunities to obtain information on bonds and notes issued. The information itself and the method of delivery of the information may depend on the bond market segment, type of instrument sought, and the market institution providing the service. In principle, most information is available online, but might also be available on a commercial basis from market intermediaries and information vendors. A list of publicly issued bonds and notes (and related information) is also available on the official disclosure website of the FSS.[27] If the publicly issued bond is listed, then information can be found on the KRX website.

1. Information on Government Bond Program

MOSF provides general information on KTBs and KTB investment—including issuance schedule, auction results, and other statistics—on a Korea Treasury Bonds website (Figure 4.2). Real-time information on KTB trading in the secondary market is also available on the KRX website as well as the KOFIA website.

[27] See http://dart.fss.or.kr

Figure 4.2: Korea Treasury Bond Information Web Page

KTB = Korea Treasury Bonds.
Source: Ministry of Strategy and Finance. https://ktb.mosf.go.kr/eng/

2. KOFIA Bond Information System

KOFIA provides information to the public on bonds and notes registered or traded in the OTC market. The KOFIA Bond Information System offers quotation yields, issuance and trading data, real-time transaction information, and real-time bond market indices, among other information (Figure 4.3); the information is available in English as well.[28]

Figure 4.3: KOFIA Bond Information System Web Page

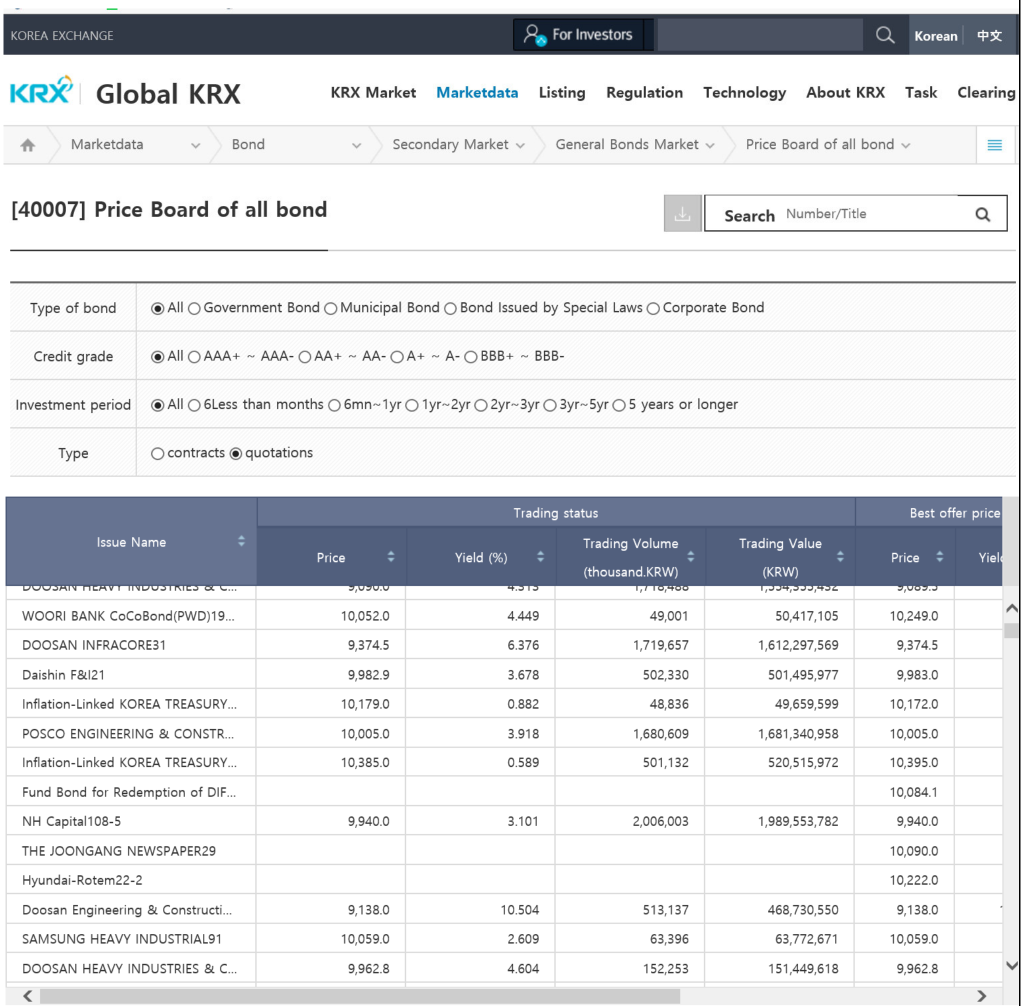
Source: Korea Financial Investment Association. http://www.kofiabond.or.kr/index_en.html

[28] See www.kofiabond.or.kr

3. Information from Korea Exchange

KRX provides prices of all bonds and notes listed on its markets as well as general data on those bonds and notes in real-time via its website (Figure 4.4). The same information will also be made available to global information vendors, including Bloomberg and Thomson Reuters, or may be subscribed to directly from KOSCOM, a subsidiary of KRX.

Figure 4.4: Korea Exchange Bond Price Board Web Page

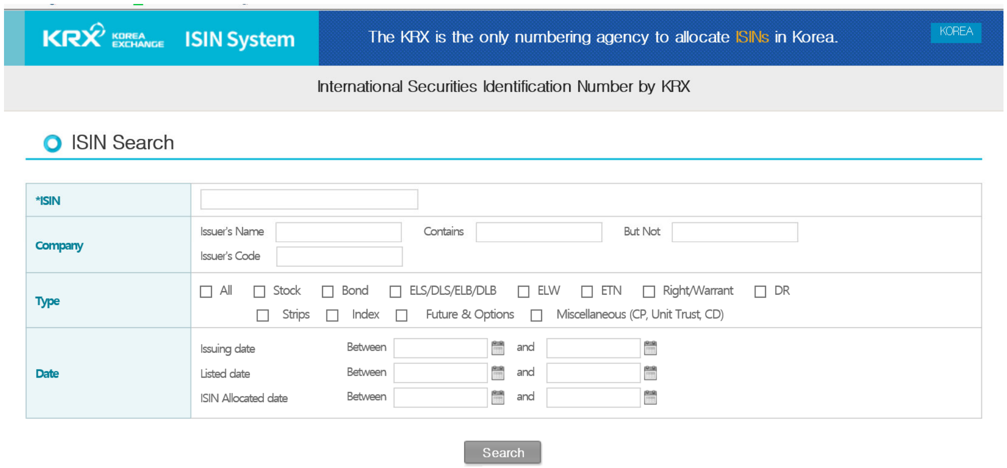


Source: Korea Exchange. https://global.krx.co.kr/contents/GLB/05/0504/0504040201/GLB0504040201.jsp

In addition, KRX is the appointed Korean institution to issue International Securities Identification Numbers; every listed bond has its own identification number, which is available at a dedicated KRX web page (Figure 4.5).[29]

[29] See www.isin.krx.co.kr

Figure 4.5: Korea Exchange ISIN System Web Page



ISIN = International Securities Identification Number.
Source: Korea Exchange. http://isin.krx.co.kr/main/eng.do?method=eng_main

4. Securities Information Service of Korea Securities Depository

KSD provides a comprehensive securities information service for its participants and their clients. KSD collects and manages all information related to deposit-eligible securities—issuance information, deposit information, lost and stolen securities, and corporate action information—and makes it available through its Securities Information Portal (SEIBro).

SEIBro is an information portal providing securities information held by KSD to both individual and financial institutions through web and mobile service. SEIBro offers a wide range of securities related information available in the Republic of Korea, with equity and bond information on as many as 3,700 issuers. It also provides comprehensive securities issuance information for equity, bonds, investment funds, derivatives securities and short-term securities, as well as information on OTC transactions including securities lending and repo.

G. Secondary Market Yields, Yield Curves, and Bond Indices

1. Yields and Yield Curves

Not every bond is traded on a daily basis. The number of the on-the-run issues that are actively traded in the secondary market is limited, and thus, the yields of most off-the-run-issues may not always be representative. In this case, the bond pricing agencies play key roles in pricing bonds which are not actively traded. In the Republic of Korea, four agencies provide bond yield or price information through the KOFIA website (Figure 4.6). The agencies are KAP, KIS Pricing, NICE P&I, and Fn Pricing (see also the section on Bond and Note Pricing in Chapter III).

Figure 4.6: KOFIA Mark-to-Market Valuation Matrix

HOME>Mark-to-Market Valuation >Mark-to-Market Benchmark Yields (Matrix)

By Date | By Period

Date: 2017-11-10 | Institution: 4 Agency Avg | Search

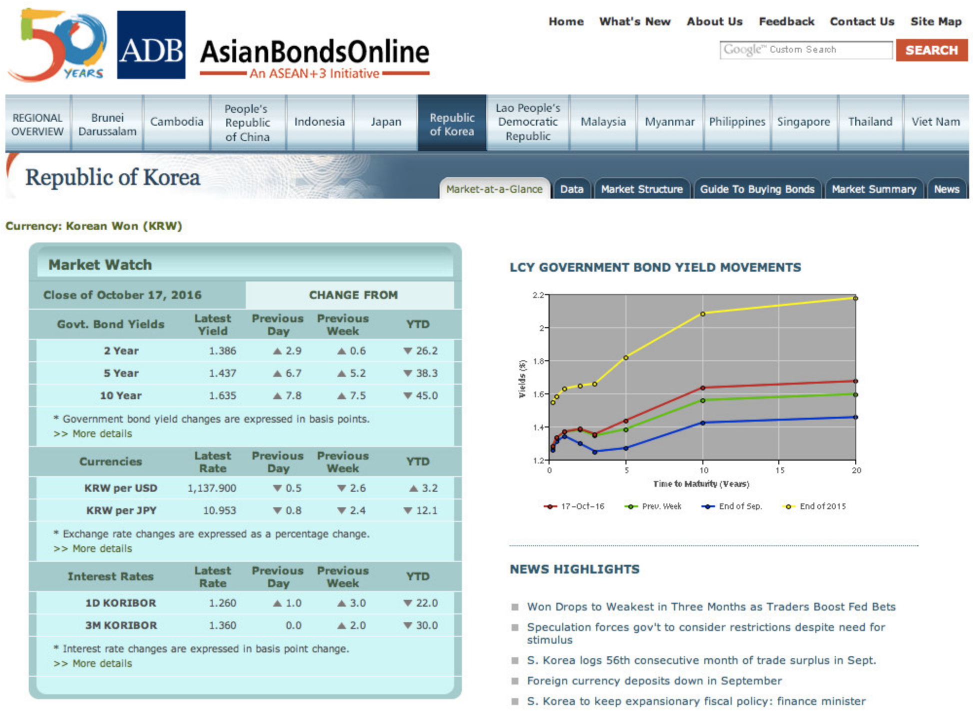
(Unit : %)

