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ADB-FSS Webinar on Crowdfunding: Lessons from Korea's Experience

27 September 2021



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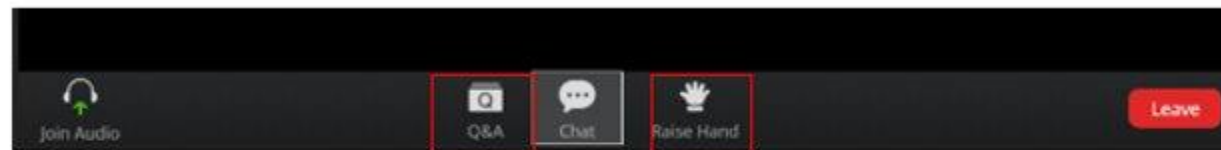
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- Sessions will have a Q&A towards the end of the session. All questions will be managed by the moderator.
- Participants may **use the message chat box or Q&A button** to post their questions and/or comments.
- Participants may **raise their hands** if they would like to join the discussion during Q&A portion.



ENABLED ICONS FOR PARTICIPANTS

Opening Remarks



Yong-tae Kim

Director General
International Affairs Department
Financial Supervisory Service of Korea

Welcome Remarks



Shane Rosenthal

Country Director
Georgia Resident Mission
Asian Development Bank

Crowdfunding Regulatory Framework in Korea



Yeseom Yoo

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CROWDFUNDING

FSS

Capital Market Supervision Department

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Agenda

1 | OVERVIEW OF CROWDFUNDING

2 | REGULATION ON ISSUERS

3 | PROTECTION OF INVESTORS

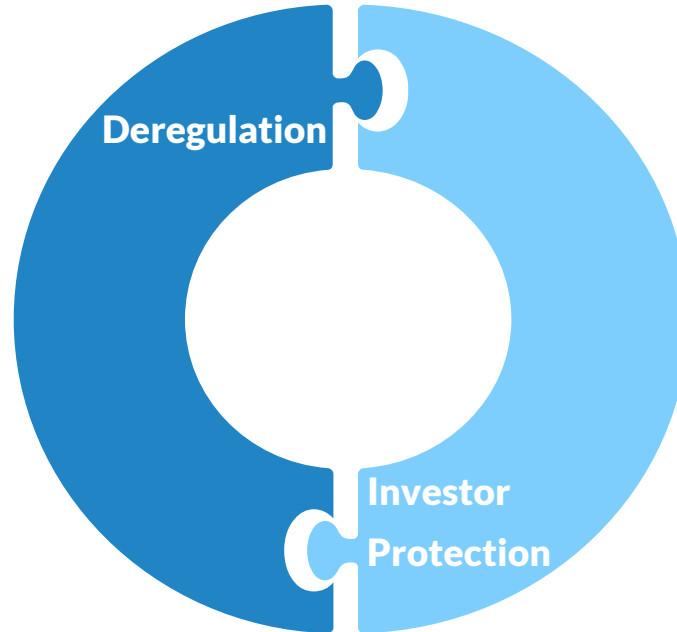
4 | REGULATION ON CROWDFUNDING BROKERS

1.

