March 2023

APAC Governance Overview

China/Hong Kong, Japan and South Korea

As responsible stewards of our clients' capital, we actively exercise our right to vote in accordance with our robust global rules- and principles-based in-house Proxy Voting and Governance Policy. We make investment and proxy-voting decisions in our clients' best interests, and support strong corporate governance structures, shareholder rights and transparency. For more details on our proxy-voting philosophy, policy and process, please see our Global Stewardship Statement.

Introduction

The year 2022 was a landmark one for the Asia-Pacific (APAC) region, as localized frameworks adapted to higher standards of corporate governance. In China, the China Enterprise Reform and Development Society (CERDS) published its first disclosure standard including environmental, social and governance (ESG) considerations, alongside rolling out amendments to the Stock Exchange of Hong Kong's Listing Rules. In Japan, the Tokyo Stock Exchange was restructured into three new market segments following significant improvements to Japan's Corporate Governance Code. Meanwhile, in South Korea, the Financial Services Commission (FSC) amended the guidelines for corporate governance reports to enhance shareholder protections. As institutional investors' expectations around corporate governance continue to rise, APAC regulators and issuers are striving to bridge the gap between best practices in other regions and local market standards.

China and Hong Kong

ESG Disclosure

Over the last few years, companies around the world have adopted various frameworks to guide their ESG disclosures—such as the Sustainability Accounting Standards Board or the Global Reporting Initiative standards. To meet the increased demand for transparent ESG data, CERDS published its Guidance for Enterprise ESG Disclosure in April 2022. The Guidance is the first Chinese ESG disclosure standard, and while not obligatory, it outlines over 118 quantitative and qualitative metrics that include localized indicators, allowing for a more comprehensive guide, which considers market-specific contexts, rather than simply applying the existing global standards. This improved guidance, therefore, serves to bridge the gap between ESG reporting practices in other regions and in China. In addition to the release of this localized, standard ESG reporting guidance, the State-owned Assets Supervision and Administration Commission of the State Council is requiring all listed central enterprises (central state-owned enterprises) to engage in ESG reporting by 2023. As of April 2022, the China Association for Public Companies reports that over 1,400 companies (30%) listed on the Shenzhen and Shanghai Stock Exchanges have disclosed their ESG reports, and it is likely that the disclosure rate will continue to increase through 2023.

While no Chinese climate change resolutions were submitted in 2022, the Ministry of Ecology and Environment released the Plan for the Reform of the Legal Disclosure System of Environmental Information, "the Plan," which came into effect on February 8, 2022. Alongside the publication of the Plan, the China Securities Regulatory Commission (CSRC) has established new environmental disclosure requirements that call on companies that have been classified as key polluting units to disclose climate-related information in their half-year and annual reports. This requirement also applies to companies that were penalized in the previous reporting year for environmental reasons.

Stock Exchange of Hong Kong Listing Rules Amendments

On July 29, 2022, the Stock Exchange of Hong Kong published amendments to the Main Board Listing Rules. The amendments extend Chapter 17—which currently only governs share option schemes—to govern all share schemes involving grants of share awards and grants of options to acquire new shares of issuers. The amendments also enhance the regulations of share schemes. Specifically, the amendments require: a minimum vesting period for options or awards of one year; disclosed performance conditions; the presence of a clawback mechanism; and shareholder approval of the scheme mandate limit, service provider sublimit, share grants to an individual participant in excess of the 1% individual limit, and grants to a director, chief executive, or substantial shareholder in excess of 0.1% of the issued shares over any 12-month period. These enhancements came into effect on January 1, 2023, and are expected to significantly bolster shareholder rights.

Separation of CEO and Chairman Role

While we acknowledge the potential benefits of a combined CEO and chairman role, this practice is generally viewed as a poor corporate governance practice due to a concentration of power under one individual. Accordingly, AllianceBernstein (AB) encourages the presence of a lead independent director when the CEO and chairman roles are combined to provide appropriate checks and balances. Partially in reflection of this common approach among institutional investors, roughly 19% of Chinese issuers separated their CEO and chairman positions from 2021 to 2022, resulting in about 84% of Chinese issuers having segregated roles.[1] It is also worth highlighting that in cases where the two roles are separated, the presence of a lead independent director further balances the power of the executive chair and the CEO in the boardroom. This principle is applicable to many large-cap Asian issuers, as it is common for companies to exist under prevalent family ownership or dominant presence of the founder.

