IHS Markit

APAC 2021 Proxy Season Review

Part 3. South Korea

ihsmarkit.com

South Korea is home to highly competitive, global business conglomerate groups such as Samsung, LG, SK, and Hyundai. However, the market has faced skepticism on its conglomerates' corporate governance structure for some time. The *chaebol* structure, in which a family controls a business conglomerate group through a holding company or circular shareholding, has been criticized for creating agency problems, standing to decrease shareholder value in the long-term. In CG Watch 2020, published by CLSA and ACGA, South Korea ranked ninth out of 12 APAC countries on evaluation of corporate governance.[1]

[1] https://conference.acga-asia.org/wp-content/uploads/2020/11/CGW2020_mini_report.pdf

The so-called "Korea discount" which closely relates to the less-transparent governance issue was pointed out as an important issue from various market participants. Both government and the National Assembly are driving changes to resolve this issue. Korea Exchange (KRX) will require all KOSPI-listed companies with assets exceeding KRW 1 trillion to disclose a corporate governance report from next year. This review will briefly point out recent changes in the market regarding corporate governance issues and voting summaries.

2021 Voting Policies

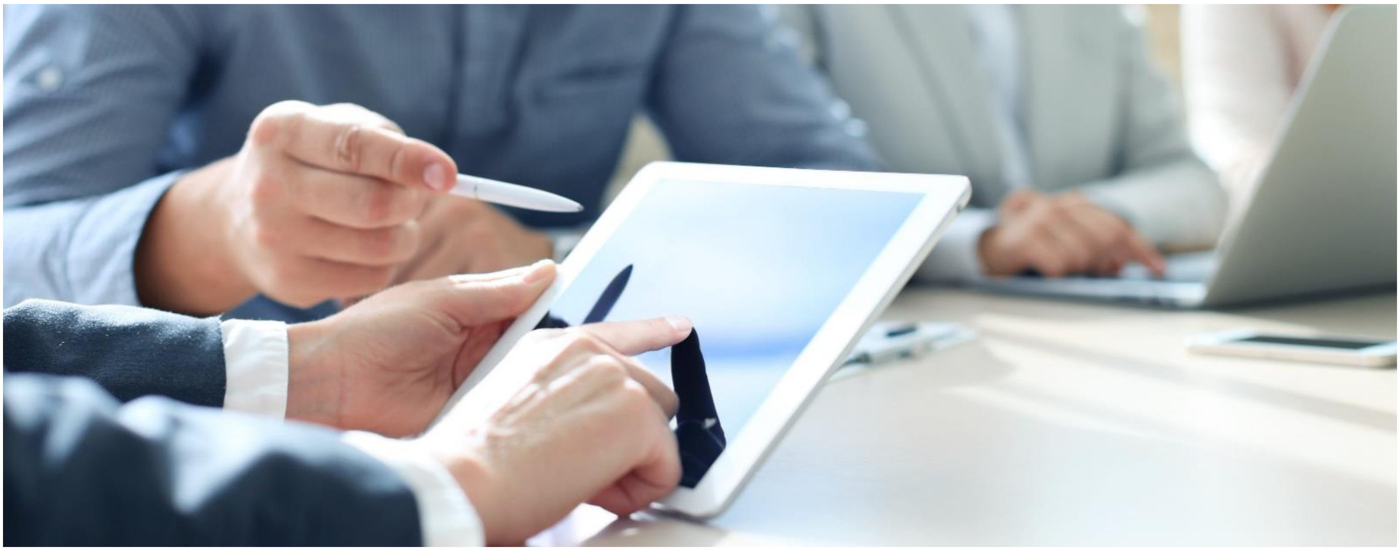
In the end of 2020, Institutional Shareholder Services (ISS) and Glass Lewis revised their voting guidelines corresponding to regulatory developments and shareholder-activism momentum, touching upon topics mainly related to board elections. Both ISS and Glass Lewis added board gender diversity requirements to all large companies. Glass Lewis' policy will officially take effect from 2022. Glass Lewis updated the definition of affiliated directors by applying a term limit for independent directors. ISS added a dedicated section regarding contested board elections. On top of board elections, Glass Lewis also updated its related-party transaction thresholds to align with global policy.

