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STRENGTHENING THE PROTECTION OF SHAREHOLDERS IN CASE OF CHANGES IN CORPORATE OWNERSHIP STRUCTURE SUCH AS SPLIT-OFFS, ETC.

REVISION OF THE CORPORATE GOVERNANCE REPORT GUIDELINES

By reflecting the normative factors of ESG management, the Financial Services Commission (the "**FSC**") amended the Corporate Governance Report Guidelines ("**Guidelines**") on March 7, 2022. Based on such amendment, the FSC announced its plans to: (1) newly establish specific principles to ensure that companies describe their policies to protect shareholders in the event of a change in the ownership structure, such as through a split-off or merger, etc.; (2) strengthen the obligation to explain any insider trading such as with an affiliate or shareholders; and (3) ensure that the CEO succession policy is clearly described, including a plan for installation of an audit committee, if any, thereby enhancing the transparency of corporate management. The key amendments to the Guidelines, and the ripple effects and implications of such amendments are as follows:

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I. KEY REVISIONS TO THE GUIDELINES

A. Application Period[1]

According to the press release by the FSC dated March 7, 2022, the Guidelines will take effect starting on May 2022 and apply to all Reports

1 Certain KOSPI-listed corporations must publicly disclose its corporate governance report (the "**Report**") by May 31 (Article 24-2 of the KOSPI Market Disclosure Regulation, and hereinafter, "**Disclosure Regulation**"). Previously, a corporation whose assets were valued at or more than KRW 2 trillion was required to file a Report ("**Filing Corporation**"). However, starting from 2022, corporations with assets amounting to KRW 1 trillion or more; from 2024, corporations with assets amounting to KRW 500 billion or more; and from 2026, all KOSPI-listed corporations are required to submit the Report (Article 7-2 of the Enforcement Rules of the Disclosure Regulation
Prior to the implementatxion of the Guidelines, the deadlines for submission of the Reports varied by company, depending on a company's settlement month. Now, the Guidelines require all Reports to be submitted by May 31 of each year (Article 24-2 of the amended Disclosure Regulation on November 25, 2021). The relevant period to be included in the Report is from the first day of the year in which the Report is prepared, to the end of such year (e.g., in case of any submission in May 2022, the "recent 2 years" means the period from January 1, 2020 to December 31, 2021).

to be submitted thereon. Furthermore, in the latter half of 2022 (from June to September), the Korea Exchange (the "**KRX**") and the Korea Corporate Governance Service will conduct an overall inspection on the status of public disclosures. If a Filing Corporation fails to submit a Report by the due date, or submits a false disclosure, omits a material fact, etc., sanctions under the Disclosure Regulation such as a request for correction of disclosure, designation as a dishonest disclosure corporation, or penalty points may be imposed on the Filing Corporation

B. Plan for Protection of Shareholders Regarding Corporate Ownership Structure or Key Business Changes (New Requirements)

- In case of a merger, business transfer, split (including split-off), or comprehensive stock exchange and transfer, or any specific plan thereof is in place, the company must disclose a method or plan to protect its shareholders
- The Guidelines lists examples of such protective measures to protect shareholders, including: (1) a meeting with minority shareholders; (2) policies regarding shareholder returns (e.g., increasing dividends, purchase of treasury shares, etc.); (3) more stringent procedures for IPOs of subsidiaries after a split-off; (4) creation of safeguards for dissident shareholders' rights in IPOs of subsidiaries; and (5) substantive due diligence on the communication efforts between a corporation and its shareholders in the course of reviewing the IPO of a subsidiary
- The Guidelines prescribe that communications with minority shareholders, as well as those with all shareholders, should be separately listed, and material information regarding the corporation should be actively provided to minority shareholders

C. Obligation to Explain for any Comprehensive BOD Resolution Regarding Insider Trading and Self-dealing (Strengthened)

- The pre-amended guidelines required explanation of control mechanisms regarding insider trading and details of such trading. However, as numerous insider trading with affiliates or self-dealings may take place within large corporations, the board of directors (the "**BOD**") comprehensively approved such trades and dealings in a prescribed period and limitations
- Now, the Guidelines prescribe that if there is any BOD resolution comprehensively approving numerous trades, the reasons why such approval was necessary, and the details of the transaction (deadlines and limit, etc.) must be disclosed to shareholders

D. CEO Succession Policy (Strengthened)

- The pre-amended guidelines required a description of the CEO succession policy and operation thereof, but such requirements were treated merely as a formality, such as including a provision regarding a substitute for CEO in case of an accident or other such instances in the BOD Regulations, or including a provision regarding appointment procedures within the articles of incorporation
- The Guidelines now require that key matters of the CEO succession policy should be clearly documented and included in the Report, and that a provision dealing with a substitute for a

CEO as an internal regulation will not be acknowledged as a CEO succession policy.

