

KAS Journal on Contemporary Korean Affairs

2014

Corporate Social Responsibility in Korea

State and Perspectives



Konrad
Adenauer
Stiftung

KAS Journal on Contemporary Korean Affairs
2014
Corporate Social Responsibility in Korea
State and Perspectives

Edited by:
Konrad-Adenauer-Stiftung Seoul; John McDonald (Language Editor)

Published by:
Konrad-Adenauer-Stiftung
Korea Office
2nd Floor, Wonseo Bldg., 13 Changdeokgung 1-gil
Jongno-gu, Seoul 110-280, Republic of Korea

+82-2-790-4774
www.kas.de/korea

ISBN 978-89-93324-75-4 93360

© Konrad-Adenauer-Stiftung, 2014

ALL RIGHTS RESERVED. This book is wholly protected by copyright and related rights. Any unauthorized reprint or use of this material is prohibited. No part of this book may be reproduced or transmitted in any form or by any means, electronic or mechanical, including photocopying, recording, or by any information storage and retrieval system without expressed written permission from the publisher.

Table of Contents

Norbert Eschborn

Editorial 5

Kwon Sung-Sik

The Level of Corporate Social Responsibility (CSR)
in Korean Firms 7

Sung Jin-Young

Sustainability Reporting Trend in Korea 27

Jeong Jae-Kyu, Yang Chun-Seung

Measures for Improving the Corporate Governance
of Listed Companies in Korea 51

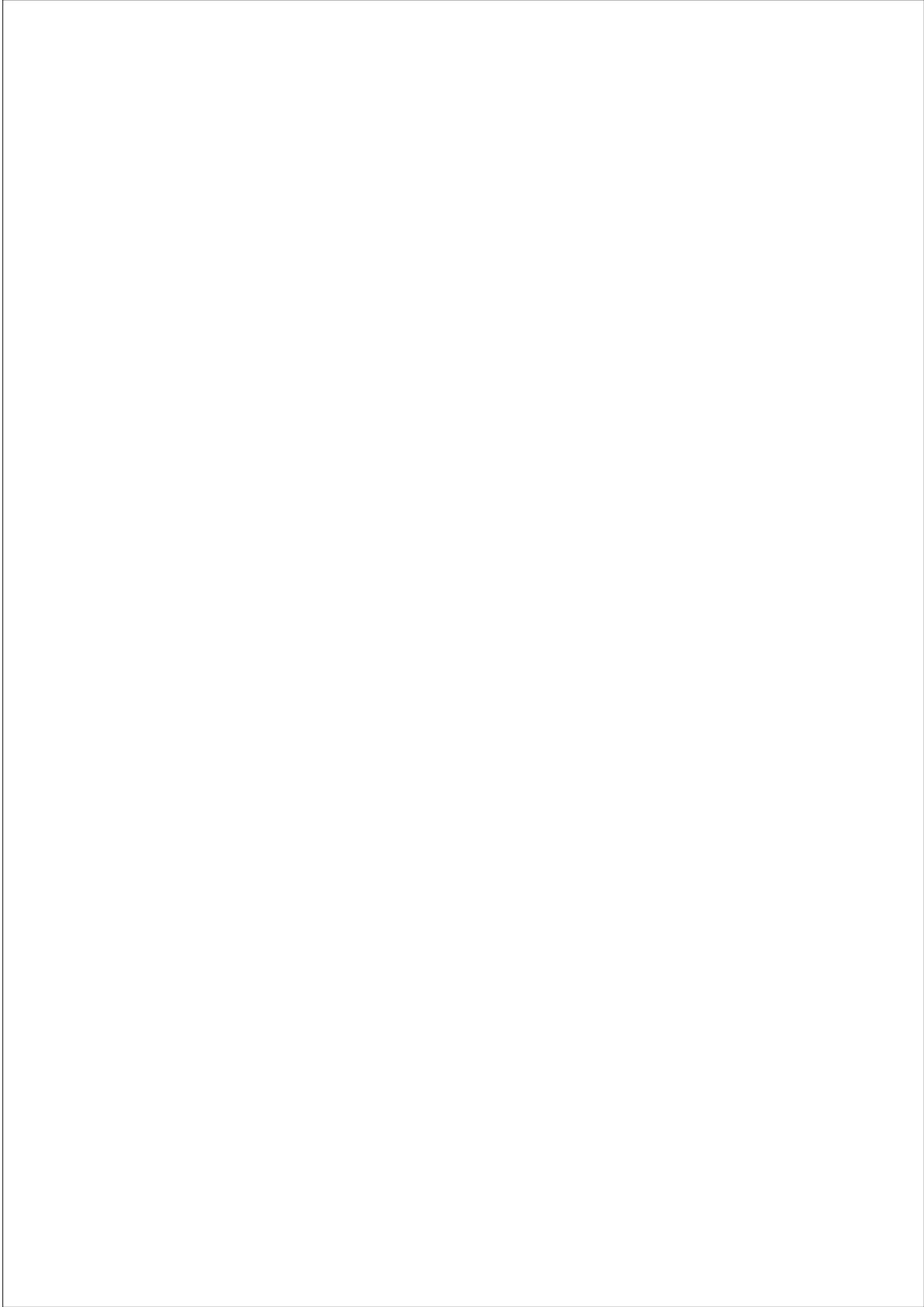
Kwak Kwan-Hoon

ESG disclosure: Legal requirement to facilitate CSR
implementation by Korean companies 91

Simon Childs

Does South Korea need Corporate Social Responsibility?
The Impact of CSR on National Competitiveness 109

About the authors 129



Editorial

Norbert Eschborn

Society is based upon a moral consensus among its members. This consensus is characterized by common values and the understanding that moral anarchy destroys society and economy. Justice, fairness, honesty, integrity, and responsibility are the values that establish the backbone of a social community. Individuals and organizations are called upon to align their operations and decisions toward these values and to contribute to their stability.

This also applies to the roles people play in business - and it particularly applies during times of economic crisis. The theory occasionally circulating that corporate social responsibility (CSR) could lose significance in face of the financial and economic crisis is misleading. The crisis can only be successfully mastered if our moral common sense and the desire and ability to cooperate are maintained to our mutual advantage.

Many companies worldwide have made Corporate Social Responsibility (CSR) a central part of their business philosophy. It is the quality parameter of sustainable economic management. Responsible companies reduce their “ecological footprint,” respect labor and social standards, and engage in community projects.

CSR means voluntary commitments that go far beyond what is required by law. This is not only good for the environment and for society at large, but also for the companies themselves. It is in the interests of companies to save energy, for example, thus reducing their production costs, or to engage in community activities, thus convincing their staff that they work for a particularly active and responsible company. Economic success and sustainability belong together - today more than ever before.

This issue of the KAS Journal on Contemporary Korean Affairs is dedicated to the analysis of CSR in Korea, its state and perspectives - a subject on which KAS has worked for many years already in close cooperation with our dedicated Korean partner organizations. The articles aim at presenting current matters of interest regarding CSR in this country where it seems to have not reached its full potential yet.

I should like to thank all authors for their important contributions and hope that this publication offers interesting insights into CSR in the Republic of Korea.



The Level of Corporate Social Responsibility (CSR) in Korean Firms

Kwon Sung-Sik

It is difficult to assess a firm's level of Corporate Social Responsibility (CSR) because the scope of CSR is extensive and the results depend on the evaluation scope. Furthermore, CSR has different definitions across countries, history, cultures, religions, social customs, and economic conditions, and also varies according to the vision and unique specificity of individual firms. Therefore, it is practically impossible to come up with criteria that allow for the comparison of different CSR levels implemented by multiple firms. Moreover, even if criteria to evaluate the level of CSR exist, they are qualitative (human rights, environment, ethics) and not quantitative, thus raising a question over the objectivity of evaluation. Then, how can the level of CSR practiced by firms be evaluated. First, to identify an appropriate method for evaluating the level of CSR in Korea, we examined current CSR evaluation methods and awards in Korea and reflected upon an effective way to assess the CSR level. Building upon such reflection, we focused on the CSR practices of Korean firms today and proposed prospects for the future.

Introduction

Since the 19th century, in a capitalist society, firms have evolved to employ a wide-range of business skills and means in order to attain traditional business objectives, i.e., profit-generation. And during this process, social issues such as environmental degradation, social polarization, and obesity occur. As a result, the public has criticized businesses for causing such social issues for their personal benefit, with businesses then responding and justifying their actions, which eventually gave birth to the concept of CSR or Corporate Social Responsibility.

The Level of Corporate Social Responsibility (CSR) in Korean Firms

In particular, in the 1990s, a number of civic groups launched global boycott campaigns due to environmental, human rights, and corruption issues caused by multinational corporations, such as the Enron·WorldCom scandals, for example, which has providing a warning that businesses disregarding CSR may be evicted from the market. As such, CSR is not an option but a necessity for business survival. This paper aims to examine the level of awareness and number of activities regarding CSR practices among Korean firms. To this end, it is essential to first discuss the definition CSR.

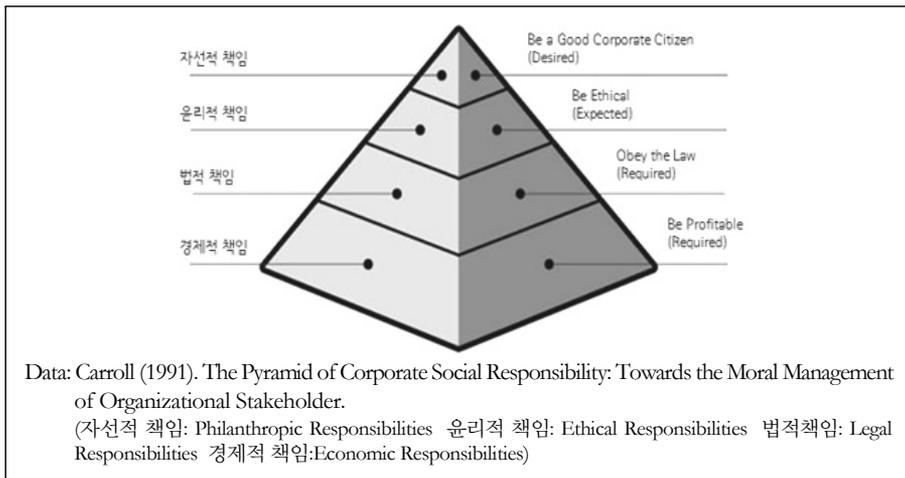
1. What is CSR?

