1-1-2013

Favoritism and Corporate Law: The Confused Corporate Opportunity Doctrine in the Hyundai Motor Case

Hwa-Jin Kim
University of Michigan Law School, hjkim7@snu.ac.kr
Seung Hwan Lee
seunghwan.lee@leeko.com
Stephen M. Woodcock
swoodcock@jenner.com

Favoritism and Corporate Law: The Confused Corporate Opportunity Doctrine in the Hyundai Motor Case

Hwa-Jin Kim, Seung Hwan Lee, and Stephen M. Woodcock*

Abstract

Core legal principles of U.S. corporate law are often met with perplexity in foreign jurisdictions – this is especially true when a particular principle remains controversial even in the U.S. This Article takes the corporate opportunity doctrine and examines how it has been exported to the civil law regime in Korea. Korean conglomerates such as Samsung Group and Hyundai Motor Group have become major players in the global market, but corporate law and practice in Korea have had a difficult time keeping up with the developments in the business sector. The Hyundai Motor Case demonstrates an ambitious but ill-fated attempt at adoption of U.S. corporate legal doctrine in Korea. This Article explains and analyzes the case and the new codified corporate opportunity doctrine rule in the Korean Commercial Code from a comparative perspective, and suggests that the dialogue surrounding the corporate opportunity doctrine in Korean legal and business communities are oriented in the wrong direction and that the new rule needs substantial refinement.

I. INTRODUCTION

Suppose you control one of the biggest corporations in the world as the "controlling shareholder-manager."[1] As you approach retirement, a succession plan becomes necessary, and you desire to pass control of the corporation to your son. To do so, you must prove to your shareholders and managers that your son is a capable and experienced leader and that he has the potential to be as successful

* Hwa-Jin Kim is a Professor of Law at Seoul National University, and William W. Cook Global Law Professor at the University of Michigan Law School; Seung Hwan Lee, LL.B. *magna cum laude* Seoul National University School of Law and Diploma (first in his class), Research and Training Institute of the Korean Supreme Court, is an associate of Lee & Ko, Seoul, Korea; and Stephen Woodcock, J.D. *magna cum laude* University of Michigan Law School, is an associate in the Chicago office of Jenner & Block LLP.

[1] The controlling shareholder-manager is one of the characteristics of the concentrated ownership economy and family-controlled firms. *See* Ronald J. Gilson, *Controlling Family Shareholders in Developing Countries: Anchoring Relational Exchange*, 60 Stanford Law Review 633 (2007); Ronald J. Gilson, *Controlling Shareholders and Corporate Governance: Complicating the Comparative Taxonomy*, 119 Harvard Law Review 1641 (2006).

as you have been in running the business. Towards that end, you form a new small firm, making 40 percent of the capital contribution yourself, with your son contributing the remaining 60 percent. He will serve as the manager of the new firm, and his success in this new role will prove his ability to take your position and lead the corporation you control once you step down. The new firm engages in the business of providing certain services necessary to your corporation and its affiliated companies and you instruct your officers and employees to purchase those services exclusively from your son's firm, sometimes for a price higher that what could be bargained for at arm's length. Over a relatively short period of time, the new firm grows into a public corporation and the relationship between your companies strengthens, resulting in massive profits for you and your son. This is the story of Hyundai Motor Company ("Hyundai Motor") and the "new firm" Hyundai Glovis Co., Ltd. ("Hyundai Glovis"), and we pose the following question: Under the corporate legal regime as it is today, has a wrong been committed, and if so, what was it and what legal principle has been violated? More specifically, is it against the law to favor your son's firm through the exercise of your managerial power?

Some activist shareholders of Hyundai Motor thought the CEO violated the corporate opportunity doctrine and must be held liable – they brought a shareholder derivative lawsuit against Hyundai Motor's chief executive. The problem was that Korean law did not recognize the corporate opportunity doctrine at that time.[2] The doctrine was eventually written into the Korean Commercial Code ("KCC"), though the court has struggled with interpreting the doctrine and the language of the statute. The KCC has since been amended to adopt the corporate opportunity doctrine as it has developed over the decades in the United States, however the confusion surrounding the doctrine amongst legal professionals and scholars in Korea has persisted. This is at least in part because the corporate opportunity doctrine is regarded as one of the most difficult legal principles in U.S. corporate law and remains open to regular reinterpretation and criticism.[3] This Article will explain and attempt to comparatively analyze the Hyundai Motor case and the new KCC rule.[4]

---

[2] For Korean business law in the English language *see* Hwa-Jin Kim ed., Korean Business Law (Edward Elgar, 2012).

[3] *See* Robert Clark, Corporate Law ch. 7 (1986); Eric Talley, *Turning Servile Opportunities to Gold: A Strategic Analysis of the Corporate Opportunities Doctrine*, 108 Yale Law Journal 277 (1998).

[4] For Korea's efforts in improvement of corporate governance *see* Bernard S. Black et al., *Corporate Governance in Korea at the Millennium: Enhancing International Competitiveness*, 26 Journal of Corporation Law 537 (2001); Hwa-Jin Kim, *Toward the "Best Practice" Model in a Globalizing Market: Recent Developments in Korean Corporate Governance*, 2 Journal of

II. BACKGROUND OF THE CASE AND COURT'S RULING

A. The Scheme and Background

The actions taken by Hyundai Motor's controlling shareholder-manager have been a widespread practice in Korea during the past decade. Korean conglomerates [5] commonly split off segments of their affiliates' existing businesses into a separate enterprise, or establish a new company to engage in a closely related business, with the chairman's family members acquiring the new company's shares at the time of the establishment or sometime thereafter. While it must be pointed out that such transactions cannot, with any certainty, be lumped together and presumed to all serve the same single purpose (especially considering the limited publicly-available information), one can easily conclude that these transactions, when combined with the so called "Funneling of Business" to the newly established company (*Mul-lyang-mol-a-ju-gi* in the Korean language), [6] [7] are used to solve the succession problem many

---

Corporate Law Studies 345 (2002); Bernard S. Black et al., *Does Corporate Governance Predict Firms' Market Values? Evidence from Korea*, 22 Journal of Law, Economics & Organization 366 (2006).

[5] Usually South Korean conglomerates are referred to as '*Chaebol*' in Korean language. They are typically global multinational companies owning numerous international enterprises controlled by a chairman who has power over all the operations. Jung Dong Hyeon, "Korean Chaebol in Transition", China Report, Vol. 40 (3) (2004), pp. 299~303. *See also* Jeong Seo, *Who Will Control Frankenstein? The Korean Chaebol's Corporate Governance*, 14 Cardozo Journal of International & Comparative Law 21 (2006).

[6] According to the report released by Korea Fair Trade Commission on August 30, 2012 regarding the current state of affairs on the transactions of goods and services between the affiliate companies of conglomerates ("inter-affiliate transactions"), the percentage of inter-affiliate transactions by conglomerates with a controlling head was 13.6%, which is 2.5% higher than that of conglomerates without a controlling head (11.1%). Furthermore, companies with high percentage of equity owned by affiliates, the chairman's relatives and the second generations of the chairman's family are found to have a relatively high ratio of inter-affiliate transactions. Especially, companies where the second generations of the chairman's family own more than 50% of company's shares, the ratio of inter-affiliate transactions was as high as 56.3%.

[7] People's Solidarity for Participatory Democracy Economic Reform Research Institute, "Report on the Share Transaction of the Head's Family Members of 38 Conglomerates" (April 6, 2006), p. 11. According to the report, 'appropriation of corporate opportunity' has been found in nearly all conglomerates, and it has been widely used as a tool for illegal succession taking advantage of loopholes in the KCC and the Korean tax act. The report has been updated four times up to the end of 2012 since its first publication, and according to the last report (Economic Reform Research Institute, "The Fifth Report on the Problematic Share Transaction of the Head's Family Members of Conglomerates"), there were 66 cases which were suspected to be an 'appropriation of corporate opportunity'. As a result, as of end of 2012, the increased amount of the wealth chairmens' family members possesses was up to approximately KRW 10 trillion 429.9 billion, and its average earning rate was 1,256%.

conglomerates face. This is not a new observation, nor have the transactions gone unnoticed or unopposed; activist shareholders have been vocal critics of the practice and an active public dialogue on the issue is ongoing.

Although many transactions have been accused by activist shareholders of being veiled appropriations of corporate opportunities, as of today there are relatively few cases in which suit has been filed and the court given the opportunity to examine the transaction and apply corporation law. This can be partially explained by Korea's unique legal system and culture.[8] A more fundamental explanation is (i) the lack of a specific and explicit regulation regarding the corporate opportunity doctrine in Korea's civil law system and (ii) the fact that despite the existence of the corporate opportunity doctrine based on the provisions on director's duty of loyalty (KCC Article 382-3[9]), there is not enough precedent or other legal basis to convincingly apply the corporate opportunity doctrine to inter-affiliate transactions. Despite this, one Korean court recently took a remarkable step in that direction; below, we discuss the court's ruling in the Hyundai Motor Shareholder Derivative Suit ("Hyundai Motor Case").

B. The Case and Court's Ruling[10]

The plaintiffs in the case against Hyundai Motor are the civic group '*Solidarity for Economic Reform*' along with minority shareholders of Hyundai Motor. The defendants are *Chung Mongkoo*, Hyundai Motor's CEO and head of Hyundai Motor Group, and *Kim Dongjin*, President of Hyundai Motor.

Hyundai Glovis is a company specializing in the distribution service business, established to unify and combine Hyundai Motor Group's distribution services. At the time of Hyundai Glovis's establishment, its shareholders were *Chung Mongkoo* (40%) and his eldest son *Chung Uiseon* (60%). Hyundai Motor Group's affiliates, such as Hyundai Motor, Kia Motors Corporation, Hyundai

[8] In Korea there is no discovery process like U.S. Furthermore, since the plaintiff has a strict liability on burden of proof; burden for a legal action to the plaintiff is relatively high. Moreover, attorneys do not have an economic incentive to file a lawsuit, as punitive damages are not allowed in Korea and contingent fees, where attorney can receive fees in proportion to the amount of a favorable judgment, are not widely used. In fact, 50 years have passed since the KCC has adopted shareholder derivative suit, yet the total number of derivative suits filed is relatively small, and most of the derivative suits that were filed were public interest lawsuits raised by civic groups.

