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APAC Corporate Governance Season Review 2023/24

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Navigating the evolving landscape of corporate governance in Asia

In 2023, the corporate governance landscape across mainland China, Hong Kong, Taiwan, South Korea and Japan experienced significant regulatory changes and market evolutions, reflecting a shift toward enhanced transparency, shareholder rights and sustainability. This review comprehensively examines these developments, underscoring the unique challenges and progress in each market.

The Shanghai and Shenzhen stock exchanges revised listing rules under the guidance of the State Council General Office (**SCGO**) and China Security Regulatory Commission (**CSRC**), significantly enhancing the role of independent directors. These changes, coupled with the introduction of new environmental, social and governance (ESG) disclosure requirements, signalled a substantial shift toward greater transparency and accountability in governance practices.

The year saw the Hong Kong Stock Exchange (**HKEX**) implementing major revisions in its listing rules, expanding the scope of equity incentive plans and placing greater emphasis on disclosure and approval processes. Notably, the cancellation of H-Share class meetings marked a shift toward simplifying decision-making processes in dual-listed companies.

The most significant development in Taiwan involved the completion of the Corporate Governance 3.0 - Sustainable Development Roadmap by the Financial Supervisory Commission (**FSC**), which heralded new sustainability-focused action plans. The year also witnessed the introduction of English disclosure requirements and initiatives enhancing board diversity and independence.

In South Korea, we saw a surge in shareholder activism, with a notable increase in shareholder proposals driven by demands for governance reform. The Korean market's unique challenges, including the "Korea discount" and transparency issues, continued to shape corporate.

And lastly, similarly to the South Korean market, in Japan, we observed a record number of shareholder proposals and an increase in shareholder activism as a whole. We examine the key contentious topics that were common among Nikkei 225 constituents throughout the year.

China: Directors in the focus of investors and regulators

Main regulatory updates and forthcoming changes

In August 2023, the Shanghai Stock Exchange (**SSE**) and the Shenzhen Stock Exchange (**SZSE**) revised the listing rules in accordance with the guidance of the SCGO and CSRC, aiming to create a formalized, modern ruleset concerning independent directors to enhance their role in the corporate governance system.[1][2][3] The main revisions include the following:

Enhance independence: Independent directors must have no conflicts of interest with the listed company, major shareholders, or the ultimate controlling entity. Additionally, there should be no other relationships that might affect their ability to make independent and objective judgments. Nomination entities are prohibited from nominating individuals without meeting these criteria, and a commitment to compliance is required.

Defining duties: Specific provisions regarding the responsibilities and rights of independent directors have been outlined. Listed companies are required to develop detailed rules following these provisions, and independent directors are mandated to actively participate in decision-making and provide professional advice.

Performance optimization: The establishment of a special meeting mechanism for committees of independent directors is stipulated. This includes detailed regulations on responsibilities, operations, safeguards, and prereview matters. Additionally, companies are required to specify the audit committee's responsibilities and establish regulations to disclose detailed information in board resolutions on the circumstances in which the board has not adopted or fully adopted the recommendations of the Nomination Committee and the Remuneration Committee based on their responsibilities.

In late August 2023, the third draft of the *People's Republic of China Company Law* was submitted for review and public opinion solicitation.[4] The revisions for listed companies included many key changes. The draft contained requirements for fiduciary duties and "substantial" directors, here understood as controlling shareholders or parties who functionally execute director roles despite not having formal directorship positions, are required to fulfil the fiduciary duties the same as directors, supervisors and management. It also established a system for directors' and senior executives' liability insurance and strengthened regulations on related-party transactions. Finally, the changes also stipulated new provisions for the audit committee and shareholder proposal regulations; shareholders with 1% or more of shares can submit proposals to the general shareholder meeting, and companies can no longer raise the proposal threshold. These revisions will be effective on July 1, 2024.

The revision of the listing rules and the upcoming revision of corporate law provide support for enhancing the independence of directors and initiating reforms in various aspects, such as appointment, performance and oversight.

In addition, there are several new regulations related to ESG disclosure being published this year. In February, the SZSE imposed annual ESG reporting requirements on major pollutant emitters.[5] In August, SCGO published the *ESG Disclosure Guidance for Central State-owned Listed Companies*[6], a standardized ESG reporting guidance that comprises three sections with 132 indicators and metrics.

Key proxy advisor topics for 2023

Institutional Shareholder Services (ISS) made no significant adjustments to its voting guidelines applicable to the Chinese market in 2023. The proxy advisor only revised the definition of market prices in employee stock ownership plans, in line with CSRC requirements. Glass Lewis modified its policy to refrain from recommending votes against individuals in cases of small board sizes. For share incentives, Glass Lewis will recommend voting against remuneration resolutions when the exercise price discount for restricted shares exceeds 50% of the market price.

1. http://www.sse.com.cn/lawandrules/sselawsrules/stocks/mainipo/c/c_20230804_5724639.shtml
   https://www.szse.cn/lawrules/rule/stock/supervision/t20230804_602477.html
2. Measures for the Administration of Independent Directors of Listed Companies
3. https://www.gov.cn/zhengce/zhengceku/2023-04/14/content_5751463.htm
4. http://www.npc.gov.cn/npc/c2/c30834/202308/t20230828_431188.html
5. https://www.szse.cn/www/lawrules/rule/allrules/bussiness/t20230210_598652.html
6. http://www.xinhuanet.com/2023-08/07/c_1212252896.htm

In practice, support rates from ISS and Glass Lewis for equity incentive plan proposals both declined in 2023. ISS had a support rate of 39.31%, marking the second consecutive year of decline. Glass Lewis' support rate was 66.55%, declining for the fourth consecutive year. Additionally, in 2023, Glass Lewis' support rate for director elections was 71.52%, showing a 6.08-percentage-point decrease compared with the previous year, whereas ISS had a marginal increase of approximately 0.5 percentage points.

Outlook and trends for 2024

Considering the latest regulatory policy changes in 2023 and the progress in the reform of state-owned enterprises in China, anticipated market development trends for 2024 include:

Increased director disclosure. Expect more disclosure related to director information, particularly for independent directors. Independent directors and their nominators will likely provide additional explanations to demonstrate independence and make commitments regarding the diligent performance of their duties.

Increased ESG report disclosure. During the 2023 annual reporting season, the number of A-share listed companies disclosing ESG reports increased by 105.32% compared with 2022. We mainly attribute this growth to the disclosure requirements of the State-Owned Assets Supervision and Administration Commission (SASAC) for ESG reports, which aims for full coverage by 2023.