When it comes to defining CSR, the most widely used concept is “The Pyramid of Corporate Social Responsibility” developed by Professor Archie B. Carroll (1991). Carroll believed that CSR includes the economic, legal, ethical, and philanthropic expectations that society has for corporations, and defined CSR into four major areas.

Table 1: Types of Corporate Social Responsibility

Type	Description
Economic Responsibility	Responsibility of a corporation, as the most fundamental economic unit of society, to create products and services that society wants and sell them at a profit.
Legal Responsibility	Responsibility of a corporation to pursue its economic missions within the framework of the law.
Ethical Responsibility	Responsibility of a corporation to embraces fair and just business activities and practices that are expected by societal members, even though they are not codified into law.
Philanthropic Responsibility	Responsibility of a corporation to utilize its resources and carry out appropriate social actions based on its discretionary or voluntary judgment or decision.

Image 1: The Pyramid of Corporate Social Responsibility



In particular, Carroll regarded economic and legal responsibilities as “required” conditions for corporations, whereas ethical responsibilities were “expected” from businesses, and philanthropic responsibilities were “desired” from corporations in order for them to become good corporate citizens.

However, this Pyramid may mislead us to think that the highest level of CSR by firms is to help the local community and underprivileged by donating proceeds or doing volunteer work, meaning that companies need to fulfil their philanthropic responsibilities to become a good corporate citizen.

Yet, the essence of Carroll’s pyramid model is that CSR starts from economic and legal responsibilities. In other words, a corporation merely promoting its CSR activities by boasting that it fulfils its philanthropic responsibilities without fulfilling its most fundamental economic legal responsibilities — for example, trying to become a good corporate citizen through donations or volunteering while engaged in malpractice such as tax evasion, fraud, embezzlement, window dressing, corruption, or unfair labour practices — is far from being true to the essence of CSR.

Scholars other than Carroll based the concept of CSR differently based on their areas of interest, with these different perspectives being summarized Table 2.

The Level of Corporate Social Responsibility (CSR) in Korean Firms

Table 2: Different Academic Perspectives on CSR

Views on CSR	Scholar	Description
Stakeholder	Maignan & Ferrell (2000)	The extent to which businesses meet the economic, legal, ethical, and discretionary responsibilities imposed on them by their stakeholders.
Stakeholder	Blomm & Gundlach (2001)	Obligations of the firm to its stakeholders, and these obligations go beyond legal requirements and the company's duties to its shareholders, and fulfilment of these obligations is intended to minimize harm and maximize the long-run beneficial impact of the firm on society.
Stakeholder	Sprinkle & Maines (2010)	CSR refers to diverse business activities that are focused on the welfare of stakeholders.
Stakeholder	Hasnas (2012)	Corporate managers should not have a collective fiduciary duty of the stakeholder group but the responsibility to make sure that all values created within the organization are distributed to all general stakeholders.
Stakeholder	Brown & Forster (2012)	Corporations must use the concept of 'justice' and 'complete right', valuing stakeholders from an economic and moral standpoint for both corporate and social satisfaction.
Social Responsibility	Brown (1953)	CSR refers to the obligations of businesses to pursue policies, to make decisions, or to follow lines of action that are desirable in terms of the objectives and values of society.
Social Responsibility	McGuire et al. (1988)	CSR refers to the obligations vis-a-vis the overall society, going beyond simple economic and legal obligations.
Social Responsibility	Petkoski & Twose (2003)	CSR refers to the commitment of business to contribute to sustainable economic development, and working with employees, their families, and the local community and society at large to improve the quality of life, in ways that are both good for business and good for development.
Social Responsibility	McWilliams & Siegel (2001)	CSR refers to the corporate activity needed to create a better society, going beyond fulfilling direct relationship of interests and regulatory conditions defined by law.
Social Responsibility	Kitzmueller & Shimshack (2012)	CSR can be expressed as an observable and measurable behaviour or output, and Corporate Social Performance (CSP) exceeds levels set by obligatory regulations or standards enforced by law.
Ethics	McFarland (1982)	CSR refers to corporations behaving based on moral, ethical, and economic values, recognizing the fact that individuals, organizations, and various social systems are interdependent.
Risk Management	Mohr et al. (2001)	CSR refers to behaviour aiming to maximize long-term positive effects while minimizing potential risks in advance.
Corporate Citizen	Marsden (2000)	A corporation is both a legal entity with both rights and obligations and a citizen constituting a member of the local community.
Corporate Citizen	Thaler (2012)	A corporation has the responsibility to pursue profits while assuming its role as a good corporate citizen.

Source: KAIST Center for Corporate Social Responsibility (2006), Present and Future of Corporate Social Responsibility Practice in Korea; Huh Young-Do et al. (2012), Study on Corporate Social Responsibility and Local Economic & Social Development. Revised for Reference.

As seen above, scholars including Carroll have expressed diverse views on CSR, with international organizations also adopting varying definitions of CSR.

Table 3: Terminology and Definition of CSR among International Organizations

International Organization	Term	Definition
Organization for Economic Co-operation and Development (OECD)	CR	Corporate responsibility involves the search for an effective 'fit' between businesses and the societies in which they operate
International Chamber of Commerce (ICC)	CR	The voluntary commitment by business to manage its activities in a responsible way
United Nations Conference on Trade and Development (UNCTAD)	CSR	Concept whereby enterprises integrate social and environmental concerns into their business policies and operations, with a view to improving their impact on society
World Business Council for Sustainable Development (WBCSD)	CSR	Continuing commitment by businesses to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families, as well as that of the local community and society at large.
International Labour Organization (ILO)	CSR	The way that enterprises consider the impact of their operations on society and CSR principles are integrated in both enterprises' internal processes and interactions with stakeholders on a voluntary basis.
International Organization of Employers (IOE)	CSR	Voluntary and positive activities carried out by corporations in various social, economic, and environmental fields, going beyond compliance with legal requirements.
International Organization for Standardization (ISO)	SR	Responsibility of an organization for the impact of its decisions and activities on society and the environment through transparent and ethical behaviour.

Source: Ko Dong-Soo (2006), Corporate Social Responsibility: Goal Discussions Trend & Our Response. Revised for Reference.

The Level of Corporate Social Responsibility (CSR) in Korean Firms

To date, scholars and international organizations have had a difficult time coming up with a single definition of CSR because the scope of CSR is too broad. The core subjects of CSR proposed at ISO 26000¹ spanned from ‘governance’, ‘human rights’, ‘labour practice’, ‘environment’, ‘fair management practice’, and ‘consumer issue’, to ‘local community engagement’ and ‘development’. As such, all business decisions made and business activities conducted seem to be in relation with CSR. Furthermore, such core CSR subjects can vary according to trends, places, time, and even the specificity of each firm and also its impact on society, making it even more difficult to adopt a single definition of CSR. Overall, since CSR is quite extensive in its scope, and at the same time the priorities of firms can change according to corporate specificity and conditions, it is extremely difficult to establish a concrete definition of CSR. Hence, it is natural that CSR has varying definitions according to areas of interest of scholars and the unique conditions of international organizations. After all, rather than adopting a single definition of CSR whose scope is quite comprehensive and flexible, businesses need to adopt a ‘practical approach’ to implement a personalized CSR practice tailored to the needs of their individual firm, since 100 different firms may require 100 different concepts of CSR.

In this regard, GE, Nestle, and IBM include best practices defined by the priority of CSR activities, which factor in the views and characteristics of stakeholders and their impact on society to establish a sound CSR definition. Since 2007, GE has employed CSR strategies: 1) ‘Ecomagination’ initiative, which aims to address global environmental issues while seeking corporate growth, and 2) ‘Healthymagination’ to develop innovative medical products and provide better quality medical services, thereby reaching out to assist more people at an affordable price. As such, the company is striving to find a balance between how to co-exist with society while seeking sustainable growth. As another example, Nestle has a best practice for investing in technology transfers and irrigation facilities maintenance in local regions in order to improve the company product ingredients, and thus address local social issues, satisfy consumers with quality ingredients, while seeking corporate growth. IBM has also successfully implemented a CSR initiative

¹ ISO 26000: Global standard on “Social Responsibility”

called Smart Planet, which aims to build on its core technology of IT solutions in an attempt to address social issues by providing free-of-charge services to IT-marginalized regions and subsequently create a new customer base and market.

2. How should we evaluate the level of CSR?

As mentioned above, given the comprehensive and flexible characteristics of CSR, it is practically impossible to compare and evaluate the level of CSR based on a single criterion. Yet, numerous CSR awards and evaluation models based on differing criteria exist. First, we will examine awards that evaluate the level of CSR of Korean firms by organizing entities,² and consider effective ways to evaluate the level of CSR based on the characteristics of said criteria.

2.1. Media-hosted Awards

Currently, the media operates the largest number of CSR-related awards. The media tends to distribute awards by using CSR-specialized organizations to assist their evaluation, or to jointly organize awards in conjunction with government sponsorships.

