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## Plenary 1

Increasing Disclosure – A Key to Improving  
Investor Confidence

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# Korean Experience of Regulation Fair Disclosure

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## **(Greetings and introduction)**

Thank you, Chairman Adhémar and good afternoon, ladies and gentlemen.

It is my great pleasure to participate in the panel to discuss whether or not investor confidence can be improved by increasing the amount of information and/or by enhancing the quality of information. I would like to address the issue by sharing with you some recent experiences of Korea after introducing Regulation Fair Disclosure late last year. Although it is still too early to assess the effectiveness of Korea's Regulation Fair Disclosure, there are a few pieces of evidence that clearly supports the claim that the regulation does, in fact, enhance the degree of investor protection and thus the soundness of the securities markets.

## **(The content of Korea's Regulation Fair Disclosure)**

Last November, Korea became the second country in the world, next to the United States, to introduce Regulation Fair Disclosure. Regulation Fair Disclosure was adopted mainly to resolve problems of asymmetry in information disclosure and to root out the unfair business practice of selectively providing material, nonpublic information to certain groups of people such as securities analysts. The essence of the regulation is that when a listed company (including KOSDAQ-registered firms) or its officers and employees who have access to material, nonpublic information provides such information to any select group or individual(s), that information must also be disclosed to the public (i.e., all investors) at the same time.

If I may briefly mention the core of the regulation, (1) the types of information subject to Regulation Fair Disclosure include any information that pertains to future business and management plans, sales or profits forecasts, provisional reports issued in advance of regular reports, and other timely disclosure items before the deadline. I think it is reasonable to assume that Regulation Fair Disclosure requires all the relevant

information be disclosed so long as it can create serious information asymmetry if the disclosure is made selectively. However, certain information given to news media for the purpose of press release is not subject to Regulation Fair Disclosure.

In case where selective disclosures are made unintentionally, it must be disclosed to the public within the same day in the form of an electronic document via the electronic disclosure system of the self regulatory organizations (SROs) such as the Korea Stock Exchange or the Korea Securities Dealers Association.

Penalties for failing to comply with Regulation Fair Disclosure include (1) the firm's stock can be placed on the watch list of the exchange and be delisted if violations persist; (2) the supervisory authority will not allow for such a firm usual exceptions to violations when making unfaithful disclosure of forecasted information; and (3) the firm will be subject to special surveillance for insider trading.

For the benefit of the audience, a table that compares Korea's RFD to US RFD is attached as an appendix of this handout

### **(The effects of Regulation Fair Disclosure)**

Now, let me explain some of the findings with regards to the effects of the introduction of Regulation Fair Disclosure. First of all, there has been a marked increase in the number of disclosure filings after the introduction of Regulation Fair Disclosure. As you can see in Table I, in the first 10 months after the regulation was put into effect, there was an average of 35 disclosures each day. Notice that this is the number of filings that would not have been disclosed unless the regulation was adopted. That is, the increase in the number of filings came largely as a result of the new rules requiring timely disclosure. This also served to decrease the number of rumor-related disclosures. It is interesting to notice that issuers actively disclosed forecast information in a timely manner. This is partly due to the regulatory exception that future business plans and sales/earnings forecasts are not subject to unfaithful disclosure violation.

The demand for timely information disclosure has also grown substantially. On average, the electronic disclosure system known as DART (Data Analysis, Retrieval and Transfer) of the Financial Supervisory Service is accessed over 60,000 times daily.

Thus, it is evident that the market received and used greater amount of information from issuers under the new disclosure regulation.

Let us turn to the quality of information that is disclosed under Regulation Fair Disclosure. This task is much more difficult than just measuring the amount of increased information. I think we have to examine this in two dimensions. (1) Do investors find the disclosed data informative? (i.e., the information content issue); (2) Does the increased amount of information reduce stock price volatility (i.e., the information environment issue).

I do not have clear results on the above issues yet. However, the market reaction to disclosed information of promotional nature as opposed to forecast results was closed to zero, suggesting that such promotional disclosure items are not biased. This is contrary to the criticism on Regulation Fair Disclosure that the new regulation will invite issuers to use the disclosure system as an avenue to promote companies rather than to generate valuation pertinent information.

However, the market reaction to a forecast disclosure is clearly related to the direction and the magnitude of the surprise in the disclosed information. This information is reflected in the market price in a much more timely manner such that when the actual results are disclosed, the market reaction is smaller and less variable than in the case where fair disclosure was not required.

In order to examine the impact of the new regulation on the market volatility and thus the investor confidence, we need more data for a longer time period. I suggest the audience to look for studies that address this question for the U.S. market.

Finally, the equal access to information for investors and analysts has also helped change the role and functions of securities analysts. Securities analysts are putting more efforts to analyzing corporate value and assessing future prospects than to acquiring selectively disclosed, non-public information..

Internal control systems of firms are also being strengthened as executives, including CEOs, are under more pressure to pay attention to the management of information and to setting guidelines for releasing information to the public.

### **(Further issues on Regulation Fair Disclosure in Korea)**

In the process of implementing Regulation Fair Disclosure, there have been drawbacks, one of them being greater burdens being placed upon companies because of the extensive scope of the regulation.

There have also been cases where companies manipulated the system by disclosing false information. This problem is serious in that this may downgrade the credibility of disclosed information. In order to resolve such problems, the scope of information subject to fair disclosure regulation must be clearly defined and strictly enforced.

### **(Closing)**

Regulatory authorities around the globe promote the practice that there should be full, timely and accurate disclosure of financial results and other material information. Regulation Fair Disclosure in Korea aims to enhance the efficiency of supervision of investor protection. We certainly recognize that a greater burden has been placed upon issuers and regulators. Nonetheless, Regulation Fair Disclosure has already begun to enhance market efficiency and it is being proven that its benefits will outweigh the costs. We will keep modifying the regulation to reduce regulatory burden and to enhance the effectiveness of the disclosure supervision. We are committed to making Regulation fair Disclosure a key pillar that supports the integrity of our capital market. Thank you for your attention.

**(Table 1) Fair Disclosure Filings**  
**(10 month period from November 2002 to August 2003)**

<b>Classification</b>	<b>KSE</b>	<b>KOSDAQ</b>	<b>Total</b>
Revenues or Profits	1092 (44%)	1174 (24%)	2266 (30%)
Forecasts or Estimates	237 (9%)	334 (7%)	571 (8%)
Future Business and Management Plans	534 (21%)	1656 (34%)	2190 (30%)
Timely Disclosure	210 (8%)	1138 (23%)	1348 (18%)
Other	440 (18%)	597 (12%)	1037 (14%)
Total	2513 cases (100%)	4899 cases (100%)	7412 cases (100%)
Daily Average Filing	12 cases	23 cases	35 cases

**(Appendix) Comparison of Regulation Fair Disclosure: Korea vs. US**

Classification	Korea	US
Issuers	Executives of listed or member companies	Securities Issuers or their representatives
Subject Information	Future business and management plans, business performance forecasts, etc.	Profits and losses, mergers, development of new products, management change, etc.
Information Recipients	Securities or investment trust companies and their executives, mass media and its executives	Brokers, dealers, investment advisors, etc.
Exclusions	Anyone who owes an issuer a duty of trust or confidence, e.g., attorney, accountant, credit rating company, etc.	Anyone who owes an issuer a duty of trust or confidence, e.g., attorney, accountant, credit rating company, etc.
Disclosure Deadline	Intentional disclosure: Simultaneously Non-intentional disclosure: Within the same day	Intentional disclosure: Simultaneously Non-intentional disclosure: Promptly