Equity incentive plan rebound. The number of equity incentive plan proposals in the Chinese market experienced a nearly 30% year-over-year decline in 2023, mostly due to factors such as the macroeconomic downturn and the stagnant performance of stock prices. We expect a significant increase in equity incentive plan proposals in 2024 as the economy stabilizes and plans from 2021 expire.

Hong Kong: More detailed share incentive regulations and the cancellation of H-share class meetings

Main regulatory updates and forthcoming changes

Effective from Jan. 1, 2023, the HKEX revised Chapter 17 of the Main Board Listing Rules[7] and Chapter 23 of the GEM Listing Rules[8]. These amendments extend the regulatory framework from share option schemes to include share award schemes, applicable to listed companies and their principal subsidiaries (subsidiaries contributing over 75% of profits). The new regulations bring more stringent requirements in scheme formulation, disclosure and approval processes for listed companies. The specific revisions are as follows:

Eligible participants: Expansion to cover more participant types. Eligible participants for share options and share award schemes include employee participants, related entity participants and service providers. Service providers encompass individuals working for the company as independent contractors but exclude placement agents or consultants providing services for fundraising, mergers or acquisitions. It also excludes providers of certification services or professionals with independence requirements, such as auditors and valuation experts.

Scheme mandate limit: Introduction of a 10% cap on the total outstanding share option and share award scheme amount relative to the company's issued share capital. For service providers, the company must establish a sublimit within the overall limit, subject to separate approval by the shareholder general meeting. Companies can apply updates to the total amount and service provider sublimit, but not more frequently than every three years. If an update is requested within three years, it requires approval by independent shareholders at a shareholder general meeting, excluding controlling shareholders, non-independent directors, senior management and their related persons.

Individual participants: The company must disclose the grant recipients, grant terms, the purpose of incentivizing these grant recipients and alignment with the incentive purpose. If the cumulative grant scale of share options or awarded shares to a single grant recipient exceeds 1% of the company's total outstanding shares (or 0.1% for non-independent directors, executives and their associates) within any 12 months, separate shareholder approval is required.

Pricing: Establishment of minimum exercise prices for options. The exercise price for options must not be lower than the higher of the closing price on the grant date and the average market price for the preceding five trading days. Share award schemes have no pricing requirement and theoretically can be granted with zero cost.

Vesting period: Establishment of a standard vesting period. In principle, the vesting period for awards should not be less than 12 months (previously 6 months). In specific cases, the vesting period for employee participants can be less than 12 months. The company must provide clear disclosure of the reason, and the board of directors must explain the rationale for adopting the shorter vesting period if the employee is a director or executive.

Performance target disclosure: Companies are mandated to disclose at least qualitative descriptions of performance appraisal targets and reward clawback mechanisms. If such mechanisms are not in place, a clear negative statement is required. If these mechanisms are not set for directors and executives, the remuneration committee of the company must explain.

For companies dual-listed in Hong Kong and mainland China, based on the regulatory requirements in both regions, certain types of resolutions necessitate the convening of separate shareholder general meetings for A-share and H-share shareholders. In response to regulatory changes to mainland China, HKEX updated its listing rules in August 2023, removing the requirement for separate shareholder meetings for A-share and H-share shareholders[9]. Listed companies must now amend their Article of Association accordingly.

In addition, HKEX issued a consultation paper in April, seeking market opinions on proposed enhancements to climate-related disclosures under the ESG framework. Originally set to be implemented on Jan. 1, 2024, the effective date for the relevant amendments to the listing rules has been postponed to Jan. 1, 2025, owing to the International Sustainability Standards Board's (ISSB's) release of the final Sustainability Disclosure Standards in June 2023, indicating the forthcoming issuance of an adoption guide to support jurisdictional regulators in considering the implementation of ISSB standards[10]. This delay is intended to afford issuers more time to adapt to the new climate-related disclosure requirements. The adoption guide is expected to be released by the end of 2023.

7. https://en-rules.hkex.com.hk/sites/default/files/net_file_store/Update_138_Attachment.pdf
8. https://en-rules.hkex.com.hk/sites/default/files/net_file_store/Update_73_Attachment.pdf
9. https://en-rules.hkex.com.hk/sites/default/files/net_file_store/Update_143_Attachment.pdf
10. https://www.hkex.com.hk/News/Regulatory-Announcements/2023/231103news?sc_lang=en

Key proxy advisor topics for 2023

In 2023, ISS adjusted its Hong Kong policy in the following key areas.[11]

Director independence: ISS provided a clear definition of directors who are considered not independent because they provide professional services to the company.

Equity compensation plan: ISS included equity incentive plans sourced by share buybacks in the calculation of dilution rates.

General share issuance mandates: ISS specified that both cash and noncash considerations must be included in the calculation of the issuance size.

Glass Lewis also made adjustments to its 2023 Hong Kong policy in three areas.

Board performance evaluation: Glass Lewis will no longer refrain from recommending shareholders vote against an overcommitted executive director who holds more than four directorships outside the company.

Equity-based compensation: Glass Lewis adjusted its policy to align with the new rules of the HKEX. It is worth noting that while the HKEX allows companies to grant share options or awards to service providers, Glass Lewis explicitly stated in its policy that they do not support companies granting awards to external individuals, such as customers, suppliers, subcontractors or agents.

ESG information disclosure: Glass Lewis also mentioned changes in the regulatory rules of the HKEX.

Regarding the cancellation of H Share class meetings, both ISS and Glass Lewis have not explicitly discussed this in their policies. Generally, investors and proxy advisors hold a negative view on matters that diminish the rights of H shareholders. However, since the change is related to adjustments in market regulatory rules, whether market opinions will ultimately change remains to be seen.

Outlook and trends for 2024

In 2023, we observed many listed companies adjusting the existing content of their equity incentive plans in accordance with the rules of the HKEX. For listed companies that will be reviewing new equity incentive plans in 2024, it is noteworthy that, with the inclusion of share award schemes within the regulatory scope, companies will need to consider prudent allocation and provide more detailed information disclosure when designing equity incentive plans.

For companies dual-listed in both Hong Kong and mainland China, the H-share class meeting has played a longstanding role in safeguarding the interests of minority H shareholders. However, it has also increased the complexity for companies in making significant decisions. Since the promulgation of new rules, many listed companies have begun exploring the simplification of decision-making processes by considering the elimination of the H-Share class meeting. We anticipate that proposals related to amendments to the Articles of Association may become a focal point of market attention in 2024.

Regarding sustainability disclosure, the market still needs to wait for more specific rules from the HKEX as of now.