OVERVIEW OF CROWDFUNDING

Objectives of Crowdfunding

Facilitating funding
for entrepreneurs
and start-ups



Setting limits on issuance
and investment amounts



\$ 127,000,000

Total amount of issuance



68,708 investors

Number of investors



873 cases

Number of successful offerings

Participants



Issuer

Seeking funding on a crowdfunding platform



Investor

Interested in investing in startups or venture businesses



Crowdfunding broker

Licensee operating a crowdfunding platform



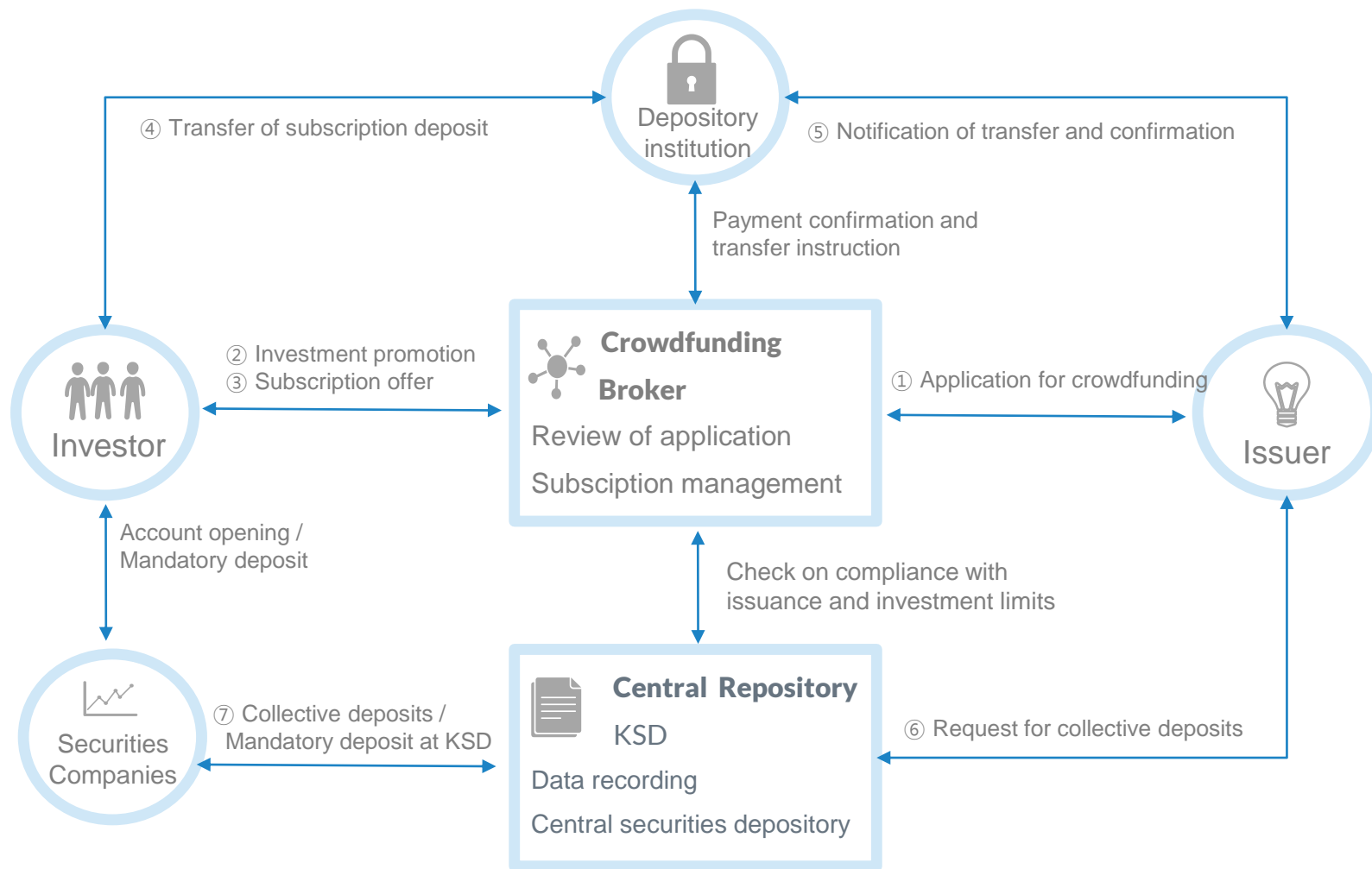
Central repository KSD

(Korea Securities Depository)
Recording and managing data related to crowdfunding



Depository institution

Keeping investors' subscription deposits safe



2.

REGULATION ON ISSUERS

Scope of Issuers

① SMEs

With their business operations less than 7 years

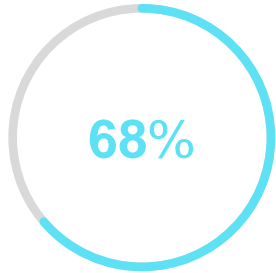
② Companies classified as venture companies and inno-biz companies

③ SMEs engaging in project-based businesses

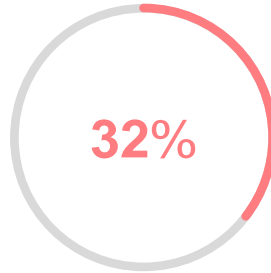
(of which accounting is independent from existing business's accounting)

* Finance, insurance, and real estate businesses are excluded.

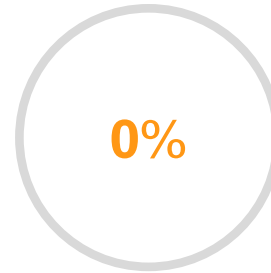
Types of Securities



Equity securities
(stocks)



Debt securities
(bonds)



Investment contract
securities

Deregulation

<Comparison of disclosure requirements>

Public Offering	Simplified Public Offering	Crowdfunding
Registration statement (around 27 documents)	Disclosure documents (around 17 documents)	Terms and conditions of issuance, financial conditions, prospectus
Acceptance by FSC is required	Submitted to FSC	Disclosure on the broker's website and CrowdNet*

* CrowdNet: Central Repository's website

Disclosure of Information

Terms and conditions of issuance

Details of the rights of securities holders
Investment risks
Intended use of proceeds

Financial conditions

Overview of the company
Documents stating the financial standing

Prospectus, etc.

Details of business
Matters concerning the organizational structure and major shareholders

Limits on Issuance

→ KRW3 billion (\$2.5 million)

KRW1.5 billion (Debt securities)

(amount of public offering+ amount of simplified public offering
+ amount of crowdfunding)

Other Regulations

Cancellation of the issuance

If subscription is less than 80% of the target offering amount

Restrictions on sale

Issuers and major shareholders may not sell their holdings for one year from the issuance

Liability for damages

Damages caused by misrepresentation or omission of information

3. PROTECTION OF INVESTORS

Types of Investors

Ordinary Investors

Any investor who is not a qualified or professional investor

Qualified Investors

Subject to financial income tax
5 times and \$12,000

Professional Investors

Venture investment funds
Angel investors



Limits on Investments

	Maximum investment per issuer	Annual investment limit
Ordinary Investors	KRW5 million (\$400)	KRW10 million (\$800)
Qualified Investors	KRW10 million (\$800)	KRW20 million (\$1,600)
Professional Investors	No cap	No cap

Other Protections

Withdrawal of subscription

Withdraw subscription before the subscription period ends

Resale restrictions for 6 months

Exception: selling to the issuer, large shareholders, and professional investors

Prohibition on changing investors' opinion

No deletion or modification

4.