Class	Instrument	Credit Rating	3m	6m	9m	1y	1y6m	2y	2y6m	3y	4y	5y	7y	10y	20y	30y	50y
Gover···	KTB	Grain, Fx &···	1.395	1.533	1.661	1.774	1.999	2.076	2.110	2.157	2.312	2.352	2.504	2.570	2.506	2.505	2.505
	NHB2	–	1.198	1.328	1.470	1.588	1.757	1.880	1.893	2.045	2.174	2.313	2.456	2.596	–	–	–
	NHB1	Other Gove···	1.453	1.589	1.732	1.847	2.019	2.137	2.146	2.264	2.380	2.521	–	–	–	–	–
Munic···	Seoul Railr···	–	1.486	1.618	1.764	1.883	2.051	2.179	2.192	2.315	2.428	2.572	2.635	–	–	–	–
	Regional D···	Other Muni···	1.486	1.618	1.764	1.883	2.051	2.179	2.192	2.315	2.428	2.572	–	–	–	–	–
Special	State-owne···		1.572	1.731	1.833	1.951	2.108	2.245	2.254	2.348	2.469	2.555	2.594	2.613	2.611	–	–
		AAA	1.594	1.757	1.858	1.981	2.140	2.270	2.282	2.366	2.480	2.579	2.628	2.656	2.656	2.681	–
		AA+	1.624	1.793	1.894	2.015	2.186	2.322	2.332	2.417	2.538	2.679	2.762	2.839	2.898	–	–
		AA	1.679	1.848	1.950	2.085	2.256	2.398	2.416	2.504	2.630	2.789	2.870	2.944	3.030	–	–
		MBS	1.595	1.759	1.858	1.980	2.140	2.272	2.285	2.370	2.479	2.580	2.629	2.656	2.658	–	–
MSB	–	–	1.429	1.580	1.711	1.810	2.007	2.122	–	–	–	–	–	–	–	–	–
Finan···	Non-guara···	AAA (KDB)	1.581	1.751	1.873	1.958	2.149	2.277	2.287	2.363	2.471	2.572	2.636	2.676	–	–	–
		AAA (SME)	1.581	1.751	1.873	1.958	2.149	2.277	2.297	2.372	2.488	2.587	2.662	2.711	–	–	–
		AAA	1.605	1.774	1.905	2.001	2.186	2.311	2.336	2.411	2.503	2.599	2.699	2.769	–	–	–
		AA	1.797	1.990	2.107	2.241	2.445	2.593	2.655	2.734	2.822	2.962	3.064	3.152	–	–	–
		A+	2.049	2.307	2.444	2.598	2.808	2.958	3.011	3.103	3.197	3.328	3.465	3.640	–	–	–
**Fina···	Non-guara···	AA+	1.751	1.933	2.094	2.177	2.357	2.543	2.574	2.614	2.714	2.857	2.962	3.233	–	–	–
		AA0	1.789	1.951	2.108	2.205	2.393	2.612	2.670	2.741	2.854	3.045	3.147	3.452	–	–	–
		AA-	1.809	1.970	2.144	2.232	2.460	2.675	2.762	2.913	3.033	3.215	3.328	3.695	–	–	–

Source: Korea Financial Investment Association. http://www.kofiabond.or.kr/index_en.html

Securities information and yield and price data, particularly on government bonds, is also available from the *AsianBondsOnline* website, under an initiative by ASEAN+3 (Figure 4.7).

Figure 4.7: Government Bond Yields and Yield Movements on *AsianBondsOnline*



CPI = consumer price index, LCY = local currency, YTD = year to date.
Source: *AsianBondsOnline*. Selected Government Bond Yields and Yield Movements. https://asianbondsonline.adb.org/korea.php

In addition to yields for specific benchmark issues, an aggregate government bond yield curve for selected periods, as well as many more data points can also be accessed using the website.[30]

2. Other Bond Yields—Corporate Bonds and Notes

The yield curve information provided by the bond pricing agencies via the KOFIA bond information website include not only the information on public sector bonds, such as government bonds and special bonds, but also private sector bonds, including corporate bonds with diverse credit ratings.

3. Daily and Real-Time Bond Indices

The calculation of real-time bond indices was made possible with the introduction of BQS (see also section E). Currently, seven types of real-time bond indices are provided, which are calculated using information sourced from BQS.

[30] See http://asianbondsonline.adb.org/singapore/data/marketwatch.php?code=government_bond_yields

Table 4.2: Status of Real-Time Bond Indices and Exchange-Traded Funds

Index	ETF	Update Interval	Source	Starting Index (Point)	Base Date
MKF KTB Index	KODEX TB	30 sec.	KOFIA BQS	100	16 Jun. 2004
KEBI KTB Index	N.A.	5 min.	KOFIA BQS	100	30 Jun. 2009
MK MSB Index	KOSEF MSB	1 min.	KOFIA BQS	10,000	2 Jan. 2010
MK MM Index	KOSEF Short-Term Money	1 min.	KOFIA BQS	10,000	1 Jun. 2010
KOBI Credit Index	Kstar High-Grade Corporate Bond	1 min.	KOFIA BQS	10,000	1 Sep. 2010
KRW Cash Index	KODEX Short-Term Bond	30 sec.	KOFIA BQS	100	2 Jan. 2006
KIS MSB 3M index	TIGER Money Market Fund	1 min.	KOFIA BQS	10,000	1 Jan. 2012
KAP Barbell Index	ARIRANG Barbell Bond	1 min.	KOFIA BQS	100	30 Jun. 2009
KAP MM Index	ARIRANG Short-Term Bond	1 min.	KOFIA BQS	100	31 Dec. 2011
KIS MSB Short-Term Index	KINDEX Short-Term Money	1 min.	KOFIA BQS	10,000	1 Jan. 2013
KIS MSB 5M Index	KStar Short-Term MSB	1 min.	KOFIA BQS	10,000	1 Jan. 2013
KRW Cash Plus Index	KODEX Short Term Bond Plus	1 min.	KOFIA BQS	100	31 Dec. 2007
KAP Bullet Index	N.A.	1 min.	KOFIA BQS	100	31 Dec. 2011
KAP Short Term Index	POWER Short-Term Bond	1 min.	KOFIA BQS	100	31 Dec. 2007
KOBI Half Credit Index	ARIRANG High-Grade Corporate Bond	1 min.	KOFIA BQS	10,000	1 Jan. 2016

BQS = Bond Quotation System, N.A. = not applicable.
Source: Korea Financial Investment Association (KOFIA).

Based on BQS indices, 12 real-time bond indices have been created. With the exception of the KEBI KTB index, 11 are used as benchmark indices for bond ETFs. As of 20 May 2015, 11 bond ETFs were listed on KRX, with a total market capitalization of KRW3.1 trillion.

KRX was calculating three indices for bonds as of October 2017. Among them, the KRX KTB Index, launched in June 2009, is utilized most and is calculated once every minute. The index is calculated based on the prices of three benchmark KTBs (two 3-year bonds and one 5-year bond), which also represent the underlying securities for the three-year KTB futures listed on the KRX derivatives market. As the constituent securities of KTB futures and bond indices are the same, the linked trade between the KTB and KTB futures markets is active. A variety of financial products that track the yield of the index have been developed; in particular, five ETFs tracking the index are listed and actively traded in the KRX ETF market.

In addition, KRX has been calculating the KRX Korea Treasury Bond Prime Index since May 2006, for Treasury bonds traded on the KRX secondary market. The constituent securities of the index are six 3-year, 5-year, and 10-year on-the-run issues, which are highly representative; the index is calculated every 5 minutes.

The KRX Bond Index, which is not a real-time index, was launched at the same time, more so to display the bond market status. This index is calculated as an end-of-day index for all bonds listed on the KRX market by bond type and maturity.

H. Repo Market

1. Repo Market Overview

The Korean repo market is divided into the exchange market launched by KRX in 2002 (now KRX Repo) and the OTC market where transactions are done directly between the counterparties or through an intermediary.

In addition to the KRX and OTC repo markets, other repo market segments consist of (i) the institutional repo market where repo trading occurs mainly for the purpose of financing and the raising of working capital between financial institutions; (ii) the customer repo market where financial institutions trade with nonfinancial corporations or individuals in terms of received deposits; and (iii) the BOK repo market, as a part of its open market operations, where BOK trades with its constituents to manage the money supply and interest rates.

Most financial institutions can participate in the OTC institutional repo market, whereas only financial institutions who are members of KRX bond market segments are able to trade in KRX Repo. Typically, almost 99% of repo transactions are traded in the OTC institutional market.[31]

2. Institutional Over-the-Counter Repo Market

The institutional OTC repo market is operated by KOFIA.

a. Eligible Securities

Securities that are allowed to be traded in the OTC institutional repo market are those prescribed in the FSCMA. Bonds, commercial paper, ETFs, and equities are eligible for the KSD’s repo system as long as these securities are deposit-eligible, subject to regular price evaluation, and denominated in Korean won.

b. Participants

The Regulation for Financial Investment Businesses issued by KOFIA prescribes that financial institutions are eligible as participants in the OTC institutional repo market. Any participant who opens a securities account with KSD and receives approval from the KSD can participate in the KSD repo system. The KSD regulates that foreign participants must appoint a standing proxy for their repo transactions.

c. Major Features of the Korean OTC Institutional Repo Market

i. Direct Trade versus Brokered Trade

Repo trades in the OTC market are divided into direct trades and brokered trades. Under direct trades, participants themselves look for counterparties. If they encounter difficulties finding a counterparty, they

[31] Adapted from Executives Meeting of East Asia–Pacific Central Banks. 2014. *EMEAP Repo Markets: State of Play—A Report by the EMEAP Working Group on Financial Markets*. http://www.emeap.org/emeapdb/upload%5CWGMeeting%5CEMEAP_Working_Group_on_FinancialMarkets_-_Report_on_EMEAP_Repo_Markets_....pdf

may request a brokerage company to find one for them. There are five brokerage companies in the OTC institutional repo market. As of 30 April 2016, the percentage of brokered trades was approximately 90% of the total trade volume in the OTC market.

ii. Triparty Repo Agent

A triparty repo agent is an independent third party that provides services, including settlement and collateral management services, after repo trades are executed. The KSD acts as a triparty repo agent that provides participants with the aforementioned services to facilitate repo trades in the OTC institutional repo market from initial execution to repurchase date.

iii. Types of Transactions

A participant normally designates a repurchase date at the time of concluding a repurchase agreement. This type of transaction is a fixed-term repo. On the other hand, an open-ended repo has no designated repurchase date. In the OTC institutional repo market, both types of transaction are used, and the repo term completely depends on the agreement between a repo seller and a repo buyer. The most common repo term is 1 day.

iv. Business Hours for Korea Securities Depository Repo System

KSD’s triparty repo services are administrated from 9 a.m. to 5:00 p.m. KSD may change these business hours, in which case the KSD shall give its participants prior notice on the change in business hours.

d. Trade Capture and Matching

i. Submission of Details of Repo Trade

Upon the execution of repo transactions, repo sellers (for direct trades) or brokerage forms (for brokered trades) shall submit the details of the repo trade to KSD. Upon receiving the details of the repo trade, the KSD shall notify repo buyers (for direct trades) of the details of the repo trade or notify repo sellers and buyers (for brokered trades) of the details of the repo trade (Table 4.3).

Table 4.3: Details of Repo Trade Submitted by Repo Sellers or Brokerage Firms

Item	Content	Option
Basic Information	Counterparty, repo position (buy or sell), purchase price, purchased securities, repo rate	
Type of Transaction	Term: fixed maturity (enter transaction period) Open: no fixed maturity (no need to enter transaction period)	Term and Open
Transaction and Single Agreement	Transaction: to separate from existing trades with the same counterparty and enter into a transaction Single agreement: combine with other repo transactions entered into with the same counterparty to form a single agreement.	Transaction and Single
Settlement Agent	If the party wishes to settle through its settlement agent, the name of the settlement agent needs to be entered. (The details of the settlement agent shall be registered in advance.)	Account no. of securities ledger held with the settlement agent
Methods of Settlement	DVP: simultaneous settlement through the DVP system between BOK (central bank) and KSD FOP: separate settlement of securities and payment (the participant may choose the type of payment)	DVP and FOP
Base Currency	A range of currencies are available for purchase	KRW, USD, JPY, and EUR
Charges	The party subject to the service charges to the KSD	Both Parties, Seller, or Buyer
Interval of Repo Interest Payment	Enter the interval if it has been agreed that the repo interest shall be paid (received) on a regular basis.	Daily, 1-,2-,3-,4-,6-Month, Repurchase date
Daily Mark-to-Market	Whether to choose the KSD's daily mark-to-market process	Yes or No
Threshold	To specify the ratio or amount of exemption from the obligation to maintain the margin (threshold)	Margin Amount or Ratio
Margin Ratio	Enter the agreed margin ratio, if any. If a margin ratio is not specified, the margin ratio is calculated by dividing the purchased securities' market value on the start-leg settlement date by the purchase price and the ratio is automatically entered into the KSD's repo system.	
Fund Information	If the sellers or buyers or both parties are asset management companies, fund information is needed	

BOK = Bank of Korea, DVP = delivery versus payment, FOP = free of payment, KSD = Korea Securities Depository.
Source: KSD.

ii. Trade Matching

If there is no discrepancy between the details of the repo trade agreed by buyers and sellers, repo sellers or buyers who are notified of the details of the repo trade shall confirm the details of the repo trade. Upon completion of confirmation, KSD shall finalize the settlement statement by allocating a repo reference number to each transaction.

e. Settlement of Repo Trade

i. Start-Leg Settlement

Settlement of repo transactions is done by book-entry transfer from the seller's securities account to the buyer's securities account. Settlement of cash is done via KSD's the account with BOK or an account with a commercial bank.