11. Source: ISS' 2023 Hong Kong Proxy Voting Guidelines Benchmark Policy Recommendations.

Taiwan: The roadmap to improved corporate governance standards

Main regulatory updates and forthcoming changes

In August 2020, the FSC launched the Corporate Governance 3.0 - Sustainable Development Roadmap (**the Roadmap**), a three-year program to strengthen sustainability and corporate governance and to align them with international standards. At its conclusion in 2023, the government launched the Sustainable Development Action Plans for TWSE and TPEx Listed Companies (2023) (**the Action Plans**) as one of the new guidelines for corporate governance development.

The Action Plans target objectives across five main dimensions, including net-zero goals, sustainable governance culture, disclosures, stakeholder communication, and sustainability evaluation and digitalization. As new regulations emerge, companies will be required to gradually adhere to them, with larger companies, in terms of market capitalization, expected to lead. Additionally, foreign investors play an essential role in Taiwan's capital market, especially in the semiconductor industry where they account for more than 44%[12] of investment. The gradual expansion of new regulations also takes foreign investors' holding into consideration.

With the purpose of enhancing transparency of information, all TWSE-listed companies must now provide English versions of shareholder meeting handbooks, annual reports and financial statements[13] from 2023. In addition, sustainability reports are now compulsory for TWSE-listed companies with paid-in capital between NT$2 billion and NT$5 billion. Additionally, regulations to enhance the timeliness of disclosures are in the process of covering all listed companies. It is now required that annual reports are provided at least 14 days before shareholder meetings and shareholder meeting handbook be provided 30 days before meetings. The requirement was first adopted by listed companies with paid-in capital of at least NT$10 billion or for those with more than 30% share capital held by foreign investors. The regulations will expand to those with paid-in capital of at least NT$2 billion in 2024 and to all listed companies in 2027. Some regulatory changes are also on the way. For example, on Aug. 1, 2023[14], the FSC proposed revisions to lower the substantial shareholding disclosure threshold to 5%. The new regulations will be effective in 2024.

In addition to transparency requirements, changes occurred to investor interaction and voting to enhance stakeholder engagement and communication. Effective from 2023, the FSC will expand the scope of companies required to provide electronic voting channels from TWSE/TPEx-listed companies to emerging stock companies[15].

Also taking place in 2023, the TWSE revised its Corporation Operation Directions for the board of directors, putting particular focus on the implementation of corporate governance. The directions stipulate that companies are required to appoint a corporate governance officer, a chief executive for corporate governance matters, from June 30, 2023. In response to concerns about board elections, the amended directions require at least three independent directors on the board, up from the previous requirement of two. By 2027, boards will be required to comprise at least one-third of independent directors, compared with the current target of one-fifth. Moreover, as one of criteria of director's independence, tenure of independent directors may not exceed three terms. By 2024, the majority of independent directors must meet the tenure criteria and by 2027 independent directors may not serve on the board for more than three terms.

Another main topic of board composition is diversity. When it comes to gender diversity, the FSC encourages at least one female director appointed by 2024 as part of the Action Plan. In 2025, listed companies, with directors of either gender accounting for less than one-third of the board, shall provide the reason and plans for improvement in annual reports.

Key proxy advisor topics for 2023

ISS and Glass Lewis revised their 2023 voting policies. The updates focus on topics including related-party transactions, director nomination, board independence, accountability for climate risks and equity-based compensation plans.

12. https://www.twse.com.tw/zh/trading/foreign/mi-qfiis.html
13. Important_Milestones_of_Corporate_Governance_in_Taiwan_January_to_March_2023.pdf (sfi.org.tw)
14. https://www.fsc.gov.tw/ch/home.jsp?id=96&parentpath=0,2&mcustomize=news_view.jsp&dataserno=202308010002&dtable=News
15. https://webline.sfi.org.tw/download/resh_ftp/CG/2022/Important_Milestones_of_Corporate_Governance_in_Taiwan_2022.pdf

In the ISS voting guidelines, the only update specific to the Taiwanese market was with respect to related-party transactions. Following new legislation in January 2022, shareholder approval is required for related-party transactions exceeding 10% of a company's total asset value. Therefore, ISS expects a substantial number of such proposals and will consider related-party transactions on a case-by-case basis going forward. The APAC-relevant changes in the ISS guidelines also apply to the Taiwanese market, which include board accountability for climate-related issues and disclosure requirements for companies with significant greenhouse gas (GHG) emissions.

Glass Lewis, on the other hand, updated its voting guidelines for several topics, including board structure, board and committee effectiveness, and equity-based compensation plans. Glass Lewis links board size and independence to nominating committee performance in two ways. First, it will recommend voting against the nominating committee chair if the size of the board is not appropriate in their view. Second, it will target the nominating committee chair if issues are identified in terms of board independence, gender diversity, or poor attendance at board or committee meetings. Other changes relate to the independence of nominating committees and their chairs. Regarding equity-based remuneration plans, Glass Lewis clarified that a 20% exercise price discount for stock options would be the upper limit that it accepts, while leaving more discretion for considering the acceleration of award vesting based on the achievement of performance targets.

Although ISS did not announce policy updates for equity-based compensations this year, it opposed a relatively high number of resolutions that addressed equity-based plans and capital increases related to equity-based compensation, including restricted share unions. Apart from the updates in their voting guidelines, ISS and Glass Lewis generally share concerns about insufficient board nominee disclosure, including where representatives of institutional or governmental shareholders remain undefined.[16]

Beyond proxy advisors, investors tended to express dissent for a wide breadth of reasons. Typical governance issues apply here including board independence, gender diversity, committee independence, as well as other concerns. However, there are also some Taiwanese market specifics that cause dissent. For example, the majority of Taiwanese companies elect their directors as a slate. Because international investors usually do not favor slate elections, they apply strict rules for supporting slates. Often, even one candidate who investors consider unqualified may result in high dissent rates for the entire slate's election. Contested director elections also often generate split shareholder opinions on candidates sitting on the board. Finally, family-owned enterprises may cause controversies and conflicts in director elections.

Other proposals that proxy advisors and investors pay close attention to are those related to capital issuances, especially private placements. ISS suggests that most Taiwanese boards have minimal or no independent representation. Given the prevalence of insider-dominated boards in Taiwan, ISS places strict limits on the authorization for issuing shares by way of a private placement to reduce the risk of abuse by insiders for their own benefit. Glass Lewis applies even tighter rules on dilutive private placements that allow share price discounts.