² Re-examined Issue Paper of The Federation of Korean Industries (2010), “CSR Evaluation System: True to its Role?” as of 2014

The Level of Corporate Social Responsibility (CSR) in Korean Firms

Table 4: Major media-hosted awards as of 2014

Award		Host & Organizer	Year of Foundation (number of times awarded)
1	Chosun Ilbo Environmental Award	Chosun Ilbo	1993 (21)
2	Quality Service No.1 by Women Consumers *Philanthropy Section	Yeoseong Shinmun	1999 (15)
3	Hankook Ethical Management Award	Hankook Ilbo, New Industry Management Academy	2003 (10)
4	Philanthropic Business Award	The Korea Economic Daily, Open Business Research Institute	2004 (10)
5	Best Workplace *Sustainability Section	Magazine Hankyung	2007 (7)
6	Customer Inspired Management Award *Sustainability Section	The Korea Economic Daily, Korea Sustainability Management Evaluation	2007 (7)
7	The Republic of Korea Ethical Management Award	Magazine Hankyung	2008 (7)
8	Korea Ethical Management Award	Hankook Ilbo, Ministry of Knowledge Economy, UN Global Compact	2008 (10)
9	Green Construction Award	Asia Today (sponsored by Ministry of Land, Infrastructure and Transport)	2009 (4)
10	Kyunghyang Financial Education Award *Philanthropy Section	Kyunghyang Shinmun, Financial Supervisory Service	2009 (8)
11	Safe Management Award *Sustainability Section	Maeil Business Newspaper, Ministry of Employment and Labor	2009 (21)
12	Creative Business Management Award of Korea *Socially responsible management	Joongang Ilbo	2009 (5)
13	Forbes Philanthropic Award	Forbes Korea, Korea Chamber Of Commerce And Industry,	2010 (4)
14	Korea Philanthropic Award	Magazine Hankyung	2013 (1)

Most awards are concentrated in the field of philanthropy, based on the size of donations or the number of volunteer activities, though awards on ethical management and green management are also worthy of particular attention. However, it is regretful that some awards hosted by the media fail to disclose the evaluation criteria, with some having no evaluation process, attesting to the fact CSR awards are sometimes used as a mere promotional tool.

2.2. Government-hosted Awards (including para-government, local government)

Since the beginning of 2000, the Korean government has given awards for ethical business management as a way to promote CSR activities, and in the second half of 2000, additional awards were established that focus on green management. As of 2014, awards prescribed by Presidential Decree hold the highest prestige, which include the National Quality Management Convention Green Business Award, and the Sustainability Management Award.

The Level of Corporate Social Responsibility (CSR) in Korean Firms

Table 5: Government-hosted Awards (including para-government, local government)

Name of Award		Host & Organizer	Year of Foundation (number of times awarded)
1	National Quality Management Convention *Green Management *Sustainable Management	Ministry of Trade, Industry and Energy, Korea Standards Association	1975 (39)
2	Korea Game Award *Corporate Philanthropy Section	Ministry of Culture, Sports and Tourism, The Sports Chosun, The Electronic Times	1996 (17)
3	Labor Management Culture Award	Ministry of Employment and Labour	1996 (18)
4	Neighbor-helping Men of Merit	Ministry for Health, Welfare and Family Affairs	2000 (13)
5	National Environmental Management Award	Ministry of Environment, Mackyung Safety Environment Research Institute	2006 (8)
6	Corporate Image *Corporate Philanthropy Section	Ulsan Ulju-gun	2008 (3)
7	Busan City corporate Philanthropy Award	Busan City	2009 (5)
8	Recycling of Resources Leading Firm Award	Korea Environment Corporation	2009 (8)
9	Green Management Award	Ministry of Knowledge Economy, Institute for Industrial Policy	2010 (4)
10	Beloved Firm in Korea	Ministry of Trade, Industry and Energy, Institute for Industrial Policy etc.	2013 (1)

These government awards evaluate the level of CSR practice based on CSR-related evaluation indexes jointly developed by the government and CSR-specialized agencies. The following table lists the 5 major evaluation indexes.

Table 6: Major Evaluation Indexes

Name of Evaluation Index		Host & Organizer (Year of Development)	Description
1	Korean Business Ethics IndeX (KoBEX)	Ministry of Trade, Industry and Energy, Institute for Industrial Policy(2003)	Korea’s representative ethical management index, evaluates the ethical leadership of the CEO, role-model, equal employment at work, human resources development, health and safety, and is used as evaluation criteria for “The Most Beloved Firm in Korea” Award.
2	BSR Guidelines	Ministry of Trade, Industry and Energy, Institute for Industrial Policy(2006)	Korea’s sustainable management index developed specifically for Korea based on GRI guidelines ³ .
3	HRD Korea Ethics inDEX (KEDEX)	HRDKorea(2008)	Qualitative, quantitative index developed to objectively measure the performance of ethical management progress of industrial complexes. Calculation based on 100 points, once per year.
4	Corporate Transparency Self-Diagnosis Model	Anti-Corruption and Civil Rights Commission (2009)	Korea’s major corporate transparency evaluation index, consisting of disclosure transparency (25%), accounting transparency (25%), responsible management (20%), shareholders protection (15%), internal control (10%), ethical management, and social responsibility (5%).
5	ISO26000 Self-Diagnosis Check List	Ministry of Trade, Industry and Energy Korea Agency for , Korean Agency for Technology and Standards(2010)	CSR evaluation index fully incorporating ISO26000, aiming to assess areas of the CSR implementation process (awareness on social responsibility, identification and engagement of stakeholder, priority setting, etc.) and performance (human rights, labour practice, environment, fair management practice, consumer issue, local community engagement and development).

The Level of Corporate Social Responsibility (CSR) in Korean Firms

Government awards are generally given based on highly credible criteria, ensuring greater professionalism and fairness compared to other award models. In particular, corporate legal responsibility, which is the most fundamental responsibility of CSR seen from the 'Pyramid of Corporate Social Responsibility' of Carroll (1991), is an element that the government used to screen most of the awards it hosts. Based on the award guidelines, the chances of firms trying winning these awards by externally assuming philanthropic responsibility while breaching legal requirements internally are minimal compared to awards hosted by other entities. However, limitations remain in that evaluation indexes have been focused on ethical management, except for the 'ISO26000 self-diagnosis checklist'. In order to incorporate more a comprehensive CSR, it seems necessary to add more evaluation items related to economic responsibility — in addition to ethical responsibility — which means that corporations, as the basic units of society, must create products and services that society needs and sell them at a profit (Carroll, 1991). Moreover, how to better screen the non-compliance of laws and regulations of awarded firms and how to objectively evaluate corporate governance and CSR implementation processes remains as tasks to be undertaken.

2.3. Awards Operated by Industry Groups and Associations

CSR awards from industry associations exist, which are based on industry-specific characteristics. These awards excel in effectively considering the flexible characteristics of CSR, and how to apply industry-specific characteristics in the evaluations. However, limitations include the fact that most of these awards are focused on one element of CSR, based on the industry-specific and associations' characteristics.

³ GRI Guideline: Sustainability reporting guidelines developed by Global Reporting Initiative (GRI), which is referenced by more than 90% of global firms reporting on their sustainable performance.

Table 7: Awards Operated by Industry Groups and Associations

Name of Award		Sponsor & Organizer	Year of Foundation (number of times awarded)
1	Labor Management Cooperation Award	Korea Employers Federation	1989 (25)
2	Best Company Chosen by Women Consumers Award	Korean Women Entrepreneurs Association Korea Business Women's Federation	1998 (16)
3	Seoul Social Welfare Convention	Seoul Council on Social Welfare	1999 (14)
4	Mecenat Award	Korea Mecenat Association	2000 (14)
5	Gratitude Award *Ethical Management Section	Korea Listed Companies Association	2000 (15)
6	Corporate Governance Award	Korea Exchange, Korea Corporate Governance Service	2001 (13)
7	LOHAS Management Award * Sustainability	Korea Green Foundation	2004 (6)
8	Transparent Management Award	Organized by five leading economic organizations in Korea, Korea Accounting Information Association	2005 (9)
9	Web Award Korea *Corporate Philanthropy Section	Web Award Secretariat	2005 (10)
10	Small and Medium Enterprise Environmental Management Support Project Award	Korea Chamber of Commerce and Industry, Institute of Corporate Sustainability Management, HSBC	2006 ()
11	Best Social Enterprise Award	Work Together Foundation	2006 (1)
12	ROK KOSDAQ Award *Corporate Philanthropy Section	KOSDAQ Association	2006 (6)
13	Good Compliance	Korea Exchange(KRX)	2007 ()
14	ROK Health Industry Award *Corporate Philanthropy Section	Health Industries CEO Summit, Korea Health Industry Development Institute, Health Insurance Review & Assessment Service	2007 (7)

The Level of Corporate Social Responsibility (CSR) in Korean Firms

2.4. Awards Operated by Professional Evaluation Agencies

Table 8: Major awards operated by CSR-specialized evaluation agencies

Name of Award		Host & Organizer	Year of Foundation (number of times awarded)
1	Corporate Governance Evaluation	Korea Corporate Governance Service	2003 (9)
2	Respected Company Award	Korean Management Association Consulting(KMAC)	2004 (10)
3	Korea Sustainability Conference	Korea Standards Association (KSA)	2008 (6)
4	CITI-KOSMI Women Entrepreneurs Award *Corporate Philanthropy Section	Korea Small Business Institute, Korea CITI Bank	2008 (6)
5	DJSI Korea No.1 Company Award	Korea Productivity Center(KPC)	2009 (5)
6	Global Standard Management Awards	Korea Management Association Registration (KMAR)	2011 (3)

These awards are generally given based on criteria jointly developed by CSR-specialized agencies, in conjunction with an outside CSR advisory group or overseas CSR-specialized agency, and the evaluation criteria are as follows.

Table 9: Evaluation Criteria

Name of Evaluation Index		Sponsor & Organizer (Year of Development)	Description
1	Korea Exchange SRI Index (KRX SRI)	Korea Corporate Governance Service(2009)	Stock index reflecting the evaluation results of the Korea Corporate Governance Service after assessing non-financial elements having an impact on the sustainability of listed companies in terms of corporate governance, and social and environmental elements.
2	Dow Jones Sustainability Index (DJSI Korea)	Korea Productivity Center (2009)	Korea Productivity Center evaluates non-financial elements of Korean firms together with Dow Jones and Swiss SAM to incorporate firms above a certain level into DJSI Korea.
3	Republic of Korea Sustainability Index (KSI)	Korea Standards Association (2009)	Experts and stakeholders evaluate the responsiveness of firms to sustainability trends and impacts based on ISO 26000 (ISO 26000 7 core subjects).