There were a few changes made in the proxy guidelines of influential South Korean proxy advisors as well. The three major advisors (KCGS, DERI, Sustinvest) mainly advise South Korean asset management firms and asset owners. It is safe to say they have significant influence on South Korean capital market in the proxy season. KCGS made a minor change to the tenure cap of independent directors as the Enforcement Decree of the Commercial Act was revised early 2020 allowing independent directors to serve in the same company up to six years. Sustinvest added an opposition criterion on reelection of non-independent executives. It will monitor attendance rates of board members and, if their participation is lower than their standard (75%), they will oppose reelection. This was only applied to independent directors previously, but Sustinvest will have stricter standards on the duty of non-independent executives. The details of the guidelines can be found in the appendix.

Table 1: Summary of changes in proxy voting guidelines

Proxy Advisory Firms	Changes
ISS	Added 1) board gender diversity requirement 2) a section regarding contested elections
Glass Lewis	Added a board gender diversity requirement, and updated 1) the definition of affiliated directors, 2) related-party transaction thresholds
KCGS	Changed the maximum tenure of independent directors (7years → 6 years) according to amended Commercial Law
DERI	No revision in 2021
Sustinvest	Included board attendance rate (minimum 75%) as new criterion on the reelection of non-independent executive members. This criterion was included for reelection of independent directors only in 2020 proxy guidelines.

Meanwhile, South Korea's biggest asset owner, National Pension Service (NPS), did not make any changes in its voting guidelines this year. Its stewardship philosophy is important because it affects the voting behavior of asset managers who are mandated with voting rights and asset management responsibilities from NPS. However, this year, NPS did emphasize its view on Environmental, Social, and Governance (ESG) integration in its investment strategy. Yongjin Kim, CIO of NPS, publicly announced in November 2020 that NPS aimed to integrate ESG into up to 50% of assets by 2022.[2] This implies that the ESG journey will impact not only South Korean equity, but fixed income and foreign equity as well. The steady increase in ESG integration implies NPS will have a greater focus on sustainability in its invested capital and enhanced engagement activities.



Voting Trends in the 2021 Proxy Season

Summary of 2021 Voting Records of KOSPI50

South Korea's Annual General Meeting (AGM) season is highly concentrated from the last week of February to the last week of March. According to the Korea Securities Depository (KSD), for the past five years (2017-2021), approximately 88.3% of companies ending fiscal years in December hosted their AGMs from 21-31 March. This so-called "Super AGM season" can affect how investors monitor their investee companies. Limited time and resources in the busy season can lead to stronger reliance on company disclosures, rather than on direct communication. In addition, the shortened voting period can deter foreign investors from casting their votes in a timely manner and tends to encourage reliance on proxy-advisor vote recommendations rather than facilitate direct engagement between corporations and investors.

For further analysis on voting trends at the most influential Korean companies, IHS Markit gathered voting results of institutional investors in KOPSI 50 companies' shareholder meetings hosted this year (from 1 January to mid-October).[3] Out of 104 meetings recorded, the against rate was 13.3%, while the support rate was 85.4%. Resolutions with highest dissent rate were on board elections (18.7% opposition in total). The next-highest dissent rate was on committees and reporting, which includes approvals for auditor compensation (70.6%), approvals of dividend payment (13%), and approvals of financial statements (15.7%).

