2013 Korea Proxy Voting Summary Guidelines

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Institutional Shareholder Services Inc.

ISS' 2013 Korea Proxy Voting Summary Guidelines

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Approval of Financial Statements (and Declaration of Cash or Stock Dividends)

ISS will generally recommend vote FOR approval of financial statements (and declaration of cash or stock dividends), unless:

- The dividend payout ratio has been consistently low without adequate justification;
- The payout is excessive given the company's financial position;
- There are concerns about the accounts presented or audit procedures used; or
- The company is not responsive to shareholder questions about specific items that should be publicly disclosed

Amendments to the Articles of Incorporation

Proposals are always presented in a bundled manner. As such, in cases where ISS believes that the negative provisions proposed in a resolution outweigh any positive ones, an AGAINST vote is recommended on a whole resolution. Shareholders are advised to carefully scrutinize any changes to a company's articles as shareholders will not likely have any chance in the future to reverse the amendments once the amended articles are in place.

The following are frequently proposed amendments in Korea:

Issuance limit on new shares or convertible securities

The most contentious aspect in this proposal pertains to articles that permit companies to issue new shares, convertible bonds, and/or bonds with warrants to non-shareholders without triggering existing shareholders' preemptive rights. When such articles are sought to be amended, ISS will recommend vote FOR the amendments, only if:

- The potential dilution ratio to existing shareholders does not exceed 20 percent; and
- The proposed issuance limit of new shares is set at no higher than 20 percent of issued shares.

Increase in authorized capital

ISS will recommend vote FOR, unless:

- The increase in authorized capital exceeds 100 percent of the current authorized capital without any justification; or
- The increase in the authorized capital results in less than 30 percent of the proposed authorized capital on issue.

Stock split / reverse stock split

ISS will recommend vote FOR unless there is potential dilution impact on existing shareholders as a result of stock split and/or reverse stock split.

Preferred stock / non-voting common shares

ISS will generally recommend vote FOR the creation of a new class of preferred stock or the issuance of preferred stock up to 50 percent of the issued capital unless the terms of the preferred stock would adversely affect the rights of existing shareholders.

Diversification / expansion of business objectives

ISS will generally recommend vote FOR proposals to expand business objectives unless the new business takes the company into risky areas.

Establishment of audit committee

ISS will recommend vote FOR the establishment of an audit committee as a replacement for the internal auditor system.

Stock option grant

ISS will recommend vote FOR a proposed stock option grant, unless:

- The maximum dilution level under the plan exceeds 5 percent of issued capital for a mature company; or
- The maximum dilution level under the plan exceeds 10 percent for a growth company.

Amend quorum requirements

ISS will recommend on this proposal on a case-by-case basis.

However, ISS will recommend vote AGAINST proposals to adopt a supermajority voting requirement for removal of directors or internal auditors.

Cumulative voting

ISS will generally recommend vote AGAINST if a company proposes to introduce a new provision that will prohibit the use of cumulative voting in director elections.

Golden parachute clause

ISS will generally recommend vote AGAINST if a company proposes to introduce a new provision that entitles the company's directors to an excessive level of remuneration in the event that they were dismissed or terminated.

Authorizing board to approve financial statements and income allocation

ISS will generally recommend a vote AGAINST if a company proposes to introduce a new provision that gives the board of directors the authority to approve financial statements and income allocation (including dividend payout). Insertion of such clause would potentially take away shareholders' right to approve the company's dividend payment decision without any countervailing benefits.

Election of Directors

ISS recognizes that Korean law imposes two different sets of corporate governance standards on listed companies – one for companies whose asset size is greater than KRW 2 trillion (large companies) and the other for companies whose asset size is below KRW 2 trillion (small companies). Under Korean law, large company boards must have a majority of outside directors and small companies are required to have a board on which one-fourth of the directors are outsiders.