[9] Article 382-3 (Duty of Loyalty by Directors) "Director shall perform their duties in good faith for the interest of the company in accordance with Acts, subordinate statues, and the articles of incorporation."

[10] Seoul Central District Court No. 2008 GaHab 47881, February 25, 2011.

Mobis Co., Ltd. ("Hyundai Mobis"), and Hyundai Steel Company did business with Hyundai Glovis in nearly all areas, including automobile, steel and component delivery, leasing services for distribution equipment, domestic PDI (Pre-delivery Inspection) work, T/P (Transporter) sector and other delivery-related services through business transfers or private contracts. As a result, the aggregate financial payments between Hyundai Motor Group and Hyundai Glovis reached KRW 568.9 billion between March 2001 and June 2004.[11] During that time, the Korean Fair Trade Commission (the "KFTC") imposed a penalty surcharge of KRW 4.7 billion on Hyundai Motor for illegally supporting Hyundai Glovis. The KFTC levied the penalty on the grounds that Hyundai Motor Group was providing excessive financial return to Hyundai Glovis by allotting most of affiliate companies' transportation needs to Hyundai Glovis on terms that were not arms' length, and noted that the business capabilities of the relatively new Hyundai Glovis had not been tested or verified.[12]

Numerous issues were raised in the litigation. Among them, the plaintiffs argued that the directors of Hyundai Motor usurped a corporate opportunity, stating: "(i) Transportation or distribution services including transportation broker service that Hyundai Glovis is engaged in, provides essential assistance to Hyundai Motor Group's affiliates. Hyundai Motor's working group has for a long time, been striving to establish an integrated distribution company through share investments by Hyundai Motor Group and its affiliates. (ii) Therefore the distribution service by Hyundai Glovis falls under the scope of business opportunity for Hyundai Motor. (iii) It can be expected that Chung Mongkoo as a controlling shareholder and CEO of Hyundai Motor would have gained enormous benefits by acquiring shares of the integrated distribution company. Furthermore Hyundai Motor's distribution service is one of the most important sectors in the company's scope of business. Therefore, since Hyundai Motor could financially afford to acquire major shares of Hyundai Glovis, such a plan should have been reviewed and reported to the board of directors and measures should have been taken, so that the board of directors could make a resolution for the acquisition of the shares of Hyundai Glovis. (iv) Nevertheless, CEO Chung Mongkoo and his son secretly acquired the shares of Hyundai Glovis, without any process of reporting such agenda to the board of directors. (v) Such an act clearly constitutes

[11] Afterwards, Jeong Mongkoo and Jeong Uiseon sold some of their shares to Wilhelmson, a Norwegian shipping company and acquired approximately KRW 100 billion from the sale. Hyundai Glovis was listed in the KOSPI stock market in January 2006 and accordingly Jeong Mongkoo and Jeong Uiseon earned about KRW 400 billion of book valuation profit. People's Solidarity for Participatory Democracy Economic Reform Research Institute, *op. cit.*

[12] Hyundai Motor Group filed for a lawsuit for revocation of the KFTC's disposition, however lost in the lawsuit (Supreme Court of Korea, No. 2009 Du 15494, October 25, 2012).

appropriation of Hyundai Motor's corporate opportunity as CEO Chung Mongkoo and his son Chung Uiseon privately gained benefits by depriving Hyundai Motor of its business opportunity."

At the time this judgment was rendered, the Amended KCC's Article on Prohibition against Appropriation of Company's Opportunities and Assets (discussed below) was not in effect.[13] Nevertheless, the court acknowledged that the appropriation of a corporate opportunity could be derived from concepts already existing in the pre-amendment KCC, the duty of good manager's due care or duty of loyalty, then defined the concept of appropriation of corporate opportunity as "a principle that anyone such as the director or executive member of the company who has duty of loyalty, shall not unfairly seize the company's opportunity for their own benefit, by using his status as a fiduciary and fiduciary relations." However, the court also ruled that the director is not obliged to actively transfer all of its business opportunities to the company he or she is aware of, since 'business opportunity' is a comprehensive and vague concept, and moreover the duty of good manager's due care or duty of loyalty is a duty during the performance of duties, not a general duty to take every action potentially beneficial to the company. Therefore, the court provided a narrow interpretation that in determining that the director has damaged the company of its expectation profits by violating duty of loyalty, the business opportunity should only be restricted to "realistically existing specific business opportunities." In other words, (i) when the business opportunity of the company was an existing, realistic, and specific opportunity, with specific discussions within the company on the promotion of business or the company being proposed a business opportunity with advantageous conditions and (ii) where there was substantial probability that the company would have promoted its business based on such business opportunity in accordance with the existing company's reasonable business judgment based on factors such as business strategy, business type, financial conditions, business characteristics, investment size, burden of risk and expected income, then the director shall have duty of good manager's due care or duty of loyalty to cause the company to promote such business. When the director has seized or usurped the company's business opportunity in such a circumstance then violation of duty of good manager's due care or duty of loyalty can be recognized.

The court ruled that, based on the considerations discussed below, there was insufficient basis to prove that the segment entered by Hyundai Glovis was Hyundai Motor's existing, realistic and specific business opportunity, and therefore CEO Chung Mongkoo did not have any duty of good manager's due

[13] The bill amending the relevant portion of the KCC was before Parliament at the time, but had not yet been passed.

care or duty of loyalty to offer Hyundai Motor the opportunity to subscribe to Hyundai Glovis shares when it was established. Thus CEO Chung Mongkoo did not unfairly seize or usurp the Hyundai Motor Group's business opportunity. The considerations behind the court's decision were: (i) While Hyundai Glovis's distribution services were related to Hyundai Motor Group's manufacture and sales, an automobile company does not have to conduct its own distribution or establish a subsidiary for its distribution – this is a business judgment decision and thus whether to establish an internal business unit, establish a subsidiary or outsource it to another company is fundamentally at the discretion of the company's business judgment; (ii) the decision to establish Hyundai Glovis started with the desire to effectively manage distribution services of all the Hyundai Motor Group's affiliates, the direct trigger for which was CEO Chung Mongkoo's order; and (iii) employees of Hyundai Motor Group's affiliates, not just those of Hyundai Motor itself, worked to establish and advance Hyundai Glovis, and Hyundai Glovis also serves Hyundai Motor Group's affiliates, including Kia Motors Corporation, Hyundai Mobis, and Hyundai Steel Company.

Although the court did not rule that CEO Chung Mongkoo had usurped Hyundai Motor Group's business opportunity, it did find that by unfairly raising freight charges to be paid to Hyundai Glovis, a loss of approximately KRW 14.3 billion was caused to Hyundai Motor. Further, the KFTC imposed KRW 4.7 billion penalty for these illegal actions, resulting in a loss totaling KRW 19 billion by Hyundai Motor. Taking the overall circumstance into consideration,[14] CEO Chung Mongkoo's liability was limited to 90% of the loss (about KRW 17.1 billion).[15] CEO Chung Mongkoo and the minority shareholders all waived their right to appeal. The litigation concluded when Solidarity for Economic Reform and CEO Chung Mongkoo mutually agreed that he would divest his interest in

[14] The Korean Court rules that "when the director has liability for damages from violating laws, decrees, regulations or articles of associations, neglecting duties, then the amount of damages can be limited, according to the ideology of indemnification for damages, equity in apportionment of damages, taking every circumstance into consideration, including but not limited to content and nature of the business, how the director has violated due process, the form of director's violation of duties, objective circumstances or degree on company's damages and expansion, director's contribution to the company, director's profit from violation of duties, lack of organizational system in the company or risk management. (Supreme Court of Korea, No. 2002 Da 60467, 60474, December 10, 2004, Supreme Court of Korea, No. 2003 Da 69638, October 28, 2005, Supreme Court of Korea, No. 2005 Da 34797, September 21, 2007, Supreme Court of Korea, No. 2006 Da 33333, October 11, 2007, etc.)

[15] In the above case, illegal supporting actions to Hyundai Mobis Co., Ltd., Kia Motors Corporation was also an issue, which is irrelevant to the subject of this article. When considering these issues, the total amount of damages was up to KRW 185.8 billion, and as a result, the total amount of damages CEO Jeong Mongkoo had to bear was KRW 82.6 billion.

Hyundai Glovis within a reasonable period of time, with the aim of avoiding any further controversy around the issue.[16]

III. THE NEW COMMERCIAL CODE

Korea amended its Commercial Code (the "KCC" or the "Code") as of April 14, 2011.[17] The amendment inserted Article 397-2, which expressly adopted the corporate opportunity doctrine. The newly inserted Article 397-2 reads as follows:[18]

KCC Article 397-2 (Prohibition against Appropriation of Company's Opportunities and Assets)

(1) No director shall use any business opportunity of the company which corresponds to any of the following subparagraphs and may be of present or future benefit to the company, for his/her own account or for the account of a third party, without the approval of the board of directors. In such cases, the approval of the board of directors shall be granted with two thirds or more of the total number of directors;

1. A business opportunity which has become known to the director in the course of performing his/her duty, or a business opportunity taking advantage of information of the company;

2. A business opportunity closely related to the business that is being currently conducted or is to be conducted by the company;

---

16 After such a settlement had been reached, Jeong Mongkoo paid out or sold some of his Shares in Hyundai Glovis as damages, donated some of the shares to Hyundai Motor Jeong Mongkoo Foundation. As of now, Jeong Uiseon owns 31.88%, Jeong Mongkoo owns 11.51%, Hyundai Motor owns 4.88%, Hyundai Motor Jeong Mongkoo Foundation owns 4.46% of Hyundai Glovis' shares.

17 The newly amended KCC came into effect on April 14, 2012.

18 Article 397-2 is very much like the U.S. American Law Institute's Principles of Corporate Governance: Analysis and Recommendations ('ALI principle') and its relevant rules. KCC, its case law and interpretation has developed in a way to incorporate laws regarding Anglo-American liability of a director. The new insertion of Article 397-2 in the KCC could be seen as a continuation of such tendency in KCC.

(2) A director who has violated paragraph (1) and thereby incurred damage to the company and the director who approved the same shall be jointly and severally liable for compensation of the damage; and the benefit earned by the director or a third party from the violation shall be presumed to be the damage suffered by the company.

