

March 9, 2023

CHANGES TO THE DOMESTIC FOREIGN EXCHANGE MARKET IMPACTING FOREIGN FINANCIAL INSTITUTIONS

On 7 February 2023, the Ministry of Economy and Finance (the “**MOEF**”) announced the “Foreign Exchange Market Structure Improvement Plan” (the “**Plan**”) which aims to transform the existing foreign exchange market structure into a more liberal and competitive market. This is the first meaningful announcement in the FX area in over 20 years. The proposed regulatory changes are expected to improve foreign investors’ accessibility to the domestic foreign exchange market and present more opportunities for foreign financial institutions to participate in the foreign exchange market.

The main takeaways are:

- A. Foreign financial institutions may participate in the domestic foreign exchange market (“**Domestic FX Market**”) as a direct market participant.
- B. Extension of the foreign exchange market hours.
- C. Enhancement of product trading and settlement infrastructure.

The key details and implications of the Plan announced by the MOEF are as follows:

I. **Registered Foreign Institutions will be permitted to participate in the Domestic FX Market.**

Currently:

- A. Only domestic financial institutions registered with the MOEF are permitted to participate in the Domestic FX Market to trade with other registered financial institutions.
- B. Foreign institutions, as offshore clients, can trade various types of FX products, such as FX spot, FX swap, FX forwards, FX options, etc. with registered domestic financial institutions in a client-dealer relationship, but is unable to directly access the Domestic FX Market.

After the Plan is implemented:

- A. In addition to the trading process in 1.B. above, new additional trading process will be made available to a Registered Foreign Institution (“**RFI**”) which meet the below conditions to obtain MOEF approval and directly participate in the Domestic FX Market.
- B. RFIs will be permitted to transact directly with other participants in the Domestic FX Market which includes other RFIs and domestic registered financial institutions.
- C. Initially, only FX spot and FX swap transactions (“**Products**”) will be available to RFIs in the Domestic FX Market. The MOEF may also consider adding more complex products such as cross currency swaps and options to the list of Products going forward.

Qualification to be a RFI:

- A. Adequate liquidity: Procurement of a credit line sufficient to carry out transactions with other market participants of the Domestic FX Market.
- B. Identification information verification: Legal Entity Identifier ("LEI") may be used to open accounts with domestic financial institutions for the settlement in Korean won ("KRW").
- C. Evaluation on equivalent regulatory regimes: Confirmation that the regulatory and supervisory regime of the relevant authorities of RFIs are substantially equivalent with that of Korean financial regulator.
- D. Undertakings for fulfilment of obligations: Agreeing to undertakings related to compliance with statutory obligations, reporting requirements, audit, supervision and data submission.

Please note that only foreign financial institutions, foreign subsidiaries and branches of domestic financial institutions, that are engaged in a business in its own jurisdiction similar to the business of a domestic financial institution who is eligible to participate in the Domestic FX Market (such as foreign banks and foreign investment dealers/brokers), will be considered for the RFI registration. In addition, RFIs are required to settle the KRW-denominated Products through a domestic foreign exchange broker.

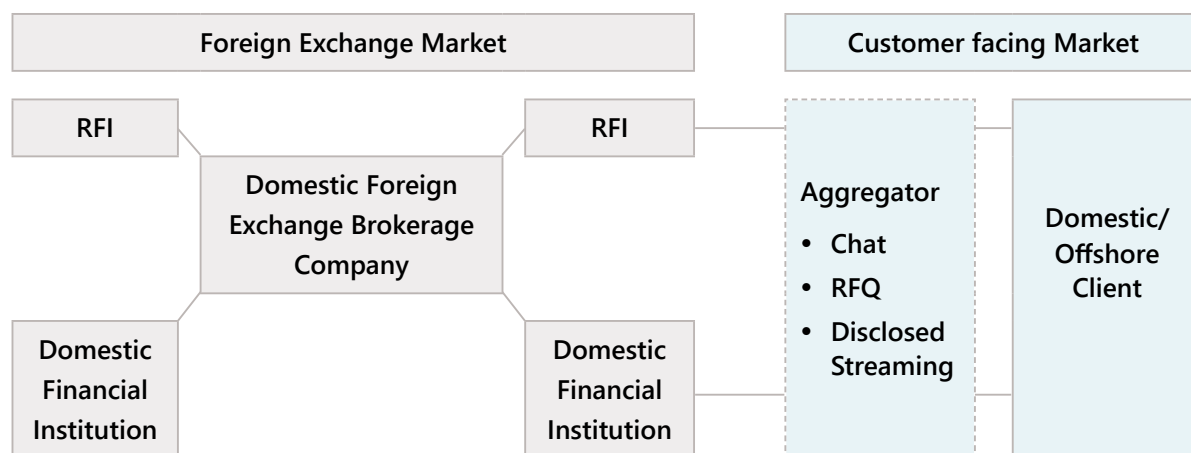
II. Extension of market hours of the domestic foreign exchange market.

The market hours of the Domestic FX Market, which is currently from 09:00am to 3:30pm (Seoul time), will be extended to 02:00am (Seoul time) on the following day, which is the closing of the London market.

III. Building advanced market infrastructure.

The implementation of the Plan will bring the following changes related to the Products and their settlement.

- A. Electronic transactions: The FX electronic brokerage business (commonly referred to as 'aggregators') will be permitted. Then, RFIs participating in the Domestic FX Market will be permitted to transact Products with domestic/offshore clients through aggregators as illustrated in the below diagram.



- B. Third party foreign exchange transactions: Currently, non-residents can only exchange currencies at domestic banks where they have opened an account. This account requirement will be waived, and RFIs will not be required to open settlement accounts with each domestic bank, therefore creating procedural and cost efficiencies.

- C. Continuous linked settlement ("CLS"): The RFI which opens a settlement account with a domestic CLS agent bank will be able to use the CLS' KRW related service.
- D. RFI reporting system: A separate and more efficient reporting system for RFIs will be established as it is currently onerous for RFIs to report transaction records by using the existing foreign exchange network operated by the Bank of Korea.

The MOEF plans to conduct a pilot operation of the Plan in the first half of 2024 after revising the relevant regulations. The Plan will be officially implemented in the second half of 2024.

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For any inquiry or questions regarding the content of this newsletter, please contact us.

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