ISS will consider the history of a particular director when deciding whether to recommend in favor of his or her (re)election. Examples of circumstances where ISS will consider recommending a vote AGAINST a director's (re)election are where:

- Adequate disclosure has not been provided in a timely manner;
- There are clear concerns over questionable finances or restatements;
- There have been questionable transactions with conflicts of interest;
- There is any record of abuses against minority shareholder interests;
- The board fails to meet minimum corporate governance standards;
- A director has had significant involvement with a failed company;
- A director has in the past appeared not to have acted in the best interests of all shareholders;
- A director has breached fiduciary duties or engaged in willful misconduct or gross negligence in his/her capacity as a director (irrespective of whether such wrongdoing brings claims of losses and damages to the company);
- A director has been indicted by the Prosecutors' Office and there are pending investigations;
- An outside director has attended less than 75 percent of board meetings in the most recent financial year, without a satisfactory explanation; or
- An outside director sits on more than two public company boards, in violation of the Commercial Act and accompanying presidential decree.

For large companies, in a case where independent non-executive directors (per ISS' classification of directors) represent less than a majority of the board, ISS will recommend a vote AGAINST the following directors:

- Inside/executive directors who are neither CEO nor a member of the founding family; and/or
- The most recently appointed non-independent non-executive director (per ISS' classification of directors) who represents a substantial shareholder, where the percentage of board seats held by representatives of the substantial shareholder are disproportionate to its holdings in the company.

Under extraordinary circumstances, ISS will recommend a vote AGAINST individual directors, members of committee, or the entire board, due to:

- Material failures of governance, stewardship, risk oversight, or fiduciary responsibilities at the company;
- Failure to replace management as appropriate; or
- Egregious actions related to a director's service on other boards that raise substantial doubt about his/her ability to effectively oversee management and serve the best interests of shareholders at any company.

Election of Audit Committee Members (or Internal Auditor)

Election of Audit Committee Member(s)

Under Korean law, large companies are required to establish an audit committee comprised of a minimum of three members, two-thirds of whom should be outside directors (including the chair). Korean law also requires that at least one audit committee member possess accounting or related financial management expertise or experience.

ISS will consider the history of a particular audit committee member when deciding whether to recommend in favor of his or her (re)election. Examples of circumstances where ISS will consider recommending vote AGAINST an audit committee member's (re)election are where:

- There are serious concerns about the statutory reports presented or audit procedures used;
- A director has had significant involvement with a failed company;
- A director has in the past appeared not to have acted in the best interests of all shareholders;
- A director has breached fiduciary duties or engaged in willful misconduct or gross negligence in his/her capacity as a director (irrespective of whether such wrongdoing brings claims of losses and damages to the company);
- A director has been indicted by the Prosecutors' Office and there are pending investigations;
- An outside director has attended less than 75 percent of board meetings in the most recent financial year, without a satisfactory explanation;
- An outside director sits on more than two public company boards, in violation of the Commercial Act and accompanying presidential decree;
- An inside director seeks to become an audit committee member (for large companies only);
- A director has engaged in some significant transactions with the company in the last three years and he/she cannot reasonably be seen to have the necessary objectivity and independence; or
- Other questions exist concerning any of the audit committee members being appointed.

Election of Internal Auditor(s)

Under Korean law, small companies are required to appoint at least one internal auditor. These companies may alternatively choose to establish an audit committee.

ISS will consider the history of a particular internal auditor when deciding whether to recommend in favor of his or her (re)appointment. Examples of circumstances where ISS will consider recommending vote AGAINST an internal auditor's (re)appointment are where:

- There are serious concerns about the statutory reports presented or audit procedures used;
- The internal auditor(s) has previously served the company in an executive capacity or can otherwise be considered affiliated with the company;
- A nominee has had significant involvement with a failed company;
- A nominee has breached fiduciary duties or engaged in willful misconduct or gross negligence in his/her capacity as an internal auditor (irrespective of whether such wrongdoing brings claims of losses and damages to the company);
- A nominee has been indicted by the Prosecutor's Office and there are pending investigations;
- A nominee has engaged in some significant transactions with the company in the last three years and he/she cannot reasonably be seen to have the necessary objectivity and independence; or
- Other questions exist concerning any of the internal auditors being appointed.