The legislative process to adopt corporate opportunity doctrine amendment was controversial.[19] Some felt the legislation was superfluous, since the appropriation of a corporate opportunity can be theoretically covered by existing articles of the Code, particularly those related to a director's duty of loyalty, a director's prohibition against competitive business (Article 397 paragraph 1) or a director's prohibition against self-dealing transactions (Article 398), derived from Article 382-3, which regulates director's duty of loyalty.[20] Others argued that ambiguities in the new legislation could lead to excessive lawsuits, discourage CEOs from pursuing innovative business opportunities and have negative effects on social welfare.[21] On the other hand, supporters the legislation pointed to the practical difficulties of holding directors responsible under a provision on the general duty of loyalty, and the fact that in Korea many corporate opportunity appropriation cases are not based on directors' prohibited operation of competing businesses or self-dealing transactions. They argued that an explicit provision for the corporate opportunity doctrine was necessary to

[19] The newly inserted corporate opportunity doctrine was one of the three major issues for the Ministry of Justice in the legislative process along with double derivative suits and executive director legislation. As the issue was so significant for the Ministry of Justice, it was the subject of a public debate in the Commercial Code Issue Mediation Committee. Koo Seungmo, "Legislative Process in Corporate law of the Commercial Code and Tasks to be solved", Advanced Commercial Law review Serial Number 55 (2011. 7), Ministry of Justice, p. 115.

[20] In the above Hyundai Motor Case, the court also acknowledged that the concept 'appropriation of corporate opportunity' could be derived from existing KCC's concepts, duty of good manager's due care or duty of loyalty.

[21] Legal professionals and scholars who are against the legislation are as follows. Choi Junseon, "The Doctrine of Corporate Opportunity", Justice Vol. 95 (2006), Choi Wanjin, "Articles : Critical Observation of the Commercial Law Draft Revision", Business Administration and Law Vol.17(2) (2007), , Kim Jeongho, "The Doctrine of Corporate Opportunity", Business Administration and Law Vol.17(2) (2007), Jae Yeol Kwon, Paik Jeongung , Lee Seungcheol, "2007 Winter Seminar : Papers ; Corporate Opportunity Doctrine - A Comparative Law Analysis of a Compromise Reform Proposal on the Commercial Code -", Commercial Law Review Vol.25(4) (2007), Korea Listed Companies Association, "Review on the amended Commercial Law", (Member Lee Sangmin of the Assembly, submit the bill as a representative: Bill Number 3753).

clarify the substantive and procedural applicability as well as liability for violation.[22]

The Korean Ministry of Justice initially announced that the corporate opportunity doctrine would be adopted only as a declaratory article, providing that "No director shall use any business opportunity of the company that may be of present or future benefit to the company, for his/her own account or for the account of a third party." However when submitted to the National Assembly, the concept of a business opportunity was materialized and amended only in the case of director's appropriation of the business opportunity through engaging in self-dealing transactions.[23] During the course of the legislative process, some members of the National Assembly argued that a powerful regulation by law was necessary. Six amendments to the bill were proposed, including one that would have expanded the range of applicability not only to directors but also to major shareholders and related persons, adopting a right of intervention in appropriation of corporate opportunity cases, which is acknowledged in the prohibition against a director's operation of competitive business (KCC Article 397 paragraph 2).[24] Eventually, an agreement was reached to insert new Article 397-2 as stated above. Such a complicated legislative history shows how sensitive the public opinion was regarding the incorporation of the corporate opportunity doctrine into law.[25] However, it also reveals that consensus on the content or legal nature of the

[22] Legal professionals and scholars who are for the legislation are as follows. Lim Jaeyeon, "The Doctrine of Corporate Opportunity", Human Rights and Justice Vol. 363 (2006), Jeong Woong Baik, "Articles : The U.S. Corporate Opportunity Doctrine and the Korea Commercial Code- Focused on the case of Guth in Delaware: Guth v. Loft, Inc., 23 Del, Ch. 255, 5 A.2d 503 (Del, 1939)", Commercial Law Review Vol.25(3) (2006), Kwon Sunhui, "Theoretical Review on Commercial Law newly inserted Article 398-3(Doctrine of Corporate Opportunity)", Commercial Law Review Vol.26(3) (2007).

[23] For appropriation of corporate opportunity that is not classified as self-dealing transaction, Article 382-3 duty of loyalty by directors applies.

[24] KCC Article 397 (1) No director shall, without the approval of the board of directors, engage in for his/her own account or for the account of a third party any transaction in the same line of business of the company or become an unlimited liability member or a director of any other company, the business purposes of which are the same as those of the company. (2) If any director has engaged in a transaction for his/her own account in contravention of paragraph (1), the company and if he/she has made a transaction for the account of a third party, the company may request the pertinent director to transfer any interest accrued therefrom. (3) Rights under paragraph (2) shall be extinct upon the lapse of one year after the date such transaction has been made.

[25] Chun Gyeonghun, "How to Interpret New Regulations on Appropriation of Corporate Opportunity under the Recent Amendment to the Korean", Corporate Private Law Review Vol. 30 Serial Number 2 (2011. 8), p. 145.

corporate opportunity doctrine has not yet been clearly or consistently formed in Korea.[26]

It must be noted that unlike the prohibition on the appropriation of corporate opportunity theory in the U.S., Korea adopted its corporate opportunity doctrine to regulate the conglomerates' so called "Funneling of Business".[27] As discussed above, major civic groups in Korea have continuously raised the issue of the transfer of wealth to controlling shareholders and their related persons through the so called "Funneling of Business" by conglomerates' affiliates and opposed such practice as a suspected case of the usurpation of corporate opportunities. This likely influenced the adoption of Article 372-2. This is also reflected in the Review Report by the Legislation and Judiciary Committee on the proposed amendment of the KCC submitted to the National Assembly. The Review Report points to the Hyundai Motor Case, stating that "[r]ecently a number of representative directors or controlling shareholders have usurped business opportunities to reinforce their control over the company or transfer their management control. However it is difficult to regulate these transactions through existing regulations such as duty of loyalty or prohibition against self-dealing transactions by directors." According to the Review Report, in order to regulate these types of transactions, a provision incorporating the corporate opportunity doctrine is needed.[28]

IV. THE U.S. LAW

Because the origins of the corporate opportunity doctrine can be traced back to case law developed under the United States legal regime, most scholars would agree that a study of Korean Commercial Code Article 397-2 and the concept of a "business opportunity" thereunder should begin with a survey of the U.S. doctrine. This is especially true considering the Korean doctrine is understood to have adopted the American Law Institute's defining principles on the corporate opportunity doctrine.[29] Consequently, preceding our analysis of

[26] Some scholars argue that, in Korea, there are only discussions about the "need" to regulate director's appropriation of corporate opportunity, although not even a consensus is reached specifically on what corporate opportunity is, what kind of liability shall be charged through which standards. Kim Hong-Ki, "Corporate Opportunity Doctrine and it`s Implication for the Interpretation and Regulations in Korea", Commercial Law Case Review Vol. 21(2) (2008.6.), p. 101.

[27] Kim Hwa-Jin, Corporate Finance and Governance, 2nd ed. (Seoul : PYBooks, 2012), p. 322.

[28] The Legislation and Judiciary Committee, *Commercial Act Proposed Amendment (introduced by the Government) Review Report (Corporate law)* (2008. 11), p. 150 et seq.

[29] American Law Institute, Principles of Corporate Governance: Analysis and

Korean Commercial Code Article 397-2, this section provides a look at the history and formulation of the corporate opportunity doctrine in the United States. The state of Delaware is the dominant jurisdiction for corporations in the United States, and as such the focus is on the development of Delaware case law.

A. History of the Corporate Opportunity Doctrine in the United States

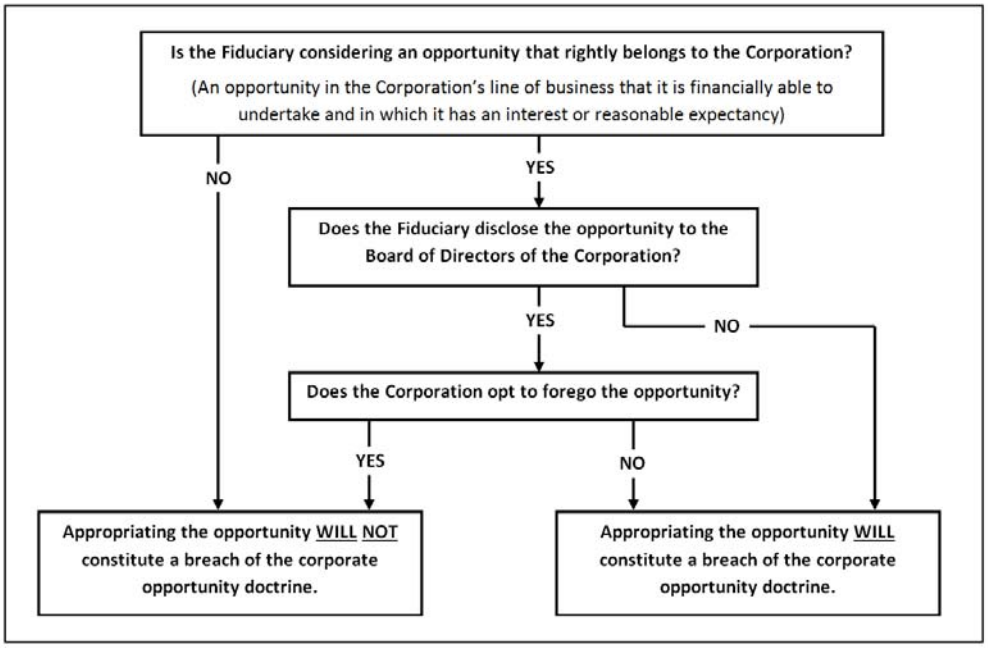
The classic statement of the corporate opportunity doctrine is set forth in *Guth v. Loft*,[30] a case decided in 1939 by the Delaware Supreme Court (discussed further below). The doctrine is a logical extension of the duty of loyalty, one of the oldest and most basic fiduciary principles. The fiduciary duty of loyalty states that one who undertakes to act on behalf of another must not place his own interests ahead of the interests of his principal; a concept that can be traced back more than eight centuries and is found in many of the earliest written codes of law.[31]

While the duty of loyalty can be stated succinctly and is widely held to be a foundational principle in many areas of law, applying the principle to a set of facts has proven to often be complicated and controversial—this has been especially true of the corporate opportunity doctrine. A reading of the opinions in *Guth* and subsequent corporate opportunity cases show a judiciary that has struggled to create a standard for the straightforward application of doctrine to facts, and in the process has created a complex body of tests, factors and case law precedent. Before exploring the path the doctrine has taken through judicial inquiry and analysis over the past 70 years, it is helpful to understand its basic framework; the simplified illustration below shows the basic steps in determining whether taking a business opportunity may constitute a breach of the corporate opportunity doctrine under U.S. law:

Recommendations, Section 5.05(b).