Institutional investors are likely to also update their voting policies based on market trends or to take ISS and Glass Lewis recommendations as reference for their voting decisions. Because of this, these updates typically come out after the proxy advisor update cycle and can be expected in early 2024.

Outlook and trends for 2024

Following the end of Corporate Governance 3.0 in 2023, the Sustainable Development Action Plans (2023) is regarded as one of the new guidelines for corporate governance best practices in Taiwan. Together with the inclusive characteristics of the Taiwanese market, the following topics will likely be dominant in 2024:

- **Board functions and independence** — Starting in 2024, boards will be expected to further improve their gender diversity and skillsets. They will be required to set numerical targets for board seats of independent directors and female representatives. Moreover, standardized tenure criteria for independent non-executive directors represent a further development in corporate governance.
- **Director overcommitment** — From 2024, Glass Lewis will lower the overcommitment threshold for directors who also serve as executives to a total of two directorships from three directorships. It will focus on executives and will recommend voting against overcommitted executives at the company where they serve as an executive if they hold more than four directorships.
- **Remuneration/compensation policy** — Reasonable performance evaluation and a fair compensation system are crucial to the sustainable governance

16. Sources: ISS' 2023 Taiwan Proxy Voting Guidelines Benchmark Policy Recommendations; Glass Lewis' 2023 Policy Guidelines - Taiwan.

culture. The TWSE is incorporating metrics linking executive compensation to sustainability-risk management performance in the Corporate Governance Evaluation indicators. In addition, the FSC stipulates that director compensation should be reported to shareholders at the AGM. In 2024, the TWSE and TPEx will consider mandatory reporting director compensation based on the feasibility study.

- **English disclosure** — Timely English disclosures and documents will be required for companies with a share capital of NT$600 million and above, and it is expected that this will expand to more listed companies.
- **ESG disclosure** — With regulatory support, investors may expect ESG disclosure to be widely available in certain industries in accordance with globally accepted standards.

The new developments show the increasing importance of sustainability in Taiwan. Nevertheless, corporate governance remains the solid foundation upon which the ESG concept functions. Good corporate governance ensures transparency, accountability and business resilience for shaping long-term success.

South Korea: Activism rife with growing number of shareholder proposals

Increasing number of shareholder proposals

In the recent few years, the South Korean market witnessed a significant increase in shareholder activism, both activist funds and individual shareholders actively exercise their votes to affect the management in efforts to enhance shareholder rights. Shareholder activism increased significantly in 2023 owing to the acceleration of actions toward governance reform. The number of shareholder proposals reached a record-high level this year, increasing about 71% from those in 2022, where the domestic investors, including some minority shareholders, have contributed momentum to the upward trend since at least 2020. Among 284 shareholder proposals in 2023, about 24% of the proposals were related to returning cash to shareholders and about 31% were related to board composition. In 2023, activist investors raised concerns related to ESG issues, capital distribution and board composition, aiming for minority shareholder protection.

ESG factors have been considered as a significant portion of activism campaigns. Activist investors make efforts to influence the management with demands for improving corporate practices related to environmental sustainability, social responsibility and governance standards.

Several significant regulatory changes as a part of corporate governance reform have been announced to enhance minority shareholders' rights. Therefore, shareholder activists targeted the entrenchment of controlling stakeholders as well as the protection of minority shareholder rights through seeking capital return. Domestic activist investors increasingly demanded capital return in the form of dividends and share buybacks.

Coupled with the new administration's National Agenda in 2022, the domestic investor community appeals for actions to enhance minority shareholders' rights and diminish South Korea–specific governance valuation discounts, the so-called Korea discount. The Korea discount has been a long-lived issue where South Korean companies are valued lower than their international peers, particularly family-controlled conglomerates.

Minority shareholder rights have been one of the main concerns in South Korea for a long time, which the characteristics of the South Korean market may contribute to. The market is dominated by large, family-controlled conglomerates, so-called "chaebols". Chaebols have complex cross-shareholding structures, which often lead to concerns about transparency and minority shareholder rights. The lack of minority shareholder right protection resulted in a significant proportion of shareholding proposals related to board composition, no matter board representation, board independence or removal of a board member. The general issues in family-control enterprises are the dominance of family members in senior management and board fights, which account for concerns about board composition. Therefore, activist investors hope to push for changes to ensure that the management acts in the best interest of shareholders, including introducing independent directors or altering the structure of the board.

Corporate governance reform: Progress and obstacles

A rising number of activist investors are targeting South Korea while domestic activist investors run a new round of campaigns that target the Korea discount. The Korea discount triggers investors' need for more transparent and efficient corporate practices and becomes a push for corporate governance reform. These reforms aim to address issues such as complex ownership structures and more independent board structures. However, corporate governance reform may face some obstacles. Fortunately, in 2023, the market still witnessed some progress in the relaxation of regulations on foreign investment, availability of English documents as well as disclosures on corporate governance practices. Foreign investors' participation may provide more possibilities for activist investors.

In February 2023, it was announced that the government would scrape complex registration requirements for foreign investors to trade Korean stocks, which would allow offshore financial companies to participate in the local currency market with its opening time for an additional 10 hours daily from the second half of 2024. The planned changes benefit foreign investors, allowing them to invest in local capital markets with internationally recognized identifications. The efforts are aiming to attract more long-term foreign fund flows into the local market.

As part of efforts to improve the accessibility of the South Korean capital market for foreign investors, the Financial Services Commission (FSC) and the Korea Exchange (KRX) will also introduce the English disclosure requirements in 2024, tackling the unequal access to information between foreign and domestic investors. Korea Composite Stock Price Index (KOSPI)-listed companies with over 10 trillion South Korean won in total assets will be required to publish English regulatory documents within three days of filing their regulatory disclosures in 2024. In addition, KOPSI-listed companies with between 2 trillion won and 10 trillion won in total will be subject to this obligation if foreign investors hold more than 30% ownership. The English disclosure will expand to the scale of listed companies with 2 trillion won in total assets in 2026.

Another process in the South Korean corporate governance reform is the availability of corporate governance reports. On a "comply or explain" basis, the corporate governance report should be against 15 key indicators, including shareholder rights, board structure and independence and so on. The report was first voluntary in 2017 and became mandatory for companies with total assets up to 2 trillion won in 2019 and companies with total assets up to 1 trillion won in 2022. The regulation will be applied to all KOSPI-listed companies in 2026.

On the other hand, however, in November 2023[17], South Korean regulators again imposed a blanket ban on short-selling in response to naked short selling. The ban came into force on Nov. 6 and is due to last until June 2024. Local retail investors have long demanded such a blanket ban on short-selling while institutional investors show concerns in response to this ban. With the announcement of the short-selling ban, institutional investors faced a new cap of a maximum of 90 days of borrowing of stocks for short selling.