For those small companies which choose to create an audit committee in place of the internal auditor system, ISS will recommend vote FOR the election of an inside director as an audit committee member only if the company's audit committee, after the election, satisfies the legal requirement.

Remuneration Cap on Directors (and Internal Auditor)

ISS will recommend vote FOR approval of remuneration cap on directors (or internal auditor), unless:

- The proposed limit on directors' remuneration is excessive relative to peer companies' remuneration caps; and/or
- The company is asking for a significant fee cap increase where:
  - The company reported sound financial performance but its dividend payout ratio has been low in the past couple of years (or for the most recent five years for widely held companies) without any reasonable justification; and/or
  - The company has generated a net loss in the most recent two financial years.

Reduction in Capital

ISS will recommend vote FOR proposals to reduce capital routine purposes unless the terms are unfavorable to shareholders.

- Reduction in capital accompanied by cash consideration
  - ISS will generally recommend FOR proposals to reduce a company's capital that accompany return of funds to shareholders and is part of a capital-management strategy and an alternative to a buyback or a special dividend. Such a resolution is normally implemented proportionately against all outstanding capital, and therefore does not involve any material change relative to shareholder value.
- Reduction in capital not accompanied by cash consideration
  - ISS will generally recommend FOR proposals to reduce capital that do not involve any funds being returned to shareholders. A company may take this action if its net assets are in danger of falling below the aggregate of its liabilities and its stated capital. ISS usually supports such proposals as they are considered to be routine accounting measures.

Stock Option Grants

ISS will recommend vote FOR proposed option grant, unless:

- The maximum dilution level under the plan exceeds 5 percent of issued capital for a mature company; or
- The maximum dilution level under the plan exceeds 10 percent for a growth company.

In Korea, the manner in which stock options are granted and exercised is stipulated under the law.

ISS recognizes that, under Korean law, companies are allowed to grant stock options up to 15 percent of the total number of issued shares pursuant to a shareholder meeting resolution. The board is also allowed to grant stock options up to 3 percent of the total issued shares and to seek shareholders' approval retrospectively at the first general meeting after the grant.

Spinoff Agreement

ISS will recommend vote FOR approval of a spinoff agreement, unless:

- The impact on earnings or voting rights for one class of shareholders is disproportionate to the relative contributions of the group;
- The company's structure following the spinoff does not reflect good corporate governance;
- There are concerns over the process of negotiation that may have had an adverse impact on the valuation of the terms of the offer; and/or
- The company does not provide sufficient information upon request to make an informed voting decision.

Merger Agreement, Sales/Acquisition of Company Assets, and Formation of Holding Company

ISS will generally recommend vote FOR the approval of a sale of company assets, merger agreement, and/or formation of a holding company, unless:

- The impact on earnings or voting rights for one class of shareholders is disproportionate to the relative contributions of the group;
- The company's structure following such transactions does not reflect good corporate governance;
- There are concerns over the process of negotiation that may have had an adverse impact on the valuation of the terms of the offer;
- The company does not provide sufficient information upon request to make an informed voting decision; and/or
- The proposed buyback price carries a significant premium at the date of writing, conferring on shareholders a trading opportunity.

The company-level transactions that require shareholders' approval include sale/acquisition of a company's assets or business unit; merger agreements; and formation of a holding company. For every analysis, ISS reviews publicly available information as of the date of the report and evaluates the merits and drawbacks of the proposed transaction, balancing various and sometimes countervailing factors.

Valuation

Is the value to be received by the target shareholders (or paid by the acquirer) reasonable? While the fairness opinion may provide an initial starting point for assessing valuation reasonableness, ISS places emphasis on the offer premium, market reaction, and strategic rationale.

In Korea, under the Capital Market and Financial Investment Business Act (CMFIB), a fairness opinion is not required for companies with listed shares because the Act specifically sets out all relevant steps and the manner in which the proportion of shares should be divided between the acquirer and target. The CMFIB requires the stock swap ratio between listed companies to be determined by a specific formula which is based on the historical prices and trading volumes.