REGULATION ON CROWDFUNDING BROKERS

Requirements for Crowdfunding Brokers

Requirement	Details
Equity capital	More than KRW5 million
Human resources	Internal control: at least 1 employee Computer management: at least 2 employees
Physical facilities	Electronic computer systems Security system
Feasibility of business plan	Internal controls and investor protection
Prevention of conflicts of Interest	Appropriate internal control standards to prevent conflicts of interest

Requirements on Crowdfunding Brokers

01 Verification of investment risk

02 Notice of the subscription result

03 Management of investment and issuance limits

Fact Check

- ▷ Financial status of the issuer
- ▷ Work history of CEO
- ▷ Specific purpose of funding
- ▷ Criminal history of the issuer and its major shareholders
- ▷ Written proof of determination to issue securities

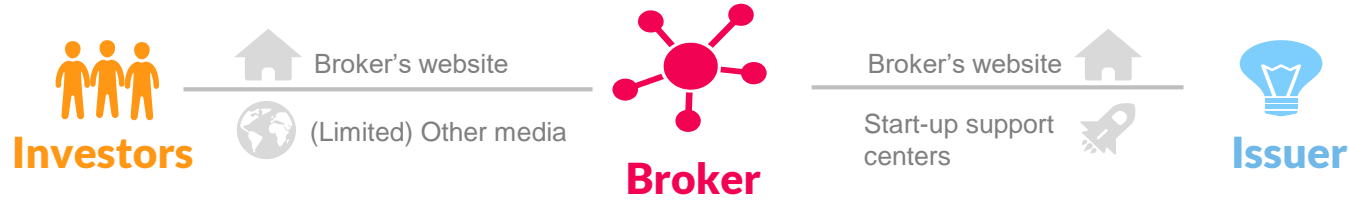
Prohibitions on Crowdfunding Brokers

- ▷ No acquisition of crowdfunded securities
- ▷ No advice to investors or issuers
- ▷ Restrictions on investment promotion and advertisement
- ▷ No discrimination
- ▷ No possession of investors' assets
- ▷ Regular report of financial performance and management status

Revenue Model



How to Promote



Liability for Damages

Caused by

Violation of law

Misrepresentation or omission of information

Thanks!

Any question?

You can contact me at:

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P2P lending structure and future challenges in Korea

Suk Jaeseung
Lead Manager
P2P Lending Supervision Team
Mutual Saving Bank Supervision Department
Financial Supervisory Service

Table of Contents

1. P2P lending growth in Korea
2. Background of legislation
3. Legislation process
4. P2P Lending Act
5. Current trends of P2P lending market in Korea
6. Future challenges

1. P2P lending growth in Korea

Background of P2P lending growth in Korea

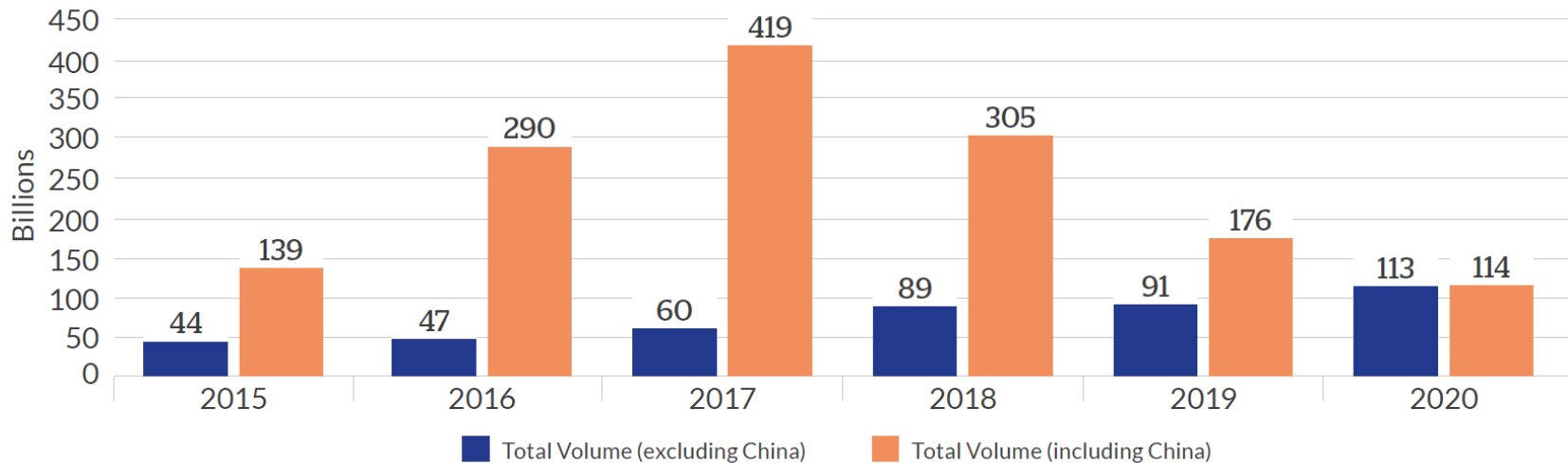
- P2P lending: a form of business in which investors provide loans to borrowers on an **online platform** without going through traditional financial institutions such as banks;
- Offering loans at **lower interest rates** to borrowers and **better returns** to investors, compared to their traditional counterparts;
- Contributing to strengthening **financial inclusion**;
- **Small investment** allowed; easier for investors to **diversify their investment** into multiple products presented by the platform and manage returns and risks accordingly;
- Generally run by tech companies; credit screening using **unstructured data such as Big Data**, which is not used by traditional lenders;