Delivery-versus-payment occurs through a direct link between KSD's securities settlement system and BOK-Wire. This allows real time and simultaneous settlement on a gross, trade-by-trade basis for start-leg settlement. If the details of the repo trade are matched, the KSD repo system checks for sufficient holdings of securities in the seller's securities account. If securities are sufficient, KSD then locks the required securities amount to prevent it from being used for other purposes, and instructs the buyer to transfer the funds via BOK. Upon the buyer's payment, the settlement of the purchased securities is concluded.

If trade parties use the free-of-payment method, payment for the start-leg settlement should be made by agreed means, and the seller needs to notify KSD that payment has been made. Upon such notice by the seller, the settlement of the purchased securities is completed.

ii. Close-Leg Settlement

In cases where the repurchase date is designated at the time of concluding a repo trade, one party may, at any time, ask KSD for the termination of the repo transaction with the consent of the other party, even before the repurchase date. In cases where there is no designated repurchase date, and unless otherwise agreed upon by the parties of the repo transaction, both parties shall request for the termination of the repo transaction, provided that such request is made at least 3 business days, including setting the desired repurchase date, in advance.

In case of an event that causes the default of a contractual obligation of a seller or buyer, the repurchase date for the relevant repo transaction shall be deemed to have been prematurely arrived. KSD shall notify the relevant participants of such a fact and terminate the repo transaction. Either delivery-versus-payment or free-of-payment method can be used for the close-leg settlement.

f. Trade Management

i. Rollover

Counterparties may apply for a rollover of the repo trade on the termination date. In this case, the existing transactions are terminated on the day when such an adjustment is made, and the parties engage in a new transaction. The settlement may be completed by making payment of the repo interest. The original trade conditions, other than the termination date, would also apply to the new transaction.

ii. Substitution of Purchased Securities

The seller in a repo transaction may substitute the purchased securities, in whole or part, for other securities with the consent of the buyer. Meanwhile, in case the redemption of purchased securities is scheduled or in case depreciation of the purchased securities' market value is expected due to insolvency, bankruptcy, commencement of rehabilitation processing, or other reasons on the part of the issuer of the purchased securities, the buyer can request the exchange of purchased securities with other securities. The seller should comply with such a request.

iii. Change in Repo Trade Conditions

Counterparties may change part of the trading conditions, if necessary. In this case, the new conditions will apply only to the changed part and all other terms and conditions will remain intact.

g. Mark-to-Market

To minimize market risk, KSD carries out MTM valuations of securities under repo on a daily basis since the value of the purchased securities as collateral must be monitored on a daily basis to ensure that it does not drop below a certain range. To absorb typical small price fluctuations in the securities, a margin payment is agreed as part of the repo trade. MTM and margin payments allow sellers and buyers to minimize exposure to price fluctuations and enhance the stability of the repo trade. When the repo transaction is terminated, the KSD repo system returns any margin involved in the transaction to each paying party.

KSD shall conduct MTM on a daily basis in the following order:

i. calculation of the required collateral value,
ii. calculation of the transaction exposure,
iii. calculation of the net margin, and
iv. calculation of the amount of the net exposure.

After conducting daily MTM, KSD shall notify repo sellers and buyers of the result of the MTM no later than 10:30 a.m. The party incurring the net exposure shall pay a margin in cash or securities with the consent of the other party. The amount of margin equals to the amount of net exposure to the other party. The margin transfer must be fulfilled no later than 2:00 p.m. on the notified date.

h. Income Payment Management

Although legal title to the purchased securities passes to the buyer in a repo trade, economic costs and benefits of the purchased securities remain with the seller. Therefore, if a coupon is paid, it will be paid to the seller on the coupon value date. KSD assists the buyer’s interest payment process to ensure convenience for repo sellers and buyers.

The method of interest payment varies depending on whether the purchased securities are held in the repo account of the buyer. If the buyer holds the purchased securities in its repo account, KSD’s repo system will directly pay the interest to the seller on the relevant interest payment date.

On the other hand, if the buyer transferred the purchased securities from its repo account to a third party, the buyer should pay the interest to the seller on the interest payment date through the KSD.

3. Repo Market of Korea Exchange

Market participants in KRX Repo are financial investment firms and government bond dealers; at the time of compilation of this Bond Market Guide, 58 institutions were participating in KRX Repo, including 35 financial investment firms, 21 banks, KSFC, and BOK. To ensure a stable market, tradable issues are limited to KTBs, MSBs, Korea Deposit Insurance Fund Bonds, and blue-chip corporate bonds.

KRX Repo is different from the OTC repo market in that trading conditions in the market are standardized; the exchange, as a central counterparty, guarantees settlement and provides integrated services, covering quotation searching, trade execution, clearing and settlement, and trade reporting.

Trading and settlement rules and regulations of KRX Repo were designed to suit the CLOB in the exchange market, based on the Global Master Repurchase Agreement as the international standard.

a. Trading Regulations

KRX Repo allows the use of E-RFQ through connected screens, as well as trade reporting, on the basis of CLOB. This section explains trading regulations of CLOB while Section D will describe E-RFQ and trade reporting.

i. Market Participants and Trade Counterparties

Market participants of KRX Repo are the same as in KRX KTB. KRX keeps trade counterparties anonymous (referred to as no name give-up), so as to not expose the position risks of each trading party. These risks are managed by KRX.

Documentation for all trades are managed by each counterparty. When a settlement default occurs, KRX takes responsibility for the completion of settlement as a central counterparty to the seller and buyer.

ii. Eligible Bonds

Securities traded by repo can be bonds, stocks, commercial paper, certificates of deposit, and MSBs, but repo transactions in the KRX market are limited to certain bonds listed in Table 4.4. Eligible bonds are limited to those with low risk, ample liquidity, and a broad investor base.

Table 4.4: Bonds Eligible for Trading in KRX Repo

Classification	Bond	Requirements
Government bonds (GA)	Treasury bonds Foreign exchange fund bonds	Outstanding amount of more than KRW200 billion vanilla bond
MSB and KDIC (SA)	Monetary Stabilization Bonds KDIC fund bonds	
Others (CA)	Corporate bonds Special bonds	Requirements above plus an issuer of bonds and/or a guarantee agency with credit rating over AA–

KDIC = Korea Deposit Insurance Corporation.
Source: Korea Exchange.

iii. Trading Term and Repurchase Date

Most of the repo transactions have a term of less than 1 year. There are 10 standardized repo terms: overnight, 2 days, 3 days, 4 days, 7 days, 14 days, 21 days, 30 days, 60 days, and 90 days. The repurchase date is the 2nd day, 3rd day, 4th day, 5th day, 8th day, 15th day, 22nd day, 31st day, 61st day, and 91st day, respectively, counting from the day on which the purchase price is settled. (When the purchase date is a trading holiday, the repurchase is postponed to the next business day.)

iv. Quotation Receipt and Aggregation

In a KRX repo trade, bid quotations are allowed to be submitted regardless of the type of issue if the bonds that serve as collateral are deemed to have a certain level of comparability to other issues. KRX refers to these as “general quotations” (quotations for unspecified issues).

In KRX Repo, KRX captures quotations by repo type to generate bid quotations for unspecified issues. The repo type indicates a combination of the classification of bonds (eligible bonds with the same risk level) and trade period. Currently, there are 30 Same-Type-Quotation-Aggregation Tables, consisting of three classifications of bonds and ten trade periods (Table 4.5). This is based on the notion that same repo rates can be established within a Same-Type-Quotation-Aggregation Table if other conditions are the same.

Table 4.5: Quotation Aggregation by Bond Classification

Classification of bond	Eligible bond	Aggregation
Government bonds (GA)	Treasury bonds Foreign exchange fund bonds	10 types of GA (overnight–90 days)
MSB and KDIC (SA)	Monetary Stabilization Bonds KDIC fund bonds	10 types of SA (overnight–90 days)
Others (CA)	Corporate bonds Special bonds	10 types of CA (overnight–90 days)

KDIC = Korea Deposit Insurance Corporation.
Source: Korea Exchange.

Then, quotations are recorded in the table in the order of receipt by bid–ask and price (repo rate), and a trade is executed within the range of the table. Since quotations within the table compete with each other, ask quotations compete with bid quotations for unspecified issues if different bonds fall into the same category. Quotations should be submitted during regular trading hours from 9 a.m. to 3:30 p.m.

v. Unit of Quotation and Trading Quantity

KRX Repo has adopted the securities-based quotation rule, in which the amount of bonds to be traded is determined first and then the amount of payment is determined accordingly. The unit of quotation and trading is an integer multiple of the face value of the bond, at KRW1 billion. The tick size is indicated as a repo rate with two decimal places (1 basis point) per KRW10,000 trade value. The repo rate indicates the annual interest rate for the trade value, not the bond face value (Figure 4.6).

Table 4.6: Quotation and Trading Unit

Classification	Detail
Type of quotation	Securities-based quotation
Quotation quantity unit	Trading value of KRW10,000
Quotation price unit	Repo rate with two decimals
Trading quantity unit	Face value of KRW1 billion

Source: Korea Exchange.

vi. Execution of Trading Contract

The bid quotations for the specified issue in the Same-Type-Quotation-Aggregation Table compete with ask quotations for the same issue while bid quotations for an unspecified issue (general quotations) compete with ask quotations for all issues. The trade is executed in CLOB by the type in the Same-Type-Quotation-Aggregation Table (Figure 4.7).

Table 4.7: Central Limit Order Book

Principle	Detail
Price priority	A higher ask quotation price for a repo rate takes priority for trade execution over a lower one, while a lower bid quotation price for a repo rate takes priority over a higher one.
Time priority	A quotation received earlier for the same repo rate takes priority for trade execution over one received later.
Price determination	Trading is executed when the highest ask quotation price and the lowest bid quotation price are matched.

Source: Korea Exchange.

The trade value is calculated based on the formula below, with the result being an integer number

Trading amount = traded bonds (total face value) x market value/10,000 ÷ (1 + haircut rate).

The market value indicates the value of the bonds calculated on the basis of every KRW10,000 of the bond par value, and is set based on the price announced by a rating institution specializing in bond price evaluation. The repurchase amount that the seller pays to the buyer is calculated as follows:

Repurchase amount = traded amount x (1+repo rate x repo transaction period/365).

b. Termination of Repo Trade and Settlement

i. Termination of Repo Trade

A repo trade terminates on the repurchasing date stipulated in the contract. However, KRX may execute a repurchasing earlier than scheduled, for the stability of the repo trade, under certain circumstances (Table 4.8). If the cause for early repurchasing stems from the bonds of the contract, only the corresponding contract terminates. When the cause arises from a trade counterparty, all agreements of non-repurchasing associated with the counterparty terminate. In the case of an early repurchasing, the repurchase date is the day when the cause occurs.