As such, professional CSR agencies try to cover all areas of CSR based on systematic evaluation criteria, compared to other CSR awards, and in particular they adopt a multi-faceted approach (media survey, external specialist pool, stakeholder survey, etc.) to assess the non-financial elements of firms. However, consulting agencies offering CSR consulting service to firms also evaluate the CSR level of these firms, which poses a risk of having a biased evaluation. Ideally, this aspect needs to be further improved.

2.5. Awards Operated by Academia

CSR awards managed by academic societies are as follows. They play a significant role in setting the theoretical context for CSR.

Table 10: CSR awards managed by academic societies

Name of Award		Sponsor & Organization	Year of Foundation (number of times awarded)
1	Korea Marketing Frontier Award *Corporate Philanthropy Section	Korea Marketing Associations	1993 (21)
2	Yonsei College of Business Administration Corporate Ethics Award	Yonsei University College of Business Administration	1996 (12)
3	Ethical Management Award	Korean Academic Business Ethic	2003 (21)

2.6. Awards Managed by Civic Groups

Furthermore, civic groups are also crucial for supervising and further promoting the CSR activities of firms.

Table 11: Awards Managed by Civic Groups

Name of Award		Host & Organizer	Year of Foundation (number of times awarded)
1	Economic Justice Corporate Award	Citizens' Coalition for Economic Justice, Korea Economic Justice Institute	1990 (22)
2	Best Foreign Corporation Award	Korea Economic Justice Institute	2001 (9)

The Level of Corporate Social Responsibility (CSR) in Korean Firms

The analysis of methods for evaluating the level of CSR among Korean firms based on the aforementioned awards and evaluation models in Korea indicate that, in general, the majority of evaluation methods focus on corporate philanthropy assessed bases on the amount of money donated or the number of volunteer activities. Next in line were awards on ethical management, which factor in elements in the areas of corporate ethical responsibility such as equal employment, health and safety, and accounting transparency, followed by awards on green management that include the areas of energy efficiency, climate change mitigation, biodiversity, etc.

Recently, awards focusing on specific elements in line with current social trends, such as 'Leading Firm in Job Creation', and 'Leading Firm in Gender Equality' have also been presented. This is probably because it is more realistically feasible to evaluate specific elements of CSR rather than to conduct an overall assessment of CSR based on one single criterion since, as aforementioned, CSR is extensive in its scope and places different priorities according to the specific conditions faced by firms.

Despite such facts, evaluation models and awards that assess integral parts of CSR still exist. Major examples include the 'National Quality Management Convention's Sustainability Award' sponsored by the Ministry of Trade, Industry and Energy, 'Korea's Beloved Company Award' and 'Respected Company Award' by Korean Management Association Consulting (KMAC), Dow Jones Sustainability Index (DJSI) of the Korea Productivity Center (KPC), and Korean Sustainability Index (KSI) of the Korean Standards Association (KSA). These evaluation models assess the performance of the overall CSR elements through different methods, and the majority of the host institutions use official documents or sustainability reports submitted by businesses as source data for the evaluation. However, since sustainability reports undergo a 3rd party audit, they help to ensure a larger degree of objectivity in the report, whereas it is very difficult to assess the authenticity of official documents, unless they are of special consideration. Moreover, other than KSA's KSI, errors can be made when standardized evaluation criteria are applied to compare and analyse different firms at the same level, without reflecting the company-specific CSR characteristics. Such failure may then lead firms to adapt their management process to the evaluation criteria or the checklist, and thus opt for 'Checklist-Management', disregarding the strategic activity of

defining the CSR concepts and their priority.

In other words, an objective CSR evaluation is practically impossible. However, evaluations should not be overlooked in the CSR implementation process because they help to improve CSR practices in firms. Therefore, it is posited here that two significant elements are required in order to evaluate the CSR level of firms.

First, before evaluating the performance of CSR activities, it is important to evaluate the concept and process of CSR pursuing firms. It is essential to identify who the core stakeholders are and what their expectations and understanding are. Then, it is crucial to evaluate the positive and negative impacts of the corporate business model on society and the environment and to then seek solutions that minimize the negative impacts and maximize the positive impacts. Lastly, it is essential to determine whether or not firms are defining priorities by analysing the competitiveness of their CSR activities based on their internal core capacity.

Second, both quantitative and qualitative methods must be employed in order to assess how corporations manage the CSR activities. To this end, it is crucial to receive performance feedback by communicating with not only CSR activity-specific experts but also different relevant stakeholders.

The KSI model run by the KSA is a CSR evaluation model developed based on these two elements, which therefore effectively embodies the true essence of CSR. However, despite such guidelines, it is not practically feasible for corporations to identify and communicate with all stakeholders during the evaluation process.

3. What is the level of CSR of Korean Firms?

In 2013, the Social Enterprise Research Institute and the East Asia Institute conducted a national survey that looked at the major CSR dilemmas of Korean firms. The following four dilemmas were selected as the final concerns.

The Level of Corporate Social Responsibility (CSR) in Korean Firms

First, despite the increased spending on CSR activities by a greater number of large corporations, public distrust of large corporations continues to grow. This distrust stems from the fact that, as aforementioned, most companies misinterpret the beginning of CSR to be a donation or volunteer activity. In order to dispel the distrust vis-a-vis large corporations, it is essential to implement CSR activities aiming to uproot tax evasion, embezzlement, fraud, window dressing, corruption, and unfair labour practices. And the process of implementing such initiatives should be disclosed to the public through communication with stakeholders. Indeed, donations and volunteer activities without such further processes will only have negative effects since they will be regarded as a mere CSR show that is being put up by firms.

Second, there is need to improve public opinion in order to strengthen CSR regulations, which is linked to the first dilemma. The public is aware that donations and volunteer work are important, but it wants corporations to be more keen to fundamental issues such as human rights and the environment, and if possible, to legally regulate these elements.

Third, there is an issue pertaining to double-minded consumers. The public calls for stronger CSR implementation by businesses, which is evidenced by survey results that reveal 77% of respondents “are willing to pay more for products coming from corporations demonstrating social and environmental responsibility for the next generation.” However, in reality, consumers tend to act in an opposite way. The fact is that stock prices or sales of firms unfairly treating their companies or violating the human rights of employees usually only decrease for one or two months and then pick back up; Korean consumers tend to be relatively indifferent regarding CSR issues. Under such circumstances, businesses will never give a serious consideration to CSR first.

Fourth, there is no channel to communicate CSR activities. Today, some 100 CSR reports are published each year by Korea’s leading corporations and public agencies; however, the majority of the public is not aware of such reports, and thus information pertaining to CSR is mostly obtained from the media. Currently, there are only a few companies committed to having two-way communications of CSR activities, but the bigger issue is that the public does not proactively wish to obtain CSR-related information.

Consequently, the level of CSR practiced by Korean firms remains very low. The CSR International Conference 2014 survey findings confirm that many corporations perceive CSR as a mere promotional activity to enhance their corporate image. Similarly, the KSI survey results conducted during the past 5 years reveal that the CSR level score of Korea is 50 points (out of 100 points). However, it should be noted that corporations alone are not to blame as consumers need to place more pressure on corporations to promote CSR.

Conclusion

An American CSR evaluation expert, Jason Saul, argued in his publication 'CSR 3.0' that only corporations considering CSR as a business opportunity will manage to co-exist with society and become future leaders. He emphasized that the CSR 3.0 era of seeking business opportunities while addressing social issues has arrived, which goes beyond 'CSR 1.0' in terms of providing mere charity and donations, and 'CSR 2.0' of complying with human rights and environmental legal regulations. However, it is posited here that it is not a true CSR to completely ignore the CSR 2.0 elements, with a view to rush into CSR 3.0. At the same time, CSR 1.0 should not be regarded as the starting line or prerequisite for ushering in the age of CSR 3.0. A genuine commitment to CSR is about fulfilling economic and legal responsibilities first. Corporations can then consider their impact on society to apply a strategic CSR policy to create business opportunities or CSR for social innovation. When defining the priorities of true CSR activities based on Jason Saul's criteria, implementing CSR 2.0 to fulfil legal requirements for human rights and environment concerns would be the first and foremost priority for businesses. Idealistically, the next step should be to apply strategic CSR policies to create business opportunities by considering the corporate impact on society and then finally the CSR 1.0 policies of charity and donation. The recent Sewol ferry disaster in Korea has profoundly taught us what kind of disaster is in store for society if firms ignore the basics of CSR. In this regard, we cannot help but think once again about the importance of CSR policies. Until today, we may have taken for granted that firms had no choice but to adopt CSR practices to ensure their sustainability. However, it should not be neglected that companies have a minimal responsibility to fulfil as a member of society; such a perspective is the first step towards

The Level of Corporate Social Responsibility (CSR) in Korean Firms

CSR implementation. Without such a sincere commitment, strategic CSR or CSV⁴ would only be superficial. Moreover, before coercing businesses to change their perspectives, consumers need to first improve their awareness by adopting ethical consumption⁵ and ‘Socially Responsible Investment’⁶ practices.

⁴ Creating Shared Value (CSV): A term coined by Michael Porter and Mark Kramer, referring to using CSR as a source to secure innovation and competitive advantage.

⁵ Ethical Consumption: Consumer movement including the fair trade movement, which is about not purchasing anti-environment, human, animal products and purchasing ethical products, even if the price is higher.

⁶ Socially Responsible Investment: Investing from a long-term perspective by considering corporations’ financial aspects as well as non-financial aspects in an environmental, social, and governance context.