[2] https://www.mk.co.kr/news/stock/view/2020/11/1150146/

[3] Voting record is from Governance Insight, and the recorded

Table 2: Summary of South Korea's voting results by resolutions

Resolution Type			Proposals	Meetings (#)	Votes (#)	For (%)	Agt (%)	Split (%)	Abs (%)
Board of Directors	Director Re/Elections	Approve Re/Election of Directors	M	94	44,678	80.4	18.3	0.8	0.5
		Approve Re/Election of Directors (Shareholder Proposal)	S	2	463	4.5	91.6	1.5	2.4
	Director Terms & Conditions	Approve/Amend Director Retirement Payments	M	11	1,233	93.7	5.7	0.4	0.2
	Total			95	46,374	80	18.7	0.8	0.5
Committees & Reporting	Audit/Fiscal Committee	Approve Election to Audit/Fiscal Committee	M	57	12,979	90.3	8.7	0.6	0.5
	Auditors	Approve Auditor Remuneration	M	4	323	29.1	70.6	0	0.3
		Auditor Ratification	M	1	60	93.3	6.7	0	0
	Financial Statements & Reports	Approve Allocation of Profits/Dividend	M	93	11,907	84.4	13	0.5	2.1
		Approve Financial Statements & Statutory Reports	M	2	351	78.6	15.7	3.4	2.3
	Total			98	25,620	86.6	11.5	0.5	1.3
Corporate Structure	Articles/By Laws	General Changes	M	58	10,031	96.9	2.5	0.1	0.5
	Capital Change	Approve/Amend Level of Treasury Shares	M	1	97	100	0	0	0
	Capital Reduction	Approve Capital Cancellation/Reduction	M	1	95	98.9	0	0	1.1
	General Company	Approve/Amend Employment Contract	M	1	115	99.1	0	0.9	0
	Mergers & Acquisition	Approve Disposal of Assets/Spin-off	M	8	972	86	12.1	0.9	0.9
	Total			63	11,310	96	3.3	0.2	0.5
General Governance	General Company			1	115	99.1	0	0.9	0
	Shareholder Meetings – General Procedures			1	119	100	0	0	0
	Total			1	119	100	0	0	0
Remuneration	Director Remuneration	Approve Aggregate Board Remuneration	M	1	203	99	1	0	0
		Directors' Remuneration (Binding)	M	91	11,855	93.2	5.8	0.3	0.7
	Equity-Based Plans	Approve/Amend Stock Option Plan	M	16	3,034	86.7	11.9	0.5	0.9
	Total			91	15,092	92	7	0.3	0.7
Total				**104**	**98,515**	**85.4**	**13.3**	**0.6**	**0.7**

M stands for management proposals and S stands for shareholder proposals

Source: Governance Insight

Controversial Proposals from Management

One noticeable feature from last year, including Extraordinary General Meetings (EGM), was that there were multiple conglomerate group spin-offs and split-offs, which were intended to split business segments into new entities. Spin-offs grant the ownership of a newly created entity to existing shareholders. In split-offs, shareholders do not gain shares of a newly created company, which may be the main reason for shareholder criticism as they can lose their voting rights in important and lucrative business divisions. In such a situation, shareholders are unable to express their opinions though shareholder meeting resolutions on spun-off/split-off business divisions.

In the table above, we see that the opposition rate of resolutions for approvals of spin-offs and disposals of assets was 12.1%, one of the highest dissent rates. From September 2020 through September 2021, there were 43 cases that approved disposal of assets/spin-offs in South Korea. Most of them were supported by proxy advisory firms, as Glass Lewis supported 94.3% and ISS supported 87.5% of the cases.[4] When faced with negative market voice on such transactions, transparent communication between management and investors as well as proxy advisory firms was likely important. In such cases, management dictates how it will convey key messages, including the objective of the reform, expected positive outcome, and how shareholder interest will be supported in the long-term.

The following table is a summary of key foreign institutional investors with significant influence on South Korean capital markets. Most of them did not have distinguished voting guidelines for spin-offs and split-off, an element not limited to these investors. As corporate restructuring is a special occasion, investors analyze impact on a case-by-case basis, taking into account the rationale of the reform (both from a strategic and governance point of view), market reaction and sentiment, and the impact on shareholders and other stakeholders. What this implies is corporates must know how to convey their objectives and concerns effectively to investors. As investors are becoming more vocal during proxy season, the degree of companies disclosing relevant information would influence how the market will view their new governance structure.

