

[HANNURI HANDBOOK]

A Practical Guide to the Shareholders General Meeting for general shareholders



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Introduction

Every March, many companies hold shareholder general meetings (SGM) in Korea. The SGM is the company's ultimate decision-making body consisting of the real owners of the company. It is our reality, however, for various legal as well as practical reasons, that the SGM is held with limited participation of shareholders.

A 2014 report on corporate governance in Asia by the 'Asian Corporate Governance Association' ranked Korea 8th out of the 11 countries in Asia, suggesting that Korea still lags behind peers in setting and implementing corporate governance standards. Various legal hurdles still adverse to shareholders as well as cultures disregarding shareholders as represented by "Super SGM day" would be the main reason for such low rank.

Despite such limitations, shareholders' participation in SGM should be encouraged and activated. While there are numerous books and articles written for companies or managements – i.e. how to conduct the SGM, practical guidelines written from the viewpoint of general shareholders, the real heroines of SGM, are hard to find. Hannuri Law has been actively advising minority shareholders including institutional investors focusing on the SGM and representing them in various SGM-related litigations. This Guide was written based on such experience with an objective of giving minority shareholders practical guidance in carrying out or using the SGM in their best interests.

● The Meaning of SGM

From the perspective of shareholders, especially institutional investors who are not in a position to participate in the company's business decision making, the SGM could be:

An official channel for asking inquiries and expressing opinions to board members

The SGM is held at least once a year. According to the Section 365 of the Commercial Act, the SGM should convene once a year, and if the company has more than one fiscal year in a calendar year, the SGM should convene every fiscal year. Thus, even excluding extraordinary shareholder meetings which convene for a special agenda, shareholders can meet the board members through the SGM at least once a year. Shareholders can ask questions and express their opinions to them in such SGM.

An opportunity to focus public attention

The SGM is also a good opportunity to focus public attention on the company's important issues. The operation of a company affects not only its shareholders but also various stakeholders such as employees, consumers, and the local society in general. Thus, the SGM where the company's pending issues such as corporate governance or issues that have a significant impact on the business are dealt with is a sort of theater stage where media and social attention are concentrated. Shareholders can have the opportunity to appeal the company's pending issues to the public through the SGM.

An opportunity to gain ground, evidence and supporters for potential legal actions

In certain cases, the SGM can be utilized for gaining ground, evidence and supporters for various legal actions such as shareholder derivative action, injunction action, etc. against board members or management. Shareholders have various shareholder rights including rights to file shareholder derivative action, rights to inspect corporate books and records, and so on. Before the actual legal action is taken, however, it is necessary to bring the issue to the board members first and to urge voluntary correction, that way shareholders can acquire justification of these legal measures and occupy an advantage in the future litigation, if any. Thus, participation in the SGM could be a preliminary step before exercising shareholder rights and the subsequent legal actions. In addition, management's remarks and attitude at the SGM could be evidence showing the problem of the management raised by the shareholders. Management rarely presents clear evidence or admits their wrongdoing; however, even if they do not answer, the non-answer itself could be seen as indirect admission. Further, the SGM is an opportunity to invite all shareholders to pay attention to the company's current issues, and thus it is a good place to find and secure supporters. Lastly, since minority shareholder rights are often only given to shareholders with a certain percentage of shares, the SGM may be used to meet those requirements.

Influencing the outcome of agenda in the direction of benefiting general shareholders

In fact, the most essential role of the SGM is in making decisions about the company's key issues. Therefore, the strongest effect that shareholders can obtain through the SGM is to influence the outcome of the agenda through the exercise of voting rights – i.e. appointing directors other than the ones recommended by management or controlling shareholders, frustrating management-led mergers or changing the bylaws in the direction that minority shareholders want. However, since in most cases shareholders are dispersed and major shareholders and management have a significant percentage of shares, it is not easy in reality for minority shareholders to draw up resolutions which are against management or major

shareholders. As discussed below, however, major shareholders have limitation on exercising voting rights in some agenda such as appointment of auditor or change of the bylaws to remove cumulative voting, and thus the influence of general shareholders is enlarged for those agenda.