[30] 5 A.2d 503, 510-11 (Del. 1939).

[31] See, e.g., Hammurabi's Code of Laws; The Great Qing Code



B. The Evolution of Case Law

Application of the corporate opportunity doctrine in Delaware generally begins with a statement of the doctrine from *Guth v. Loft*. In *Guth*, the president and director of Loft Incorporated (a candy, syrup and foods manufacturer) acquired a controlling interest in the Pepsi-Cola Corporation and began secretly using the resources of Loft to support Pepsi's operations. Loft sued Guth, alleging that Guth had an obligation, as the president and a director) to offer the opportunity to acquire the interest in Pepsi to Loft. The court found in favor of Loft, and the Delaware Supreme Court has since stated:

> The rule of the *Guth* case is that when there is presented to a corporate officer a business opportunity which the corporation is financially able to undertake, and which, by its nature, falls into the line of the corporation's business and is of practical advantage to it, or is an opportunity in which the corporation has an actual or expectant interest [(respectively, the "line of business" test and the "interest or expectancy" test)], the officer is prohibited from permitting his self-interest to be brought into conflict with the

> corporation's interest and may not take the opportunity for himself.[32]

The court also observed that the prohibition against corporate officers and directors using their position of trust and confidence to further their private interests is essentially public policy; it is derived from a profound knowledge of human characteristics and is merely one of the manifestations of the general duties of loyalty and good faith.[33] The court foresaw the application problems that would arise in the following decades as the judiciary struggled to apply the *Guth* rule and to adapt it to factual scenarios, stating "[t]he occasions for the determination of honesty, good faith and loyal conduct are many and varied, and no hard and fast rule can be formulated. The standard of loyalty is measured by no fixed scale."[34]

Johnston v. Greene came before the Delaware Supreme Court 17 years later, and presented a more complex set of facts.[35] The director who was offered the opportunity was involved in the management of many similar businesses (each of which plausibly had an interest in the offer), and received the offer in his individual capacity rather than as a director of any corporation (the offeror was not aware of his affiliations). Furthermore, the Court found that the key corporation in question had no well-defined "line of business." Though the court stated it was applying the *Guth* rule it focused almost exclusively on the line-of-business test, and found the fact that the director received the offer in his personal capacity to be highly relevant. The court held that where an officer receives an offer in his individual capacity, a much stricter standard should be applied to determine if the opportunity is one to which the corporation is entitled. Essentially, in such a scenario the opportunity must be shown to be vital to the corporation or one to which it has a specific interest or expectancy. The court also repeatedly referenced "fairness" in the analysis, stating that "whether an opportunity is corporate or personal depends on the facts—upon the existence of special circumstances that would make it unfair for the director or officer to take the opportunity for himself.[36] *Johnston* presents an especially difficult question for the line-of-business test, as a finding that the director took a corporate opportunity raises the challenge of determining which of the corporations the

[32] Equity Corp. v. Milton, 221 A.2d 494, 497 (Del. 1966).

[33] *Supra*, 5 A.2d 503, 510.

[34] *Id*.

[35] Johnston v. Greene, 121 A.2d 919 (Del. 1956).

[36] *Id.*, at 924.

opportunity would belong to—likely pushing the court to employ a fact-based fairness analysis.

In 1971, the Delaware Supreme Court identified two additional factors in *Kaplan v. Fenton* that it found relevant in affirming the Delaware circuit court's holding that a director had not usurped a corporate opportunity.[37] In *Kaplan*, the director purchased shares in a corporation for his own account, but only after (i) a similar offer was rejected by the board of the corporation months before and (ii) the director disclosed the second offer to the CEO of the corporation and asked him if it should be presented to the entire board (the CEO said that it should not). In the opinion, the Delaware Supreme Court found both of these events to be relevant to their analysis and to their findings that (i) the offer was not one in which the corporation has an interest (as it had been expressly disclaimed), (ii) it was not an opportunity that was essential to the Corporation and (iii) it was not one in which the corporation's resources had been improperly put to use.

Science Accessories Corp. v. Summagraphics Corp., decided by the Delaware Supreme Court in 1980, demonstrates the ongoing struggle in the application of the corporate opportunity doctrine, now interpreting the *Guth* and *Johnston* standard as a straightforward three-prong analysis: "[An] officer may not seize the opportunity for his own if: (a) the corporation is financially able to undertake it; (b) it is within the corporation's line of business; (c) the corporation is interested in the opportunity.[38] Furthermore, the facts in *Science Accessories* caused the court to consider the doctrine alongside a competing public interest, the "policy recognized by the courts . . . of safeguarding society's interest in fostering free and vigorous competition in the economic sphere."[39] The court, citing the Restatement of Torts, concluded that "while an agent may not put himself in a position antagonistic to his principal, an agent is not thereby prevented from acting in good faith outside his employment even though it may adversely affect his principal's business," and further may "make arrangements or plans to go into competition with his principal before terminating his agency, provided no unfair acts are committed or injury done his principal."[40]

Broz v. Cellular Information Systems later incorporated this balancing consideration into the corporate opportunity doctrine test by adding a fourth prong: Does an officer or director create a conflict between his self-interest and

[37] Kaplan v. Fenton, 278 A.2d 834 (Del. 1971).

[38] Science Accessories Corp. v. Summagraphics Corp., 425 A.2d 957, 963 (Del. 1980).

[39] *Id*.

[40] *Id.*, at 962, citing *Restatement (Second) of Agency* § 387, Comments b and e (1957).

the interests of the corporation by taking the opportunity for himself?[41] Again however, applying *Broz* in a later case, the court has emphasized that "no single factor is dispositive . . . [i]nstead the Court must balance all factors as they apply to a particular case."[42] Broz is also important for its consideration of the requirement that an opportunity be presented to the board before it is usurped (discussed further below).

C. Presentment of Opportunity to the Corporation as a Safe Harbor

In *Broz,* Robert Broz was a director of Cellular Information Systems (CIS) and also the sole shareholder of RFB Cellular. The suit was brought when RFB Cellular purchased a cellular license over a bid (presented to Broz in his capacity as the owner of RFB) by Price Cellular, a company that was simultaneously attempting to acquire CIS. Price Cellular brought suit in the name of CIS, alleging that Broz usurped a corporate opportunity of CIS and that he had a duty to Price Cellular since they were trying to acquire CIS. Broz argued that his duty was only to CIS, and that CIS was unable to purchase the license because it was undergoing a Chapter 11 reorganization and selling the cellular licenses it did have. Broz did not take steps to hide the transaction from CIS and discussed the opportunity with a number of CIS officers and directors individually. He took the position that formal presentation of the opportunity to the board was unnecessary since the company was in no position financially to take advantage of the opportunity (among other reasons). Although the Delaware Chancery Court held that Broz had usurped an opportunity rightfully belonging to CIS, the Delaware Supreme Court overturned the decision, holding that no single factor is dispositive and formal presentment to the board is not strictly necessary.[43] The court went on to state, however, that where a director or officer does take the step of formal presentment, he may enjoy the protection of a safe harbor and will be free from the danger of later being found to have usurped an opportunity since the board has disclaimed it.

Cases following *Broz* have reaffirmed the safe harbor, holding that where the corporation had a clear interest in the opportunity, a director or officer who chooses not to formally present the opportunity to the board "acts at his peril, unless he is ultimately able to demonstrate post hoc that the corporation was not deprived of an opportunity in which it had an interest in or capability of

[41] Broz v. Cellular Info Sys. 673 A.2d 148, 154 (Del. 1996).

[42] Beam ex rel. Martha Stewart Living Omnimedia, Inc. v. Stewart, 833 A.2d 961, 972 (Del.Ch.2003).

[43] *Supra,* at note 39, 158.

engaging."[44] In *Telxon Corp. v. Meyerson*, the court held that the safe harbor applied only where the opportunity was presented to the board of directors; where a director presented an opportunity to an officer of the corporation (in this case, the CEO) who considered and rejected the offer, the protections of the safe harbor were not available because approving or rejecting a corporate opportunity is a decision that correctly lies with the corporation's board of directors.[45]

V. DISCUSSION AND ANALYSIS

A. Corporate Opportunity Doctrine and the "Funneling of Business"

As discussed above, KCC Article 397-2 is recognized as a tool to regulate the so-called "Funneling of Business," which is often used to increase or transfer the wealth of controlling shareholder-managers. However, there are fundamental doubts about whether the corporate opportunity doctrine applies to the "Funneling of Business." Whether a company transfers its existing business activities to a third party, or consigns its necessary existing business (or changes its consignee to another party) is at the discretion of the company (i.e., it is a choice of 'allocation of business activities').[46] Therefore it is difficult to consider "Funneling of Business" as a new corporate opportunity. A corporate opportunity should be distinguishable from the company's existing business. The "Funneling of Business" is not so much a matter of corporate opportunity, as it is a choice between internalizing or outsourcing its existing business; when outsourced, the question is how and to whom to outsource. In other words, while possibly considered as a corporate opportunity for the company receiving the business, outsourcing part of an existing business cannot be seen as a corporate opportunity, since an opportunity created by the company's active conduct using its existing business is not deemed to be a corporate opportunity.[47]

Hyundai Motor has been outsourcing its non-core businesses, including distribution, since well before Hyundai Glovis was established. The distribution

---

[44] Thorpe v. CERBCO, Inc., 676 A.2d 436, 442 n. 7 (Del. 1996).

[45] Telxon Corp. v. Meyerson, 802 A.2d 257, 263 (Del. 2002).