Global P2P lending market size

[Global alternative finance market size]

The Size and Growth of the Global Alternative Finance Market

Figure 1.1: Total Global Alternative Finance Volume 2015 - 2020, USD

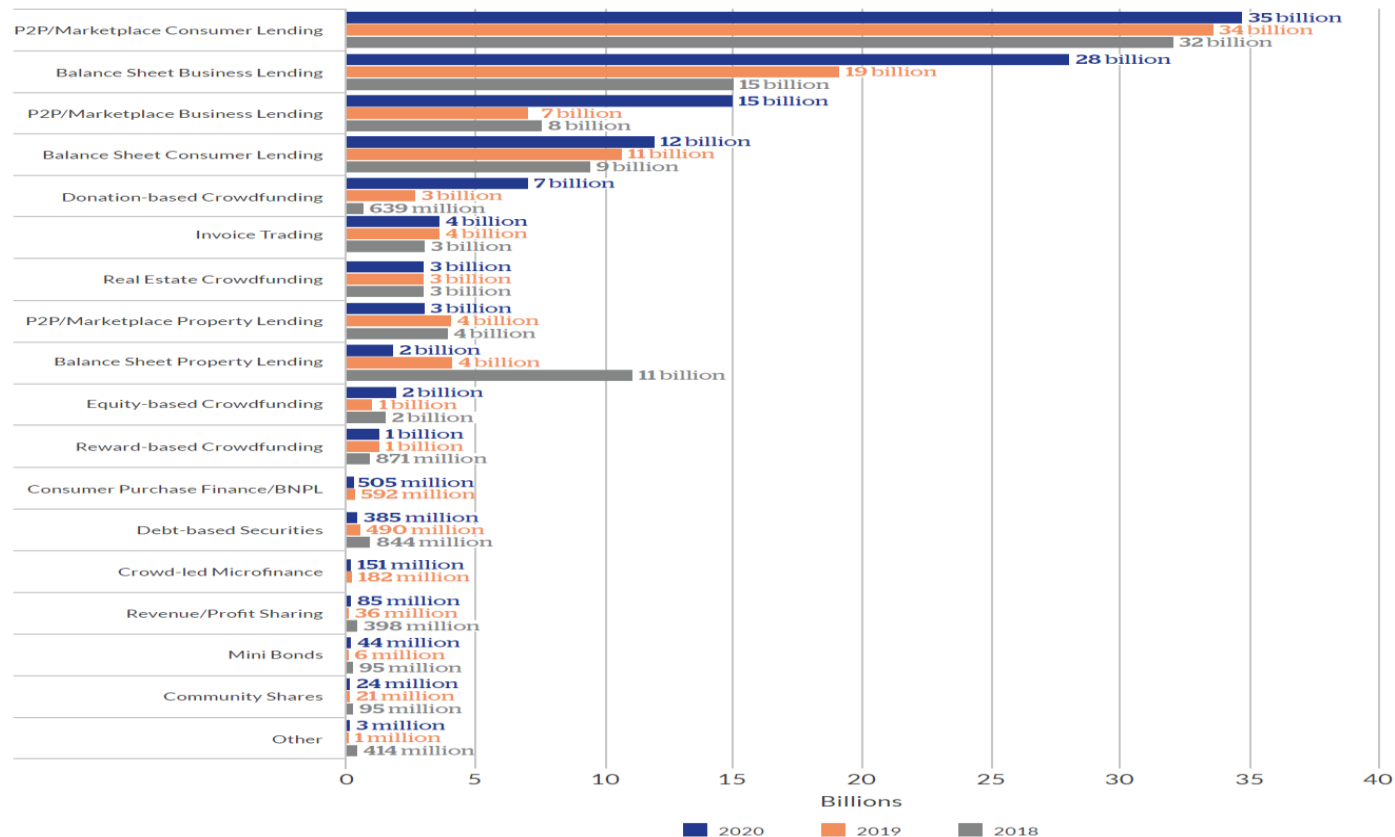


- Source : Global Alternative Finance Market Benchmarking Report(Cambridge Centre for Alternative Finance, June 2021)

Global P2P lending market size

[Size by type]

Figure 1.10: Global Volume by Model, 2018-2020 (Excluding China)