E. Notice of General Meeting of Shareholders or Information Provision Period (Strengthened)

- The Korean Commercial Code requires that written notice be provided two weeks in advance of a general meeting of shareholders, while the pre-amended guidelines requires notice of a "sufficient period" before a general meeting of shareholders
- The Guidelines now clearly stipulate that such a sufficient period should be at least four weeks before a general meeting of shareholders, and in the case that such notice period is not complied with, the Guidelines require that an explanation be provided, including the reasons for such failure and subsequent remedial measures

F. Evaluation on Outside Directors (Strengthened)

- The pre-amended guidelines provided no example or explanation on the evaluation of outside directors, while the Guidelines stipulate that the "evaluation of outside directors' activity" is deemed to be conducted only when actual details of evaluation conducted on outside directors are compiled (i.e., such as evaluation results reflected in the re-election decision, etc.)

G. Description Regarding Audit Organization (Strengthened)

- The pre-amended guidelines provide no examples or explanations on audit committee members or audit-related items
- According to Guidelines, (1) a remuneration policy for "outside directors who are also audit committee members" should be described separately from "outside directors who are not audit committee members;" (2) if there is no audit committee, a plan for the installation of an audit committee or reason for non-installation of the audit committee should be provided; and (3) a meeting with an external auditor and audit-related education is only allowed to be conducted in person or via a video conference system, and strictly prohibits communications in writing or by email as substitutes.

H. Other Matters to be Described in the Report (Strengthened)

- Age and gender ratios of the BOD are required to be disclosed in the description of the BOD in order to promote diversification thereof
- Any improvements from the previous year of the 15 key indicators of the compliance table must be disclosed

II. RIPPLE EFFECTS AND IMPLICATIONS

A. Required Shareholder Protection Policy for any Change in a Public Corporation's Corporate Governance such as Split-off, etc.

The main objective of the Guidelines is to "create an adequate shareholder protection policy after sufficient communication with the shareholders of a parent company before any changes in the

corporate ownership structure such as a split-off, etc." The shareholder protection policy mentioned by the FSC refers to a policy to hold meetings with minority shareholders, have more stringent IPO procedures for split-off subsidiaries, and strengthen policies regarding shareholder returns, including increased dividends/purchase of treasury shares. If there is no such shareholder protection policy, the reasons therefor should be explained and disclosed to shareholders. In addition, the FSC has included communications with minority shareholders so that material information of corporations are actively provided to their minority shareholders.

Accordingly, under the Guidelines, any corporation that undergoes a change to its corporate ownership structure in any form of a split-off, merger or business transfer should describe any relevant plans to protect the existing shareholders' rights in the Report, which is to be published every May, including whether the minority shareholders were given an opportunity to voice their opinions and plans to protect dissident shareholders' rights.

The Guidelines are not mandatory rules but recommendations. However, the actual application and operation of the Guidelines remain to be seen in that they are likely to be interpreted as de facto regulatory measures with respect to IPOs of split-off subsidiaries. Further, the FSC's announcement may be an indication that it is seeking to devise various policies regarding the IPOs of split-off subsidiaries, in addition to the recommendations contained in the Guidelines.

B. Strengthened Obligation to Explain any Insider Trading with Affiliates, etc. to Shareholders, and Disclosure of Specific Plans for CEO Succession Policy

In an attempt to strengthen disclosure requirements and control of information on corporations' insider trading, the FSC requires that public corporations should actively describe the reasons and details (deadlines and limit, etc.) regarding BOD resolutions containing comprehensive approval for related transactions, including any insider trading with affiliates or self-dealing with management and controlling shareholders.

In addition, the main objectives of a CEO succession policy (a principle that establishes and operates the succession policy, and selection/management/education of candidates) should be documented and clearly described in the Report, and for a corporation that is newly required to make a public disclosure, a plan to install the audit committee should be described, if any.

It is expected that such revisions will enhance the internal control mechanisms and transparency of the management within corporations.

C. Potential Effects on Listing Review by the KRX

In principle, the Guidelines are only applicable to companies that are listed on the KOSPI market of the KRX, pursuant to the disclosure regulations. However, it is impossible to neglect the possibility that the Guidelines will become an important criteria in determining the suitability of a listing applicant during the KRX's listing review process considering that KOSPI listing applicants with a capital valuation of over KRW 1 trillion are already obligated to submit such corporate governance reports. Such obligations are expected to be expanded to include a wider group of listing applicants. The KRX has also recently been conducting more stringent reviews on whether listing applicants have adequate

corporate governance structures in place during its listing review process. In this regard, adoption (amendment) of and compliance with internal regulations relating to insider trading and self-dealing, and activities of outside directors, statutory auditor and audit committee will be important indicators of adequate corporate governance structure during the listing review process by the KRX.

It would therefore be necessary for companies preparing for IPOs to check their corporate governance structures and if required, align their internal regulations to be consistent with the Guidelines, and operate their corporate governance structures in a substantive and consistent manner.

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As you may be well aware, the domestic market has recently experienced significant changes in corporate governance due to increased activities of activist funds, institutional investors' active exercise of shareholders' rights, and reorganization of applicable capital markets laws. Corporations need to consider their direction to increase enterprise values such as through ESG investment, and recognize the environmental transition for business management, understand shareholders' preference in this regard, and efficiently manage potential concerns.

For any inquiry or questions regarding the content of this newsletter, please contact BKL's ESG Task Force. BKL has experts with extensive experience in advising numerous ESG cases, including shareholder activism and corporate governance.