Table 4.8: Cause for Termination of Repo Trade and Repurchasing

Cause for Termination	Repurchasing Way	Classification of Repurchasing
- Repurchase date is due	Repurchasing the individual contract	Scheduled repurchasing
- The seller does not agree on an exchange - De-listing of the bonds or early payment - A case where termination of a repo trade is deemed necessary	Repurchasing the individual contract	Early repurchasing
- Default of the seller (buyer) - A cause for a bond exchange occurs to the seller (buyer)	Repurchasing all contract as a single agreement	

Source: Korea Exchange.

ii. Settlement in the Repo Market

KRX guarantees the settlement of a repo trade as a clearing agency, pursuant to provisions in the FSCMA, thus assuming the role of a central counterparty to seller and buyer. As a triparty agent, KRX provides each counterparty with buy-back services for an agreement of non-repurchase until the original repo contract terminates. As a result, market participants may participate in the repo market without concerns about risks of default.

KRX has adopted settlement by netting, which combines settlement for daily trading, settlement for repurchasing, and additional margin and netting by market participant. KRX conducts settlement on a delivery-versus-payment basis.

c. E-RFQ and Trade Reporting

iii. E-RFQ in the Repo Market

Similar to KRX KTB and KRX BondsAll, a trade in KRX Repo can be conducted at a repo interest rate predetermined by consultation between a quotation requester and quotation proposer. The quotation requester may designate a maximum of five quotation proposers to request a quotation, and the quotation stays effective for 30 minutes. What is different from KRX KTB and BondsAll is that the trade period may be within 365 days (including trading holidays) and the trading unit is set at a trade value of KRW100 million.

iv. Trading Report in the Repo Market

When market participants agree on a repo trade and report to KRX, it is deemed exchange-traded. Counterparties may determine trading unit, repo term, repo rate, and other conditions on a discretionary basis, and report to KRX. However, the trade period should be no more than 360 days.

I. Securities Lending and Borrowing

SLB is an active part of the Korean bond market. When involving debt securities, this transaction type is referred to as bond lending and borrowing.[32]

1. Market Participants

Bond lending and borrowing market participants comprise lenders, borrowers, and intermediaries. Major lenders are pension funds, asset management companies, banks, insurance companies, and securities companies. The borrowers are those who are in need of borrowed securities for any number of reasons. Major borrowers are securities companies, hedge funds, and asset management companies.

Major intermediaries are KSD, investment brokerage companies, and KSFC.

2. Characteristics of Bond Lending and Borrowing in the Republic of Korea

a. Bond Lending and Borrowing a "Consumption Loan" under the Civil Code

In an SLB transaction, the lender lends bonds to the borrower, thereby transferring title of such bonds to the borrower. After a certain period of time, the borrower must return to the lender the same type and number of bonds as the loaned securities. As a result, SLB transactions have the characteristics of "consumption loans," as defined under the Civil Code.

b. Collateralization

The borrower must provide to the lender collateral that corresponds to the value of the loaned bonds. The loaning of the bonds and provision of collateral must occur simultaneously.

c. Transaction Term

The term for SLB transactions is negotiated between lender and borrower (excluding for settlement transactions which have a fixed term of 3 business days). In practice, most transactions have a term of 1 year from the date of execution of contract. However, any transaction may be unilaterally terminated by any party at any time without penalty.

3. Eligible Debt Securities

Eligible debt securities for bond lending and borrowing differ between intermediaries such as KSD, KSFC, and investment brokerage companies. Those eligible under KSD regulations are listed debt securities with the exception of option-embedded bonds.

[32] This business is variously called securities lending and borrowing or securities borrowing and lending, depending on the use by individual institutions in the Korean market; both forms are used in international practice. For the Korea Bond Market Guide, the term securities lending and borrowing was adopted, as used by KSD, since its SLB platform is considered the most active.

J. Interest Rate and Fixed-Income Futures

1. Korea Treasury Bond Futures

A KTB futures contract is a forward contract to transfer a specific amount of KTBs (underlying asset) traded in an organized market (KRX) at a predetermined price at a specific time in the future (maturity).

a. Korea Treasury Bond Futures on KRX

The Government of the Republic of Korea introduced 3-year KTB futures in 1999 to establish means to hedge against risks arising from the expansion of its bond issuance. It subsequently introduced 5-year KTB futures (2003) and 10-year KTB futures (2008), which have since been traded on KRX.

b. Trading of Korea Treasury Bond Futures

It is difficult to standardize trading conditions of bond futures contracts compared to other futures contracts since trading conditions, such as the time to maturity, coupon rates, and interest payment methods, are diverse. Therefore, a standardized virtual bond is used as the underlying asset with a standardized face value, duration to maturity, and coupon rate.

i. 5-Year and 10-Year Korea Treasury Bond Futures

A 5-year KTB futures contract takes 5-year virtual Treasury bonds as an underlying asset, with a coupon rate of 5% and interest payments every 6 months. A 10-year KTB futures contract takes 10-year virtual Treasury bonds as an underlying asset, with the same conditions. 5-year KTB futures are almost the same as 3-year and 10-year KTB futures, except that the underlying asset is 5-year standardized bonds; the final settlement price is calculated based on the formula $\sum_{i=1}^{10} \frac{5/2}{(1+r/2)^i} + \frac{100}{(1+r/2)^{10}}$; and the price limit is base price $\pm$(base price x 1.8%). 10-year KTB futures contracts take 10-year standardized bonds as an underlying asset, and the final settlement price is calculated according to the formula $\sum_{i=1}^{20} \frac{5/2}{(1+r/2)^i} + \frac{100}{(1+r/2)^{20}}$. The price limit is base price $\pm$ (base price x 2.7%).

ii. 3-Year Korea Treasury Bond Futures

A 3-year KTB futures contract has 3-year KTBs as the underlying asset. The KRX contract assumes a virtual Treasury bond with a coupon rate of 5%, a maturity of 3 years, and coupon payments every 6 months. Details on the 3-year KTB futures contract are shown in Table 4.9.

Table 4.9: Contract Details for 3-Year Korea Treasury Bond Futures

Classification	Details
Underlying asset	3-year KTB with 5% coupon rate and semiannual coupon payment
Contract size	KRW100 million
Contract months	The first 2 consecutive months in the quarterly cycle (March, June, September, and December)
Price indication	Indicated based on the face value of KRW100 (marking to the second figure after the decimal point, (e.g., 105.69, 105.85)
Tick size	0.01 point
Tick value	Value of 1 tick = face value KRW100 million x 0.01 x 1/100 = KRW10,000
Price limit	Base price ±(base price x 1.5%) (e.g., When the base price of the day is 105.69, the upper limit is 104.10 and the lower limit is 107.28.)
Position limit (limit of open interest)	None. However, KRX may limit open interest when it deems necessary.
Trading hours	9 a.m.~3:45 p.m. (9 a.m.~11:30 a.m. on the last trading day)
Last trading day	Third Tuesday of the settlement month
Final settlement day	The following trading day after the last trading day
Final settlement method	Cash settlement
Futures basket	Treasury bonds with interest payments every 6 months, designated by KRX on the trading day immediately preceding the trade beginning date in the corresponding settlement month
Final settlement price	The figure calculated according to the formula as follows (rounding the number to two decimal places): - Final settlement price = $\sum_{i=1}^{6} \frac{5/2}{(1+r/2)^i} + \frac{100}{(1+r/2)^6}$ - "r" is the yield of futures basket divided by 100 - The final settlement yield is the arithmetic mean of the mid-yield excluding the highest and the lowest yield among yields at 10:00 a.m., 10:30 a.m., and 11:00 a.m., and the yield at 11:30 a.m. on the last trading day. - The yield of each time point is the yield of futures basket announced by the Korea Financial Investment Association. However, if there are multiple futures baskets, the yield is the figure calculated by averaging the yields of each futures basket and rounding to three decimal places.

KRW = Korean won, KRX = Korea Exchange, KTB = Korea Treasury Bond.
Source: Korea Exchange.

V

Description of the Securities Settlement System

This chapter, as included in the original ASEAN+3 Bond Market Guide published in 2012 has been discontinued in favor of a more comprehensive and updated description in the Phase 2 Report of the ABMF Sub-Forum 2 (SF2), *Information on Transaction Flows and Settlement Infrastructures*, dated 13 June 2014. The SF2 Phase 2 Report contains information on the post-trade features of the Korean bond market, its market infrastructure and settlement systems, interest payment and redemption practices, as well as market and message standards (pp. 166–185). In addition, the SF2 Phase 2 Report contains detailed infrastructure and transaction flow diagrams for the bond market in the Republic of Korea (pp. 464–490).

The SF2 report is available on a dedicated ADB website, as well as through a number of mirror sites.[33]

[33] See http://www.adb.org/publications/asean3-information-transaction-flows-and-settlement-infrastructures

VI

Bond Market Costs and Taxation

This chapter details the typical costs incurred by issuers and investors in the Korean bond market, with a particular emphasis on costs associated with bond or note issuance and settlement.

For ease of reference, the descriptions of the types of costs are given in the context of the actions to be taken by issuers or investors (as explained in this document) and follow the lifecycle of a bond or note in the Korean bond market.

A. Costs Associated with Bond and Note Issuance

1. Application for Issuance via Public Offer (Mandatory)

Issuers intending to offer bonds or notes via a public offering need to file an SRS with the FSS. For the process of SRS submission and review, the FSS levies a fee on the issuer, referred to as allocated contribution. The rate of allocated contributions is determined by the FSC, pursuant to Article 388 in the Enforcement Decree of FSCMA (Table 6.1). The fee is payable at the time the SRS is submitted to the FSS.

Table 6.1: Allocated Contributions for Submission of Securities Registration Statement

Condition	Fee rate
Maturity ≤ 1 year	0.05% of total issue value
1 year < Maturity ≤ 2 years	0.06% of total issue value
2 years < Maturity	0.07% of total issue value

Source: Financial Supervisory Service.

2. Registration of Bonds in the Over-the-Counter Market

KOFIA administers the OTC market in the Republic of Korea. Bonds and notes to be traded on K-Bond need not be registered with KOFIA by default. Only bonds and notes issued by private placement to be traded among QIBs (QIB-eligible securities) are required to be registered with KOFIA.

At present, KOFIA does not charge a fee for the registration of bonds and notes in the QIB Market.

3. Managing Company Fee

The appointment of a managing company in the Korean bond market is not mandatory. The managing company is, among other roles, responsible for the submission of issuance applications, issuance documentation and disclosure items, and supporting information to the relevant regulatory authorities.

The managing company and underwriters will charge a fee, which should be expected to follow established market practice and may be subject to negotiations between the issuer and the managing company and underwriters. Under current market practice, KRW20~KRW25 per KRW10,000 face value of the bonds or notes is charged as the total fee. Of the total fee charged, a portion of about KRW5 per KRW10,000 face value (or about 20%–25%) is distributed to the managing company. The share of a managing company tends to increase with the introduction of a book-building system.

4. Underwriter Fee

Issuers are not required by law to appoint one or more underwriter(s) in the Republic of Korea; often, the managing company performs the role of underwriter as well. However, some offers of bonds and notes may require the services of one or more underwriters to place the debt securities with institutional investors or distribute the issuance to the public.

Underwriters charge a fee, typically commensurate with the effort and risk of taking over parts or all of a bond or note issue from the issuer. This fee or service charge is charged to the issuers as part of the total cost billed by the managing company, and should be expected to follow established market practice and may be subject to negotiations between issuer and underwriter(s). After the share due to the managing company, the remaining fee amount (about KRW15–KRW20 per KRW10,000 face value) is distributed to the underwriters proportional to the amount of the bonds or notes underwritten by each underwriter.

5. Agent Fees

The appointment of a number of agents in the context of a bond or note issuance is mandated to ensure effective and professional administration of the issue, a division of duties, and the observance of international best practice. The managing company will administer the issuance process of debt instruments into the market, while a paying agent is responsible for handling the cash flow at issuance and for benefits arising from the issue and upon redemption. The indenture trustee holds the fiduciary responsibility toward the bond- or note-holders, and acts in the case of default or distress.