[46] Stephen J. Choi/Eric L. Talley, "Playing Favorites with Shareholders," 75 Southern California Law Review 271(2002), pp. 305~307.

[47] According to U.S. Law, appropriation of corporate opportunity is limited to opportunities from outside, that is opportunities created by a third parties or that arise from the company's existing business. It is not an opportunity created by the company's active conduct using its existing business. However, since the KCC Article 397-2 has a broad definition on corporate opportunity, there is a strong argument that in Korea, Article 397-2 can be applied to the so called "Funneling of Business" in the Hyundai Motor Case. Chun Gyeonghun, *op. cit*., p. 200, Koo Seungmo, *op. cit*., p. 125.

business was previously outsourced to Dongsuh Dynasty Co. Ltd. and SungWoo Corporation. The efficiency and customer service issues that characterized those business arrangements led the management of Hyundai Motor to conclude that it was necessary to establish an affiliate specializing in distribution, and Hyundai Glovis was born. The initial decision to outsource Hyundai Motor's distribution needs to a non-affiliated company is a typical business decision falling under the business judgment rule.[48] Furthermore, the business judgment rule also applies to the decision to internalize a function, or establish an affiliate to meet business needs. In the Hyundai Motor Case, no questions were raised about the outsourcing of distribution to other companies before the establishment of Hyundai Glovis. However, civic groups and shareholders vocalized series concerns when Hyundai Motor began to direct that business to a firm controlled by the chairman and his son.[49] Thus, the point of contention regarding the "Funneling of Business" in Korea is not on the funneling itself, but to whom the business is funneled and whether it is done on terms that are fair and negotiated at arm's length.

As discussed above, the company's existing business and the opportunities related to it could be opportunities for a third party, but it is not an "corporate opportunity" for the company. Therefore it is fundamentally not an issue of corporate opportunity. In Korea, cases that are scrutinized as potential "Funneling of Business" cases mostly involve, (i) issues on scope of applicability of the prohibition on self-dealing transactions from the perspective of corporate law,[50] (ii) issues regarding the wealth acquired by controlling shareholders through "Funneling of Business" from the perspective of tax law, (iii) illegal supporting actions from the perspective of the anti-trust law. Thus it is appropriate to resolve these issues under those applicable laws. The KCC, as amended as of April 14, 2011, tightened its regulations on self-dealing transactions (KCC Article 398[51]). Not only are transactions between a director and the Company regulated,

[48] The above reviewed Hyundai Motor Case (Seoul Central District Court No. 2008 GaHab 47881, February 25, 2011) clearly points out these points.

[49] People's Solidarity for Participatory Democracy Economic Reform Research Institute, *op. cit.*. Such arguments seem to be even clearer since, according to the Report, nearly all of the cases that are doubtful to have usurped corporate opportunity are almost, without exception, cases regarding mega transactions of a company's existing business part between a company and a company where controlling shareholders' families have significant shares.

[50] The regulation of self-dealing transactions emphasizes 'fairness", while the regulation of appropriation of corporate opportunity emphasizes 'disclosure'. E. G. Orlinsky & G. J. Benoit, *The Treacherous State of Director and Officer Conflicts of Interest*, 37 Maryland Bar Journal 36, 38 (2004).

[51] KCC Article 398 (Transactions between Directors, etc. and Company): When a person falling under any of the following subparagraphs intends to engage in a transaction with the company for his/her own account or for the account of a third party, he/she shall in advance

but transactions between the Company and its major shareholders, their spouses or relatives and affiliated companies within a certain range are also regulated. According to the amended Inheritance Tax and Gift Tax Act, for corporations whose total turnover to a specially related corporation (the "Beneficiary Corporation") is more than 30% of all its turnover, the controlling shareholders and their spouse and relatives (having more than 3% of company's shares) are presumed to reap the company's business profits as their own,[52] and gift tax is imposed on these profits (Korean Inheritance Tax and Gift Tax Act Article 45-3 and its Enforcement Decree 34-2). The Monopoly Regulation and Fair Trade Act prohibits "Assisting a specially related person or companies by providing advanced payment, loans, manpower, immovable assets, securities, goods, services, right on intangible properties, etc. at significantly higher or lower rates and thus providing excessive economic benefit" and imposes regulatory measures such as penalty surcharges, corrective measures and criminal punishment (Monopoly Regulation and Fair Trade Act Article 23 paragraph 1 subparagraph 7, Article 24, Article 24-2, Article 68 subparagraph 2 and its Enforcement Decree attached Table 1-2).

In conclusion, "Funneling of Business" is fundamentally not related to appropriation of corporate opportunity; insofar as the legislative intention behind KCC Article 397-2 was to address the funneling problem, it has been flawed from its inception.

B. Drawbacks within the KCC 397-2

---

disclose material facts of the relevant transaction at the board of directors and shall obtain approval therefrom. In such cases, the approval of the board of directors shall be granted with two thirds or more of the total number of the directors, and the relevant transaction shall be fair in terms of its particulars and procedures: 1. A director or a major shareholder under Article 542-8(2)6; 2. The spouse and lineal ascendants or descendants of a person falling under subparagraph 1; 3. Lineal ascendants or descendants of the spouse of a person falling under subparagraph 1; 4. A company in which a half or more of the total number of issued and outstanding shares with voting rights is held by a person falling under any of subparagraph 1 through 3, solely or jointly with others, or its subsidiary company; 5. A company in which a half or more of the total number of issued and outstanding shares with voting rights is held by a person falling under any of subparagraph 1 through 3, together with a company falling under subparagraph 4.

[52] Gift Tax presumption is calculated as follows: after-tax business profit of Beneficiary Corporation X (Transaction rate with specially related corporation – 30%) X (percentage of share ownership – 3%).

Apart from the issue of whether the new Code provision should apply to the fact pattern in the Hyundai Motor Case, the doctrine as adopted has inherent drawbacks, which we discuss below.[53]

1. The Ambiguity of the Meaning of 'Corporate Opportunity'

KCC Article 397-2 (Prohibition against Appropriation of Company's Opportunities and Assets) specifies business opportunities that directors are prohibited from usurping as follows: "A business opportunity which has become known to the director in the course of performing his/her duty, or a business opportunity taking advantage of information of the company (subparagraph 1)" and "A business opportunity closely related to the business that is being currently conducted or is to be conducted by the company (subparagraph 2)." Such business opportunities, at the same time, must have "present or future benefit to the company." However it is difficult to determine whether a certain transaction falls under the scope of the "corporate opportunity" concept, since the article uses abstract terms such as "business opportunity", "future benefit to the company", "business that to be conducted by the company", "closely related to" and "taking advantage of".[54] One year after adoption, there are still not enough precedents or sufficient academic analysis on the corporate opportunity doctrine's specific meaning and requirements under the Code. Therefore, while discussions in U.S. must be looked to, the problem is that even in U.S., where corporate opportunity doctrine has been developed for the last 100 years, no precise definition has been truly settled on. Indeed, leading corporate law scholars in the U.S. continue to wrestle with the imprecise nature of the doctrine, even with the benefit of decades of analysis and case law.[55]

In Korea, theoretical attempts to specify business opportunities that cannot be usurped are based on principles of U.S. case law.[56] Most U.S. cases that recognized a director's liability based on his appropriation of corporate opportunity are either (1) self-dealing transactions in a vertical relationship: where

---

[53] Sketched originally in B. S. Moon & Kim Hwa-Jin Kim, "Corporate Opportunity Doctrine in the Draft New Commercial Code," Corporate Governance Review Vol. 30 (2007), pp.15~35, 30~33; Kim, Hwa-Jin, *op cit*, pp. 326~329.

[54] Of course, subparagraph 1 seems to be clearer in a way that it can be read as information obtained at company's costs. However, subparagraph 2 "closely related to the business" is a very vague concept.

[55] *See, e.g.*, Stephen Bainbridge, *Rethinking Delaware's Corporate Opportunity Doctrine, Research Paper No. 08-17*, UCLA School of Law - Law & Economics Research Paper Series (2008).

[56] Chun Gyeonghun, *op. cit*., pp. 162~182.

there is a (material supply, purchase, sale, etc.) transaction between the director and the company, when the director usurps the corporate opportunity (such as the *Guth* case, discussed above), (2) competitive business (horizontal relationship) scenarios: where a director's business is in competition with the company's business (such as the *Broz* case, discussed above). Accordingly, it is difficult to apply the doctrine to a business opportunity without a vertical or horizontal relationship, even in a broad sense. (Theory A). On the other hand, some argue that the standard applied by the Korean Supreme Court in the Hyundai Motor Case, restricting the scope of business opportunity to "realistically existing specific business opportunities", is reasonable, because it relieves businesses' anxiety over the unsettled standard and achieved legal stability, at least until a clear application of the KCC Article 397-2 is established (Theory B).[57]

Theory A is useful in the sense that it implies that appropriations of corporate opportunity mainly exist where there is a "close relationship" to the business of a corporation because of a "competitive business relationship" or "self-dealing relationship".[58] Nevertheless, it still does not clearly define any standards on what a corporate opportunity is.[59] Theory B is criticized on the basis that there are no grounds to restrict business opportunity to "realistically existing specific business opportunities" anymore, after the newly amended KCC came into effect. The standard the Korean Supreme Court applied in the Hyundai Motor Case was only reasonable since at the time of the judgment there was no explicit article regarding corporate opportunity, so that business opportunity could only be derived from director's duty of loyalty.[60]

[57] Choi Junsun, "Commentary on the amended Corporate Law 2011" (2011), pp. 128~129, Shin Heungcheol, "Main Contents of the amended Commercial Code and Business Actions Seminar Sourcebook", Korea Chamber of Commerce and Industry, p. 16, Park Sun Jong, "Appropriation of Corporate Opportunity under the Revised Commercial Code", Han Yang Law Vol. 22(2) (2011), p. 255.

[58] However, the above theory raises the question whether, even without the new Article on corporate opportunity, the same result could have been achieved by supplementing KCC Article 397 Prohibition against Competition or Article 398 Self-Dealing Transaction.

[59] Even according to the theory, since KCC Article 397-2 defines "corporate opportunity" very comprehensively, there are rarely cases where corporate opportunity may not be found under Article 397-2. Furthermore, it is the aim of the amended KCC not to block any attempt to apply Article 397-2 due to the comprehensive non-formal nature of corporate opportunity itself. Applying Article 397-2 in individual cases is a separate question, though.