Additionally, the timeliness of disclosures, as well as the concentration of shareholder meetings, remain obstacles for investors to actively exercise their shareholder rights. In South Korea, the notice and circular for a general meeting is publicly available at least 14 days before the meeting date, as mandated by the Commercial Act, while public notice of audited financial statements is at least seven days prior to the annual general meeting. Although the availability of English regulatory documents makes it convenient for foreign investors to conduct analysis and exercise voting rights, the discrepancy in the timing of disclosures could also be a challenge not to mention during the proxy season when institutional investors may deal with the concentration of shareholder meetings. Despite the government's effort to mitigate the concentration of the meetings, the market still witnesses more than 64% of companies hold their AGM during the last week of March and 93% in the last two weeks of March in 2023.

Outlook and trends for 2024

Governance issues, such as a lack of audited financial statements, board independence, gender diversity, capital distribution and excessive cross-holdings between companies, remain significant concerns for many investors and the main reason for the Korea discount. Poor transparency will continue to be a leading issue in these governance concerns. These concerns will likely remain popular targets for activist complaints in 2024.

Disclosure and transparency: The discrepancy in the timing of disclosures suggests that audited financial statements are not necessarily available when investors review the proposals regarding approval of financial statements. On one hand, the mandatory English disclosures, to some degree, will resolve issues of unequal information between foreign and domestic investors. On the other hand, the English disclosure could be published after regulatory disclosures, making the situation challenging for foreign investors. While transparency may improve in 2024, the timeliness of disclosure remains a challenge.

Gender diversity: After a two-year grace period from 2020, the gender quota law in South Korea became effective in August 2022. The law demands listed companies with total assets of more than 2 trillion won to have more than one gender on the board. However, despite the required quota and a two-year grace period, some large companies still have no female directors on the board. Glass Lewis, in response to increasing demands for board diversity, set a target of at least 10% gender diversity on the board in its 2024 South Korea voting policy[18], shifting from a fixed numerical approach, at large companies subject to the mandatory gender quota. The percentage-based approach reflects further demands from investors for board diversity.

17. https://www.ft.com/content/1dd9b025-9007-401e-9010-ebc083e67a38

18. https://www.glasslewis.com/wp-content/uploads/2023/11/2024-Korea-Benchmark-Policy-Guidelines-Glass-Lewis.pdf?hsCtaTracking=a2f686cd-6a76-46c9-820c-52b124d35f7f%7Cd8f0ec76-b969-4b09-8e3f-1cde2d63da51

Board independence: The long-debated argument on the lack of minority shareholder protection may be eased through improvement in board independence. Therefore, board independence will remain one of the main targets for activist investors. Notably, the classification of employee representatives may become a new argument. The employee representative, also known as “labor director” in Korean, was introduced for government-owned companies in August 2022, as required but the Act on the Management of Public Institutions (the Act). While the Act requires an employee representative appointed as a non-executive director, the commercial law allows non-executive directors to be registered only as independent or non-independent, lacking a specific classification for employee representatives. Consequently, this has led to confusion on the classification as well as board independence.

Capital distribution: As a significant consideration for protecting minority shareholders, shareholder demands in capital distribution, including dividends, share repurchases and return cash to shareholders, have remained an increasing trend in the last four years, from 8.3% of shareholder proposals in 2020 to 23.6% in 2023. The momentum is likely to continue in 2024, considering the rising trend in activist demands and campaigns.

Japan: Record shareholder proposals and the rise of activism

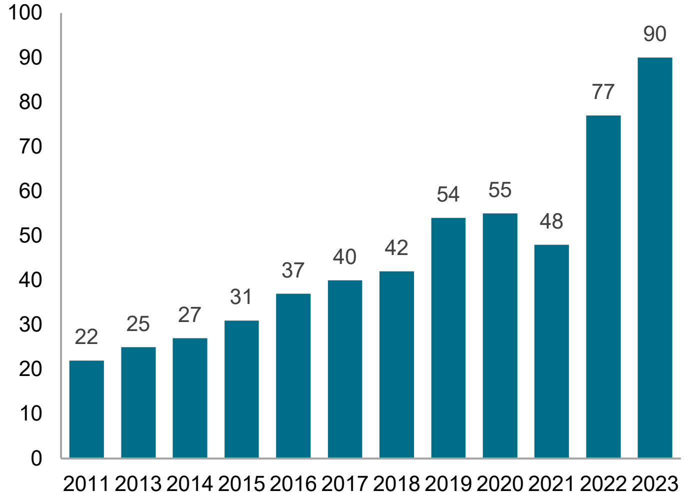
In 2023, a record number of shareholder proposals were submitted in the Japanese market. While activist efforts focused on the low capital efficiency of Japanese companies have been on the rise for some time, other topics such as board independence and remuneration also contributed to the growth. Furthermore, the Tokyo Stock Exchange's (TSE) March 2023 notice reinforced this trend by urging the top management of listed companies to take action and be conscious of both the cost of capital and stock prices.

Increasing shareholders activism in Japan

Shareholder proposals were submitted to 90 companies in June 2023, which is significantly higher than the previous record of 77 companies set just in the previous year (Figure 1). Shareholder proposals most frequently addressed shareholder returns. This category was followed by article amendments related to corporate governance, which typically focused on issues such as increasing the ratio of outside directors. (Figure 2)