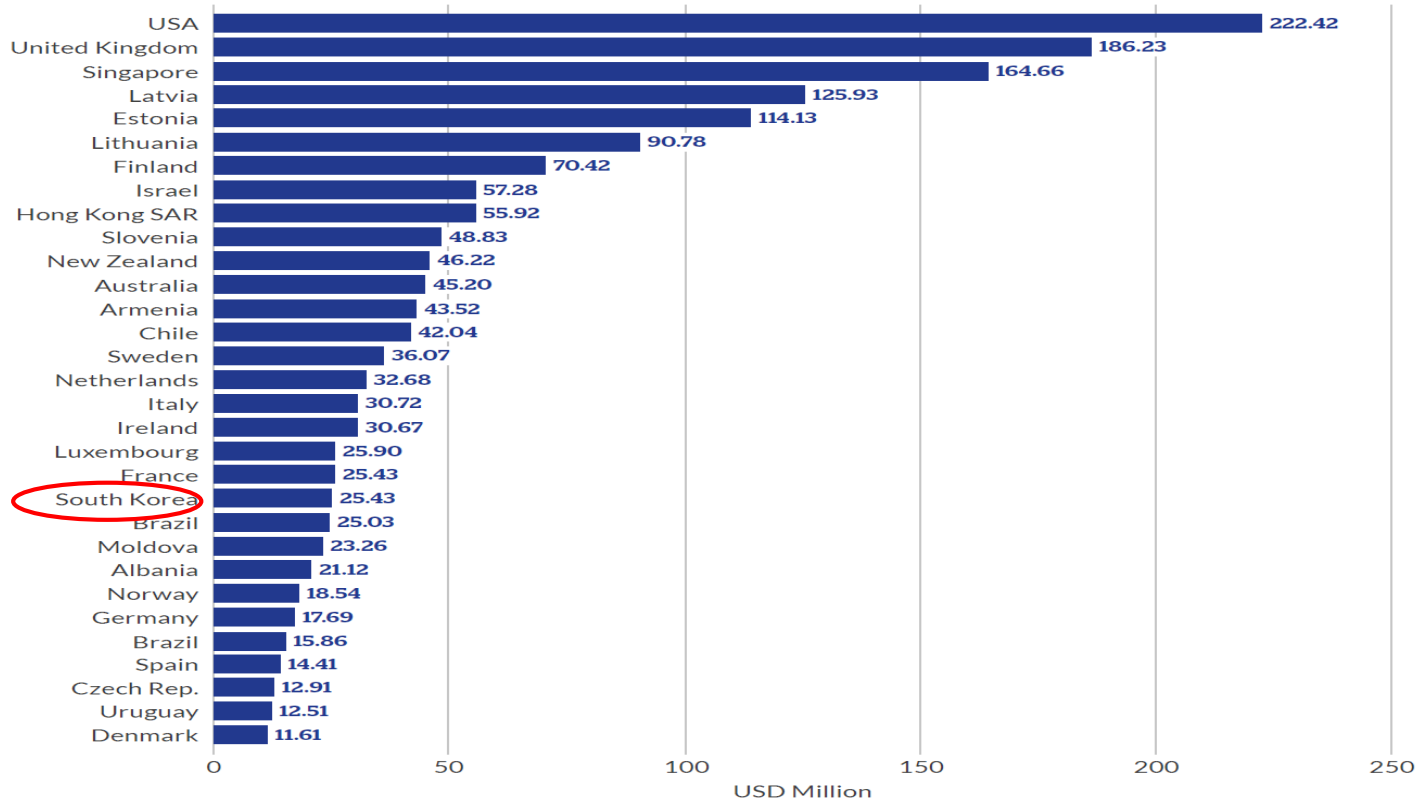


- Source : Global Alternative Finance Market Benchmarking Report(Cambridge Centre for Alternative Finance, June 2021)

Global P2P lending market size

[Size by country]