[60] Koo Seungmo, *op. cit*., p. 125, Chun Gyeonghun, *op. cit*., p. 181, Lee Eonju, "Main Contents of the amended Commercial Code and Business Actions Seminar Discussion Paper", Korea Chamber of Commerce and Industry (2011. 5. 26.), p.3.

Therefore, as there is no distinct standard under the law (or accepted theories or case law on the question) as to what constitutes a "corporate opportunity", there is concern that the court could arbitrarily apply the corporate opportunity doctrine.[61] Furthermore, such an ambiguity may not only prevent Article 397-2 from functioning as a standard norm for future action, but also induce risk aversion,[62] impose unnecessary burdens on companies, and repress entrepreneurial spirit. The theory of corporate opportunity has the competitive benefit of preventing appropriation of corporate opportunities by directors or fiduciaries, but by the same token has the drawback of potentially interfering with the establishment of new businesses.[63] A balanced solution is required that accounts for both impacts of the doctrine. This is a difficult and nuanced question; indeed, in the U.S. the courts wrestled with this issue in the 1980's in *Science Accessories* and *Broz*, recognizing that public policy interests in allowing free competition. U.S. law employs fiduciary principles to deal with the issue by allowing agents to plan and develop new enterprises while in the employ of another, so long as the agent acts in good faith and such undertakings do not put the agent in a position antagonistic to his principal. As discussed above, the *Broz* case incorporated this issue into its corporate opportunity doctrine elements,

[61] Kim Hwa-Jin, *op. cit*., p.327.

[62] According to KCC Article 400 paragraph 2, "A company may, in accordance with its articles of incorporation, absolve the liability of a director under Article 399 with respect to the amount exceeding six times (in cases of outside directors, three times) his/her remuneration (including bonuses and the profit from exercise of stock option) for the latest on year prior to the date of the act or misconduct of the director.", however liability of a director is strictly regulated since according to the KCC Article 397-2, the liability of a director cannot be absolved, furthermore according to KCC Article 397-2 paragraph 2, "the benefit eared by the director or a third party from the violation shall be presumed to be the damage suffered by the company" (Since it is presumed (not deemed), there is still a chance to disprove the fact. Nevertheless the director has to prove that the company would have had less profit if it had such an opportunity, and that is very hard to prove for the director). Moreover, according to the Korean Criminal Act Article 355, 356, "A person administering another's business, obtains pecuniary advantage or causes a third person to do so from another in violation of ones duty, thereby causing loss to such person, shall be punished by imprisonment for not more than ten years or by a fine not exceeding thirty million won.", and the Supreme Court of Korea broadly interprets "in violation of ones duty" as "including any act that loses trust to a person, from not acting in trust and good faith, which is expected to be done or not to be done, according to the relevant contents, nature, detailed circumstances of the business." (Supreme Court of Korea, No. 94 Do 902, September 9, 1994) Therefore directors should consider the danger of a criminal penalty resulting from the appropriation of a corporate opportunity. There are discussions in Korea against punishing a director for crime of misappropriation. See Lee Jongsang, "A Critical Review on liability of director and crime of misappropriation", Business Finance Law Vol. 19. (2006. 9), pp. 44~64.

[63] Choi Junsun, *op. cit*., p. 124.

considering whether the agent's actions create a conflict with the interests of his principle.[64]

2. **The Meaning of "director who approved" According to KCC Article 397-3 paragraph 2**

The KCC Article 397-2 paragraph 2 states that "A director who has violated paragraph (1) and thereby incurred damage to the company and the director who approved the same shall be jointly and severally liable for compensation of the damage", and since paragraph 1 states that "in order to use any business opportunity of the company, an approval of the board of directors (by two thirds or more of the total number of directors) is required", it seems to be clear that "a director who has violated paragraph (1)" is a director that usurped corporate opportunity without the approval of the board of directors. But who is "director who approved" referring to? If there was approval of the directors, then it would mean that at least there was no breach of paragraph (1); the provisions do not seem to be coherently integrated. There are two main interpretations of the contradicting provisions: (i) the first is that the above phrase only applies to directors whose approval has violated their duty of good manager's due care, and as a result approved the appropriation of corporate opportunity (Theory I);[65] and (ii) the second is that the "director who approved" refers to a director who gave a personal or de facto approval (which abets, aids, or supports) with a knowledge of the appropriation of corporate opportunity and without the formal approval of the board of directors (Theory II).[66]

Both theories do not entirely resolve the contradiction of KCC Article 397-2 paragraph 2. According to Theory I, directors whose approval had violated their duty of good manager's due care could be regulated by the violation of their duty of good manager's due care itself, so that there is not really a need to provide an independent Article 397-2. Furthermore it is unreasonable that a director who actively usurped corporate opportunity and a director who only approved the process face the same liability. According to Theory II, it doesn't seem to be abnormal to interpret the "approval" in paragraph 1 and paragraph 2 differently.

[64] *Supra*, n. 39.

[65] Chun Gyeonghun, *op. cit*., p. 205, Chang Jaeyeong/ Jung Junhyeok, "Prohibition of Appropriation of Corporate Opportunity according to the amended KCC", Business Finance Law Vol. 51. (2012), p. 52.

[66] Ko Changhyeon, "Main Contents of the amended Commercial Code and Business Actions Seminar Discussion Paper", Korea Chamber of Commerce and Industry (2011. 5. 26.), p.2, Kim Heecheol, "An Analysis of the Newly Enacted "Restriction of usurping corporate opportunity and assets" in the KCC", Judicial Officers, Vol. 660 (2011), p. 217.

Furthermore, if a director has usurped a corporate opportunity without the approval of the board of directors, then the director has violated KCC Article 397-2 paragraph 1 and directors who detected such an act must report it to the company and ask for corrective measures according to their inspection[67] or reporting obligations.[68]

The legislative intent is known to be driven by a motivation more closely related Theory I,[69] and Theory I is reasonable according to a textual interpretation. However, it nonetheless seems that KCC Article 397-2 paragraph 2 "director who approved" ought to be deleted, and directors who did not usurp a corporate opportunity to be liable only for violating their duty of good manager's due care.[70]

3. Liability of Approving Directors

Where a director pursues a corporate opportunity in the manner contemplated in Article 397-2 (the opportunity is reported to and approved by the board of directors) and the other directors approve the pursuit in violation of their duty of good manager's due care, it is counterintuitive for such a director did to face liability for his actions. According to the U.S. Model Business Corporation Act § 8.70. Business Opportunities, "(a) A director's taking advantage, directly or indirectly, of a business opportunity may not be the subject of equitable relief, or give rise to an award of damages or other sanctions against the director, in a

[67] According to the court, a director of a corporation not only has to approve or disapprove the agenda introduced in the board of directors, but is also obliged to inspect the overall business, including his/her business, other active director's business. Even a part-time director has such obligations (Supreme Court of Korea, No. 2005 Da 51471, December 11, 2008). "Inspection obligations could be different according to company's size, organization, business type, regulations, business conditions and financial standings, and in a highly divided and specialized company, it could be inevitable that a joint representative director and active director has its own specialized area to handle, but such circumstances cannot exempt directors from their inspection obligations, and in such a case each director of the board of directors has liability to construct reasonable information, reporting system and internal control system, and when there was not such an effort or when directors intentionally disregarded company's inspection or supervision although there was such a system, and as a result did not know the danger that directors had to care about including illegal improper business, then directors cannot escape from their liability for a reason that that they did not know the illegal or improper act of other directors, and if damages occur from continuous organizational carelessness of inspection, directors have liability for these damages occurred from other directors or officers." (Supreme Court of Korea, No. 2006 Da 68636, September 11, 2008).

[68] KCC 412-2 (Director's Duty of Reporting) If a director finds any fact that is likely to inflict a substantial loss on the company, he/she shall immediately report such to its auditors.

[69] Koo Seungmo, *op. cit*., p. 127.

[70] Chun Gyeonghun, *op. cit*., p. 205, Chang Jaeyeong/ Jung Junhyeok, *op. cit*., p. 52.

proceeding by or in the right of the corporation on the ground that such opportunity should have first been offered to the corporation, if before becoming legally obligated respecting the opportunity the director brings it to the attention of the corporation and: (1) action by qualified directors disclaiming the corporation's interest in the opportunity is taken in compliance with the procedures set forth in section 8.62, as if the decision being made concerned a director's conflicting interest transaction, or (2) shareholders' action disclaiming the corporation's interest in the opportunity is taken in compliance with the procedures set forth in section 8.63, as if the decision being made concerned a director's conflicting interest transaction; except that, rather than making ''required disclosure'' as defined in section 8.60, in each case the director shall have made prior disclosure to those acting on behalf of the corporation of all material facts concerning the business opportunity that are then known to the director. (b) In any proceeding seeking equitable relief or other remedies based upon an alleged improper taking advantage of a business opportunity by a director, the fact that the director did not employ the procedure described in subsection (a) before taking advantage of the opportunity shall not create an inference that the opportunity should have been first presented to the corporation or alter the burden of proof otherwise applicable to establish that the director breached a duty to the corporation in the circumstances." Nevertheless, many Korean scholars still argue that when the approval of other directors[71] violates the duty of good manager's due care, then the act usurping corporate opportunity itself is considered illegal, and the director who personally acted illegally shall be jointly and severally liable for the damage, since such compensation is based on post-benefit correction.[72]

It stands to reason that such a result is rather excessive where a director has reported the corporate opportunity to the company, has provided sufficient information for the board to determine whether to take the opportunity and has not exert any improper influence on other directors. Where there is potential liability that can arise despite a person's adherence to protocol, incentives to pursue or participate in a new business for directors will decrease, leaving only negative effects of the prohibition on appropriation of corporate opportunities. In other words, in practice, most of the business opportunities that may fall under scrutiny

[71] KCC Article 391 paragraph 3, Article 368 paragraph 4 states that "no person who has special interest in a resolution by a meeting of board of directors shall exercise his/her voting rights thereupon." Therefore, a director who is willing to use corporate opportunity shall not exercise his/her voting rights by a meeting of board of directors for approving appropriation of corporate opportunity.