Figure 1

Number of company AGMs with shareholder proposals



Data compiled December 2023.
Data for each year looks at meetings that occurred in June.
Source: S&P Global Market Intelligence.
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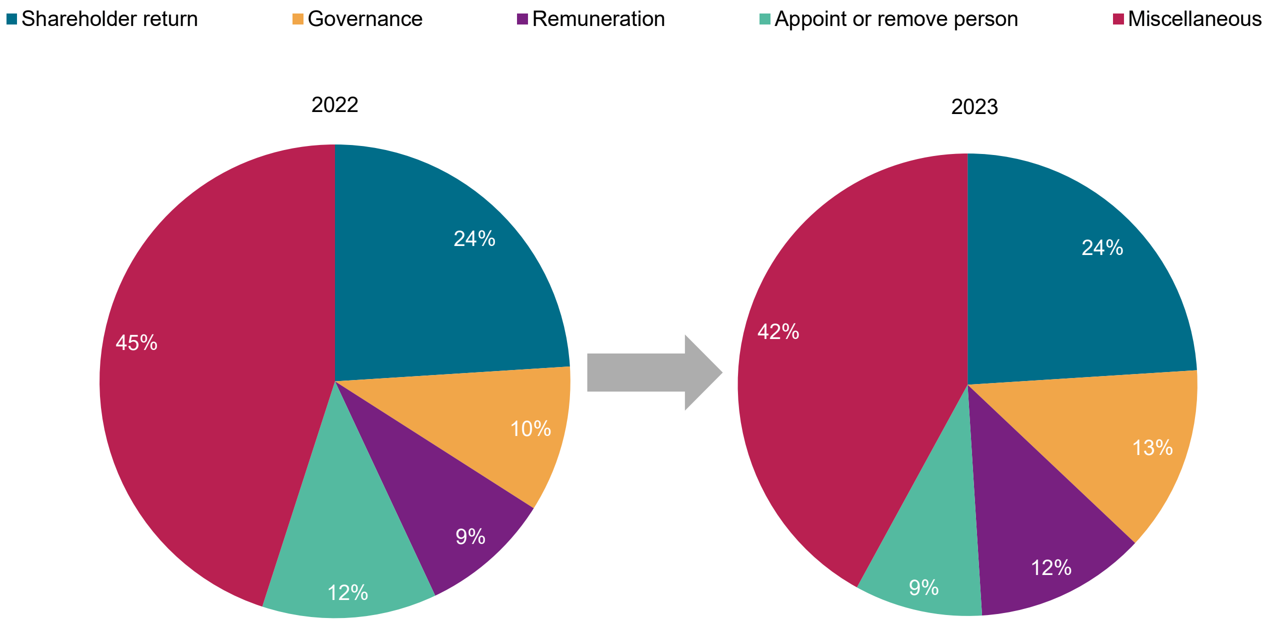
Remuneration concerns were also frequently targeted. Finally, since a relatively large number of Japanese companies are considered cash-rich, proposals calling for increased shareholder returns were commonly submitted by activists.

Figure 2

Types of shareholder proposals



Data compiled December 2023.
Data for each year looks at meetings that occurred in June.
Source: S&P Global Market Intelligence.
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Changes in voting guidelines

ISS introduced new guidelines for 2023, stipulating that they would recommend against top executives when there are no female directors on the board. Glass Lewis, which already introduced similar criteria previously, raised its gender diversity requirements from a single female director to 10% of the board. In line with both proxy advisors, many large institutional investors also introduced similar criteria or sharpened their guidelines.

Opposition to management proposals

The following table lists the 10 management proposals with the highest dissent this year among the Nikkei 225–adopted companies (Table 1). As in previous years, investors tended to strongly sanction non-independent outside directors and auditors. However, in accordance with the changes in voting guidelines mentioned above, there was also an accumulation of votes against proposals based on gender criteria this year. Activist voting and the TSE's notice regarding cost of capital and stock price awareness, led to deeper discussions on the nature of the board of directors of listed companies. These discussions center increasingly on board composition, diversity and independence — topics that will only continue to grow in importance in the coming years.

Outlook and trends for 2024

Activists and institutional investors will continue putting pressure on companies to improve their boards, which can be seen in investor guidelines that have already been published for the Japanese market. Nomura Asset Management Co. Ltd. was the first investor to announce its 2024 policies, stating that it will vote against chairman and president (re-)appointments for boards that do not comprise a majority of outside directors.[19] Sumitomo Life Insurance Co. also strengthened the independence criteria, although its requirements only specify one-third of outside directors.

Daiwa Asset Management Co. Ltd. aims to strengthen the role of the board of directors by requiring all listed companies to establish a nominating and a compensation committee[20], whereas JPMorgan Chase

Table 1

2023 AGM, ranking of against ratio (%) of Nikkei 225

	Company	Agenda	Against	Main Reason
1	Dowa Holdings Co. Ltd.	Elect Shingo Komuro	49.8	Lack of Independence
2	Canon Inc.	Elect Fujio Mitarai	49.3	Lack of genders
3	NGK Insulators Ltd.	Elect Hiroyuki Kamano	43.6	Long tenure
4	Sumitomo Mitsui Financial Group Inc.	Elect Yasuyuki Kawasaki	42.7	Corporate scandal
5	Taiheiyo Cement Corp.	Elect Akihisa Sada	41.7	Lack of independence
6	Fujikura Ltd.	Allocation of profits/dividends	40.2	Financial results delay
7	Sumitomo Osaka Cement Co. Ltd.	Elect Hirotsune Morohashi	39.6	Due to big shareholders' criteria
8	Kansai Electric Power Co. Inc.	Elect Takamune Okihara	39.2	Lack of independence
9	Kikkoman Corp.	Elect Toshihiko Fukui	35.7	Long tenure
10	Toppan Inc.	Elect Yoshinobu Noma	35.4	Long tenure

Data compiled December 2023.
Date of Nikkei 225 ranking period: July 2022–June 2023.
Source: S&P Global Market Intelligence.