Sustainability Reporting Trend in Korea

Sung Jin-Young

1. Introduction

As demand for the disclosure of corporate social responsibility performances and multiple-stakeholder communications surrounding business issues continues to grow, the number of firms implementing sustainability reporting is increasing accordingly. Ever since the World Commission on Environment and Development (WCED) defined the concept of “Sustainable Development” in its report “Our Common Future” published in 1987, global leading firms have taken the lead in issuing “Environmental Reports,” disclosing their environmental management practices and accomplishments. In 1995, in his publication “SustainAbility,” John Elkington further divided sustainable development into the “Triple Bottom Line (TBL)” of economic, environmental, and social agendas, and since then businesses began to release “Sustainability Reports” that include not only their environmental but also their economic and social achievements.

Korea has had a relatively short history of sustainability reporting. Korean companies developed a growing interest in sustainable development since the Rio Summit in 1992, and in 1995, the top steelmaker POSCO was the first in Korea to publish its “Environmental Report.” Following this report, Kia Motors released an “Environmental/Social Report” in 2003, and Samsung SDI, Hyundai Motors, and DowCorning Korea issued reports entitled “Sustainability Report,” thus leading the sustainability reporting trend in Korea. In the beginning, sustainability reporting was focused on large conglomerates having abundant human and financial capital, whereas today, sustainability reporting attracts expanded interest from public agencies, SMEs, and NGOs as well.

This paper aims to analyze the sustainability reports released in Korea and to then review the current trends of sustainability reporting in Korea, including the publication state of sustainability reports, use of global guidelines and norms (GRI guidelines, ISO26000, UNGC), implementation of integrated

Sustainability Reporting Trend in Korea

reporting, third-party assurances, etc. Moreover, this paper reviews feedback from sustainability report readers in order to assess the awareness of sustainability reporting by Korean readers, while also looking at the future prospects of sustainability reporting in Korea.

2. Trends for Sustainability Reporting

1) Reporting Terminology

In the sustainability management reports disclosed by Korean and global firms, terminology used for their reporting varies from “sustainability reporting,” “corporate social responsibility report” to “corporate citizenship report.” Korean firms seem to prefer the term “sustainability,” which relates to sustainable development rather than “responsibility,” which is suggestive of obligations and burdens to fulfill. An analysis of 115 sustainability reports released in 2013 suggested that 97 companies used the term “Sustainability Report” (84.3%), followed by “Corporate Social Responsibility Report”(7.8%) .

Table 1: Number of Sustainability Reports Published by Title

Terminology	Number of Publications	Ratio
Sustainability Report	97	84.3%
Corporate Social Responsibility Report	9	7.8%
Integrated Report	7	6.1%
Corporate Citizenship Report	1	0.9%
Report	1	0.9%
Total	115	100%

2) Korean and Global Reporting Guidelines

As there is no legal requirement for sustainability reporting, Korea does not have any standardized reporting guidelines regarding the report content or format. Since Korean firms tend to prefer universally applicable global

standards, the majority report on their sustainability activities based on the Global Reporting Initiative (GRI) guidelines, which are the most widely recognized guidelines. A study of KPMG International (2013) revealed that of 41 countries worldwide, Korea had the highest uptake of GRI guidelines, which seems to attest to the high confidence that Korean firms have in global guidelines.

Among the sustainability reports released in 2013, 108 reports adopted GRI guidelines (93.9%), while others were based on internal guidelines, Korean guidelines, and other guidelines.¹ In 2013, the percentage of firms having implemented sustainability reporting based on GRI G3.1 was the highest at 83.5%; however, since the release of GRI G4 guidelines in May 2013, the number of companies using G4 guidelines is also increasing.²

Many Korean firms report on their sustainability operations by adopting GRI guidelines, as well as ISO26000 and UNGC. To date, 72 sustainability reports were based on ISO 26000, global CSR standard (62.6%), and 54 companies released reports aligning to the 10 major principles and 4 major areas of human rights, labor, environment, and anti-corruption (47%). It appears that the reporting firms were making efforts to draft credible reports based on global norms by using a correlation table between the GRI and ISO 26000 indices and preparing independent UNGC implementation reports (CoP).

¹ 8 reports applied the Korea's business sustainability reporting guidelines (B.E.S.T sustainability Reporting Guidelines), 6 implemented the International Integrated Reporting Council (IIRC) guidelines, 2 adopted Electronic Industry Citizenship Coalition (EICC) guidelines, and 1 applied IPIECA/API sustainability reporting guidelines from the petroleum industry.

² As of the end of May 2014, a total of 5 companies produced sustainability reports based on GRI G4. In 2013, the Korea Mine Reclamation Corporation was the first to report its sustainability performance based on GRI G4, followed by Yuhan Kimberly. In 2014, Hyundai Motors, Kia Motors, and POSCO produced sustainability reports based on G4 guidelines.

Sustainability Reporting Trend in Korea

Table 2: Number of Sustainability Reports Published in 2013 based on Korean and Global Guidelines

Type		Number of Reports
GRI Guideline	G3.1	96
	G3	9
	Non-GRI	7
	G4	2
	G3.1 and G4 index partially applied	1
ISO 26000		72
UN Global Compact		54
Other guidelines		19

3) Integrated Reporting

Firms producing Integrated Reports incorporating both financial and non-financial results are also emerging in Korea, and there is a growing move in listed companies to release integrated reports. In 2011, Hyundai Engineering & Construction was the first in Korea to take part in a pilot program using integrated reporting, led by the International Integrated Reporting Committee (IIRC), to produce a sustainability report in an integrated reporting format, and in 2013 SK Telecom released an integrated report entitled “Integrated Sustainability Report.”

In 2013, other companies also implemented integrated reporting: 8 companies published reports entitled “Integrated Report,” representing 7% of all reports, and 6 out of 9 companies explicitly mentioned adoption of IIRC guidelines in their reports. However, there were many cases in which the supposedly integrated report was a mere combination of a sustainability management report and an annual report, without fully providing an integrated report by the firms in question. Therefore, a common belief is that it is too premature to shift to full implementation of integrated reporting in Korea.

4) Assurance of Report

Firms reporting on their sustainability activities have typically had their reports assured via internal assurance, expert assurance, or third party assurance in order to gain credibility from their stakeholders and to enhance the perceived quality of their reports. Since most countries, excluding few such as France and South Africa, do not legally require report assurance, slightly more than 20% of reports released worldwide undergo this type of assurance (CorporateRegister.com, 2013). Conversely, Korean companies seem to place more importance on the credibility of reports. Among the 115 reports published in 2013, 96 companies conducted an independent external assurance, representing 83.5% of all reports produced.

In general, external assurance is carried out by accountancy organizations, engineering firms, or small consultancy/boutique firms. In 2013, a total of 22 independent organizations engaged in verifying sustainability reports, and contrary to global statistics showing that accountancy organizations are leading the assurance market; most reports in Korea were assured by specialized assurance organizations.³ Out of the 115 reports published in 2013, 58 were assured by specialized assurance organizations (60.4%), followed by engineering firms and certification organizations (25.0%), and accountancy organizations (14.6%).

Table 3: Sustainability Assurance Providers in Korea

Organization Type	Organization Name	Number of Reports	Ratio
Accountancy Organizations	KPMG, Deloitte, PwC, E&Y	14	14.6%
Engineering Firms	DNV, LRQA	24	25.0%
Specialized Assurance Organizations	Korea Standards Association (KSA), Korea Productivity Center (KPC), The Institute for Industrial Policy Studies (IPS), and other 13 organizations	58	60.4%
Total		96	100.0%

³ According to a CorporateRegister.com (2013) study, the 4 major accountancy organizations assured 51% of the overall reports, followed by 15% by consultancy boutique/firms, 7% by other institutions, and 27% by certification organizations.

Sustainability Reporting Trend in Korea

AA1000AS (Assurance Standard) was developed by a company called Accountability with a Goal to assure the credibility, excellence, fundamental process, and system of sustainability reports, and has been the most commonly used, internationally-applied norm for performing assurance on sustainability reports. An analysis of “third-party assurance opinions” of sustainability reports in Korea has revealed that 81 reports were assured based on AA1000AS, accounting for 84.4% of all externally assured reports, and that assurance opinions were drafted based on the three principles of AA1000AS (inclusivity, materiality, and responsiveness) and attached to the reports.

3. Key Statistics on Sustainability Report

1) Target and Methodology

The Korea Standards Association (2013) examined the type of companies and reporting frequency of the 115 reports published in 2013 as a sample base. Given that sustainability reports used varying reporting terminology, all reports, if incorporating the three major pillars (economic, environment, and social achievement) of sustainable management, were included in the study. Environmental reports, the UNGC implementation report (Commitment of Progress, CoP), and annual reports were excluded from the assessment.

Some companies, with a goal to report on their sustainability achievement of 2012, published reports entitled “Sustainability Management Report 2012,” whereas others published “Sustainability Management Report 2013” based on the actual publication year. This study included all reports released in 2013 based on the publication year. Moreover, to identify the different types and characteristics of reporting companies, a classification is shown in [Table 4] below.

Table 4: Organization Classification

Type	Sub-type	Description
Company	Listed company	1,832 companies listed on Korea Exchange (KRX) ⁴
	Unlisted company	Companies excluding listed companies
	NGO	Other companies (NPO, social enterprises included)
Public Agency ⁵	Public Corporation	30 agencies designated by the Minister of Strategy and Finance among public agencies with 50 or more employees, whose per se income is 1/2 or more than the total income
	Para-Governmental agency	87 agencies designated by the Minister of Strategy and Finance among public agencies that are not public corporations with 50 or more employees
	Other public agency	178 public agencies that are neither public corporations nor para-governmental agencies
	Local government and other agency	Other public agencies not among 295 designated public agencies

2) Sustainability Reporting Trend for Private Firms in Korea

In 2013, a total of 78 sustainability reports by private firms were released in Korea, revealing a higher percentage of listed companies compared to unlisted companies. A total of 59 listed companies reported on their suitability performance (3.2% of all listed companies), showing a low reporting performance by listed companies; 16 unlisted companies produced sustainability reports, and 3 NGOs including environmental foundation reported on their sustainability efforts.