[72] Chun Gyeonghun, *op. cit.*, p. 200, Choi Junseon, *op. cit.*, p. 126~127, Lee Cheolsong, 2011 Commentary on amended KCC (Seoul : PYBooks, 2012), p. 154, Jung Chanhyeong, "Contents and Assignments for 2011 amended Corporate Law", Seoul Bar Association/Korean Legal Center cohosted Symposium Questions about 2011 amended Corporate Law, p. 30.

will arise from the apt relationships and undertakings of the manager, and unless the law provides a safe harbor for the director, strict scrutiny is being imposed on director's entrepreneurial activities while failed business establishment (action of the board of directors) is being overlooked.[73] The focus of the corporate opportunity doctrine should be on the due process of law (regulating scope of providing information, contents of information and independence in the approval process by the board of directors).

4. Quorum for Resolution by Board of Directors

KCC Article 397-2 requires two thirds of the board of directors[74] to approve the taking of a corporate opportunity. The quorum requirement is stricter than the general quorum requirement under the KCC which requires a majority of the directors to be present at the meeting, and the affirmative votes of a simple majority of those present.[75] The stricter quorum is specially applied to resolutions approving self-dealing transactions and appropriations of corporate opportunities under the amended KCC. Such rules are uncommon elsewhere in the world, and there is no persuasive reason for increasing quorum for such resolutions only for the above two cases. In the U.S., a director or officer seeking to take an opportunity that may belong to the corporation does not require even a formal presentment to the board of directors;[76] if such a presentation is made, the board may vote on the matter but there is no special quorum requirement. The reasoning for requiring approval by the board of directors in corporate opportunity cases is to ensure the company is aware of the potentially beneficial opportunity so that it can decide whether to forego or pursue the opportunity –this is accomplished without the stricter quorum and approval requirements.[77]

Interestingly, where the board considers a resolution to override the prohibition against a director's ability to compete with the company (Article 397 paragraph 1), the general quorum for resolution by the board of directors is

[73] Kim Hwa-Jin, *op. cit*., p.326-327.

[74] When counting the total number of directors, directors who are willing to use corporate opportunity is excluded. As discussed above, such directors have special interest in a resolution by a meeting of the board of directors, so that such director shall not exercise his/her voting rights thereupon.

[75] KCC Article 391 paragraph 1, "A resolution of the board of directors shall be adopted in the presence of a majority of directors in office by the affirmative votes of a majority of directors present at the meeting: Provided, that the voting requirement may be increased by the articles of incorporation."

[76] *Supra*, n. 41.

[77] Park Sun Jong, *op. cit*., p. 250.

applied according to KCC 391 paragraph 1 (the majority of board must be present at the meeting and the affirmative votes of a majority of directors present must be obtained). However, operation of a competing business is much more likely to directly endanger the present existing business of the company, and a powerful right of intervention is adopted in case of the violation of the prohibition against competitive business, so that stricter liability is imposed compared to appropriation of corporate opportunity. Therefore, it is unbalanced to increase the quorum for a resolution by the board in the case of an appropriation of a corporate opportunity.[78] Furthermore, the increased affirmative vote requirement has the *de facto* effect of preventing any operating committees within the board of directors[79] from approving the resolution, often preventing rapid decision making.[80]

5. Outside Director Liability

The KCC imposes the same liability on inside and outside directors for appropriation of corporate opportunities. This is questionable logic considering there is a significant difference between directors who manage the company and outside directors in terms of the accessibility to internal information and the opportunity to divert property or resources of the company. Considering these differences, corporate opportunity regulations applicable to outside directors should be less stringent than those applicable to directors who manage the company.[81] In practice, ALI Principles of Corporate Governance in U.S. applies the "line of business test" to CEOs and "interest or expectancy test" to outside directors. There are also arguments in Korea that an outside director's liability should be restricted to the cases involving use of the company's information or assets closely related to current or future business.[82]

6. Defense on the Ground of Corporate Inability

As discussed above, in the U.S. a director or officer may take a corporate opportunity without consulting the board on the grounds that the company is unable to pursue the opportunity (usually for financial reasons). In any case,

---

78 Lee Cheolsong, Corporate Law 20th ed. (PYBooks. 2012), p. 730.

79 According to KCC Article 392-2, the board of directors may establish committees composed of two or more directors, within the board, as prescribed by the articles of incorporation, and allows the board of directors to delegate its power to the committees (other than as prohibited by law).

80 Chun Gyeonghun, *op. cit*., p. 188~189.

81 Kim Hwa-Jin, *op. cit*., p.327.

82 Lee Yun Seok, "A Study on Appropriation of Corporate Opportunity", YGBL Vol. 3(1). (2011), pp. 147~148.

where the corporation is not able to pursue an opportunity, wrongful appropriation of the opportunity may not be established merely by the company merely by virtue of the fact that it was taken by a director or officer. However according to KCC Article 397-2, there is no explicit provision setting forth a defense based on corporate inability. Generally, the reasons for corporate inability are financial inability, legal inability (based on articles of association[83] or law), or a refusal to deal with the company by a potential counterparty. In Korea there is an ongoing discussion over whether such a defense *could* be justified by KCC Article 397-2.[84]

In many situations it is difficult to determine objectively that a company is unable to pursue an opportunity, and approval by the board of directors may be needed in order to establish ability/ or inability. For example, in cases where (i) there is short-term shortage in funds that are to be overcome by loans, (ii) business objectives are limited by articles of association but could be resolved by amendment of articles of association or (iii) there is a way to persuade a third party or regulators to support the transaction, the inability may be overcome through reasonable efforts of the company or the board and potential corporate inability can be overcome. However when there is an objective inability that cannot be overcome by action of the board, then such a situation should be recognized as a ground for defense (but the burden of proof does lay with the director). Not recognizing such defense would force directors to disclose

[83] According to the Supreme Court of Korea, "Company's capacity of enjoyment of rights are limited to objects of laws that act as establishment basis for the company and company's articles of association, but an act in the area of company's competence is not limited to the competence stated in the articles of association, but includes direct, indirect necessary acts, and when determining whether it is needed for performing its obligations, it will be judged according to the act's objective nature, not the performer's subjective, specific will" (Supreme Court of Korea, No. 86 Daka 1349, September 8, 1987).

[84] According to Kim Hong-Ki, *op. cit*., pp. 117~118, corporate financial inability can be established as a ground for defense, but according to Park Sun Jong, *op. cit*., p. 257, it cannot be allowed that a ground for defense is established according to a director's personal determination, which is what financial ability is, not the determination of the board of directors. Meanwhile, according to Bae Do, "A Study on the corporate opportunity doctrine", Soongsil University Law Review Vol. 21, (2009), p. 18, when a third party has provided opportunity to the director, but the director refused to provide it to the corporation, then no corporate opportunity is established, on the other hand, according to Kim Hong-Ki, *op. cit*., pp. 117~118, director's ground for defense cannot be allowed from legal inability or third party refusal to deal, since it is against the director's duty of loyalty, and according to Kim Jeongho, "Appropriation of corporate opportunity", Business Administration and Law Vol. 17(2) (2007), p. 167, Lee Yun Seok, *op. cit*., p. 100, even corporate opportunity that is not allowed according to its laws or articles of association, these must be provided to the corporation, and measures must be considered to amend its articles of association or evade laws. Whereas according to Lee Cheolsong, *op. cit.*, p. 732, since corporate opportunity for approval is limited to existing, future corporate's benefit, corporate's inability should be a judgment factor in determining whether benefit exists.

unnecessary information (a business opportunity may be lost because of such disclosure) and the corporation has to call an otherwise unnecessary meeting of the board.[85] As noted, the KCC approach to corporate inability is currently quite different than the rule under U.S. law. While many aspects of the U.S. corporate opportunity doctrine are imperfect, the safe harbor rule propagated by the *Broz* and *Texelon* line of cases and discussed above is an efficient and practical way to approach the sensitive matter of corporate inability. Allowing the director or officer who is taking the opportunity to avoid formal presentment and a discussion of corporate inability, while at the same time rewarding him for undertaking such discussions when appropriate by protecting him from later liability, properly incentivizes the parties to consider the issue but allows them to avoid disclosing sensitive information and calling unnecessary meetings when appropriate.

7. No Consideration of Conglomerates

Unlike the U.S.,[86] Korea faces problems with appropriation of corporate opportunities in conglomerate environments, not just with individual corporations. The Delaware Supreme Court did deal with a similar issue in the 1956 case *Johnston v. Greene* (discussed above), where a finding that the usurped opportunity was a corporate one then necessitated a decision regarding which of a number of corporations had the strongest right to the opportunity—a very complex question for a court to decide. As discussed previously, KCC Article 397-2 was inserted so as to regulate appropriation of corporate opportunity inside conglomerates. In Korea, many corporations operate under as part of a conglomerate, and therefore it can be hard to determine whether a corporation's business opportunity could also be regarded as another affiliated corporation's business opportunity.

Such problems arise when a director of a corporation is also a director of another corporation under the same conglomerate. However since the KCC Article 397-2 also regulates appropriation of corporate opportunity for a third party, such issues are not only limited to concurrent directorship. In order to solve this issue, according to some scholars, the opportunity's nature should be evaluated. First, it should be considered whether the opportunity can be used together by several corporations. When an opportunity can only be used by one

[85] Kim Hwa-Jin, *op. cit*., p.327-328.

[86] In U.S. cases, nearly all issues regarding appropriation of corporate opportunity are about individual corporations. There are not many cases besides *Sinclair Oil Corp v. Levien* (280 A. 2d 717 (Del. 1971) where appropriation between affiliates of conglomerates was concerned (and *Johnston v. Greene* (discussed above), which contained a different but somewhat analogous fact pattern).

corporation, then the opportunity should belong to the most appropriate company; if the company chooses not to pursue the opportunity then it should pass to the next appropriate company.[87] This argument can only be applied when there is a fixed standard to regulate how to allocate common business opportunities between affiliates. In reality it is very hard to have such a standard.[88]

Especially in Korea, shareholders and corporations are treated as entirely different personalities. The court has ruled internal transactions of wholly-owned subsidiaries unfair as it did not recognize that the transactions of wholly-owned subsidiaries create agency costs.[89] While focusing on the need for regulation, the legislation of KCC Article 397-2 overlooked the unique conglomerate situation in Korea and left many unresolved issues caused by special considerations for conglomerates.