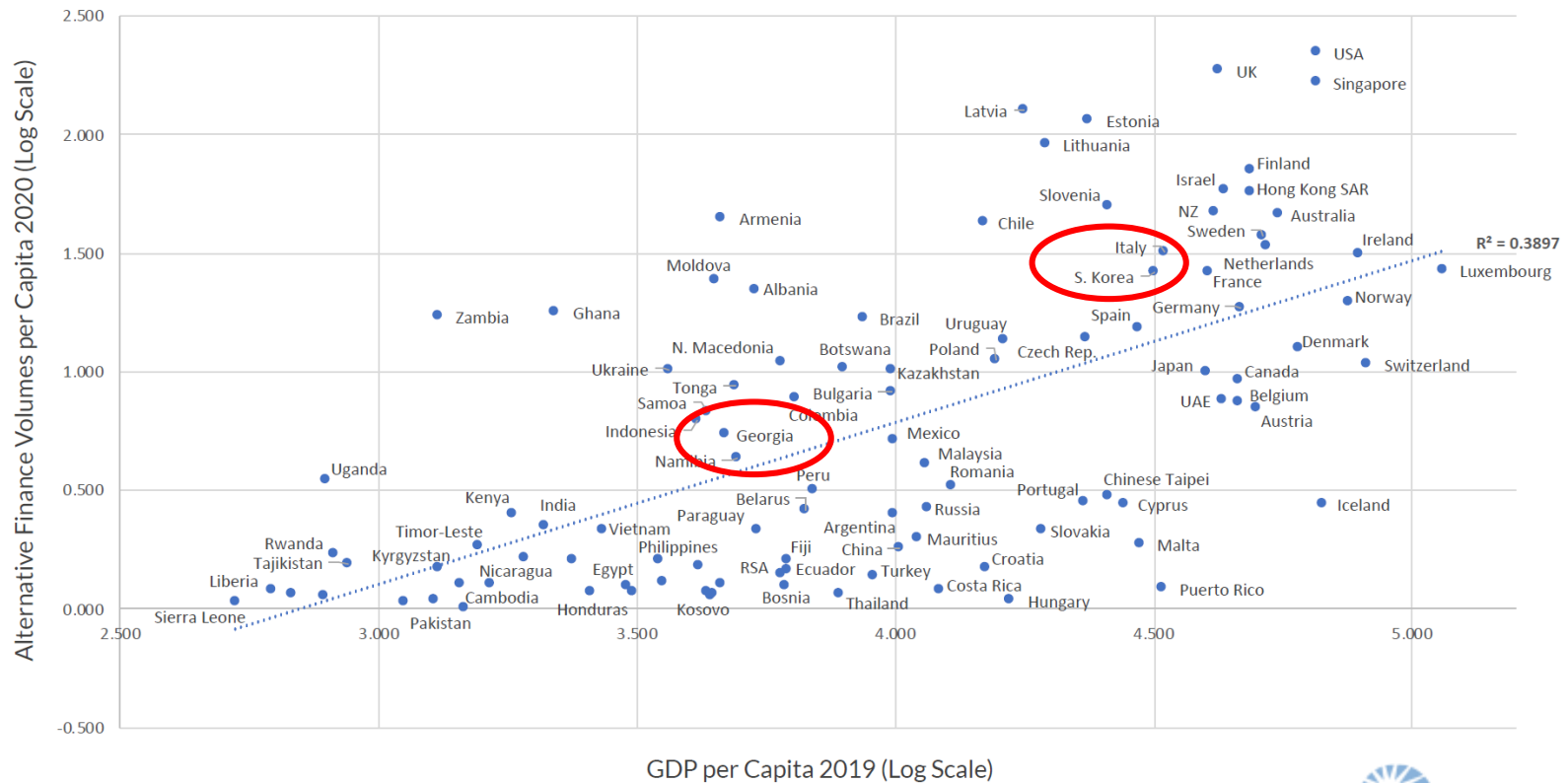
Figure 1.30. Alternative Finance Volumes per Capita 2020



- Source : Global Alternative Finance Market Benchmarking Report(Cambridge Centre for Alternative Finance, June 2021)

[Correlation with GDP]

Figure 1.31: Alternative Finance Volumes per Capita 2020 vs. GDP per Capita 2019



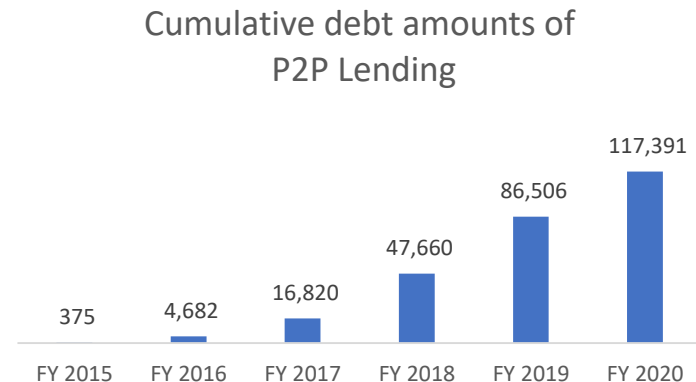
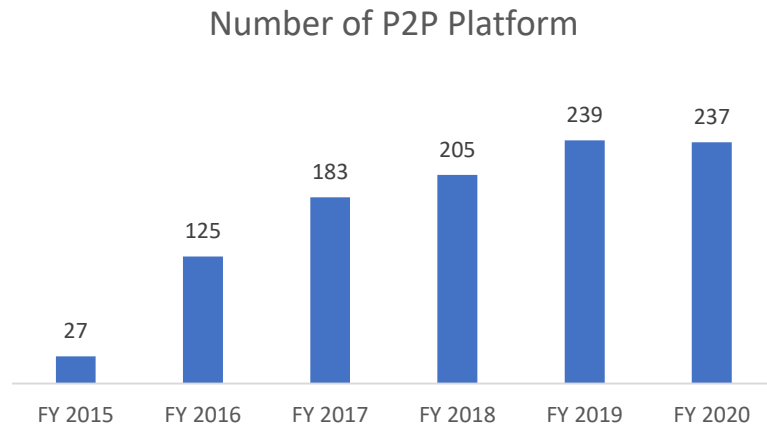
- Source : Global Alternative Finance Market Benchmarking Report(Cambridge Centre for Alternative Finance, June 2021)