The paying agent and the indenture trustee are also remunerated for their services based on market practice. The standard contract for an indenture trustee for non-guaranteed corporate bonds stipulates that the fee for, and costs incurred by, the indenture trustee are paid by the issuing company.

6. Korea Securities Depository Registration Fees

KSD charges a registration fee for the creation of new debt securities in its book-entry system, as shown in Table 6.2. The fees differ between the debt securities issued by resident and nonresident issuers, and have a maximum amount.

Table 6.2: Debt Securities Registration Fee at Korea Securities Depository

Classification	Fee Rate
Domestic entity issuing bonds	• KRW10 billion and less: KRW100,000 • KRW10 billion and more: Registration amount x 1/100,000 (ceiling: KRW500,000)
Foreign entity issuing bonds	• KRW10 billion and less: KRW500,000 • KRW10 billion and more: Registration amount x 5/100,000 (ceiling: KRW10,000,000)

Source: Korea Securities Depository.

Information on the public and corporate debt securities registration fee and fee levels is available in the fee schedule published on the KSD website (presently only in Korean).[34]

B. Listing Fees

In the Republic of Korea, only bonds and notes issued via a public offering may be listed on KRX. A listing is optional. If an issuer decides to list its debt securities, KRX applies the following fees to such listings. Listing fees are paid when the listing request is made, but for shelf-listed bonds, fees are paid when the results of the issuance are announced.

1. Listing Review Fee

KRX requires prospective issuers—both resident and nonresident—to submit to a listing eligibility review prior to actual listing. If a listing is intended for a public offer, the issuer should include the results of a listing eligibility review in its SRS to be filed with the FSC.

KRX charges a listing review fee of between KRW100,000 and KRW1.7 million for the review of the issuer's, as well as a bond's or note's, listing eligibility, depending on the size of the issue. The fee is not refundable in case of an unsuccessful application. KRX does not charge for the listing eligibility consultation for a foreign issuer.

2. Annual Listing Fee [or another continuous fee, as applicable]

KRX also levies an annual listing fee, fixed at KRW100,000, payable for the first 5 years or depending on the maturity of the debt securities, whichever comes first. If a bond has a maturity beyond 5 years, the issuer will pay a maximum of KRW500,000 in annual listing fees.

The current listing fee schedule is available from the KRX website.[35]

C. Ongoing Costs for Issuers of Corporate Bonds and Notes

Once an issuer has issued bonds or notes in the Korean market, regardless of whether those are listed, and whether they are traded in the OTC market or on exchange, a number of recurring costs may apply throughout the lifecycle of the bonds

[34] See http://www.ksd.or.kr/static/KB1200000000.home?menuNo=84
[35] See http://global.krx.co.kr/contents/GLB/03/0303/0303080400/GLB0303080400.jsp

or notes. These recurring costs may be charged by agents or service providers appointed by the issuer, such as a paying agent or an indenture trustee.

1. Paying Agent Fees [as applicable]

Corporate bond issuers may appoint a paying agent, who will remit principal and interest payments to KSD for further distribution. The paying agent is expected to charge a fee commensurate with the role and in line with market practice.

KSD distributes principal and interest payments for the corporate bonds and notes deposited in its book-entry system to its participants who, in turn, onward distribute the payments to their clients. At the time of compilation of this Bond Market Guide, KSD did not charge the issuer for the provision of interest payments or redemption processing.

2. Indenture Trustee [as applicable]

The issuer of corporate bonds offered or sold to the public shall appoint an indenture trustee. The indenture trustee will charge a fee commensurate with the expectations of its function, which is expected to follow market practice.

D. Costs for Deposit and Withdrawal of Bonds and Notes

The Korean market is considered immobilized. Securities continue to coexist with securities created and kept as book-entry records only. In the event that an investor or their agent, as KSD participant, wishes to deposit physical securities certificates into an account with KSD, a deposit fee is applicable (Table 6.3).

Likewise, should an investor or KSD participant choose to withdraw securities from their account with KSD in the form of physical certificates, KSD would charge a withdrawal fee.

1. Deposit Fee

The deposit fee policy was amended in January 2010 to compensate for the costs incurred by KSD in executing its deposit-related operations, which grew in proportion with the increasing deposit balance of a particular security.

Table 6.3: Deposit Fee at Korea Securities Depository

Range	Fee Rate per KRW 10,000 Face Value
KRW1 trillion and less	KRW0.00125
More than KRW1 trillion up to KRW3 trillion	KRW125,000 + KRW0.001
More than KRW3 trillion	KRW325,000 + KRW0.00075

Source: Korea Securities Depository.

For registered bonds that do not exist in physical form, KSD applies a discount rate of 50%.

2. Withdrawal Fee

There is no withdrawal fee. KSD now only accepts bonds in registered form without physical certificates, with the exception of National Housing Bond Type 2.

E. Costs for Account Maintenance and Safekeeping at Korea Securities Depository

KSD does not impose an account maintenance fee on its participants. Participants are charged either the deposit fee or the securities company fee.

F. Costs Associated with Bond and Note Trading

Bonds and notes issued in the Korean market may be traded in the OTC market or, for publicly offered debt securities only, listed and traded on KRX. The fees applicable to a debt securities transaction differ between these two trading options, as further explained in this section.

1. Exchange Trades

Investors carry out transactions in debt securities on the exchange by submitting an order to, or via, investment brokerage companies, which are members of KRX.

a. Brokerage Fee (investor pays to securities firm)

A securities firm may levy brokerage fees on investors for a trade in bonds or notes on the KRX market. When fee levels and methods are determined or changed, this should be notified to KRX within 5 business days. Securities firms apply their own fee levels, but they determine the levels corresponding to the remaining time to maturity of bonds traded.

b. Trading Fee (securities firm pays to Korea Exchange)

KRX may levy a trading fee on a securities firm when the firm conducts principal trading on its own account or executes trading orders received from investors for the KRX market. A trading fee is determined by multiplying the traded amount by the fee level; the trading fee for KRX KTB is KRW10,940 per trade amount up to a value of KRW10 billion.

c. Clearing and Settlement Fee (securities firm pays to Korea Exchange)

KRX also levies a clearing and settlement fee since every order placed within the KRX market needs to be processed via the clearing and settlement system of KRX. The clearing and settlement fee for KRX KTB is KRW1,710 per trade amount up to a value of KRW10 billion.

The securities firm may decide to defray its costs incurred for an exchange trade by including it into the securities price or its own fee, or bill these fees to the investor as out-of-pocket expenses.

2. Over-the-Counter Trades

Market participants trading debt securities for their investor clients in the OTC market may charge a brokerage fee or levy other such charges for each trade, subject to their own conditions and considerations.

Such brokerage fees in OTC trading are determined by each broker company. Typical brokerage fee rates are set as follows: for bonds or notes with residual time to maturity of less than 1 year, the fee is set at around KRW0.5 per KRW10,000 face value; for bonds and notes with residual time to maturity of 1 year or more, the fee is set at around KRW1 per KRW10,000 face value.

G. Costs for Settlement and Transfer of Bonds and Notes

To defray its cost of settlement and depository operations, KSD levies a settlement fee and a book-transfer fee for transactions instructed by its participants. The fees are levied on a transaction basis and billed to the KSD participant on a monthly basis, payable by the 20th day of the following month.

1. Settlement Fee

KSD applies a settlement fee for bonds and notes that are transacted in the OTC market as well as on the exchange. The fee is charged at 0.001646 basis points on the total transacted amount.

2. Book-Transfer Fee

KSD also charges a fee for conducting the book transfer activities, being one of the major cost centers that require great amount of resources. As a result, KSD charges a transfer fee (official name: book-transfer fee) of KRW1,000 to the transferor of a given transaction.

There are exceptions to this rule however. Book-entry transfers that are made upon request from the transferor who wishes to use services offered by KSD such as securities borrowing and lending and repo are exempt from book-transfer fee obligations.

H. Taxation Framework and Requirements

The tax authority in the Republic of Korea is the National Tax Service. The provisions for the taxation of income and capital gains from debt securities are contained in the Income Tax Act and the Corporate Tax Act, for individual and institutional investors, respectively. Nonresidents are also subject to income tax in the same manner as residents. However, individuals or corporates resident in any country that has a tax treaty with Korea are taxed on their income in accordance with the relevant tax treaty.

Table 6.4 provides an overview of the taxes relevant for investments in the bond market in the Republic of Korea and their applicable rates, with relevant details explained in the subsequent sections.

For their individual tax treatment and the applicability of double taxation treaties, entities investing or wanting to invest in the Korean bond market are encouraged to seek tax advice from a professional firm.

Table 6.4: Duties and Taxes on Fixed-Income Securities in the Republic of Korea

Duties and Tax	Type of Bonds	Tax Rate
Corporate Income Tax	Government	10%–22%[a]
	Corporate	10%–22%[a]
Withholding Tax	Government	15.4%[b]
	Corporate	15.4%[b]
Capital Gains Tax	Government	10% or 22%[c]
	Corporate	10% or 22%[c]
Stamp Duty	N.A.	N.A.
VAT	N.A.	10%

N.A. = not applicable, VAT = value-added tax.
[a] Depending on tax base of individual corporation.
[b] 15.4% applicable for government bonds and domestic corporate bonds, which constitute almost all debt securities issued in the Korean bond market.
[c] 10% of gross proceeds from sale, or 22% from net capital gains, whichever is lower.
Source: Clearstream, KPMG.

1. Corporate Income Tax

The corporate income tax in the Republic of Korea ranges from 10% to 22%, depending on the amount of the tax base (assessable income). Other related taxes may be levied in individual years of assessment.

A corporation is considered to reside in the Republic of Korea if the corporation has its head or main office, or place of effective management, in the country. A resident corporation is liable in the Republic of Korea for corporate income tax on its worldwide income. Resident corporations include the subsidiaries of foreign corporations, but not their branches.

A nonresident corporation is liable for corporate income tax on income from Korean sources only.[36]

The Corporate Tax Act stipulates that corporate tax shall be imposed on all income of a company for each business year, including interest income and capital gains from bonds and notes. In the case of interest income from bonds, the tax must be withheld at the time the income is generated. The amount of tax withheld shall be deemed to be prepaid as corporate tax and, thus, is deducted in computing and levying the corporate tax.

2. Taxable Income

According to the Income Tax Act, interest and discount amounts are considered taxable interest income.

[36] This and other relevant information was adapted by SF1 consultants from KPMG. 2015. *Korea Tax Profile*. https://home.kpmg.com/content/dam/kpmg/pdf/2015/10/korea-2015.pdf

The taxable discount amount stipulated in the Income Tax Act only refers to the issuance discount (the amount according to the market interest rate at the point of bond issuance), not the market discount (the amount according to the market interest rate at the point of early bond redemption). Persons redeeming their bonds before maturity only have to pay tax on the amount of interest accrued during the possession of the bonds.

To help promote and develop the government bond market, exemptions exist for (i) government bonds, (ii) industrial finance bonds, (iii) deposit protection fund bonds and compensation fund bonds for deposit protection fund bonds, and (iv) MSBs issued by BOK in the open market. In these cases, only the amount of interest accrued by the coupon rate exclusive of the discount amount is considered to be taxable interest income, pursuant to Article 22-2 (2) of the Enforcement Decree of the Income Tax Act.

Under normal circumstances, persons transferring their bonds to another person before maturity could accrue capital gains due to the difference between the interest rate at the point of bond issuance and at the point of the transfer. But the Republic of Korea's taxation law does not levy tax on capital gains accrued from the transfer of bonds. When calculating taxable income, the amount of interest income shall be included in the total gross income accrued during the corresponding year, pursuant to Article 16 (2) and Article 17 (3) of the Income Tax Act.