⁴ As of January 27, 2014 from the Korea Exchange Listing Disclosure System (<http://www.krx.co.kr>).

⁵ 295 institutions established and run by government investment, financing, or funding and designated by the Minister of Strategy and Finance pursuant to Article 4.1 of the Act on the Management of Public agencies (as of 2013).

Sustainability Reporting Trend in Korea

3) Sustainability Reporting State for Public Agencies in Korea

In Korea, 32 public agencies released sustainability reports in 2013, accounting for 10.8% of all public agencies, indicating a relatively lower reporting ratio for public agencies. By public agency type, 15 out of 30 public corporations implemented sustainability reporting (50.0%), followed by 14 out of 87 para-governmental agencies (16.1%), and only 3 out of 178 other public agencies (1.7%). The number of sustainability reports produced by local governments such as Incheon Metropolitan City and other agencies was 4.

In rank order, the reporting trend for relevant ministries found that 42.9% of public agencies under the Ministry of Land, Infrastructure, and Transport released sustainability reports, followed by agencies under the Financial Services Commission (33.3%), the Ministry of Environment (25.0%), Ministry of Trade, Industry and Energy (24.4%), Ministry of Maritime Affairs & Fisheries (14.3%), Ministry of Agriculture, Food and Rural Affairs (11.1%), Ministry of Employment and Labor (8.3%), Ministry of Culture, Sports and Tourism (6.1%), Ministry of Health and Welfare (5.6%), Ministry of Education (4.8%), and Ministry of Science, ICT and Future Planning (2.6%).

Table 5: Sustainability Reporting State by Private Companies and Public Agencies in 2013

Type	Sub-type	Number of Organizations
Private Company	Listed company (1,832)	59
	Unlisted company	16
	NGO	3
Private Company Sub-total		78
Public Agency	Public corporation (30)	15
	Para-governmental agency (87)	14
	Other public agency (178)	3
	Local government & Other agencies	4
Public Agency Sub-total		36
Total		114

4) Sustainability Reporting Frequency

In Korea 92 companies have released sustainability reports on a yearly basis (80.7%), with 10 produced bi-annually (8.8%), and 2 companies tri-annually (1.8%). Moreover, 3 companies, including CJ Cheiljedang, reported on their sustainability performance on an irregular basis, and 7 companies that published sustainability reports for the first time in 2013 did not report on their reporting frequency.

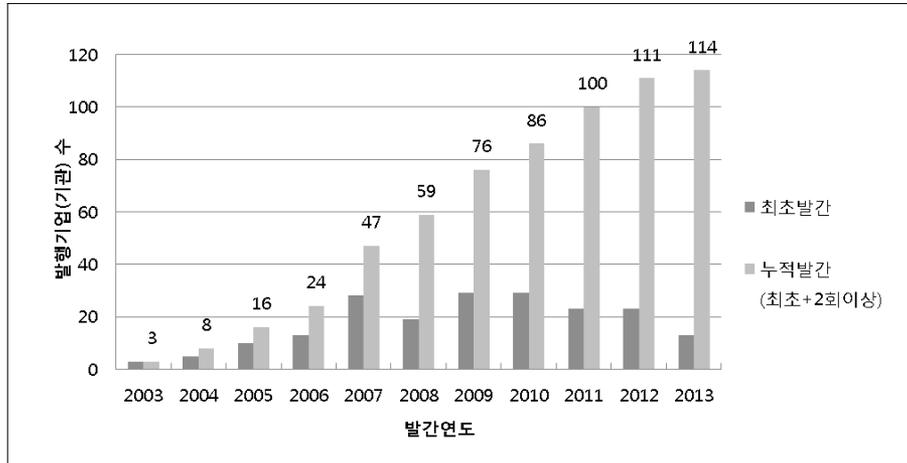
5) Sustainability Reporting Trend

During the decade from 2003 to 2013, a total of 195 organizations released sustainability reports at least once, with a total of 644 reports being published to date. There are a number of key characteristics to consider when considering the sustainability reporting trend in Korea.

First, compared to the relatively low level of awareness on sustainability management, the release of relevant reports has rapidly expanded. According to reporting statistics based on the publication year of 2013, a total of 114 companies produced sustainability reports, which is a 38-fold increase compared that in 2003. However, the number of companies newly releasing reports has continued to decrease from 2010

Sustainability Reporting Trend in Korea

Image 1: Sustainability Reporting Implementation Trend among Companies (Agencies) in Korea



*발행기업(기관)수: No. of Publication Company (Agency); 발간연도: Publication Year.
 최초발간: Initial Publication; 누적발간: Accumulated Publication (initial +twice or more)

Image 1 indicates that between 2007 and 2009, the number of companies releasing sustainability reports for the first time slightly increased. In the mid- to late-2000s, as the Johannesburg Stock Exchange (JSE) first published the Socially Responsible Investment (SRI) index and the GRI G3 guidelines were released, the global movement rapidly shifted towards sustainability management. Likewise, in Korea, the Roh Moo-Hyun administration established an institutional framework on sustainable development and promulgated the “Framework Act on Sustainable Development (2007),” which aims to achieve balanced economic growth, social integration, and environmental preservation, requiring evaluation of sustainability and then drafting and disclosing sustainability reports via the central government and local governments every two years. All of these efforts have had a great impact on the overall trend of sustainability reporting in Korea. Following this trend, in 2009, the government amended the Industrial Development Act, encouraging businesses to voluntarily adopt sustainability management practices, including measures for setting global standards and norms for sustainability management, for enhancing industrial competitiveness through sustainability management, and for building and expanding the base for voluntary sustainability management by businesses, thereby drawing companies’ interest in sustainability business practices.

Table 6: Chronology of Sustainability Reporting

Year	Key Event	Remarks
1976	OECD issues the world's first guidelines on global corporate citizenship	Global
1987	The World Commission on Environment and Development (WCED) releases definition of "Sustainable Development" in its "Our Common Future"	Global
1992	Establishment of the United Nations Conference on Sustainable Development (UNCSD) during the Rio Summit	Global
1995	<i>POSCO: First Korean company to produce an environmental report</i>	<i>Domestic</i>
1997	US environmental group Ceres and United Nations Environment Program (UNEP) partner to establish the Global Reporting Initiative (GRI)	Global
2000	GRI released sustainability reporting guidelines	Global
2000	Kofi Annan UN Secretary General created the UN Global Compact (UNGC)	Global
2000	Establishment of non-profit organization the Carbon Disclosure Project (CDP) headquartered in the U.K.	Global
2000	<i>Kim Dae-Jung administration established the Presidential Advisory Group "Commission on Sustainable Development"</i>	<i>Domestic</i>
2001	France enacted the Nouvelles Regulations Economiques Act (NRS Act), legally binding CRS implementation for the first time in Europe	Global
2002	<i>Ministry of Environment established "Environmental Reporting Guidelines"</i>	<i>Domestic</i>
2003	<i>Samsung SDI: first in Korea to issue a Sustainability Report</i>	<i>Domestic</i>
2003	Accountability based in U.K. published assurance standard AA1000	Global
2004	Johannesburg Stock Exchange (JSE): First to issue a Socially Responsible Investment (SRI) Index	Global
2005	<i>Ministry of Trade and Commerce issues Korean Sustainability Management Reporting Guideline BSR guideline (B.E.S.T sustainability Reporting Guidelines)</i>	<i>Domestic</i>
2006	Publication of GRI G3 guidelines	Global
2006	International Finance Corporation (IFC) issues "Policy and Performance Standards on Social and Environmental Sustainability"	Global
2007	<i>Rob Moo-Hyun Administration enacted a "Framework Act on Sustainable Development"</i>	<i>Domestic</i>
2009	<i>Industrial Development Act defined sustainable industrial development as a major goal and amends provisions regarding sustainability management practice</i>	<i>Domestic</i>
2009	<i>Lee Myung-Bak administration enacted a "Framework Act on Low Carbon, Green Growth" and established a Presidential advisory group "Presidential Committee on Green Growth"</i>	<i>Domestic</i>
2010	International Organization for Standardization (ISO) issues corporate social responsibility management standard ISO 26000	Global
2011	Prof. Michael Porter and Mark Kramer presented the concept of "Creating Shared Value" through Harvard Business Review	Global
2012	<i>Released guidance on social responsibility KS A ISO 26000:2012</i>	<i>Domestic</i>
2012	<i>Korea Environmental Industry & Technology Institute (KEITI) published Green Management Reporting Manual</i>	<i>Domestic</i>
2013	Publication of GRI G4 guidelines	Global
2013	IIRC unveiled Framework on Integrated Reporting	Global

Sustainability Reporting Trend in Korea

Second, large corporations having huge capital are taking the lead in implementing sustainability reporting. Among those released in 2013, 59 reports were by listed companies (3.2%), showing a very low level of publication rate. In contrast, among the top 30 listed companies designated by the Korea Fair Trade Commission, 23 produced sustainability reports, showing the highest percentage of sustainability reporting, and that large corporations dealing with multiple stakeholders such as investors, management and staffs, partners, and consumers tend to use their sustainability reports to accommodate the needs and requirements of internal /external stakeholders in their business practice and facilitate communication.⁶

Table 7: Implementation of Sustainability Reporting by Korea's Top 30 Companies

Ranking	Company Name	Reporting	Ranking	Company Name	Reporting
1	Samsung	O	16	LS	O
2	Hyundai Kia Motors	O	17	Dongbu	O
3	SK	O	18	Kumho Asiana	O
4	LG	O	19	Daewoo Shipbuilding & Marine Engineering	O
5	Lotte	O	20	Daelim	O
6	POSCO	O	21	Hyundai	O
7	Hyundai Heavy Industries	X	22	Boo Young	X
8	GS	O	23	S-Oil	O
9	Hanjin	O	24	OCI	O
10	Han	O	25	Hyundai Department Store	X
11	KT	O	26	Hyosung	O
12	Doosan	O	27	Daewoo E&C	O
13	STX	O	28	GM Korea	X
14	CJ	O	29	Dongguk Steel	X
15	Shinsegae	X	30	Youngpoong	X

* includes reporting by affiliates

⁶ The Korea Fair Trade Commission annually issues a list of Korea's Top 30 Large-scale Companies, excluding non-privatized public corporations.