[4] From Governance Insight

Table 3: Guidelines of foreign institutional Investors on split-offs and spin-offs[5]

National Pension Service	The Vanguard Group, Inc.	BlackRock Fund Advisors	Norges Bank Investment Management	J.P. Morgan Asset Management (Asia Pacific), LTD
Company spin-off and spin-off merger 1. Will review on a case-by-case basis, but object if it is there is damage to shareholder value. 2. If the Fund intends to secure the stock purchase right, NPS may object or abstain.	A fund will vote case-by-case based on a number of criteria, including the following: • Board and management oversight of the deal process • Valuation • Prospects for long-term enterprise value • Market reaction • The surviving entity's governance profile • Fairness opinions from independent financial advisors • Effect on stakeholders, if relevant to long-term value In evaluating board oversight, independence, potential conflicts of interest, etc (from US guideline)	In assessing mergers, asset sales, or other special transactions, BlackRock's primary consideration is the long-term economic interests as shareholders. Boards proposing a transaction need to clearly explain the economic and strategic rationale behind it. We will review a proposed transaction to determine the degree to which it enhances long-term shareholder value. We would prefer that proposed transactions have the unanimous support of the board and have been negotiated at arm's length.	We will not support mergers, acquisitions and other corporate transactions where there is insufficient transparency. We will not support mergers, acquisitions and other corporate transactions that do not treat all shareholders equitably, or where there are conflicts of interest that could negatively affect shareholders. We will not support mergers, acquisitions and other corporate transactions that do not create long-term value for shareholders.	Votes on spin-offs should be considered on a case-by-case basis depending on the tax and regulatory advantages, planned use of sale proceeds, market focus, and managerial incentives.

Source: Investors' Voting Guidelines

Conclusion

In conclusion, proxy fights between management and shareholders are not so common in South Korea, where a founding family normally owns the majority of total voting rights. However, shareholder activism has surely increased over the years due to multiple factors such as the adoption of the Korea Stewardship Code and easing regulations for shareholder activism.[6] As of October 2021, there were 170 market participants who adopted the code.[7] Also, the growing interest in new ESG investment trends, such as issuance of ESG bonds, are raising the market's awareness. According to the Korea Herald, South Korea has floated more bonds associated with environmental, social, and sustainability issues this year than in all of 2020.[8] This dynamic market momentum will surely impact the future AGM season.

[5] Most investors do not have distinguished guidelines for split offs and spinoffs
[6] http://www.businesskorea.co.kr/news/articleView.html?idxno=35755
[7] http://sc.cgs.or.kr/eng/participation/investors.jsp
[8] http://www.koreaherald.com/view.php?ud=20210812000717

Appendix

Table 4: Summary of major changes in proxy guidelines in South Korea

Proxy Advisory	Changes	2021 Guideline
ISS	1. Added board gender diversity requirement 2. Added section regarding contested elections	Board Diversity: Generally vote against the chair of the nomination committee (or other senior members of the nomination committee on a case-by-case basis) up for election if the company is non-compliant with the board gender diversity regulation. In making any of the above recommendations on the election of directors, ISS generally will not recommend against the election of a CEO, managing director, executive chairman, or founder whose removal from the board would be expected to have a material negative impact on shareholder value. Voting on Director Nominees in Contested Elections: ISS will make its recommendation on a case-by-case basis, determining which directors are best suited to add value for shareholders. The analysis will generally be based on, but not limited to, the following major decision factors: ▪ Long-term financial performance of the company relative to its industry; ▪ Management's track record; ▪ Background to the contested election; ▪ Nominee qualifications and any compensatory arrangements; ▪Strategic plan of dissident slate and quality of the critique against management; ▪ Likelihood that the proposed goals and objectives can be achieved (both slates); and ▪ Stock ownership positions. When analyzing a contested election of directors, ISS will generally focus on two central questions: (1) Have the dissidents proved that board change is warranted? And (2) if so, are the dissident board nominees likely to effect positive change (i.e., maximize long-term shareholder value).
Glass Lewis	1. Added board gender diversity requirement 2. Updated the definition of affiliated directors 3. Updated related party transaction thresholds	Board Diversity: We have decided to apply the board gender diversity requirement to all large companies from January 1, 2022, which is 6 months earlier than the legal deadline. For 2021, we will only include a mindful note in our reports for large companies if their boards consist of only one gender. From January 2022, we will recommend voting against the nomination committee chair (or the board chair in the absence of nomination committee) if the board consists of only one gender. We will, however, exempt from recommending against anyone in particular in the case that board gender diversity is our only concern regarding the board. Affiliated Director: A director whose maximum term of office exceeds the legal thresholds of total six years at the company or total nine years within the Company and its affiliated companies. Related Party Transaction Threshold: We will recommend voting against a director if his/her direct/indirect related party transactions exceed any of the following thresholds: (i) US$50,000 or no disclosure for personal direct