For transactions between an unlisted company and a listed company, a fairness opinion should be obtained from the independent advisers who review the fairness of the stock swap ratio and the compliance with the governing laws and regulations.

Market reaction

How has the market responded to the proposed deal? How did the company's stock price react following the announcement compared to those of its peers? A negative market reaction will cause ISS to scrutinize a deal more closely.

Strategic rationale

Does the deal make sense strategically? From where is the value derived? Cost and revenue synergies should not be overly aggressive or optimistic, but reasonably achievable. Management should also have a favorable track record of successful integration of historical acquisitions.

Conflicts of interest

Are insiders benefiting from the transaction disproportionately and inappropriately as compared to non-inside shareholders? ISS will consider whether any special interests may have influenced these directors and officers to support or recommend the merger.

Governance

Will the combined company have a better or worse governance profile than the current governance profiles of the respective parties to the transaction? If the governance profile is to change for the worse, the burden is on the company to prove that other issues (such as valuation) outweigh any deterioration in governance.

Trading opportunity from the dissident's right

Does the proposed buyback price carry a premium or confer on shareholders a trading opportunity?

In Korea, the Corporate Act entitles shareholders to exercise a dissident's right (also known as a right of withdrawal, appraisal right, or buyback right) when the company resolves to engage in such transactions as a sale/acquisition of business, merger, or formation of a holding company.

A dissident's right is the right of shareholders to have their shares bought back by the company at a pre-determined buyback price in the event that shareholders dissent with management on a proposed merger. The manner in which the share buyback price is determined is stipulated under Korean law.

ISS considers whether the proposed buyback price carries a significant premium as of the date of analysis and states in the analysis whether the proposed buyback price confers on shareholders a trading opportunity at the time of analysis. However, shareholders who are interested in exercising the right of withdrawal are advised to reevaluate the size of premium/discount attached to the proposed buyback price, if any, closer to the meeting date and ensure that a written notice of intention of dissent is submitted well in advance of the general meeting.

Amendments to Terms of Severance Payments to Executives

ISS will recommend vote FOR approval of the establishment of or amendments to executives' severance payment terms, unless:

- The company fails to provide any information in regard to the changes to the terms of severance payments to executives;
- The negative provisions proposed in a resolution outweigh any positive ones; and/or
- The company proposes to introduce a new clause that is effectively a golden parachute clause.

Shareholder Proposals

ISS will recommend vote FOR shareholder proposals that would improve the company's corporate governance or business profile at a reasonable cost. However, ISS will recommend vote AGAINST proposals that potentially limit the company's business activities or capabilities or result in significant costs being incurred with little or no benefit.

In addition, ISS will recommend vote AGAINST shareholder-nominated candidates who lack board endorsement, unless they demonstrate a clear ability to contribute positively to board deliberations.

Social/Environmental Issues

Global Approach

Issues covered under the policy include a wide range of topics, including consumer and product safety, environment and energy, labor covered standards and human rights, workplace and board diversity, and corporate political issues. While a variety of factors goes into each analysis, the overall principle guiding all vote recommendations focuses on how the proposal may enhance or protect shareholder value in either the short term or long term.

Generally vote CASE-BY-CASE, taking into consideration whether implementation of the proposal is likely to enhance or protect shareholder value, and in addition the following will be considered:

- If the issues presented in the proposal are more appropriately or effectively dealt with through legislation or government regulation;
- If the company has already responded in an appropriate and sufficient manner to the issue(s) raised in the proposal;
- Whether the proposal's request is unduly burdensome (scope, timeframe, or cost) or overly prescriptive;
- The company's approach compared with any industry standard practices for addressing the issue(s) raised by the proposal;
- If the proposal requests increased disclosure or greater transparency, whether or not reasonable and sufficient information is currently available to shareholders from the company or from other publicly available sources; and
- If the proposal requests increased disclosure or greater transparency, whether or not implementation would reveal proprietary or confidential information that could place the company at a competitive disadvantage.

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