● **Strength and Weakness of Management and Minority Shareholders at SGM**

Both management and minority shareholders have their own strength and weakness at the SGM as listed below:

	Management	Minority shareholders
Strength	<ul style="list-style-type: none"> ▪ Can lead the proceedings on the podium ▪ In most cases, have voting rights of major shareholders ▪ Can have official legal assistance 	<ul style="list-style-type: none"> ▪ Have symbolic authority as the owner of the company ▪ Can embarrass management by asking unexpected questions ▪ The media and public opinion are generally favorable to minority shareholders
Weakness	<ul style="list-style-type: none"> ▪ Have difficulty in predicting minority shareholders' action ▪ Cannot just ignore minority shareholders, because they are legal stakeholders of the company ▪ Can lead to social criticism by clumsy response 	<ul style="list-style-type: none"> ▪ Has no effective weapon against management's abuse of point of order procedure ▪ Can play simply limited role of making noise beneath the podium due to lack of voting rights

● **Art of Questioning at the SGM**

Questions that give an opportunity for excuse should be avoided

Management is usually well aware of the current issues and ready to answer questions. Obvious questions, therefore, could give just a chance for excuse to management. It is necessary to invent creative questions as followings:

- 1) *Questions that cannot disagree* (i.e. if there is a conflict of interest between a major shareholder and the company, representing the interests of the company rather than the ones of the major shareholder would be right?)
- 2) *Factual questions that cannot deny* (i.e. was the purchase price the lowest during the last

one month?)

3) *Questions that cannot escape* (i.e. which party proposed the deal first? The major shareholder or the company?)

Need to prepare questions to refute the anticipated excuse

If the answers from management are predictable, it is necessary to prepare questions that refute those answers in advance. But because the chairman might block additional questions on pretense of giving others chance to talk, preparing others who will ask additional or subsequent questions is something to consider. Also the chairman might demand to ask questions all together rather than one for one, and in such case, it would be hard to continue to ask questions as in cross-examination in court. Even in such circumstance, you need to stand fast and not step back. Questioner' s experience, the chairman' s attitude, overall atmosphere of the meeting, etc. are all important here.

Need to ask questions related to the agenda

It seems obvious, but it is important to ask questions related to the agenda, so that you are not denied or ignored. But because the agendas are very broad and comprehensive, you will not find it hard to ask such agenda-related questions if you can connect the contents of the questions wisely with the agenda.

Procedural motion is necessary in certain circumstances

Sometimes it is necessary to make a procedural motion in order to take the initiative at the SGM. Especially when the SGM is conducted in significantly unfair manner, it could be the ground of cancellation of the SGM, and thus it is important to record such situation. The Supreme Court found the manner of resolution of a SGM significantly unfair against good faith where a certain shareholders could not attend the SGM in time due to the other shareholders' hindrance and the proceedings of SGM were not conducted in a way that maximizes the exercise of voting rights of the belated other shareholders.

Need to respond firmly to chairman's restraint of questions

Sometimes the chairman says he will accept the questions later, but this promise usually fails to materialize, and even further such questions lose their meanings if the relevant agenda has already passed. Thus, in such circumstance, it is necessary to express opinions strongly about the urgent need of questions and answers.

● What Should Be Prepared Before the SGM?

1. Shareholder proposal

Because only pre-announced agenda can be discussed and voted at the SGM, if you want to discuss and vote on an issue that was not listed as agenda, you need to propose such item beforehand.

1) Who can submit a shareholder proposal?

According to the Section 363-2 of the Commercial Act, only shareholders who hold no less than 3% of the company's stocks excluding non-voting stocks are permitted to initiate a shareholder proposal. In the case of public company, shareholders who have been holding no less than 1% (or 0.5% in the case of a company whose paid-in capital is no less than 100 billion won) for at least 6 months also can submit a shareholder proposal, according to the Section 542-6(2) of the Commercial Act.

2) What can be proposed?

A shareholder proposal should not be an ambiguous rant, but a well-conceived recommendation to take a specific course of action. The subject of shareholder proposal is relatively broad as long as it is not in violation of laws and regulations or bylaws of the company. But where the contents of a shareholder proposal fall under any of the followings, they cannot be raised as shareholder proposal

- 1) Where another proposal is presented again within three years from the date on which a proposal with the same contents was rejected because it obtained less than 10/100 of the votes at previous SGM
- 2) Where the proposal concerns a shareholder's personal grievance
- 3) Where the proposal concerns a matter that involves a right of minority shareholders
- 4) Where the proposal concerns a matter that involves the removal of an incumbent officer (applicable only to a public company)
- 5) Where the proposal concerns a matter that the company is unable to materialize, is based on an evidently false ground, or defames a particular person.

3) When should be proposed?