VI. HOW TO APPROACH FAVORITISM

A. Was Tunneling Involved?

Favoring someone in a commercial transaction should not be *per se* illegal. The freedom of contract protects our choice of counterparty. The trouble is that corporate managers exercise their power to choose the counterparty. What if the personal interest of the manager wrongly affects the choice? Even in such

[87] Chun Gyeonghun, *op. cit*., p. 186. *Cf.* Terence Woolf, *The Venture Capitalist's Corporate Opportunity Problem*, 2001 Columbia Business Law Review 489, 496-497: "VCs (Venture Capitalists) do not make investment in a single enterprise, but instead allocate resources across a different number of companies." So "If fiduciary duties were strictly enforced, VCs like Apex would not be able to make investments in multiple ventures." "If fiduciary duties do not provide any ascertainable benefit to a company or its shareholders, but instead create negative costs by preventing directors, officers and VC firms from investing their human and economic capital in other ventures, logic would dictate that the imposition of such duties should be relaxed. The Revised Uniform Partnership Act and the Uniform Limited Liability Company Act provide a means to address this misallocation, by allowing parties to waive their fiduciary duties through a system of disclosure, negotiation and contract."

[88] Choi Munhui, "Appropriation of corporate opportunity in conglomerates", BFL Vol. 19. (2006), pp. 38~41, in theory, there are other standards of allocation discussed as follows; (i) a way to calculate net present value of business opportunity of each company and give the opportunity to the company with the highest value, (ii) give the opportunity to a subsidiary instead of a holding company, when there is more than on subsidiary, then give the opportunity to the subsidiary with the lowest holing company's shares, (iii) allocate the opportunity proportional to the market value of the company. Yet none of these standards provide complete standard in allocation.

[89] Supreme Court of Korea, No. 2001 Du 7411, September 5, 2003.

cases, if nobody in the company is worse off after the managerial decision, *i.e.*, if the price was fair, what is the problem?[90]

Let us revisit the Hyundai Motor Case. Hyundai Motor has been outsourcing its distribution services since before the establishment of Hyundai Glovis, and simply shifted existing outsourced business to a new provider (Hyundai Glovis). The only difference for Hyundai Motor is that the other party was previously a non-affiliate, and now the business is given to an affiliate, the shareholders of which are CEO Chung Mongkoo, director of Hyundai Motor and controlling shareholder of Hyundai Motor Group, and his son. Yet, is it really important for Hyundai Motor who the other party to a transaction is and what corporate governance the other party has? For Hyundai Motor only the business terms of the relationship really matter. For example, let us assume that Apple Inc. ("Apple") decided to change its manufacturer/supplier for its product's display device from Samsung Electronics Co., Ltd. ("Samsung Electronics") to LG Electronics Inc. ("LG Electronics"). What matters for Apple is which of Samsung Electronics or LG Electronics is better capable of satisfying Apple's manufacturing/supply requirements. Arguably, it does not really matter who owns Samsung Electronics or LG Electronics, whether it is Lee Geonhui or Koo Bonmu (at least from the perspective of the corporation and its shareholders).

Then why did the shareholders of Hyundai Motor question the transaction with Hyundai Glovis? Maybe the shareholders thought that Hyundai Motor's damage occurred since Hyundai Motor could have gained all the profits of Hyundai Glovis through cost cutting, a share dividend or an increase in share prices if Hyundai Motor established Hyundai Glovis as a wholly owned affiliate. Yet such questions are unreasonable. According to theories of law and economics, there are two ways to organize production and establish order between divisions in the society; through a market or an organization such as a corporation. When organizing through market, transaction costs are needed, and when organizing through organizations, organization costs are needed.[91] If a corporation, by itself or through affiliates, internalizes any function, transaction costs would likely decrease and organization costs increase. Organization costs depend on corporation's initial investment costs (including opportunity costs), risk of failure, likely ability to continue its business, investment capability, financial situation, ability to hire professionals, maintenance costs, goods and services quality

[90] *See* Stephen Choi & Eric Talley, *Playing Favorites with Shareholders*, 75 Southern California Law Review 271 (2002).

[91] Oliver Eaton Williamson & Sidney G. Winter, The Nature of the Firm – Origins, Evolution, and Development 18 et seq. (Oxford University Press, 1993).

regarding each corporation's situation.[92] If Hyundai Motor conducts its own distribution or establishes Hyundai Glovis as a wholly owned affiliate, then it could reduce its transaction costs, lessen the risk of not finding a competitive price, and gain the direct profit from transacting distribution services. Yet it should be noted that it also bears the risk of business failure, organization costs and its maintenance costs. Therefore it is hard to conclude that Hyundai Motor would have gained all the profits that Hyundai Glovis has gained. Furthermore, it is impossible to calculate the profits of Hyundai Glovis as loss of profit (damages) to the shareholders of Hyundai Motor.

Even if the decision not to internalize the distribution business was appropriate and made by due process, why did the business have to be given to a corporation established by controlling shareholders of Hyundai Motor Group? If the outsourcing of distribution services itself was appropriate, then damages wouldn't have occurred by having it outsourced to a corporation established by controlling shareholders of Hyundai Motor Group. On the other hand one could expect transactions between Hyundai Motor and Hyundai Glovis not to be at arm's length and for one or the other to come out ahead; in fact the court acknowledged that above-market freight charges caused damages equivalent to KRW 14.3 billion to Hyundai Motor. There does appear to have been tunneling,[93] at least to this extent. Yet such tunneling did not occur from outsourcing its distribution services, but from unfairly high freight charges. Conflict of interest issues arising from counterparty identity should be regulated by the KCC Article 398 (section regulating self-dealing transactions). If it is not in the realm of Article 398,[94] then it should be regulated by director's duty of good manager's due care in determining the terms of a transaction.[95]

---

[92] Transactions will be internalized to the extent the increased organizational cost does not exceed transaction cost. The corporation will be extended to that level.

[93] *See generally*, Vladimir Atanasov, Bernard Black & Conrad S. Ciccotello, *Law and Tunneling*, 37 Journal of Corporation Law 1 (2011). For a discussion of tunneling from a Korean perspective, *see* Kee-Hong Bae et al., *Tunneling or Value Added? Evidence from Mergers by Korean Business Groups*, 57 Journal of Finance 2695 (2002).

[94] As discussed above, the KCC Article 398 expanded who the other party of self-dealing transaction is. Yet the transaction between Hyundai Glovis and Hyundai Motor is (like under the former KCC) not regulated as a self-dealing transaction.

[95] Meanwhile the KFTC, which imposed a penalty surcharge, raised questions that Hyundai Motor had outsourced its distribution business to Hyundai Glovis, which as a new established company, its business ability not even verified. However, Hyundai Glovis took over an existing company, which has been entrusted with the distribution business by Hyundai Motor before. Furthermore, since the court recognized in the Hyundai Motor Case that Hyundai Glovis developed an integrated distribution system and increased effectiveness in the distribution system of affiliates, it is hard to consider that any damages occurred to Hyundai Motor due to Hyundai

B. The Business Judgment Rule

In the end, the business judgment rule underlies our entire discussion.[96] In the Hyundai Motor Case, whether to internalize Hyundai Motor's distribution service or outsource it is a matter of directors' duty of good manager's due care by comparing transaction cost and organization cost (a matter of the business judgment). The same applies to who the other party should be when outsourcing distribution service and under what conditions it should be outsourced. The court ruled on the issue as follows: "Hyundai Glovis's distribution services are in fact, an assistance service for Hyundai Motor Group's manufacture and sales, however an automobile company does not have to directly conduct its distribution services or establish a subsidiary for its service on grounds that distribution services are related to or contingent upon automobile businesses. Whether to outsource its business is not depended upon relevance to or contingency upon the company's business, rather it is determined according to business judgment. Thus, whether to establish an internal business unit, establish a subsidiary or outsource it to another company for already outsourced the distribution serves, is fundamentally at the discretion of the company's business judgment." IThe court recognized that the decision to outsource was legal according to the business judgment rule, but held that increased freight charges for Hyundai Glovis could not be legitimized as business judgment.

Although "Funneling of Business" such as that occurring in the Hyundai Motor Case is not an appropriation of a corporate opportunity, it is also a matter of business judgment. If the information on the corporate opportunity is fully disclosed, and the board of directors judged through careful reasonable due process that it is for the benefit of the corporation not to use such opportunity, then such decision should be protected by the business judgment rule.

VII. CONCLUDING REMARKS

This Article reviewed the controversial corporate opportunity doctrine as it was discussed and promulgated as law in Korea and analyzed the doctrine in the context of the Hyundai Motor Case. One cannot question that the corporate opportunity doctrine has a certain legitimacy and useful function as a well-

---

Glovis's lack of ability.

[96] In Korea the business judgment rule is generally accepted as follows. "Although damages to the company have occurred by resolution of directors, if such a resolution had sufficient grounds and was determined by careful and reasonable due process, then directors do not have liability to compensate." *Cf.* Hwa-Jin Kim, *Directors' Duties and Liabilities in Corporate Control and Restructuring Transactions: Recent Developments in Korea*, 2006 Oxford University Comparative Law Forum 2 http://ouclf. iuscomp.org/articles/kim.shtml.

founded iteration of the director's duty of loyalty. However the incorporation of the corporate opportunity doctrine into the KCC may have been premature, as the debate surrounding the concept and the legal nature of duty of loyalty is not yet settled sufficiently. The corporate opportunity doctrine is derived from U.S. case law (still a somewhat abstract concept there) and takes on different elements and analysis framework as the fact patters change; it is nearly impossible to establish a workable and flexible doctrine in a few codified provisions. Moreover, the corporate opportunity doctrine was promulgated as law in Korea to regulate the so-called "Funneling of Business"; a concept that lies quite outside the corporate opportunity doctrine's focus, application framework and body of precedent in the US. This makes the development of the KCC Article 397-2 in Korea even more difficult (and calls for an approach that is unique from that in the U.S., and more tailored to the Korean business environment). On these bases, we conclude that the corporate opportunity doctrine of Korea needs substantial refinement before it can become a workable solution to the specific problems facing Korean corporate law today.