		transactions; (ii) US$120,000 for indirect transactions with an entity in which a director holds more than 50% interest; (iii) US$120,000 for indirect professional services transactions with a professional services firm in which a director works for; or (iv) 2% of a company's consolidated gross revenue for indirect transactions with an entity in which a director serves as an executive.
KCGS	Changed the maximum tenure of independent directors (7years → 6 years) according to amended Commercial Law	2.1 (Reasons for Disqualification of Outside Director Candidates) Those who have been in office for more than 6 years, including the new term, as an outside director at the company or affiliated company.
DERI	No revision in 2021	
Sustinvest	Included Board attendance rate (minimum 75%) as new criterion on reelection of non-independent executive member This criterion was included for reelection of independent director only in 2020 proxy guideline.	III.1 Appointment of inside directors. III.1.2 On the basis of objective facts, we oppose the candidates nominated by the Board of Directors in the following cases. 5) Persons who have less than 75% of the company's board of directors in the last year of the previous term (considered only in case of re-election).

Authors

Yura Ahn
Senior Associate, Strategic Governance and ESG Integration Advisory
Yura.Ahn@ihsmarkit.com

Ms. Ahn joined IHS Markit ESG, M&A and Corporate Governance Advisory Team in 2020 and is part of global Issuer Solutions team. She is currently guiding Korean and other APAC based client issuers to successfully prepare and host shareholder meetings, mitigating any possible risks in communication with shareholders and other stakeholders. She also has experience of managing proxy solicitation projects, engaging with proxy advisory firms and foreign institutional investors. Prior to joining IHS Markit, she worked as ESG analyst in Korea Corporate Governance Service (KCGS) based in Seoul, specializing in Responsible Investment Analysis and Proxy Advisory for buy-side. Her main role was to analyze corporate governance risks of listed companies and guide asset owners and managers on shareholder engagement. She also provided proxy advisory service to asset owners including National Pension Service (NPS) and Korea Post. She has experience and knowledge on investment stewardship as she worked in Korea Stewardship Center, supporting the establishment of Korea Stewardship Code.

Emily Wang
Senior Associate, Strategic Governance and ESG Integration Advisory
Emily.WangW@ihsmarkit.com