19. Sources: Nomura Asset Management's "Global Proxy Voting Policy" and "Proxy Voting Standards for Japanese Companies".

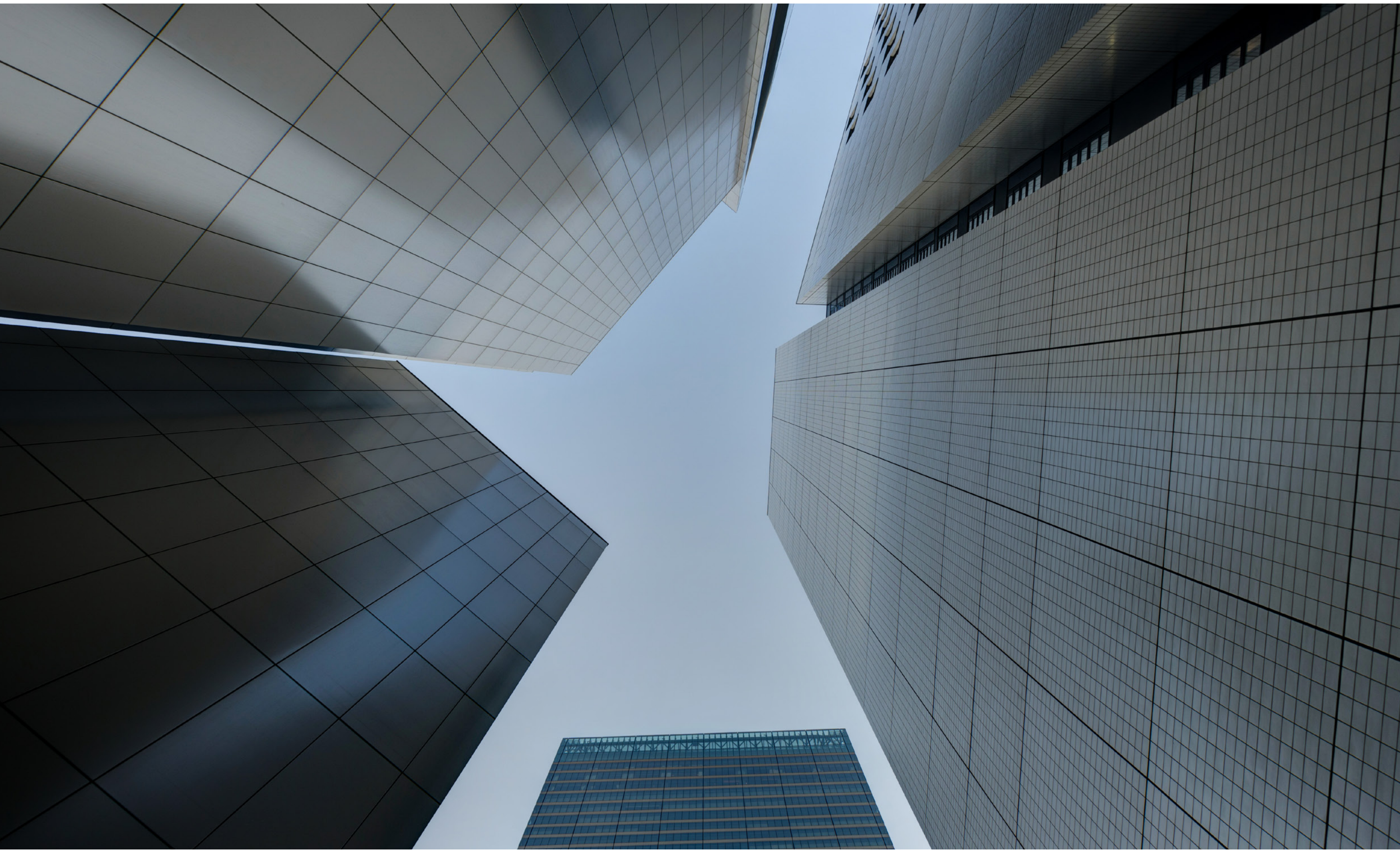
20. Source: Daiwa Asset Management's Voting Policy (for domestic stocks).

& Co. expects at least two female board members by 2024, and even 30% by 2030.[21] All these developments show that the board of directors has come into focus for investors, and companies should be aware of their stricter expectations in terms of composition, independence and gender diversity.

This year was marked by the rise of activism and improved corporate governance. Shareholder proposals reached a record high. At the same time, the role of directors was often controversial. In addition to proxy fights at shareholder meetings, there were activist campaigns that questioned directors' representation of shareholder interests, director expertise, and the adequacy of the director selection process in the first place. However, shareholder proposals are only one part of the full picture. The following perception section presents the opinions of key market participants on the state of the board of directors.

21. Source: JPMorgan's 2023 Global proxy voting guidelines.

Appendix I: The perception of corporate governance in Japan



Investor intelligence

In anticipation of the 2023 shareholder meeting season, S&P Global Market Intelligence's Corporate Governance Solutions team interviewed portfolio managers, sector analysts and corporate governance specialists from major market participants. The interviews centred on the state of corporate governance and the challenges that Japanese companies are facing in maximizing corporate value. The following are representative opinions of these analysts:

Management to increase corporate value

"In order to increase corporate value, it is only natural for a company to rebuild the performance of its core business and secure sufficient earnings, but if the company does not focus on achieving results that exceed its cost of capital in conjunction with this, the market will not value the company highly." (European Asset manager)

"I feel that many Japanese companies are not managed in a way that maximizes corporate value. Unless there is a mechanism to have the same perspective as shareholders or to share risks with shareholders more, seriousness of management will not be conveyed. For example, it would be possible to convey seriousness by devising a compensation system by introducing a stock compensation system that is more linked to business performance and stock price. If management does not come up with measures that convey that they are serious about the company, we will not see management's will to truly raise the share price and corporate value." (Domestic Pension Fund)

The state of the medium-term management plan

"The mid-term management plan should set financial KPIs and link this to directors' compensation. Just showing the right sense of direction is not enough to truly achieve it. It is also difficult to know how committed the management team is. For example, if performance falls short of the mid-term management plan, directors' remuneration should be reduced, etc. There should be a clarification of each management responsibility and an internal and external demonstration of the management team's commitment to change." (Domestic Asset manager)

"I would like to see an explanation of the long-term vision in the medium-term management plan. For example, even if it is supported that the company will carry out structural reforms by 2025, if it is unclear what will happen after the structural reforms are carried out, it will be difficult to read the future prospects of the company." (US sell-side analyst)

"Many Japanese companies are hoarding cash and building up retained earnings to prepare for future risks as the Japanese market shrinks due to population decline. As a result, there are many examples of Japanese companies, five or six in number, surviving in what would be a global market with only two or three competitors, and continuing to compete for a limited piece of the domestic pie. In a shrinking domestic market, it is not an appropriate business decision to have many companies competing for a limited and shrinking pie. However, I cannot support the mid-term management plan, which I suspect is driven by an unwillingness to relinquish the current position or an incentive to protect vested interests." (US Asset manager)

"The medium-term management plan that the company has developed should not be compromised simply because it is an improved strategy. We should not give up on further earnings gains because of the difficult business environment. At this point, should we give up our efforts to maximize corporate value and allow corporate value and stock market valuations to remain as they are now, or should we pursue our efforts and double or triple our value? The decision here will be the watershed for corporate value in the future." (US Asset manager)

The state of directors and the board of directors

"With regard to the supervisory function, the emphasis is on quality rather than formality. Recently, the ratio of outside directors, gender, management experience, and whether the directors have the required knowledge in line with management strategy are also important, but these are formal requirements, so to speak, and we do not judge whether the supervisory function is sufficient based on these alone. However, these are formal requirements, so to speak, and are not the only criteria used to determine whether the supervisory function is sufficient. Since this is not properly monitored by outside directors and the board of directors, no actions or comments have been issued, and we believe that the supervisory function is not being fulfilled." (European Asset manager)

“There are cases where outside directors do not grasp management issues. Before exercising appropriate supervisory functions, outside directors do not have a proper grasp of the company’s issues. On the other hand, there is also a problem with the way directors are selected. For example, in cases where acquisitions of foreign companies are key to management, we would like to see outside directors with international management experience. It is difficult to believe that a board of directors that lacks the appropriate skills and expertise and cannot grasp management issues can properly manage an overseas subsidiary.” (Domestic sell-side analyst)