A shareholder proposal should be submitted no later than six weeks before the SGM. But because the shareholders cannot know in advance the exact date of the SGM, the law permits to calculate the deadline based on the date of SGM of the preceding year.

2. Request to inspect and copy the list of shareholders

From the point of view of minority shareholders, it is of great importance to muster the fellow shareholders in order to maximize the influence at the SGM, and its first step is to request to inspect and copy the list of shareholders. The Section 396 of the Commercial Act requires the company to keep a list of shareholders at the principal office (or at the transfer agent's¹ business office as applicable), and any shareholder may request, at any time during the business hours, to inspect and copy the list of shareholders.

The problem is that, in the case of public company, the physical securities are deposited with the Korea Securities Depository and most of the shares in the shareholder list are recorded in the name of the Depository. Thus, whether the list of shareholders mentioned in the Commercial Act includes the beneficial owners list could be a question and it is generally construed that way.

The beneficial owners list is created after 10 business days from the closing date of the shareholder list and it is important to submit a formal request to inspect and copy the shareholder list including the beneficial owners list in advance so that you can have the list around that time. If the company does not respond or refuses to allow you to inspect the list, then you may obtain an order from the court forcing the company to allow for the inspection and copying of the list. If despite the court order the company refuses such request or it takes too much time to obtain a court order, you may move a motion for an injunction to prevent the holding of SGM, or in the alternative, to move a motion seeking to negate or cancel any resolution of SGM ex post.

3. Analysis of various company disclosures or open resources

Minority shareholders usually have limited information about the company, but in order to raise effective questions or muster fellow shareholders, as much information as possible should be obtained. In the case of public company, you may obtain considerable resources simply by searching disclosed information, which exist in the electronic disclosure systems of the Financial Supervisory Service (dart.fss.or.kr) and the Korea Exchange (<http://kind.krx.co.kr>). The followings are the must-search items in preparation of the SGM:

1) Company bylaws

It cannot be emphasized enough to review the bylaws to check the numbers, the term as well

¹ A transfer agent is an institution assigned by the company to maintain records of shareholders and to change their names when necessary; for example, the Korea Securities Depository, KEB Hana Bank, Kookmin Bank, etc. are those transfer agents.

as the qualification of directors, the exclusion of cumulative voting, the adoption of voting by writing or electronic voting, etc. The bylaws are attached to the annual report of the company, and thus you can find it in the attached documents after searching annual reports.

2) Audit report

A company should retain its internal auditor' s report at its principal office from one week prior to the date of SGM by the Section 448 of the Commercial Act, as well as external auditor' s report if applicable (the Section 14(1) of the Act on External Audit of Stock Corporations). Because the internal/external auditor' s reports are disclosed in the DART, you need to check the financial information or auditor' s opinions.

3) Other non-periodic disclosures

In order to raise questions at the SGM, it is important to check the minute of board meeting discussing the key issues of the company. If resolutions of board meeting are subject to disclosure requirements, they are disclosed through the aforementioned disclosure systems, and thus it is necessary to review such disclosed contents.

4) Googling

Lastly, but certainly not the least, don' t forget 'Googling' . You need to collect information related to the current issues using search sites such as Google, Naver, etc. which have sometimes high quality information. In modern society, it is very important to find useful information in the sea of overflowing information because the excess of information is more problematic than the lack of information.

4. Request to inspect the minutes of board meetings

Minute of board meeting contains information on major business judgments and thus inspecting the minute beforehand is necessary. Not all minute of board meeting, however, are disclosed in the DART, which means you need to inspect the minute of board meeting retained by the company in order to check the current issues. Shareholders may request to inspect or copy the minute of board meeting during the business hours by the Section 391-3(3) of the Commercial Act. If the company refuses such request which is often the case, shareholders may request to inspect or copy the minute of board meeting by the court order as granted by the Section 391-3(4) of the same Act.

5. Request to inspect the accounting books

In order to raise questions about embezzlement, accounting fraud, etc., checking the financial statements alone is not enough and broader inspection of corporate records are necessary.

The Section 466 of the Commercial Act provides the shareholders with no less than 3% of the company' s stocks may request to inspect the accounting books. In the case of public company, shareholders who have been holding no less than 0.1% of the company' s stocks (0.05% in the case of a company whose paid-in capital is no less than 100 billion won) for at least 6 months also may request to inspect the accounting books, according to the Section 542-6(4) of Commercial Act. The problem occurs when the company refuses such request. Because the procedure on the merits could take considerable time leading to meritless claim, it is necessary to move a motion to the court to order the inspection of accounting books.