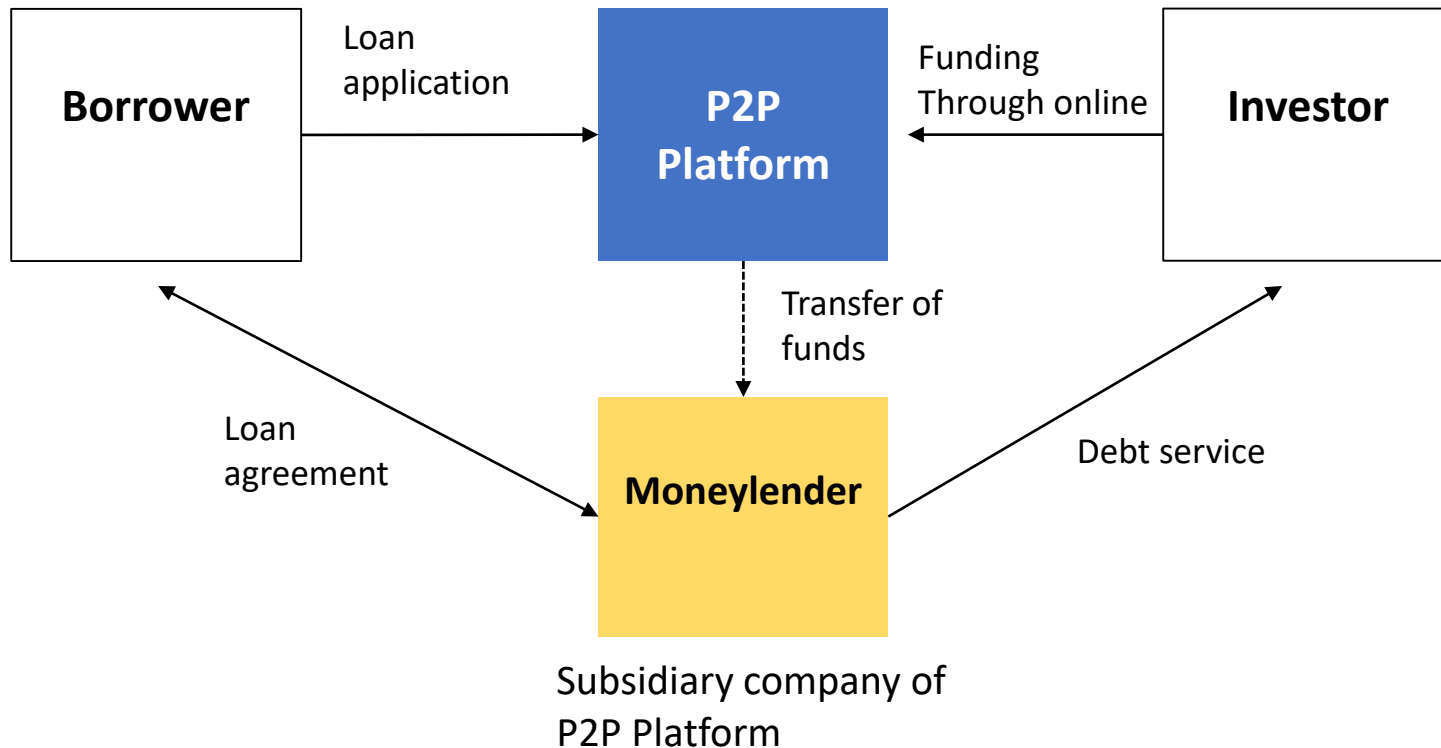
2. Background of legislation

P2P lending market before legislation

- P2P platforms growing fast after they first emerged in the market in the mid-2000s;
- Number of P2P platforms increasing rapidly from 27 in 2015 to 125 in 2016, and then to 237 at the end of July 2020;
- 25-fold increase in the cumulative loan amount from KRW468.2billion (USD400 million) at the end of 2016 to KRW11.7 trillion (USD10 billion) in December 2020;



P2P loan business structure before legislation



Background of legislation

- P2P lending guidelines, a flexible regulatory device, set by financial authorities to harmonize the policy goals of fintech growth and investor protection (February 2017);
- P2P platforms regulated under the guidelines, and moneylenders (credit service providers) indirectly supervised in accordance with the Credit Business Act;
- P2P market overheating leading to investor damage such as fraud, embezzlement, and bankruptcy;
- Need for an independent law for the supervision of P2P platforms raised to make the guidelines compulsory;

3. Legislation process

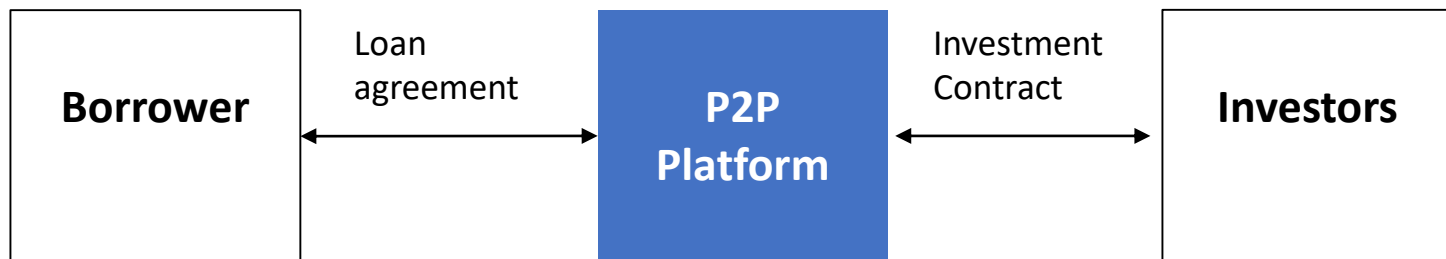
Legislation process

- Multiple bills proposed in the National Assembly (2017 to 2018);
- Need for legislation also raised from the industry to clear legal uncertainty;
- Discussions held over the enactment of a separate law or revision of existing laws;
- A separate law enacted due to limitations of the existing legal system in governing P2P lending activities, in which investors and borrowers should both be protected;
- The Act on Online Investment-Linked Financial Business and the Protection of Users enacted in November 2019;