Stock Connect Program Launch

In February 2022, the CSRC revised the Provisions on the Supervision and Administration of Depository Receipts under Shanghai-London Stock Connect to include issuers listed on the Shenzhen Stock Exchange and European markets, allowing them to issue depository receipts across markets. Following this revision, on July 28, 2022, the CSRC launched the China-Switzerland Stock Connect, providing an opportunity to cross-list of Chinese issuers on the Swiss Exchange (SIX). According to Institutional Shareholder Services (ISS), as of October 2022, 12 of the 13 companies issuing global depository receipts chose to do so on SIX, likely as a result of the comparatively high degree of market openness and fairness.[2] The launch of the China-Switzerland Stock Connect signifies a milestone in China's expansion of cross-border financing and cooperation.

1 Ada Xu, Yuan Yao, Rui Ning Cheng, Elodie Zeng and Yafei Zeng, "2022 China Proxy Season Review," ISS Insights, Institutional Shareholder Services, October 6, 2022.
2 Xu, Yao, Cheng, Zeng and Zeng, "2022 China Proxy Season Review."

Board-Level Gender Diversity and Independence

China currently has no regulatory requirements for board-level gender diversity and maintains a male-dominated board composition, with only 13.1% of board seats held by women in China, as of 2021.[3] Since the beginning of 2022, however, revisions to the Stock Exchange of Hong Kong Limited's Corporate Governance Code and Listing Rules now require the boards of listed companies in Hong Kong that are composed of a single gender (32.9% of companies in 2021) to appoint at least one director of a different gender to the board.[4] Issuers will also have to establish quantitative board-level gender diversity targets and timelines, review their board diversity policy annually, and disclose workforce gender ratios. The Listing Rule Amendments further require that boards appoint new independent non-executive directors (INEDs) if all INEDs have served over nine years, beginning in 2023. In addition, companies will need to publish annual ESG reports, including plans to improve gender diversity and the factors included in appointing new INEDs. It is expected that these changes will result in significant improvements to board-level gender diversity and independence in Hong Kong moving forward. In Mainland China, on the other hand, boards are only required to be one-third independent and have an average of 37.2% independent directors.[5]

3 Deloitte, *Women in the Boardroom: A Global Perspective*, February 2022.
4 Fiona Webster and Stephanie Rosseau, "Hong Kong to Require Gender Board Diversity, Corporate Governance," Mercer, December 22, 2021.
5 Xu, Yao, Cheng, Zeng and Zeng, "2022 China Proxy Season Review."

Japan

Tokyo Stock Exchange Restructuring

On April 4, 2022, the Tokyo Stock Exchange (TSE) was restructured into three new market segments: Prime, Standard and Growth. Previously, TSE had four sections (First Section, Second Section, Mothers and JASDAQ) that were maintained when TSE and Osaka Securities Exchange integrated their cash equity markets in 2013. Before the 2022 changes, the "main markets" consisted of the first and second sections and included the large- and medium-sized companies, while Mothers and JASDAQ were devoted to start-ups—each section had its own unique listing requirements. In justifying the restructuring, the Japan Exchange Group argued that the change addressed two key issues with the prior format: the ambiguity of each market section and the lack of sufficient incentives for listed companies to sustainably increase corporate value. Notably, the new Prime market segment has more stringent listing requirements, following the revisions made to Japan's Corporate Governance Code. Arguably the most important of these changes is the new minimum independence threshold of 33% for Prime-listed issuers (majority for controlled companies). For Standard-listed issuers, the new requirement is at least two independent directors for uncontrolled companies and one-third for controlled companies. On a comply or explain basis, Prime companies are also expected to disclose the impacts of climate change based on the Task Force on Climate-related Financial Disclosures framework and enhance both board-level and workforce diversity (gender, ethnicity and age). While the Prime-listed issuers must comply with a higher standard of governance, and the Standard-listed companies are required to comply with the full governance standards set out in the revised Corporate Governance Code, the issuers listed on the Growth segment are only expected to adhere to the general principles of the Code.

Gender Diversity and Pay Gap

The TSE revised Japan's Corporate Governance Code in June 2021. Alongside its enhancements to ESG disclosures and board-level independence requirements, the revised Code calls for policy development and voluntary targets with respect to gender diversity in senior management positions. In addition, the Act on the Promotion of Women's Participation and Career Advancement in the Workplace was revised on July 8, 2022, to require companies with 301 or more employees to annually disclose the gender pay gap within three months, for the financial year ending on or after July, 8 2023.[6] Companies with 101 to 300 employees now have to report on other gender balance information, such as the representation of females throughout the workforce or details on diverse hiring initiatives. Both of these regulatory improvements to gender equity have likely contributed to the year-over-year increase in female representation at the board level. According to ISS, the number of boards with at least one female director increased to 63.4% in 2022, up from 52.7% in 2021. While this is a significant step in the right direction, the number of females at the C-suite level remains constant at about 12%.[7] Hopefully, the enhancements to gender diversity regulation will continue to drive improvements on this front and provide investors with a greater degree of transparency regarding the representation of females in leadership roles and in the workforce more broadly.