6. Proxy solicitation reporting

Minority shareholders alone cannot influence on the SGM, and musting fellow shareholders are essential. In the case of public company, however, it is not something you can do freely. You should go through certain legal procedures as set out in the Capital Market Act. Such mustering activity is called 'proxy solicitation' and to engage in proxy solicitation of 10 or more people requires in-advance reporting with Financial Supervisory Service through the DART.

Not only obtaining proxy form from another shareholder but also various actions such as demanding the exercise or non-exercise of voting rights, demanding the revocation of delegation of voting rights, sending a proxy form to a shareholder for the purpose of securing, or persuading to revoke delegation of a voting right, or presenting an opinion in any other way are viewed as proxy solicitation, according to the Section 152 of the Capital Market Act.

7. Sending proxy material

If you reported proxy solicitation through the DART, you can send proxy forms and proxy materials to other shareholders after two business days from the date of disclosure. Ordinarily a letter of notice is accompanied by a proxy form as well as proxy material. It is recommended to enclose a return envelope for receiving a proxy form.

8. Communication with major shareholders as well as proxy firms

The increasingly important players in SGMs are proxy advisory firms. Institutional investors tend to be advised from proxy firms in order to exercise voting rights properly and such tendency is getting stronger. In Korea, not only ISS (Institutional shareholders Service) which plays an important role in foreign shareholders' voting decision, but also other proxy advisory firms such as CGS (Korea Corporate Governance Service), Sustinvest, CGCG (Center for Good Corporate Governance) and DERI (Daishin Economic Research Institute) have

significant influence on the Korean institutional investors' opinion. Thus, communication with such proxy advisory firms should not be neglected.

9. Letter of cooperation to the company

Sometimes it is necessary to send a letter of cooperation to the company in advance to prevent the company's interference in relation with the SGM as well as to make an issue of the company's wrongful action if any. Shareholders can request the company not to interfere with the shareholders' attendance or to secure the opportunity to ask questions through such letter. While it is possible to send questions in advance for the purpose of getting more in-depth answers from the company, beware that it could expose your strategy and give the company just opportunities for excuses.

10. Analysis on voting rights

If a voting rights battle is anticipated, analyzing voting rights in advance is necessary. In such analysis, it is important not only to analyze the distribution of voting rights but also to identify the limitations on voting rights so that the calculation of numbers of voting rights can be done correctly.

11. Distribution of press release at each stage

It is also necessary to conduct public relations activities such as publishing and distributing press releases at each stage before the SGM. If you release too late, it will not work, but if you do it too early, your strategy will be exposed in advance. The best option would be to distribute a press release containing the general shareholders' opinion and the gist of demands on the morning of the SGM date. When you are making issues of wrongful acts of management, the demands that can be requested would be either 1) corrective measure (restitution), 2) punishment against the person in charge or 3) measure to prevent a recurrence (verbal or written promise, systemic measure, etc).

12. Rehearsal

Having a SGM rehearsal is also useful in preparing the SGM with a scenario. Because too much detailed rehearsal could reduce the liveliness and make it hard to cope with changing circumstances, however, the scenario for SGM needs to put things such as goal, strategy, major points, questions for each agenda, etc. into perspective and to be written loosely so that you can cope with various situations flexibly.

13. Injunctions

In certain cases, it could be necessary to apply to court for assistance; for example, a motion to enjoin SGM in the case where the calling procedure seriously violates any law or regulation or a motion to enjoin exercise of voting rights in the case where there is a sign of exercise of voting rights in violation of the applicable restrictions.

● How to Respond at Each Stage of SGM

Chairman' s greetings

It is not common to make an issue when the chairman says words of greeting; however, if there is serious problem in proceedings, moving a procedural motion could be an option. It can start with this: "Mr. Chairman! It is a point of order. I need to say a word because it is very important with regard to the legality of this SGM.

Auditor' s reporting

During the auditor' s reporting time, the auditor (or chairman of the audit committee, standing audit committee member) reports to the shareholders on the result of the audit. If you want to argue there are violations of laws and regulations, bylaws, or fiduciary duty related to accounting, you need to point out and raise questions one by one. Even if the chairman tries to avoid your questions by promising giving another time to ask questions or saying there are too many questions, you should not back off and push forward strongly. The chairman would not accept your argument; however, at least a certain level of answers such as 'we will correct if there is a problem or will check on any legal problem' should be received.