As a result, expenses incurred by an investor during the disposal or sale of securities are not recognized as tax-deductible expenses.

3. Receipt Date of Income

The date of receipt of income in the form of bond interest shall be the date of receipt of such payments for interest and discount amounts in the case of bearer public bonds, and the payment date under the agreement for interest and discount amount in the case of non-bearer public bonds, according to Article 45 (2) (3) of the Enforcement Decree of the Income Tax Act. The receipt date of income accrued from coupon interest shall be the date of the coupon. As for the discount, the receipt date of income shall be the date of the maturity, which is the receipt date of such payment.

In the case of the sale of bonds before maturity, the receipt date of income from interest shall be the sale date of the relevant bonds. Therefore, when discount bonds are sold before maturity, the receipt date of income from the sale of the relevant bonds shall be the sale date, and if the bonds were redeemed at maturity, the date of redemption at maturity shall be the date of income from such payment according to Article 45 (10) of the Enforcement Decree of the Income Tax Act.

In contrast, in the case of commercial notes or cover notes (discounted notes) with short maturity terms traded using a passbook held in custody, the receipt date of income shall be the date of the sale of the notes at a discount, if the owner of the notes decides to pay the withholding tax on the same day. Consequently, such bonds are referred to as prepaid interest bonds.

4. Withholding Tax

Interest paid to a nonresident is subject to a withholding tax of 15.4% for interest on bonds issued by the Government of the Republic of Korea, a local government, or a domestic corporation, unless the withholding tax rate can be reduced under a tax treaty.

5. Capital Gains Tax

The capital gains and losses of a resident corporation are included in its taxable income and taxed at the standard corporate income tax rates.

Generally, nonresidents of the Republic of Korea are liable for capital gains tax on domestic securities at the lower of the following rates:

- 11% of the gross proceeds realized from the sale (including the 10% surtax), or
- 22% of the net capital gains (including the 10% surtax).

Residents of countries that have concluded a Double Taxation Treaty with the Republic of Korea, or countries with reciprocity rules, will either be exempted or taxed depending on the Double Taxation Treaty.

The selling broker is responsible for the calculation and withholding of the capital gains tax and for its payment to the National Tax Service.[37]

6. Stamp Duty

There is no stamp duty withheld on transactions in securities held with custodians. A stamp duty may, however, be payable on specific transactions, typically related to direct investment.

7. Value-Added Tax

The standard rate of VAT is 10%.

8. Double Taxation Treaty

As of 2017, the Republic of Korea had signed treaties for the avoidance of double taxation with 92 countries, including most of the ASEAN+3 countries.

The provisions of an applicable tax treaty shall preferentially apply to the classification of domestically sourced income of a nonresident or foreign corporation, notwithstanding the provisions in the Income Tax Act and the Corporate Tax Act, respectively.

Article 29 of the Adjustment of International Taxes Act prescribes that the lower of the limited tax rate provided by a tax treaty or any of the tax rates in the Income Tax Act or Corporate Tax Act shall apply to interest that constitute the domestically sourced income of a nonresident or foreign corporation under the tax treaty.

9. Tax Exemption for Nonresident Investors

The Republic of Korea had previously exempted nonresident investors from withholding tax on interest income earned from investment in KTBs and MSBs. The exemption, however, was abolished in 2011. Currently, nonresident investors may avail themselves of tax relief under applicable tax treaties.

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[37] This and other relevant information was adapted by SF1 consultants from Clearstream Luxembourg. *Market Taxation Guide 2018*.

10. Tax Treatment of Investment Funds

Investment funds are subject to a specific treatment under the Corporate Income Tax Law. The provisions focus on the legal beneficiary level. While the IRC is set at the fund level, the tax form submission requires disclosure of the holding shares of the various domiciles of the fund holders. Thereafter, a blended tax rate is formed according to the relevant double taxation treaties for the domiciles declared. This practice only applies to funds or investment vehicles with more than 100 beneficial owners. In case a fund or investment vehicle has fewer than 100 beneficial owners, the details of each investor must be submitted. The necessary information is collected and submitted to the tax authorities by the custodian, as the standing proxy of the investor, here being the fund or investment vehicle.

VII

Market Size and Statistics

The original ASEAN+3 Bond Market Guide was published in April 2012 and included several pages of Korean bond market statistics, including historical data such as bond holdings, bondholder distribution, outstanding amounts, and trading volumes. Not surprisingly, this data became stale soon after publication.

Since the ASEAN+3 Bond Market Guide is most likely to be updated only on a biennial basis, it is not the best channel for the dissemination of market statistics. Hence, a chapter comprising bond market statistics has been discontinued and replaced with a list of recommended sources for detailed, accurate, and current information sources on the Korean bond market. These sources are listed below in alphabetical order.

- *AsianBondsOnline* (an ASEAN+3 initiative led by ADB)
  https://asianbondsonline.adb.org/korea.php
  - Market-at-a-Glance
  - Data (market size, yields, indicators, ratings, including historical data)
  - Market structure
  - Market summary
  - News (latest statistics)

- Bank of Korea
  http://ecos.bok.or.kr/EIndex_en.jsp
  - Payment and Settlement Trends (as downloadable PDFs)

- Financial Statistics Information System
  http://efisis.fss.or.kr/fss/fsiview/indexw.htmlhttp://efisis.fss.or.kr/fss/fsiview/indexw.html

- Korea Exchange
  http://global.krx.co.kr/
  - Introduction of KRX bond markets
  - Listing and trading statistics on KRX bond market
  - Issuance information
  - KRX regulations regarding listing, disclosure, and trading
  - Fixed-income indices calculated by KRX (http://enindex.krx.co.kr)
  - International Securities Identification Numbers information (http://isin.krx.co.kr)

- Korea Financial Investment Association
  http://www.kofiabond.or.kr/index_en.html
  - Bond interest rates
  - Primary market information (issuance, maturity statistics)
  - Secondary market information (trading records, turnover, etc.)
  - Bond indexes
  - Mark-to-market benchmark yields

VIII

Presence of an Islamic Bond Market

At present, the Korean bond market does not yet include legislative and market features that would enable the issuance of Islamic bonds, or *sukuk*.

IX

Korean Bond Market Challenges and Opportunities

This chapter discusses some of the real and perceived challenges facing the Korean bond market and its participants, and also describes the possible mitigating factors or market developments that could address these challenges in an appropriate manner.

A. Challenges in the Korean Bond Market

1. Obligations and Procedures Applicable to Nonresidents

A number of obligations and procedures required for nonresidents would benefit from being improved to the extent possible.

a. Registration Requirement for Foreign Investors

Nonresident investors wishing to invest in the Korean bond market are required to register with the FSS and obtain an IRC (see also Chapter II.M.1); this practice has been in place for many years and had previously been considered a challenge, due to the initially cumbersome documentation requirements.

Today, obtaining an IRC has become an integral part of the service provision by the appointed custodian of the nonresident investor, and the process has been improved to be as smooth as possible. However, the need to obtain an IRC and to match the IRC against the legal ownership of assets continues to pose challenges for investment managers and other entities (see also Chapter VI.H.9).

Regulators have since introduced that foreign nationals, foreign-incorporated entities, and local branches of a foreign corporation engaging in business activities in the Republic of Korea that qualify for "foreigner under national treatment" status shall be exempt from this registration upon submitting documents verifying their status. Such exemption from registration will also apply to cases where government bonds and market stabilization bonds are acquired and sold using "omnibus accounts" under the name of the ICSD through an ICSD account.

At the same time, regulatory developments in other ASEAN+3 and international markets increasingly favor practices that allow the identification of legal or beneficial owners by means of investor IDs or account structure. In this context, the Korean practice continues to be relevant.

b. Restrictions on Over-the-Counter Transactions by Nonresidents

As a general rule, nonresidents must buy and sell listed securities only through the securities exchange unless authorized or allowed otherwise by the FSC under Article 188 (2) in Enforcement Decree of FSCMA.

Nonresident investors, naturally, can transact listed securities through KRX by placing orders to the securities companies that are members of KRX.

Direct access to the OTC market is not possible for nonresident investors. If a nonresident investor wants to trade listed bonds OTC, the trade must be conducted through the intermediation of Korean securities companies. Articles 6–7 of the Regulation on Financial Investment Business apply to almost all bonds issued in the Republic of Korea since most publicly issued and offered domestic bonds are listed on the exchange market.

If a transaction in the OTC market has to be made through a Korean securities firm, it is possible that foreign investors will have to pay additional costs or lose the possibility of finding an advantageous trading opportunity in comparison to having direct access to trading counterparties. Such possibilities may keep foreign financial companies from investing in Korean bonds or recommending Korean bonds to their customers.

2. Withholding Tax on Interest Income

In the Republic of Korea, tax on interest income is withheld as a rule, with different rates applied depending on the investor's residency. For residents, a 15.4% withholding tax is regularly levied on interest income from bonds (see Chapter VI.H for more details), unless a different tax rate is available for residents of countries that have signed a tax treaty with the Republic of Korea.

Nonetheless, the inconvenience arising from the submission of information for tax purposes, or the processing of tax returns, and the need to adjust tax based on the holding period add a level of complexity to bond trading and investment. For this reason, some countries, including developed countries, encourage bond investments from nonresident investors by abolishing or zero-rating withholding tax, or by exempting nonresidents from withholding tax on interest income.

Similarly, the Asian Bond Markets Initiative's Working Group 2 recommended abolishing or lowering withholding tax on interest income for foreign investors to attract increased foreign investment in domestic bonds.

3. Exemption from and Re-Imposition of Withholding Tax

In January 2009, in the middle of the currency crisis caused by the global financial crisis, the Government of the Republic of Korea decided to exempt nonresidents from withholding tax on interest income from all government bonds and MSBs. However, the government re-imposed a flexible tax on interest income and a 20% tax on capital gains from KTBs and MSBs held by foreign investors, effective 1 January 2011. This followed the passage of legislative bills in December 2010, which called for the restoration of the withholding tax in order to mitigate capital flow volatility and minimize systemic risks to the domestic economy.

In line with the general challenge of implementing withholding tax mentioned in section 2, the exemption and re-instatement of withholding tax for nonresidents caused confusion among foreign investors and led to a heightened caution toward investing in the Korean bond market.

4. Slow Development of Professional Bond Market

The development of a bond market segment for professional investors, or a professional bond market in the Republic of Korea, is lagging behind. One recent policy measures was the launch of the QIB Market in 2012, which was intended as the bond market segment for professional investors (see further details in section B.1). However, at the time, eligible issuers were limited to only SMEs, which greatly reduced the attractiveness of the issued debt securities to the targeted investor universe due to credit rating and other considerations.

In its Measures to Boost Competitiveness of Financial Investment Business, released in October 2015, the FSC announced the further deregulation of this market segment by shaping it as a more inclusive QIB Market with the use of international standards. The relevant regulations for the operation of the revised concept became effective on 1 August 2016.

The deregulation of the QIB Market broadened the issuer range from SMEs to medium-sized corporations, and allowed foreign issuers to raise capital in the domestic QIB Market, regardless of their size. Yet, in this improved QIB Market, there remains a restriction with regard to the participation of large domestic corporations. Large domestic corporations, with assets totaling KRW2 trillion or more, are unable to issue bonds and notes in the QIB Market, limiting the market's attraction to nonresident QIBs who may favor recognized issuer names.

Some of the intended objectives of the revised QIB Market have been put into practice. Pursuant to the new measures introduced by the FSC, KOFIA launched a QIB Market debt securities registration and disclosure platform on 1 August 2016. Issuers of debt securities—including foreign issuers—are required to register their instruments with KOFIA for them to be eligible for trading on the professional OTC market. The key feature of the new disclosure platform is that foreign issuers may utilize their standard issuance documentation and disclosure information in English; this was a first for an issuance in the Korean bond market.

