



6 September 2023

**To: Financial Services Commission
The Republic of Korea**

**Attn: Mr. Joo-Hyun Kim
Chairman**

**Attn: Mr. So-Young Kim
Vice-Chairman**

**Re: Strengthening Capital Markets and Investor Confidence
through Improved Corporate Governance**

Dear Chairman Kim,

We are writing on behalf of the Korea Working Group of the Asian Corporate Governance Association (ACGA), an independent research and advocacy organisation whose institutional investor members manage more than US\$40 trillion in assets globally. As longstanding capital market investors, we firmly believe that robust laws and regulatory frameworks constitute the backbone for building good governance within listed companies, which is crucial to their long-term success and economic value. With this in mind, we wish to share our views on a number of governance-related regulations and also pose some practical suggestions for your consideration.

Before going into detail, we would like to mention that we gratefully acknowledge the efforts of the Financial Services Commission (FSC) under your leadership to address long-held investor concerns over the past 12 months. These include such things as the (re)introduction of a mandatory takeover rule, mandatory English disclosure rules that start to take effect in 2024, and tightened regulations around split-offs. As long-term investors in Korea, we welcome the FSC's decisive move to improve these regulations. Building on this positive momentum, we would like to draw your attention to other significant issues that remain equally entrenched and unresolved, namely:

- **Long-held treasury shares:** Contrary to their original purpose as a shareholder-friendly measure, treasury shares have been misused by many Korean companies and we believe it is time for the FSC to consider putting stronger and clearer regulations in place. Our view is that companies should cancel treasury shares as soon as possible unless they have a purposeful use for them, such as to reward executives/employees, prepare for imminent M&As, or capital-raising needs. We would also welcome any regulation to make it clear that it is the management and board's responsibility to provide shareholders with a sufficient explanation for uncancelled large volumes of treasury shares, preferably at the AGM.

- **Creeping spread of cross-shareholdings:** Cross-shareholdings remain prevalent in Japan and are regarded as one of the main reasons behind the valuation discounts for corporates there. Unfortunately, we have seen an increasing number of similar cases in Korea since 2015. From our experience investing in Japan, we fear that if Korea followed Japan’s trajectory—ending up with deep cross-held market—then the ability of minority investors to exercise their duties as stewards of capital would be severely curtailed. This would apply even if companies ran their businesses at the expense of sustainability issues and/or minority shareholders’ interests, undermining their long-term viability. We would be left with extremely limited means to resolve these issues. We hope that the FSC can investigate existing regulations and close the gap to prevent additional abuse.
- **Executive compensation:** In many markets around the world, laws and regulations enable shareholders to express their views on executive compensation by exercising votes at AGMs. This is one of the most effective ways to make corporate management align their interests with those of shareholders. Korea has a similar regulation, but it is considered incomplete. This can be attributed to two main factors: 1) Poor disclosure requirements—as companies are not required to disclose the amount of individual executives’ pay, not to mention a detailed breakdown such as fixed pay, short-term and long-term pay/incentives, and key performance indicators that form the basis of incentive awards; and 2) The relevant agenda item at the AGM is usually treated a mere formality. Shareholder votes are sought for ‘the ceiling of total aggregate compensation for board of directors’ that can be paid in the ensuing fiscal year. It is time for the FSC to upgrade the relevant regulations to be on par with those of the advanced markets.
- **Lead-independent director in case of non-independent chair:** Listed financial companies in Korea are required to designate a lead/senior independent director in case the board is chaired by a non-independent director. This effective piece of regulation should be applied to all listed companies, not just financial firms.
- **Independent directors – tenure limit and directorship:** According to the enforcement ordinance of the Commercial Law, independent directors in Korea are allowed to serve on the board of a listed company for up to six (6) years and take up a maximum of two (2) board directorships. We believe that these rules are overly restrictive. Contrary to the original intent to improve board independence and director responsibility, the ordinance forces seasoned independent directors with accumulated industry, technology, and company knowledge to quit a board too early. It is likely that most independent directors will be reaching their peak performance after five or six years and still have much value to add to the company. Given the challenge of finding the right candidates that meet regulations pertaining to directorships, companies typically turn to the easiest solution—academia.

While fully respecting the intent of the relevant enforcement ordinance, we suggest that the FSC consider allowing independent directors to serve up to nine years but with stricter conditions imposed on their re-election for a third term. For example, this could include greatly enhanced disclosure requirements and a higher shareholder approval threshold, such as a super-majority vote. We also suggest that you consider lifting the current maximum limit of directorships to



four or five, but introduce additional conditions, such as counting executive directorships as three and board chairmanships or audit chairs as two, for instance.

We greatly appreciate having the opportunity to express our views to you and would welcome a follow-up meeting or call to discuss our proposals further in the near future. Please contact Ms. Y.K. Park at APG (yk.park@apg-am.hk or 852-3769 0339) or Mr. Jamie Allen at ACGA (jamie@acga-asia.org or 852-2160 1789).

Sincerely yours,

A handwritten signature in black ink, appearing to read 'YK Park'.

YK Park

Managing Director
APAC Responsible Investment & Governance
APG Asset Management
(Chair of ACGA Korea Working Group)

A handwritten signature in black ink, appearing to read 'Jamie Allen'.

Jamie Allen

Secretary General
Asian Corporate Governance Association
(<https://www.acga-asia.org/>)