Board Independence

With the launch of the new Prime Market of TSE, board-level independence has improved year over year in Japan. ISS reports that as of June 2022, 82.3% of boards have at least one-third of board members as outsiders, as compared to 73.3% in 2021. Despite this improvement, only 12.9% of Japanese companies had a majority-independent board (per the ISS definition).[8]

While the revised independence standards for Prime-listed companies in Japan is a noteworthy improvement to corporate governance standards, AB's approach to board-level independence will remain unimpacted. This is because AB holds Japanese issuers to a higher standard than local market practice; specifically, AB requires a majority-independent board for all uncontrolled Japanese companies that do not have a three-committee structure.[9] If companies fail to meet this requirement, AB will vote against the most tenured nominee on the ballot (usually the president or chairman). In addition, AB expects that statutory auditors and audit committee members are not affiliated outsiders, as this could undermine the board's ability to provide independent oversight. This approach aligns with the philosophy of AB's Proxy Voting and Governance Policy more broadly, as AB strives to advance our holdings toward global best practices, rather than just the minimum requirements in a given market. While considering market contexts, this method allows AB to more effectively push companies to maintain best-in-class corporate governance practices globally.

6 Rina Bando, Reiko Sasaki and Fiona Webster, "Japan to Introduce Gender Pay Disclosures for Certain Companies," Mercer, October 28, 2022.
7 Japan Research Team, "2022 Japan Proxy Season Review," ISS Insights, Institutional Shareholder Services, October 17, 2022.
8 "2022 Japan Proxy Season Review."
9 The three-committee structure refers to a board that consists of compensation, audit and nominating committees.

Shareholder Proposal Trends

There was a 49% increase in the total number of shareholder proposals from 2021 to 2022 (a record of 351 proposals within ISS coverage), making 2022 a landmark year for Japanese shareholder proposals.[10] In addition, for the first time in Japanese history, there was a successful Vote No Campaign. Another "first" of 2022 was the submission of Japan's first investor group–led climate proposal, which was put forward by Man Group, Amundi and HSBC Asset Management at the AGM of Electric Power Development Company (J-Power). The proposal, which AB supported, asked for J-Power to formulate and disclose a Paris-aligned decarbonization strategy. This proposal was one of 10 climate-related shareholder proposals calling for companies to amend their articles of incorporation, none of which passed. Despite the failure of these shareholder proposals, the increasing investor interest in climate-related issues, in combination with enhanced environmental disclosure regulations, may result in a higher number of Japanese issuers advancing their climate-related practices in the next few years.

Cross-Shareholding

It is common practice in the Japanese market for companies to hold—over the long-term—shares of other issuers for purposes other than simple investment reasons, for example, to reinforce relationships with customers or suppliers. This practice is referred to as cross-shareholding, and it is generally considered an example of capital misallocation. It demonstrates a company's prioritization of business partnerships over sustainable shareholder value because the capital used to buy these shares is not available for acquisitions, capital expenditures, dividends or share buybacks. Cross-shareholding can further undermine minority shareholder rights and market discipline because management-friendly shareholders are universally supportive of management-slated resolutions. With this context in mind, AB's approach is to vote against the most senior executive if a company allocates 20% or more of its net assets to cross-shareholding. In doing so, AB seeks to hold senior management accountable for material capital misallocation, because it is a practice that generally misaligns with long-term shareholder value.

The successful Vote No Campaign, led by Oasis, targeted President Takakazu Uchiyama at Fujitec, for unlawful related-party transactions that allegedly benefited his family. Immediately ahead of the annual general meeting (AGM) on June 23, 2022, Fujitec withdrew President Uchiyama from reelection and then appointed him as the company chairman (which does not require shareholder approval) following the AGM.

10 "2022 Japan Proxy Season Review."

South Korea

Similar to other Asian markets, South Korea has corporations that play significant roles in its economy. The dominant, primarily family-owned conglomerates called "chaebols," have been at the center of controversies around various corporate governance–related issues. Namely, under the founding families' controlling stake and leadership positions, the independent oversight capacity of relevant companies merits a discussion on how such structures should be assessed from a long-term minority shareholders' perspective.