Despite taking into consideration the above limitation, AMBIF issuances may be able to be accepted in this revised QIB Market. However, the issues under discussion in relation to AMBIF, such as taxation and foreign exchange, are not reflected in the QIB Market regulatory process and still need to be addressed separately.

B. Opportunities in the Korean Bond Market

1. Introduction of Professional Market Segments

The QIB Market, which launched in 2012, is the first professional market for bond investment. It also introduced the ability for bond market participants to be recognized as professional investors (QIBs) and to attract treatment suitable for professional investors (limited disclosure) and access to eligible instruments. The QIB Market is currently operated by KOFIA.

A market for professional investors should be characterized by (i) lowered entry barriers for a wide range of securities issuers through concise or relaxed disclosure requirements, (ii) the participation of qualified investors who possess sophisticated information gathering capability and large amounts of capital to invest, and (iii) free trading only among qualified investors and without resale restrictions. The QIB Market satisfies these characteristics and provides a great opportunity for issuers and professional investors alike.

This professional market concept has also been applied to the stock market. Case in point is the KONEX, launched by KRX in 2013, which is the SME stock market for professional investors.

KONEX is the stock market platform in KRX for professional investors, but its professional investor concept for the primary and secondary markets is very similar to that for the professional bond market. This means that the possible extension of this professional investor concept for a listed bond market for professional investors, with the participation of a wide range of domestic and foreign issuers, should easily attract the attention of eligible investors already familiar with the professional stock market segments.

Moreover, KRX opened the KSM Market in 2016, which imposes much more relaxed registration requirements on issuers. Using the KSM registration concept, KRX may introduce a new bond registration process that will satisfy AMBIF registration guidelines.

2. ASEAN+3 Multi-Currency Bond Issuance Framework

The introduction of AMBIF in regional markets over the course of 2015 signaled an opportunity for additional bond and note issuance activities in the domestic bond markets. Among the requirements for participation in AMBIF are the existence of a professional market segment to safeguard the investor protection framework for retail or general investors in each market, the need for bonds and notes to be registered or profile listed to ensure adequate continuous disclosure throughout the tenor of the bond, and the ability for issuers to use standardized issuance documentation in English across all participating markets.

With the latest developments of the QIB Market (i.e., a market for private placements to be traded in the OTC market under the governance of KOFIA), the Korean bond market now features a market segment that fulfills such key requirements for the implementation of AMBIF (see also section 1). With KONEX, KRX has also opened a professional market.

These markets define participants as professional investors. Companies listed on such markets, or issuers registering their debt securities in the case of the QIB Market, are subject to limited or defined initial and continuous disclosure obligations compared to main or retail markets.

In the process of opening the markets mentioned above, KRX has established a professional market scheme and accumulated know-how for building a professional market. Therefore, KRX expects that successful experience may easily be adopted to a professional bond market as well and would ensure that it will be a sustainable and well-organized market. The KONEX market infrastructure is ready to be utilized for a new professional market segment on KRX, equivalent to the QIB Market.

If AMBIF, as the issuance concept for bonds and notes for professional investors, were to be applied in the professional bond market segments in the Republic of Korea, it would provide opportunities for Koreans to invest in bonds issued by foreign issuers and also would give Korean firms easier access to capital in the region.

Moreover, the Republic of Korea can contribute to regional financial development by participating in ASEAN+3 bond markets. In turn, it would help strengthen regional cooperation and play a part in regional co-development. The implementation of AMBIF is expected to benefit the Korean bond market at large.

X

Recent Developments and Future Direction

A. Recent Major Developments

Recent major developments are considered those that occurred or have been announced in the Korean market since the first publication of the Bond Market Guide in April 2012.

1. Implementation and Improvement of Qualified Institutional Buyer Concept and Private Placement Market

In a first step toward a defined professional market segment in the bond market in the Republic of Korea, the FSC introduced the QIB system in May 2012. The market was designed to give opportunities to SMEs to raise capital as an alternative to bank loans or going public.

With the Regulation on Issuance, Public Disclosure, etc. of Securities, the market segment was extended on 30 December 2014 to securities that are issued by foreign entities and or bonds denominated in a foreign currency. These regulations gave rise in the Korean market to the issuance of bonds denominated in offshore Chinese renminbi.

In its Measures to Boost Competitiveness of Financial Investment Business, the FSC announced a further deregulation of this market segment by shaping it as a QIB Market with the use of international standards. The relevant regulations for the operation of the revised concept were amended on 1 August 2016.

2. Establishment of the KOFIA QIB (Qualified Institutional Buyers) Debt Securities Market

Pursuant to the QIB Market measures introduced by the FSC, KOFIA launched a QIB Market debt securities registration and disclosure platform with effect from 1 August 2016. The key feature of the new disclosure platform is that foreign issuers may utilize their standard issuance documentation and disclosure information in English for the first time for an issuance in the Korean bond market.

Similar to the previous practice, issuers of debt securities—including foreign issuers—are required to register their instruments with KOFIA for them to be eligible for trading in the professional OTC market.

3. Introduction of Electronic Short-Term Bonds

Electronic short-term bonds, which are electronically issued bonds with a maturity of 1 year or less, were introduced on 15 January 2013, pursuant to the Act on Issuance and Trading of Electronic Short-Term Bonds. These instruments were intended to provide an easily tradable alternative to commercial paper (see also Chapter III.C for more details).

4. First Issuance of 30-Year Treasury Bonds (September 2012)

The Government of the Republic of Korea needed a means to finance prolonged demands for public expenditures on a long-term and stable basis. As a result, and to diversify its portfolio of bond maturities, the government issued 30-year Treasury bonds (in addition to existing 3-year, 5-year, 10-year, and 20-year bonds) for the first time in September 2012.

5. Introduction of Treasury Bond Pre-Issuance (March 2015)

To mitigate a liquidity reduction after the change of benchmark bonds, the government introduced the pre-issuance concept in March 2015, under which it issues a benchmark bond as well as a subsequent benchmark bond at the same time, 3 months before new issuance.

6. Introduction of When-Issued Trading (December 2015)

In December 2015, the government adopted “when-issued trading,” which allows trading of newly issued KTBs from 2 days before the bidding day to the bidding day, in order to improve the capability to explore interest rates before bidding and to create new demand. Now the government is able to identify demand for KTBs in advance and, hence, to more flexibly control the amount of bonds to be issued. Dealers are provided an opportunity to hedge against risks of interest rate fluctuation and holding bid orders.

7. Introduction of Request-For-Quote in the KRX Market (March 2016)

KRX introduced an RFQ function in the KRX bond market in March 2016, as an addition to the CLOB, in order to enhance trade convenience and market efficiency. RFQ facilitates the execution of block trades—since RFQ trading counterparties consult with each other on trading conditions, including prices and quantities, before trade execution..

8. Fragmentation of Tick Size in the KRX Market (June 2016)

Effective June 2016, KRX adopted three tiers of tick size, taking into consideration the remaining time to maturity of the listed bonds and notes, thereby abolishing the existing tick size of KRW1 regardless of the residual tenor of the bonds (Table 10.1). Thanks to the three-tiered tick size, more precise and fairer prices are calculated and the narrowing of quotation spreads can reduce the costs of trading for bond investors.

Table 10.1: Fragmentation of Tick Size on the Korea Exchange

Residual Tenor of Bonds and Notes	Tick Size
Less than 2 years	KRW0.1
2 years or longer to less than 10 years	KRW0.5
10 years or longer	KRW1.0

Note: For benchmark 10-year KTBs and 10-year inflation-linked bonds, the tick size remains KRW1, regardless of outstanding tenor.
Source: Korea Exchange.

9. First Issuance of 50-Year Treasury Bonds (October 2016)

In October 2016, the government issued 50-year KTBs worth KRW1.1 trillion for the first time. It is expected that the government's ability to finance long-term expenditure and its capacity to adequately control the issuance of KTBs will be enhanced after the successful issuance of the bonds. The issuance also allowed the government to have a longer-term fiscal outlook and develop ultra-long-term financial assets through the setting of an attractive interest rate for the bonds.

B. Future Direction

1. Participation of Nonresident Issuers and Investors

Underpinned by the growth of the bond market, foreign investor holdings of domestic bonds have steadily increased since the mid-2000s. Their bond investment was merely KRW1 trillion in the early 2000s but exceeded KRW100 trillion in 2015.

However, the volume of bonds and notes issued by nonresidents is still insignificant in the Republic of Korea. As of 2016, the volume of outstanding bonds issued by nonresidents through public and private placements stood at KRW320 billion and KRW440 billion, respectively, together representing only 0.04% of total outstanding bonds in the Republic of Korea.

In this situation, AMBIF, which represents a professional bond market, can provide op portunities for Korean investors to invest in bonds issued by foreign issuers and give K orean firms easier access to capital in the region. Moreover, the Republic of Korea can contribute to regional finance by participating in ASEAN+3 bond markets. In turn, it wo uld help strengthen regional cooperation and play a part in regional co-development.

The market for professional investors has gradually opened its doors to foreign issuers. Deregulation of the QIB Market, which came into force in 2016, for the first time allowed foreign issuers to raise capital in the private placement market, of which the QIB Market is a part.

This professional market concept was also applied to the exchange market. Cases in point are the KONEX, which was launched by KRX in 2013 and represents the SME stock market for professional investors, and the KSM, which opened in 2016 as the startup stock market for professional investors.

As such, infrastructure is in place for foreign entities to issue bonds in the Republic of Korea. However, foreign bond issuance remains insignificant. Considering the volume and share of foreign investment in domestic bonds and notes, bond issuance by nonresident issuers is very likely to grow. An increase in foreign bond and note issuance will not only enable foreign borrowers to raise capital in the domestic market, but also provide domestic investors with diverse investment opportunities to seek certain levels of expected returns.

To this end, the Republic of Korea should improve its capital market infrastructure as well as its bond market infrastructure. In addition, policy makers should evaluate a variety of options and their feasibility as the government continues its research into and preparations for participation in AMBIF. The implementation of AMBIF is expected to benefit the Korean bond market at large. A formal announcement on the Republic of Korea's participation in AMBIF is expected to be made by the relevant policy bodies or regulatory authorities soon.

2. Global Regulatory Trend for More Transparent Bond Trade

Since the global financial crisis, the regulatory framework of global financial markets has been evolving to pursue more transparency and greater access to information. New regulations seek to transform the existing method in which trading in the OTC market is conducted by voice into trading based on e-commerce principles and more transparent trading facilities (e.g., a regulated market or a multilateral trading facility). The International Organization of Securities Commissions also emphasized the importance of information in the secondary corporate bond market in its report released in August 2017. This consultation report recommends that supervisory institutions of member countries establish obligations of reporting corporate bond trades and requirements to bolster the transparency of trade information.

While authorities in the existing bond market segments in the Republic of Korea, both OTC and on-exchange, have put significant efforts toward transparency and information disclosure over many years, as described in this Bond Market Guide, the Korean bond market needs to take additional steps in response to global trends. Furthermore, these trends are very likely to affect the regulatory direction of other markets around the world, including the ones where issuers and investors with an interest in the Korean bond market are domiciled.

Appendix 1
Group of Thirty Compliance

The Group of Thirty recommendations were originally conceived as the group's Standards on Securities Settlement Systems in 1989, detailing, in a first-of-its-kind report, nine recommendations for efficient and effective securities markets covering legal, structural and settlement process areas. The recommendations were subsequently reviewed and updated in 2001 under the leadership of the Bank for International Settlements and through the efforts of a joint task force of the Committee on Payment and Settlement Systems and the Technical Committee of the International Organization of Securities Commissions. Compliance with the Group of Thirty recommendations in individual markets is often an integral part in securities industry participants' and intermediaries' due diligence process.