“There is a problem of ‘Keiretsu’ in the governance of Japanese companies. Outside directors are invited from banking groups. For example, in the alcoholic beverage industry, the largest company has an affiliated director with Sumitomo, the second with Mitsubishi, and the third with Mizuho. There is a colour division by bank affiliate, and the issues of transactions, personal relationships, and pride associated with this division make restructuring more difficult in some areas. This is why it is important for the composition of the board of directors to break away from the bank’s colour with a view to restructuring.” (US Asset manager)

“There are still few companies that disclose succession plans. We are confirming through dialogue whether or not successors have been properly allocated. We are also using the skill sets in the overall composition of the board of directors to engage in dialogue. Many companies have developed skill sets for their boards, and in some cases it is unclear why each item has been selected or checked, but it is better than nothing. By reviewing the skill sets and interacting with them, it is possible to understand the thinking of the company and its management. Then, items that are considered necessary can be presented and the future direction can be discussed. For the company’s part, we hope that through these discussions, they will reconfirm the qualities and roles required of directors, and create or reconsider a succession plan.” (European Asset manager)

Market participants’ expectations on the board of directors

“My understanding is that they almost never contact outside directors. That has been a welcome improvement, but they probably need to gather more feedback from market practitioners to really understand how the market is That has been a welcome improvement, but they probably need to gather more feedback from market practitioners to really understand how the market is looking, how the market is thinking, and what their concerns are.” (Asian asset manager)

“If outside directors cannot raise questions about whether the company’s investment policy is really safe, then they cannot be said to speak for the shareholders. Outside directors of foreign companies are likely to have a higher sense of urgency in their supervision. If outside directors with such a sense of urgency make up the majority of directors, a governance system that is trusted by shareholders can be established. Outside directors who are serious about increasing corporate value can be trusted to work with shareholders in mind. If they then engage in a vigorous dialogue with shareholders, they will gain the trust of the market. As long as they treat stock market participants as if they were living in a different world, they will never be outside directors who can speak for shareholders.” (Domestic Pension Fund)

“Japanese companies need people who understand corporate finance at both the management and working level. The skill to view management from the shareholder’s perspective is necessary, and a fundamental knowledge of corporate finance is needed. For example, why should a company buy back its own shares when the share price is low? Why are share buybacks better than dividends? What are the tax benefits behind it? What is the perspective of the business portfolio? Why should excess retained earnings be returned to shareholders? Many Japanese companies buy back their own shares without understanding the technicalities and basic philosophies of corporate finance, so shareholder return policies often do not function effectively.” (European Asset manager)

* Statements by persons who are not S&P Global Market Intelligence employees represent their own views and opinions and are not necessarily the views of S&P Global Market Intelligence.

Appendix II: Proxy advisors' 2024 guidelines' updates summary

Executive summary

As the 2024 proxy season approaches, S&P Global's Corporate Governance Solutions Team has meticulously reviewed the guideline updates from prominent proxy advisors ISS and Glass Lewis. This paper focuses on the changes to mainland China, Hong Kong, Taiwan, South Korea and Japan voting policies and identifies significant developments vital for investor engagement and voting decisions.

ISS guidelines overview

Hong Kong

ISS amended its policies to now recommend against the election of nominee(s) who are part of the nomination committee if all the independent non-executive directors of the company have served more than nine years on the board, and the company fails to:

- Disclose the length of tenure of each existing independent non-executive director on a named basis in the circular to shareholders and/or explanatory statement accompanying the notice of the annual general meeting
- Appoint a new independent non-executive director on the board at the company's next annual general meeting.

Japan

Resumption of the "return on equity" policy after the impact of the pandemic subsides.

- Vote for the election of directors, except top executive(s) at a company that has underperformed in capital efficiency, unless an improvement is observed.

Adjusting the exceptions around takeover defense plans (poison pills) to reflect the latest development in the Japanese market:

- A new condition has been added where ISS will vote for the takeover defense plans (poison pills) if independent directors who meet ISS guidelines on attendance comprise a majority of the board after the shareholder meeting.

Glass Lewis guidelines overview

Mainland China, Hong Kong, Taiwan

Director commitment

Glass Lewis has reduced its overcommitment threshold for directors who also serve as executives of any external public company to a total of two directorships (previously three), and for executives who hold more than four directorships.

Equity-based compensation plan

- Glass Lewis revised its policy related to the vesting period of an equity-based compensation plan.
- For the mainland China and Hong Kong markets, Glass Lewis specified some entities that can be incentivized.

Independent director tenure

Glass Lewis explicitly delineates the impact of the tenure of independent directors on independence in different markets, providing specific thresholds and exceptions.

Mainland China and Hong Kong

Issuance of debt instrument

Glass Lewis explicitly outlines the disclosure requirements for the issuance of debt instruments.

South Korea and Japan

Gender diversity

For Japanese listed companies and large South Korean listed companies (assets of 2 trillion won or more), Glass Lewis applies board gender diversity thresholds of 10%.

Cyber risk oversight

Glass Lewis will seek to hold directors accountable if they fail to diligently oversee cybersecurity matters or disclose information adequately, particularly when the company is significantly affected by a cyberattack.

Market-specific updates

- **Mainland China:** Glass Lewis adjusts its evaluation criteria for the performance of the audit committee and nomination committee. In addition, Glass Lewis will examine the reason for the postponement of director elections on a case-by-case basis.
- **Hong Kong:** Glass Lewis will hold the members of the remuneration committee accountable when it believes the director's compensation is not reasonable or sufficiently disclosed. Glass Lewis also provides a detailed list of factors to be analyzed and its principles in related party transactions.
- **Taiwan:** Glass Lewis has removed content related to the election of supervisors and the exemption for directors related to noncompete restrictions.
- **South Korea:** Glass Lewis will align the employee representative with the company classification. It also added the policies related to virtual-only meetings and modified the evaluation criteria for proposals related to financial reports.
- **Japan:** Glass Lewis introduces new policy related to the board accountability for climate-related issues, and future policy adjustments to excessive strategic shareholding positions and board composition and refreshment.

Conclusion

ISS and Glass Lewis' updates for 2024 focus on director-related matters. In addition, Glass Lewis has introduced new policies on compensation and incentives, related party transactions, and general governance. Overall, the voting guideline changes are noteworthy, as they indicate a shift toward more robust governance practices and could significantly influence investment performance across different regional markets.

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