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Mr. Young-hun Song
Senior Vice President
Listing Rules & Regulations
KOSPI Market Division
Korea Exchange
33, Yoido-dong, Youngdeungpo-gu
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Dear Mr. Song,

I hope this letter finds you well. I would like to thank you and your team again for hosting the ACGA Korea Study Group's visit to the KRX in September.

As we promised, I am pleased to send you in the attached document ACGA's contribution to your corporate governance reform roadmap. These recommendations were put together with input from our members who are active investors in the Korean stock market. I hope you find the information useful and, should you have any questions, please do not hesitate to contact us.

For your information, we will also be sending a copy of the document to the Financial Services Commission and the Commercial Legal Affairs Division of the Ministry of Justice.

I look forward to continued dialogue with the KRX on corporate governance issues in Korea, and wish you very Happy Holidays.

Yours sincerely,

Jamie Allen
Secretary General

ACGA Feedback to KRX

Issue 1 - Board independence

In general, we feel Korea has so far focused more on ensuring the quantity of outside directors on boards than on their quality. Even though Korea introduced the outside director system in 1998 soon after the Asian financial crisis, we believe that it has not fostered genuinely independent boards among listed companies. In fact, many outside directors seem weak either because they are too friendly with company owner/controlling shareholder or because they lack deep business experiences to question or challenge management's decisions effectively. Also, many outside directors in Korea are professors or former government officials, whose independence can easily become compromised thanks to the relatively high director compensation—especially at bigger *chaebol* companies.

Moreover, there have been a number of cases where inside directors have been convicted of corporate crimes but were reappointed to the board because they are controlling shareholders (eg, SK Group, Hyundai Motor Group). As for the boards of privatised state companies and financial institutions, they still seem to suffer from excessive government influence (eg, KEPCO, Kookmin Bank).

ACGA recommendation:

We recommend Korean market authorities strengthen board independence by:

- More strictly defining who can become an outside director to ensure his/her independence, and setting a ceiling on how long he/she can serve;
- Changing the terminology of directors from “inside” and “outside” directors, to the Korean equivalents of “executive”, “non-executive” and “independent non-executive” directors, to more clearly indicate a director's relationship with a company;
- Separating the roles of chairman and CEO;
- Where the chairman is an executive director or member of a controlling family, creating a new position called “lead outside director” (for a reference, see Section A.4.1 of the “UK Corporate Governance Code 2010”);
- Further enhancing the role of outside directors on board committees, including on audit, nomination and compensation; that is, these committees should be composed of all (audit) or majority (nomination and compensation) outside directors who are genuinely independent and chaired by one; and
- Requiring a certain amount of training for all directors every year.

ACGA's definition of independent director

An independent director should:

- Have an 'independent mind' and be capable of bringing an independent perspective to major corporate decisions.
- Be able to read company accounts and ask sensible questions about them.
- Have the expertise and authority to discuss issues with executive directors as equals.
- Be capable of considering the interests of all shareholders and the company as a whole, including the broader environmental and social risks facing the company.

An independent director should not:

- Have close family or personal ties with any of the company's advisors, directors or senior employees.
- Be a former employee or manager of the company.
- Hold cross-directorships or have significant links with other executive or non-executive directors.
- Be a representative of a major shareholder connected to the controlling shareholder or management, or be representatives of any special interest group, or former employees of such groups.
- Have commercial involvement with the company as professional advisers, major suppliers or customers.
- Be entitled to performance-related pay, stock options, or pensions.
- Hold other directorships in competing companies in a closely related industry.

After an independent director has served for 8-10 consecutive years, the shareholders of the company should evaluate his/her continuing role on the board.

Issue 2 – Shareholder meetings & voting

Access to a transparent and fair shareholder meeting and voting process is a fundamental right of shareholders. Ensuring it is also a reflection of a company's commitment to good corporate governance. Listed Korean companies, however, often treat Annual General Meetings (AGMs) and Extraordinary General Meetings (EGMs) as perfunctory events. Meeting notices are usually sent out only two weeks in advance in line with the minimum requirement in the Commercial Act. But for most foreign investors—who face voting deadlines set by their global custodian banks that are often set 7-10 days before the actual deadline—14 days is simply not enough time to digest all the information and cast their votes intelligently.

At AGMs and EGMs, voting itself is usually carried out by show of hands, rather than by poll—meaning someone with 100 shares and someone with 1m shares would be counted as casting only one vote each. While we know of at least one large listed company that counts the proxy votes received before an AGM/EGM, almost no company publicly discloses detailed voting results (that is, separate counts for votes for, against and abstained) after the meeting. So it is impossible for minority shareholders to see how others have voted on tabled resolutions; many investors would be interested in knowing if a resolution passes with 99%, 80% or 51% of the votes.