Third, sustainability reporting by public agencies also accounted for a large share (32%), mainly for the purpose of responding to business performance evaluation and public relations (PR) in order to promote their organizations. In April 2007, with the implementation of the “Act on the Management of Public Agencies,” all data relevant to business performance and the operations of Korean public agencies subject to business performance evaluations were disclosed in the “Public Agency Management Disclosure System (ALIO).” Moreover, pursuant to Article 48 of the Act, public corporations and para-governmental agencies shall be evaluated on their business performance.⁷ Since the government reviews and utilizes business evaluation data during budget allocation for public agencies including incentive payment, relevant agencies are investing much labor and time to obtain high scores in their business performance evaluation. Ra Young-Jae et al. (2010), in a study on the use of sustainability reports for public agency performance evaluations has revealed that the sustainability report publication agency for public agencies or UN Global Compact member agencies can be correlated with business performance evaluations by the government, confirming that sustainability indicators and business performance indicators are correlated, making it statistically likely that detailed indicators impact each other. The study thus supports the idea that public agencies are implementing sustainability reporting as a way to receive good scores for their business performance. Moreover, as is the case with private companies, public agencies distribute their reports to multiple stakeholders or disclose them on their websites in order to promote their organizations and use them as agency presentation materials when seeking a global presence.⁸

⁷ Business performance evaluation has become a key management and evaluation method by the government over the past 3 decades, motivating public agency CEOs to improve their business efficiency and instilling in agency members a sense of responsibility and motivation to attain their goals (Korean Association for Policy Sciences, 2010).

⁸ Korea Electrical Power Corporation uses its sustainability as a means to promote its organization for IR activities and develop overseas businesses, with agencies such as the Korea Resources Corporation, Korea Airport Corporation, KEPSCO Plant Service & Engineering, Korea Hydro & Nuclear Power, Korea Minting, Security Printing & ID Card Operating Corp. also utilizing their sustainability reports as annex materials for overseas sales, PR, and marketing (Ra Young-Jae et al., 2010).

4. Readers' Feedback on Sustainability Reports

Every year, the Korea Standards Association conducts a study on the “Usage & Attitude of Sustainability Reports” and presents the Korean Readers' Choice Awards (KRCA) with the goal to examine the current use of sustainability reports in Korea and to look at future prospects. KRCA are given to the top report as selected on-line by readers of sustainability reports of Korean companies, and aims to enhance the quality of sustainability reporting by Korean firms by incorporating the study. Subsequent feedback from the multiple stakeholders on business agendas encourages firms not to draft a mere promotional report but a user-oriented report that discloses their practical sustainability performance.⁹

This section, based on findings of the “Korea Standards Association Report on Usage and Attitude of Sustainability Reports in 2013,” focuses on the diverse feedback obtained from Korean readers towards sustainability reports.

1) Target and Methodology

For the “Study on the Usage and Attitude of Sustainability Reports in 2013,” the Korea Standards Association conducted a survey of different stakeholders and experts who have read sustainability reports by Korean firms for a nearly 1 month period from July 22 to August 23, 2013. A group of 2,505 readers and users of sustainability reports took part in the on-line survey, and a group of 57 experts took part via e-mail. As a result, a total of 2,562 samples were obtained for this study. The study was conducted separately for readers and non-readers of sustainability reports, and the questionnaire was comprised of 13 questions.

⁹ Korean Sustainability Conference 2014 website (http://ksi.or.kr/ksi/contents/intro_krca.asp)

Image 2: Survey Questionnaire on Usage and Attitude of Reports in 2013

- Why do you read sustainability management reports?
- Why don't you read sustainability management reports?
- Source of sustainability information (excluding reports).
- Condition for changing attitude toward reports.
- Level of agreement regarding reports.
- How to effectively demonstrate stakeholder engagement?
- Considerations for future stakeholder engagement.
- Key elements of a successful report.
- Frequently omitted items in reports.
- Key elements showing commitment to sustainability management.
- Items required for assurance.
- Sustainability reporting assurance providers.
- Sustainability performance assurance providers.

Sections (2) to (11) will elaborate on the responses provided to 10 out of the 14 questions.

2) Why Do You Read Sustainability Reports?

75.61% of respondents said they read sustainability reports “to improve their overall understanding of the relevant company,” which achieved higher ratios than 2011 (74.8%) or 2012 (71.7%). Other key responses included “to learn about the performance of the relevant company (53.26%)” and “to seek information on the relevant market (43.58%).”

Sustainability Reporting Trend in Korea

Response	2011 (n=294)	2012 (n=703)	2013 (n=537)
To obtain an overall understanding of the relevant company	74.8	71.1	75.61
To deeply understand issues that are exclusive to the relevant company	52	36.8	38.73
To establish the accountability of the relevant company	26.3	14.5	15.64
To learn about the performance of the relevant company	60.9	48.7	53.26
To seek information on the relevant market	51	39.3	43.58
To benchmark the relevant company	42.5	27.1	32.03
For education/research purposes	24.8	14.2	15.46
For public use (journalist, PR specialist)	20.4	7.1	8.75
To use the report as primary data for making decisions on the relevant company	20.8	12.9	16.2
Others	1	0.4	0.19

3) Why Don't You Read Sustainability Reports?

When asked the reason for not reading sustainability reports, the largest number of respondents said because they “do not know the value of sustainability reports (29.05%).” Others replied that they “lack time to search information (28.04%),” followed by “because there is no information that is relevant to them (27.36%).”

Response	2011 (n=283)	2012 (n=590)	2013 (n=296)
There is not much information in the report that is relevant to me	39.2	34.6	27.36
I have other ways to examine sustainability performance of companies or agencies	10.6	9.49	8.45
Because it is difficult to have credibility in the information contained in the sustainability report	19.4	7.8	10.81
Sustainability report fails to fully satisfy my curiosity	19.4	15.1	14.19
Sustainability report does not impact my decision-making regarding relevant company or agency	15.2	18.5	14.19
I don't know in which context sustainability report is valuable	42.1	27.6	29.05
I do not have time to search information on complicated websites or read long reports	37.8	25.7	28.04
Company or agency I am interested in does not seem committed to sustainability management	16.3	5.1	4.39
Because I do not know how to use the information contained in sustainability report for my decision-making	29.3	22.9	26.69
Others	8.8	3.9	5.74

4) Source of Sustainability Information (excluding reports)

The majority of respondents obtained information on the corporate sustainability management (excluding reports) “generally from the mass media (58.14%),” which was followed by “directly contacting the relevant company and agency (37.21%).”

Response	2011 (n=54)	2012 (n=80)	2013 (n=43)
Possible to directly contact relevant company/agency	44.4	33.7	37.21
Seek information through individuals or groups involved with relevant company/agency	22.2	18.8	20.93
Utilize benchmarking reports or diverse materials from credit assessment bodies, sustainability management evaluation bodies, etc.	42.5	31.2	25.58
Usually from mass media	85.1	50	58.14
Others	5.56	3.7	4.65

Sustainability Reporting Trend in Korea

5) Conditions for Changing Attitude Towards Reports

When non-readers were asked about conditions for changing their attitude towards sustainability reports, 38.51% replied that they would change their attitude “when the disclosure and communication on sustainability performance is improved.” The answers also included “identification of the interests of diverse stakeholders (36.82%),” followed by “increased link between corporate strategy and performance reports (36.15%).”

Response	2011 (n=283)	2012 (n=590)	2013 (n=296)
Reinforced disclosure and communication of sustainability performance	44.17	44.58	38.51
Increased link between corporate strategy and sustainability performance within sustainability reports	45.23	34.58	36.15
Clear evidence that responding to sustainability issues means contributing to business performance	27.92	25.25	27.03
Increased engagement to identify the needs of diverse stakeholders including myself	42.4	40	36.82
Expanded worldwide education on the existence of sustainability reports and their value	34.63	22.88	29.73
Improved quality to enhance the credibility of sustainability reports	32.51	23.73	25.34
Independent assurance to enhance the credibility of sustainability reports	27.56	14.24	17.23
Others	1.01	0.85	1.41

6) How to Effectively Demonstrate Stakeholder Engagement?

The best way to show stakeholder engagement is through “designation of key stakeholders and a presentation of the involvement process,” which topped list for three consecutive years from 2011 (66.83%), followed by a “demonstration of the correlation between stakeholder engagement and identified issues (53.9%).”

Response	2011 (n=251)	2012 (n=503)	2103 (n=410)
Designate key stakeholder and present engagement process	70.5	62	66.83
Include key results of stakeholder engagement	56.5	49.1	44.88
Show link between stakeholder engagement and identified issues	60.1	47.7	53.90
Show link between stakeholder engagement and strategy, and goal-setting	57.7	48.1	49.27
Include 'Feedback Card' or e-mail addresses in reports	44.2	29.6	33.17
Include detailed feedback of key stakeholders in reports	19.5	8.3	11.46
Others	-	-	0.24

7) Considerations for Future Stakeholder Engagement

As the most important considerations for future stakeholder engagement, readers indicated “improving relations by minimizing conflicts and risks (61.64%) and “recognizing the impact on stakeholders (58.29%)” as key factors.