Business reporting

In this session, the chairman or one of the officers reports on the general business as well as financial issues of the company, and often times the reporting is substituted with printed handouts. While you can raise a question during the reporting session of financial statements, you need to raise such question at this session because you might not be able to get such opportunity at the reporting session of financial statements. If the chairman says you to wait for the reporting session of financial statements, don' t forget to have his word to give the chance to ask at the session.

Approval of financial statements

You need to point out and raise questions about inaccurate or problematic issues on financial statements. Because it is related to accounting, it is desirable for a person with knowledge of accounting to ask questions.

Change of bylaws

In this session, you can point out whether the proposed agenda could infringe on shareholder's interests, violate corporate governance charter or be against the guideline of National Pension Service or Korea Corporate Governance Service.

Election of directors, auditors or members of audit committee

You need to ask whether the director candidate or auditor candidate are attending, and can point out their history including the problem of resolutions for which the candidates voted. In the case of appointment of auditor or audit committee member, the restriction on voting rights (so called 3% rule) is applicable, and thus you need to be prepared in advance.

Approval of remuneration of directors or auditors

In this session, you can make issues of whether the maximum compensation is excessive in comparison with other companies or previous years.

● After SGM

Media interview and distribution of press release

Right after the SGM, it might be necessary to have an interview with media or distribute press release, and thus you need to be prepared in advance for such circumstance.

Legal measures

It might be necessary to take legal actions including request to inspect the minutes of SGM, motion for the preservation of evidence, motion for an injunction to enjoin implementing resolutions of SGM or motion for revocation of resolutions of SGM. In the case of motion for revocation of resolutions of SGM, it should be noted that there is a time limit for filing the motion - six months from the date of SGM. Sometimes, filing a motion for the preservation of evidence could be necessary to preserve the evidence related to voting of the SGM. All these legal actions should take place in the court where the company's head office is located.

■ Hannuri Law Handled Cases

Since its inception as a plaintiff lawfirm specializing in securities-related litigation and shareholders advisory service in 2000, Hannuri Law has been actively advising and litigating on behalf of shareholders, or sometimes companies, in matters related to SGM. Here are some examples of Hannuri Law's accomplishments.

■ KB Insurance case

Hannuri Law advised the minority shareholders of KB Insurance on blocking the share exchange initiated by KB Financial Group, the largest shareholder of KB Insurance, and had KB Financial Group to purchase general shareholders' shares at higher price than market price.

■ Auction case

Hannuri Law advised foreign institutional investors such as Tiger Management on defeating delisting efforts through a tender offer at low price by E-Bay, the largest shareholder of Auction, and successfully appointed minority shareholder-side auditor at the SGM. This increased the tender offer price from 70,000 won (the initial price offered by E-Bay) to 125,000 won.

■ Hanaro Telecom case

Hannuri Law advised the employee stock ownership association on exercising of voting rights to achieve independence from LG Group, one of the major shareholders of Hanaro Telecom, and successfully obtained an injunction order to prohibit exercise of voting rights of LG Group, thus having won at the vote.

■ Daewon Pharmacy case

Hannuri Law advised board members and the major shareholder of Daewon Pharmacy on defeating a takeover bid by minor shareholders and how to improve corporate governance of Daewon Pharmacy, thus succeeding in rejecting shareholder proposal of minority shareholders.

■ G2R(formerly LG AD) case

Hannuri Law helped management of G2R fighting against a foreign major shareholder and successfully appointed management-side director at the SGM by obtaining support of multiple foreign institutional investors.

■ KB Bank case

Hannuri Law, on behalf of minority shareholders of KB Bank, successfully argued a motion for revocation of resolutions of SGM resulting in cancellation of the stock option given to directors..

■ Daewoo Electronics case

Hannuri Law advised minority shareholders of Daewoo Electronics on the attendance of the SGM, and successfully persuaded the court to prohibit debt/equity swap resolution voted for at the SGM where the minority shareholders' attendance was hindered by management of Daewoo Electronics. As such, Hannuri Law for the first time in history succeeded in stopping the workout led by creditors which passes the loss only to the existing shareholders.

■ Dangin Tank Terminal case

Hannuri Law helped Hana Energy in obtaining the control of Dangin Tank Terminal based on the victory at the SGM by advising on takeover as well as management stabilization.

■ Other cases

Other than the aforementioned cases, Hannuri Law successfully obtained injunction orders in multiple SGM-related cases such as Tongyang, BYC, Gravity, Telephus, Bridge Securities, 3Soft, Seoul Ship Finance, and so on.



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