Table A1: Group of Thirty Recommendations—Compliance for the Republic of Korea

Recommendation		Implemented
1	Eliminate paper and automate communication, data capture, and enrichment.	No
2	Harmonize messaging standards and communication protocols.	No
3	Develop and implement reference data standards.	No
4	Synchronize timing between different clearing and settlement systems and associated payment and foreign exchange systems.	Yes
5	Automate and standardize institutional trade matching.	Yes
6	Expand the use of central counterparties.	No
7	Permit securities lending and borrowing to expedite settlement.	Yes
8	Automate and standardize asset servicing processes, including corporate actions, tax relief arrangements, and restrictions on foreign ownership.	No
9	Ensure the financial integrity of providers of clearing and settlement services.	No
10	Reinforce the risk management practices of users of clearing and settlement service providers.	No
11	Ensure finals, simultaneous transfer and availability of assets.	Yes

Recommendation		Implemented
12	Ensure effective business continuity and disaster recovery planning.	No
13	Address the possibility of failure of a systematically important institution.	No
14	Strengthen assessment of the enforceability of contracts.	No
15	Advance legal certainty over rights to securities, cash, or collateral.	Yes
16	Recognize and support improved valuation methodologies and closeout netting arrangements.	No
17	Ensure appointment of appropriately experienced and senior board members (of the boards of securities clearing and settlement infrastructure providers).	Yes
18	Promote fair access to securities clearing and settlement networks.	Yes
19	Ensure equitable and effective attention to stakeholder interests.	No
20	Encourage consistent regulation and oversight of securities clearing and settlement service providers.	Yes

Source: Group of Thirty. *Global Clearing and Settlement–A Plan of Action*. http://newsite.group30.org/publications/detail/123

Appendix 2
Practical References

For easy access to further information about the market features described in the Korea Bond Market Guide—including information on the policy bodies, regulatory authorities, and securities market-related institutions—interested parties are encouraged to utilize the following links (all websites available in English):

AsianBondsOnline (Asian Development Bank)
https://asianbondsonline.adb.org/korea.php

Bank of Korea
http://www.bok.or.kr/eng/engMain.action

Financial Hub Korea
http://www.fnhubkorea.kr/fhk_eng/laws/securities/list.jsp

Financial Supervisory Service
http://english.fss.or.kr/fss/eng/main.jsp

Korea Capital Market Institute
http://www.kcmi.re.kr/eng/main/main.asp

Regulations on KOSPI Market:
https://global.krx.co.kr/contents/GLB/06/0601/0601000000/GLB0601000000.jsp

Korea Exchange
https://global.krx.co.kr/main/main.jsp

Korea Financial Investment Association
http://eng.kofia.or.kr/index.do
KOFIA Regulations: http://eng.kofia.or.kr/brd/m_15/list.do

Korea Securities Depository
https://www.ksd.or.kr/eng/index.home
KSD Regulations: http://www.ksd.or.kr/eng/bbs/bbsList.home

Ministry of Strategy and Finance
http://english.mosf.go.kr/

National Law Information Center
http://www.law.go.kr/eng/engLsSc.do?menuId=1&query=financial+services+and&x=42&y=34#liBgcolor13 / http://www.law.go.kr/eng/engMain.do

Appendix 3
List of the Regulations and Rules Issued by KOFIA, KRX, and KSD

Table A3.1: Overview of Major Regulations and Standards issued by the Korea Financial Investment Association

Regulation, Bylaw, or Agreement
Articles of Association
Regulations on Business Conduct and Services of Financial Investment Companies (
Enforcement Bylaws of the Regulations on the Business Conduct and Services of Financial Investment Companies
Regulations on Management and Sanctions of Self-Regulation Committee
Regulations on Management of Agreements of Financial Investment Companies Agreement on Opening of Trading Accounts Agreement on Opening of Foreign Currency Securities Trading Accounts Agreement on Loan Transactions of Securities Agreement on Repo with Customers Agreement on Repo between Institutions Agreement on Commercial Paper Trading Agreement on Using Electronic Financial Transactions
Regulations on Securities Underwriting Business, etc.
Regulations on Investment Professionals and Qualifying Examinations
Enforcement Bylaws of Regulations on Investment Professionals and Qualifying Examinations
Regulations on Dispute Resolution
Regulations on Credit Rating Agency Assessment
Working Rules on Investment Recommendations
Standards for Internal Control of Financial Investment Companies
Standard Code of Ethics

Note: Information as of 10 October 2016.
Source: Korea Financial Investment Association. http://eng.kofia.or.kr/brd/m_15/list.do

Table A3.2: Selection of Other Regulations, Rules, and Codes by Korea Financial Investment Association

Regulation, Bylaw, Code of Best Practices, Agreement
Standard Criteria for Book-Building of Non-Guaranteed Bonds
Guidelines on Non Face-To-Face Financial Investment Business
K-OTC Market Regulations
Standard Regarding Yield Reporting for Disclosure of Last Quoted Yield
Standards on Yield Reporting for Disclosure of Last Quoted Yield
Standard Working Rules of Ethics of Financial Investment Companies
Operation Rules for the Trading System of Qualified Institutional Investors
Deliberation Standards of Exclusive Rights on New Products
Standard Criteria for Book-Building of Non-Guaranteed Bonds
Working Rules on Investment Recommendations
Regulations on the Trading System for Qualified Institutional Investors
Regulations on Registration and Management of QIB Market-eligible Securities
Regulations on financial investment professionals and certification
Standards for Internal Control of Financial Investment Companies

OTC = over-the-counter, QIB = Qualified Institutional Buyer.
Note: Information as of 10 October 2016. Not all regulations may always be available as latest versions in English.
Source: Korea Financial Investment Association. http://eng.kofia.or.kr/brd/m_15/list.do

Table A3.3: Overview of Korea Exchange Regulations

Type of Regulation	Title of Regulation
General Regulations	Articles of Incorporation Membership Regulation Enforcement Rules of Membership Regulation Regulation on Operation of the Broker–Dealers Guideline on Connection to Member System Criteria for Member Admission
Regulations on KOSPI Market	KOSPI Market Business Regulation Enforcement Rules of KOSPI Market Business Regulation KOSPI Market Disclosure Regulation Enforcement Rules of KOSPI Market Disclosure Regulation KOSPI Market Operational Guidelines on Fair Disclosure KOSPI Market Listing Regulation Enforcement Rules of KOSPI Market Listing Regulation
Regulations on KOSDAQ Market	KOSDAQ Market Business Regulation Enforcement Rules of KOSDAQ Market Business Regulation KOSDAQ Market Disclosure Regulation Enforcement Rules of KOSDAQ Market Disclosure Regulation KOSDAQ Market Listing Regulation Enforcement Rules of KOSDAQ Market Listing Regulation KOSDAQ Market Operational Guidelines on Fair Disclosure
Regulations on Derivatives Market	Derivatives Market Business Regulation Enforcement Rules of Derivatives Market Business Regulation Petroleum E-Trading Business Regulation Guideline for Recommending Quota Tariff for Imported Petroleum Products OTC Derivatives Clearing Business Regulation Enforcement Rules of OTC Derivatives Clearing Business Regulation
Regulations on Market Oversight	Market Oversight Regulation Enforcement Rules of Market Oversight Regulation Dispute Mediation Regulation Enforcement Rules of Dispute Mediation Regulation

OTC = over-the-counter.
Note: Information as at 10 October 2016.
Source: Korea Exchange. https://global.krx.co.kr/contents/GLB/06/0601/0601000000/GLB0601000000.jsp

Table A3.4: Overview of Korea Securities Depository Regulations

Regulation Title
Regulation on Clearing Services
Enforcement Rule on Clearing Services
KSD SLB Regulation
Detailed Enforcement Rules for SLB Transaction
Regulation on Settlement Service for Securities
Detailed Enforcement Rules for the Regulations on Settlement Service for Securities
Regulation on Management of Beneficiary’s List
Delegation Agreement on Management of Beneficiary's List
Regulation on Deposit and Settlement of Foreign Securities
Detailed Enforcement Rules for the Regulation on Deposit and Settlement of Foreign Securities
Regulation on Deposit Service for Securities
Detailed Enforcement Rules for the Regulation on Deposit Service for Securities
Regulation on Collateral Management of Securities
Detailed Enforcement Rules for the Regulation on Collateral Management of Securities
Regulation on Bond Registration Business
Detailed Enforcement Rules for the Regulation on Bond Registration Business
Regulation on Issuance of Depositary Receipt
Agreement on Intermediation of SLB Transaction
Eligible Collateral and Evaluated Rates

KSD = Korea Securities Depository, SLB = securities lending and borrowing.
Note: Information as of the time of compilation of this Bond Market Guide. Not all regulations may always be available as latest versions in English.
Source: KSD. http://www.ksd.or.kr/eng/bbs/bbsList.home?menuNo=48

Appendix 4
Glossary of Technical Terms

Account Management Institution	Participant at KSD, effectively a custodian for securities on behalf of customers or own holdings
allocated contribution	Term used for the fee levied by the FSS for the submission and review of an SRS
Alternative Bond Scheme	Denotes *sukuk* arrangements as an alternative to conventional bonds and notes (in most recent legislation)
authorization	licensing from the relevant regulator
Authorized Institutions	Licensed banks, restricted license banks, and deposit-taking companies as defined in the Banking Ordinance
BOK-Wire	National high-value payment system operated by Bank of Korea
filing	Action of submitting documentation
financial investment business	Summary term for entities carrying out activities in the capital market under authorization by and oversight of the FSC
FreeBond	Original OTC bond trading platform developed by KOFIA, upgraded to K-Bond in 2016
Information Memorandum	Synonymous with Offering Memorandum; term typically used for key documentation for a private placement mainly to professional investors
investment brokerage business	Term used in law and regulations to describe a secondary bond market participant authorized to buy and sell securities
investment trading business	Term used in law and regulations to describe an authorized participant in the primary market; activities include issuing, underwriting, and offering debt securities
K-Bond	OTC bond trading supporting platform operated by KOFIA; updated version of original FreeBond system
listing	Typically, action of submitting a bond issue or other securities to an exchange for the purpose of trading, price finding, disclosure, or profiling
Offering Memorandum	Synonymous with Information Memorandum; term typically used for key documentation for a private placement mainly to professional investors

managing company	Term used in the Korean market for the lead manager of a bond or note offer; the offer may involve more than one managing companies
Monetary Stabilization Bond	Key instrument in BOK's open market operations to steer market liquidity
Qualified Institutional Buyer	Professional investor concept in the Korean bond market
QIB Market	Bond market where the bonds and note issued by private placement are traded among QIBs
QIB Market-debt securities	Bonds and notes that are eligible to trade on the QIB Market
registration	Refers to the act of registering a bond with KOFIA as a prerequisite to be tradeable in the OTC market
registration application form	Form requires to be submitted for the registration of bonds to the QIB Market; in contrast to Securities Registration Statement which is required for publicly offered securities
Securities Registration Statement	Format to be submitted to the FSS as key disclosure document in the case of a public offering of debt securities
short-term electronic bonds	Financial instrument that is only issued, registered, and traded an in electronic form (in contrast to other debt securities which may be issued in physical form)
sukuk	Islamic bond or note
uncertified securities (regime)	describes the movement toward a dematerialized market

Source: ADB consultants for SF1.

ASEAN+3 Bond Market Guide 2018 Republic of Korea

ASEAN+3 Bond Market Guide is a comprehensive explanation of the region's bond markets. It provides information such as the history, legal and regulatory framework, specific characteristics of the market, trading and transaction (including settlement systems), and other relevant information. The ASEAN+3 Bond Market Guide 2018 Republic of Korea is an outcome of the strong support and kind contributions of ASEAN+3 Bond Market Forum members and experts, particularly from the Republic of Korea.

About the Asian Development Bank

ADB's vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries reduce poverty and improve the quality of life of their people. Despite the region's many successes, it remains home to a large share of the world's poor. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

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