Minority Shareholders' Rights

In 2022, there were developments on improving minority shareholder rights. The South Korean FSC amended the guidelines for corporate governance reports, which are mandatory for KOSPI-listed firms with total asset of ₩1 trillion or more.[11] The guidelines include efforts to protect minority shareholders. Companies in scope of the mandated corporate governance disclosure under the guidelines are now required to follow their minority shareholder protection policy in a major event, like a split-off or change of ownership structure. Companies must also disclose relevant minority shareholder engagement regarding the event.

The FSC's amended guidelines for corporate governance reports also require companies to disclose explanations when multiple related-party transactions are bundled as a single proposal for board resolution. The change was an effort to discourage the common practice of bundling related-party transaction proposals, which often limits the disclosed information available for shareholders to make an informed decision.

Discussion of succession plans is another key point to note from the guidelines, given the historical practice of dynastic successions among chaebols. This new requirement can be seen as a notable attempt to encourage more inclusive and merit-based pipeline development at the senior executive level. The impact of these guidelines on shareholder votes of these amendments has yet to be observed with the deadline for compliance being May 2022. The 2023 AGMs may be the initial year where shareholders' views on respective companies based on corporate governance disclosures are reflected through proxy votes.

Fair Trading

In an attempt to limit the influence of insiders and to enhance fairness in the market, the South Korean FSC expanded the scope of the initial public offerings (IPO) lockup rules in its Listing Rules in 2022. The former IPO lockup rules applied only to the shares acquired through stock options prior to the IPO but not to the shares acquired via exercising stock options after a company has gone public. With the amendment to the Listing Rules, the IPO lockup rules were changed to apply to all insider holdings regardless of the timing of exercising stock options. The Korean FSC is seeking to introduce a staggered lockup contracts system through which newly listed companies may require different lockup periods (initial six months plus up to two years) on different stakeholders (CEO, board members, etc.) on a voluntary basis. The system may help address the likely concentration of selling directly after the six-month lockup period.

Impact of Global Regulations on South Korea

The emergence of regulations outside of South Korea, such as disclosure requirements on ESG factors for investment advisers, the Sustainable Finance Disclosure Regulation and the US Securities and Exchange Commission, has resulted in foreign institutional investors asking for higher standards on corporate governance and companies' approaches to sustainability outside their local markets. This is partially reflected through South Korean companies receiving an increased level of dissent against directors for governance failures or concerns. Board-level diversity and independence, as well as involvement in controversies around corruption and bribery scandals, are some of the most prevalent concerns raised by public shareholders.

Indeed, South Korean companies have some of the least gender diverse boards in the world—The average is about 5.5% female directors in 2022, (up from less than 4.5% in 2020).[12] In 2019, the Korea Exchange made amendments to the Capital Markets Act, which require at least one female director to be appointed at large companies (equal to or greater than ₩2 trillion in total assets; the grace period in order to do so ended in August 2022). As a result, board-level gender diversity has improved slightly year over year, with large companies having worked to comply with the new

11 Korean Financial Services Commission, *Revised Guidelines on Corporate Governance Disclosure to Strengthen Shareholder Protection*, March 7, 2022.
12 Candice Kim, Jieun Chang and Jaesung Lee, "2022 Korea Season Review," ISS Insights, Institutional Shareholder Services, February 1, 2023.

regulation. According to ISS, 80% of companies subject to the regulatory board gender diversity requirement have at least one female director on the board. Among 120 large-sized companies under the ISS Korea universe, 43% of new outside director candidates this year were female. Board independence is another area that South Korea is working to improve.

For the KOSPI, non-executive directors should be at least one-fourth of the total number of directors. However, for large companies with total assets of ₩2 trillion or more, there should be at least three non-executive directors, equaling half of the total number of directors. Then, with KOSDAQ, at least three directors should be appointed, with outside/non-executive directors making up at least one-fourth of the total number of directors. For large companies with total assets of ₩2 trillion or more, they should appoint at least three directors with the number of non-executive directors making up at least half of the total number of directors. In an attempt to encourage greater board-level independence, AB requires majority independence for the boards of large companies in South Korea. For small companies, AB requires one-third independent director representation.

With respect to companies failing to reach investor expectations on environmental practices/disclosures, some directors have received a high level of dissent for the first time. Such emergence of focus around climate-related accountability at the board level has resulted in a number of companies committing to climate action in 2022. However, progress on climate reporting continues to lag in South Korea.

Conclusion

Overall, we believe that the highlighted efforts to improve independence and diversity at the board level, as well as protect the minority shareholder rights are noteworthy in the three markets discussed in this report. While the market and company-specific contexts should be considered when evaluating an issuer's approach to corporate governance, AB expects that markets and companies who demonstrate systemic and structural accountability at the top management- and board-levels in the interest of minority shareholders, employees and other stakeholders may win the investors who have long-term interest in the company's business.

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