4. P2P Lending Act

P2P Act and P2P business structure

- **(Main content)** Entry barriers and prudential regulation set not at a strict level considering the nature of the P2P platform business;
 - Regulation focused on **investor protection** as P2P lenders' credit risk is insulated by investors;
- **(P2P business structure)** P2P platforms attracting investors and borrowers and conducting credit screening, loan execution, as well as follow-up management;



Main content of the P2P Act

[Entry]

- (Registration) Registration with the FSC required to perform P2P lending business;
- (Net worth requirement) More than KRW500 million (USD430,000) (can also be up to KRW3 billion (USD2.6 million))
- IT experts and IT infrastructure including communication and security facilities
- Feasible business plans, internal control plans, investor protection plans, etc.;
- Records of criminal convictions or sanctions of executives;
- Sound financial status and criminal records of the applicant company;

Main content of the P2P Act

[Regulation of business conduct]

- Obligation to **disclose P2P platform information** (financial and management status, loan size, delinquency rate, etc.);
- Regulation of **interest rates and fees** (the rates set within the legal maximum interest rate);
- Loans to **major shareholders** of P2P platforms **prohibited**;
- **Maturity mismatch** between investments and loans **not allowed**;
- P2P platforms' investment in its own loan products **with its own property** allowed; the investment limited to be within 20% of the amount of solicited investment;
- **Subjects not to be involved in P2P loans specified** for investor protection;

Main content of the P2P Act

[Investor protection]

- P2P platforms required to provide investors with loan information, borrower information, and investment information (yield, etc.);
- Investments required to be separately managed to ensure their safety from bankruptcy and/or embezzlement of P2P platforms;
- Investors given the right to receive repayment prior to third parties (“right to preferential payment”) when a P2P platform goes bankrupt;
- A central record management agency designated to collect investment and loan information and manage investment limits;

Main content of the P2P Act

[Loan limit and investment limit]

- **Loan limit:** Either 7% of the outstanding balance of loans from a P2P platform to the same borrower or KRW7 billion (USD600,000), whichever is smaller;
- **Investment limit:** Limits varying by investor type (retail investors, income-qualified investors, professional investors, and corporate investors);
- Trading of principal and interest receivables available among investors through P2P platforms;
- Financial firms also able to invest on P2P platforms (within 40% of the amount of solicited investment);

5. Current trends in P2P lending market in Korea

Enforcement of P2P Act and registration review

- The Act on Online Investment-linked Financial Business and the Protection of Users taking effect on August 27, 2020;
- Existing P2P platforms **given a grace period of one year** to register and **new business prohibited** if not registered until the period is over;
- A total of **40** P2P platforms applied for registration under the law (the remaining companies estimated to have been closed or switched to credit service providers).
- According to regulators' review, **32** P2P platforms completed registration as of September 27, 2021.
- New companies also planning to apply for registration beginning in September;

Current status of registered companies

- The total balance: about 1.2 trillion won (\$1 billion)
- Business type: credit loans, real estate mortgage loans, accounts receivable mortgage loans, movable property mortgage loans, PF loans, renewable energy loans, stock mortgage loans, etc.
- The financial authorities set up P2P Lending Supervision Team and P2P Lending Examination Team.

LENDIT™



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6. Future Challenges

Future challenges

- Since P2P platforms mainly increase profits by expanding the size of loans, they will likely to focus on expanding their size rather than considering investor interest.
- In particular, P2P platforms not responsible for loss, making them careless about follow-up management;
- P2P platforms in charge of loan screening, loan interest rate decision, and post-loan management; but investors responsible for all the risk caused by loan insolvency;
→ Moral Hazard and Agent Risk

Future challenges

- Borrowers using P2P lending highly likely to face insolvency since most of them finding it difficult to take out loans from the conventional financial service providers;
- The workforce of the P2P lending industry smaller than that of traditional financial companies, leading to a shortage of experts necessary to examine and manage loans;
- P2P loans possibly serving as a means of avoiding regulations applied to traditional loans;

Thank you!
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Examples of P2P Crowdfunding in Korea



Young Ileen Jo (Everine Jo)

Head of Strategy/Legal Department
8Percent Inc.



Joey Kim

Founder and Chief Executive Officer
PeopleFund

Panel Discussion on Recommendations for Georgia Based on Korea's Experience

Moderator



Junkyu Lee

Chief of Finance Sector
Group
Sustainable Development
and Climate Change
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Panelists



Yeseom Yoo

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Jaeseung Suk

Lead Manager
Mutual Savings Bank
Supervision Department
Financial Supervisory Service
of Korea



Malik Kotadia

Fintech Expert and Co-
Founder
Finnovation Labs

Way Forward and Next Steps



Otar Gorgodze

Head of Financial and
Supervisory Technologies
Development Department
National Bank of Georgia

Closing Remarks



Tariq Niazi

Director, Central and West
Department and Co-Chair of the
Finance Sector Group Committee
Asian Development Bank

Thank you for your participation!