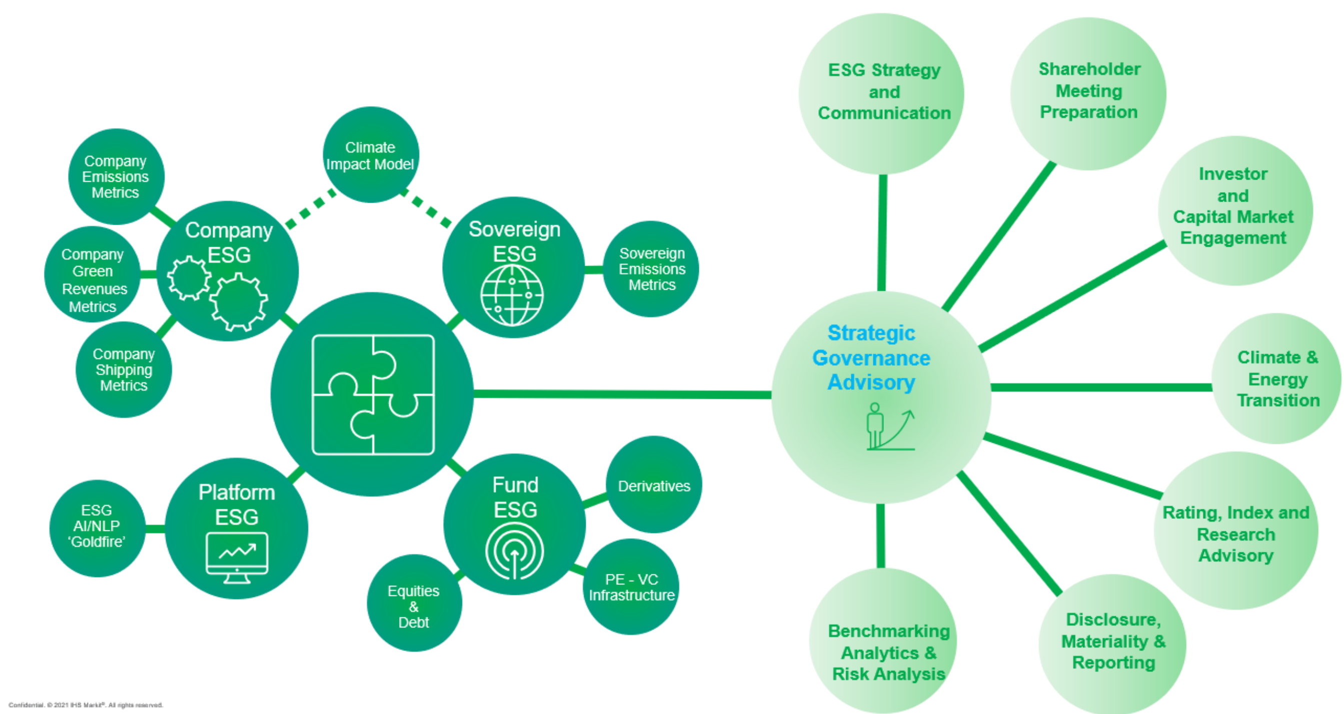
Ms. Wang is responsible for advising issuers on ESG risks and investor engagement for different transactions and shareholder meeting resolutions. Before IHS Markit, Ms. Wang was a senior consultant at Ernst & Young's Climate Change and Sustainability Services (CCASS) team based in Shanghai advising an extensive list of onshore companies and also offshore MNCs with onshore investment ventures. Her primary coverage is on the advisory for ESG-related strategy, management, capital market engagement, data and reporting, while also having experience providing due diligence for cross-border M&As on the ESG-risk dimension. She has participated in numerous ESG projects within corporates across a wide spectrum of sectors, including technology, real estate, retails, resources, and tourism, and have experience in elevating corporate ESG performances in various leading indices, rankings, or ratings that result in the alignment of ESG and business interest.

How IHS Markit can add value…

Our advisory program helps companies position themselves to benefit from the growing ESG-linked capital pool and proactively prepare for the regulatory, reporting and industry trends that are relevant to each business. Our global team advises at board and management level as well as with investor relations, communications, and sustainability teams.

Our team will tailor the solutions so that companies can:

- Analyze top investors' ESG DNA
- Target existing and potential ESG-focused investors
- Advise, plan, and facilitate investor engagement on ESG issues
- Assess capital market sentiment with ESG focus
- Understand the influence of a particular ESG rating and various of disclosure framework
- Automation in multi-ESG framework reporting and ESG portfolio management
- Develop ESG strategy with ESG management system and capacity building program
- Implement a climate transition program in line with carbon neutral scenario



For more information visit ihsmarkit.com

CUSTOMER CARE

NORTH AND SOUTH AMERICA

T +1 800 447 2273
+1 303 858 6187 (Outside US/Canada)

EUROPE, MIDDLE EAST AND AFRICA

T +44(0) 134 432 8300

ASIA PACIFIC

T +604 291 3600

JAPAN

T +81 3 6262 1887

E CustomerCare@ihsmarkit.com

About IHS Markit

IHS Markit (NYSE: INFO) is a world leader in critical information, analytics and expertise to forge solutions for the major industries and markets that drive economies worldwide. The company delivers next-generation information, analytics and solutions to customers in business, finance and government, improving their operational efficiency and providing deep insights that lead to well-informed, confident decisions. IHS Markit has more than 50,000 business and government customers, including 80 percent of the Fortune Global 500 and the world's leading financial institutions. Headquartered in London, IHS Markit is committed to sustainable, profitable growth.