ACGA recommendation:

We urge Korean market authorities to improve the shareholder meeting and voting process end-to-end by:

- Lengthening the deadline for listed companies to release the meeting notice and agenda to at least 28 days before an AGM;
- Encouraging listed companies to translate into English their detailed meeting agenda;
- Actively promoting listed companies to adopt voting by poll;
- Actively promoting listed companies to disclose within 24 hours full voting results broken down by votes for, against and abstained on each resolution; and
- Actively promoting listed companies to use the Korea Securities Depository's new e-voting system.

How to vote by poll

For many companies, the term “voting by poll” conjures up the dreaded notion of “voting by ballot”. A ballot refers to cases where companies have to organise an impromptu count of all votes on one resolution, because a few shareholders have called for it. The count is usually done manually—a process that normally takes about half an hour to 45 minutes. The assumption, therefore, is that counting the votes for all resolutions at an AGM would take most or all of the day (since 10-12 resolutions x 30-45 minutes = 5-9 hours).

This is not how modern polls are taken. One cheap and simple method involves collecting completed voting forms from shareholders at the end of the meeting, then closing the meeting and quickly counting the vote (either manually or with computers) before announcing it later the same day, or first thing the following morning, to the stock exchange. This system is common in Hong Kong, where shareholders do not mind waiting a few hours for the final results. Another method is more immediate—using electronic voting pads to cast votes in the meeting, with results shown after just a few seconds. This system is prevalent in the UK and Europe, and is gradually being adopted in Singapore. It is more expensive than the first option, but usually quite affordable for large firms and not unreasonable given the total cost of preparing for and holding an AGM. Many firms also find that the enhanced communication with shareholders and the PR benefits of using wireless voting technology help to outweigh the costs.

It is important to point out that in both cases described above, the length of the AGM is not extended by taking a poll.

Issue 3 – Protection of minority shareholders

The interests of minority shareholders in listed Korean companies are often ignored during corporate and financial dealings initiated by the controlling shareholder or management. For example, only board, rather than shareholder, approval is required for related-party transactions and acquisitions of other companies, while there are no automatic pre-emption rights for existing shareholders when companies issue new shares.

Most recently, SK Telecom was able to acquire a controlling stake (20%) in Hynix Semiconductor despite the opposition of many minority shareholders of SK Telecom who saw little synergy between mobile-telecom operations and computer-chip manufacturing. Moreover, Hynix enabled SK Telecom to raise its overall stake by issuing 101.85m new shares (12.5%) to it at the same time the telecom company acquired half of the 15% Hynix stake held by a consortium of Korean banks. In both instances, neither SK Telecom nor Hynix put their decisions to a shareholder vote—despite the significance of the deal.

ACGA recommendation:

We recommend that Korean market authorities endeavour to bring the rules protecting the rights of minority shareholders closer to global best-practice standards by:

- Requiring shareholder approval for major corporate and financial transactions above certain thresholds, including related-party transactions, takeovers and capital-raising exercises. Furthermore,
 - For related-party transactions, the controlling shareholder should be excluded from voting; and
 - For new share issuances without pre-emptive rights, there should be a ceiling of no less than 20% of total outstanding shares.

A useful reference on thresholds for major transactions can be found in Chapters 14 & 14A of the Listing Rules of the Stock Exchange of Hong Kong. Details on pre-emption rights can be found in Chapter 13. We also recommend the OECD “Guide on Fighting Abusive Related party Transactions in Asia (2009)”.

Issue 4 – CG code

It has been almost a decade since Korea last updated its “Code of Best Practices for Corporate Governance, 2003”, which was first issued in 1999. As a result, some of its recommendations have not kept pace with changing criteria for best practices in other markets globally—or in Asia (eg, director training, voting by poll at shareholder meetings). In recent years, Singapore, Hong Kong, Taiwan, Malaysia and Thailand have all updated their equivalent codes.

ACGA recommendation:

We suggest that KRX make a revision of the Code a high priority and take the lead in reconvening the Committee on Corporate Governance with its other members (Korea Securities Dealers Association, the Korea Listed Companies Association, the Korea Investment Trust Companies Association and the KOSDAQ Listed Companies Association).

- As a preparatory step to a revision, we would like to see the Committee seek out the views of both domestic and international investors in a public consultation process; and
- To give more teeth to the Code, we suggest KRX consider incorporating the Code’s existing “comply or explain” provision (“V.2.3 In the annual report, a public corporation shall explain the differences between its corporate governance and this Code, and the reasons for such; any plans to make future changes shall also be explained.”) into the KOSPI and KOSDAQ Market Listing Regulations. If needed, we would be pleased to provide relevant references from other Asian markets.