Response	2011 (n=294)	2012 (n=703)	2013 (n=537)
Improve relations by minimizing conflicts and risks	64.9	59.3	61.64
Identify new issues that can impact business	62.5	53.2	51.02
Recognize company's impact on stakeholders	64.9	54.6	58.29
Provide solutions to address dilemmas	42.1	26.8	33.52
Choose sustainability report content that reflects stakeholder interests	23.4	10.1	9.87
Others	-	0.1	-

8) Key Elements of a Successful Report

Sustainability report users chose “commitment of company/agency” as the most important element to be included in sustainability reports (83.8%), ranking

Sustainability Reporting Trend in Korea

number one for two consecutive years from 2012, followed by “alignment with the overall strategy (70.95%)” and “concrete performance indicator (64.8%).”

Response	2013
Company/agency's commitment to sustainability	83.8
Include alignment methodology between overall strategy and sustainability management strategy	70.95
Concrete performance indicator	64.80
Strategy and agenda setting	63.87
Goal and KPI setting	61.64
Include risk and opportunity factors of relevant company agency	61.45
Practical tips for implementing sustainability management by relevant company /agency	59.78
Case analysis and best practice	57.73
Innovative thinking	57.36
Role of leadership	56.80
Activities of company/agency to address sustainability management issues	56.61
Process & methodology for selection and evaluation of important issues	55.49
Include performance company/agency	54.75
Analysis of market trend and developments	54.56
Impact on external factors regarding sustainability of company/agency	51.58
Deep listening and consideration of stakeholder feedback	48.79
Include dilemma and concerns of company/agency	45.44
Include procedure and process for controlling sustainability management	43.39
Worst practice	42.64
Link with annual financial report	38.36
All items above	17.88
Others	0.37

9) Key Elements for Showing Commitment to Sustainability Management

Sustainability report users replied that in order for companies/agencies to show full commitment to implementing sustainability management, “disclosure of corporate performance data” was the most important, with the highest percentage of 47.01% or responses, followed by “thorough stakeholder engagement process (42.72%)” and “role of leadership (38.81%).”

Response	2011 (n=294)	2012 (n=703)	2013 (n=536)
Thorough stakeholder engagement process	57.5	44.1	42.72
Disclosure of corporate performance information	53.4	39.1	47.01
Role of leadership	48.6	40.1	38.81
Full disclosure of data that is of advantage and disadvantage to company, agency	47.3	29.1	34.14
Extensive scope of theme and data in sustainability report	29.6	13.3	13.43
Alignment with enterprise-wide business strategy	44.9	36.1	36.75
Disclosure of improvement items of company, agency	41.8	28.4	33.58
Disclosure of important sustainability issues mentioned	43.9	25.3	32.65
External assurance of data contained in report	40.1	19.7	25.19
Disclosure of the details of the goals and related action /implementation plan	21.1	15	20.15
Others	-	0.4	0.19

10) Items Requiring Assurance

In order to enhance the credibility of sustainability reporting in 2013, when asked which items required assurance during reporting, the largest number of respondents answered that both items “related to sustainability reporting by company, agency” and “related to sustainability performance by company/agency” were required (42.64%). Between the two items of “report” and “performance,” respondents indicated that assurance of “sustainability performance” was preferred (27.93%).

Sustainability Reporting Trend in Korea

Response	2011 (n=294)	2012 (n=703)	2013 (n=537)
Related to Sustainability Reporting by company/agency	20.4	17.6	16.2
Related to Sustainability Performance by company/agency	21.8	30.5	27.93
Both items above needed	49.7	38.6	42.64
Both items above not needed	2.00	3.00	4.28
No comment	6.1	10.1	8.94

11) Report Assurance Providers

When asked who should provide sustainability report assurance, respondents preferred “Specialized Assurance Agency (59.42%)” for three consecutive years from 2011, followed by an “expert (43.83%)” and “head of a multiple-stakeholder group (32.4%).”

Response	2011 (n=205)	2012 (n=384)	2013 (n=308)
Expert	52.8	45.3	43.83
Specialized assurance agency	65.6	48.9	59.42
Head of multiple-stakeholder group	43.1	37.2	32.4
Internal audit team of company, agency	25.1	7.2	8.12
Others	0.5	0.5	0.3

5. Conclusion and Implications

With stakeholders’ growing interest in corporate sustainability management, the sustainability reporting requirements in countries like Denmark, India, Singapore, and the U.S. have increased, leading to a greater number of sustainability reports being produced each year. Concurrent with this global trend, sustainability reporting in Korea is expected to further accelerate. For example, Park Geun-Hye administration, newly established in 2013,

highlighted economic democracy, and called for stronger social responsibility from businesses. And in April 2014, the “other public agency” category – which had long been excluded from business performance evaluations – was included in the evaluation; it is expected to add momentum to sustainability reporting after its slight slowdown since 2012.

Reporting on sustainability performance by businesses is a crucial activity, as it means that the relevant organization is not merely seeking financial benefits but also working to understand its future direction by identifying organizational issues from a sustainability context. Moreover, the trend for organizations to voluntarily build a governance system for sustainability management, establish and implement mid-term goals, and utilize guidelines and assurance norms aligning with global standards to enhance credibility of the report, seems to be an appropriate way to move forward.

However, it is difficult to ascertain whether the level of an organization’s sustainability is growing at the same pace as the increase in sustainability reporting. There are also organizations that view sustainability reports as a once-a-year task to get over with or as a promotional brochure. Numerous companies have failed to internalize sustainability management deep within their organizations, as evidenced by organizations that issue sustainability reports to obtain good business performance evaluations, have disparate sustainability management and company-wide strategies, and intentionally omit negative performances and issues in their reports.

Readers in Korea want to know whether the sustainability reports they read include “company/agency’s commitment to sustainability management” and a “practical system and solutions to enhance the economic/environment/social values of businesses by “aligning enterprise-wide strategies with sustainability management strategies.” Therefore, it is asked of Korean companies and public agencies to practice more mature sustainability management, one that befits Korea’s economic standing as the world’s 15th largest GDP, having achieved US\$1 trillion in trade for three consecutive years.

Sustainability Reporting Trend in Korea

References

Korea Standards Association (2013), Current Status on Sustainability Report Publication in 2013

Korea Standards Association (2013), Usage & Attitude of Sustainability Reports in 2013

Korea Economic Research Institute (2013), Statistical Analysis of Korea's Top 30 Companies in 2013

Korean Association For Policy Sciences (2010), Feasibility Analysis and Improvement of Business Performance Evaluation of Public Agencies

Ra Young-Jae, Yoon Tae-Beom (2010), Accomplishments and Limitations of Sustainability Management by Public Agencies, Korea Institute of Public Finance

KPMG International (2013), The KPMG Survey of Corporate Responsibility Report 2013

CorporateRegister.com (2013), CR Perspectives 2013: Global CR Reporting Trend and Stakeholder Views

Measures for Improving the Corporate Governance of Listed Companies in Korea¹

*Jeong Jae-Kyun
Yang Chun-Seung*

I . Introduction

In Korea, considerable public and private efforts have been made to improve the corporate governance of listed companies, especially since the financial crisis in 1997, and as a result many practical improvements have been implemented². Nevertheless, both internal and external criticisms persist, casting doubt on the degree of corporate governance practiced by Korean listed companies³. This uncertainty is attributable to the fact that corporate governance cannot be improved in a short period of time, and that changes should consider the diverse political, economic, and social contexts that are specific to Korea.

This paper focuses on the evaluations of the corporate governance of listed companies, which is one of the annual ESG evaluations carried out by the Korea Corporate Governance Service in order to identify the level of corporate governance practiced by listed companies in Korea. Furthermore, the paper will look at the current corporate governance practice by listed companies in

¹ This paper is revisited, complemented, and reorganized based on the paper entitled “Corporate Governance of Listed Companies” published in Volume 5 No. 2 (2013.12) of the *Yonsei Global Business Law Review* (YGBL) of the Yonsei University Global Business and Legal Center.

² Since 1998, the government has continued to reform the Commercial Code, Securities and Exchange Act, Act on External Audit of Stock Companies to introduce various schemes attempting to improve the corporate governance of many companies: systems for cumulative voting, written ballots, outside directors, auditing committees, etc. The 2004 OECD research on the corporate governance of member countries also includes Korea’s remarkable progress in terms of institutional framework in this field. “OECD, Corporate Governance — see “A SURVEY OF OECD COUNTRIES” (2004).

³ For example, according to the CLSA/ACGA joint study on corporate governance in Asian countries in 2012, Korea ranked 8th among 11 countries, even lagging behind Thailand, Malaysia, and India. See CG Watch 2012”, Asia Corporate Governance Association.

Measures for Improving the Corporate Governance of Listed Companies in Korea

Korea, with the idea that the right prescription for changes can only be made based on an accurate review of the current situation. From this diagnosis, the paper will then discuss the Commercial Code reform bill, which has been initiated from an institutional context in an attempt to improve the corporate governance of listed companies, with a particular focus on controversial issues surrounding the mandatory introduction of the cumulative voting and electronic voting systems, the separate election of directors serving on the Audit committee, and subsequently proposing recommendations for improvement. Finally, the paper will offer guidance on future directions in terms of how to achieve practical results in a Korean business environment regarding issues of enhancing the qualification requirements of directors and auditors, and the rationalization of shareholders' meetings.

II . Situation on Corporate Governance of Listed Companies in Korea

1. Evaluation of Governance of Listed Companies in Korea

In this section, we will briefly present the Korea Corporate Governance Service (KCGS), which conducts an annual ESG evaluation survey among listed companies in Korea, aiming to identify the level of governance practiced in these companies. Here, the E (Environment), S (Social), G (Governance) evaluation models and the evaluation process of KCGS will be also presented.

A. Overview of KCGS

The Korea Corporate Governance Service (KCGS) is a non-profit incorporated association that was established in June 2002 pursuant to Article 32 of the Civil Act, under the mandate to provide specialized services in terms of evaluation and research pertaining to corporate governance and the social responsibility practice of businesses. KCGS aims to conduct evaluations and research on corporate governance and corporate social responsibility (CSR) to then propose sustainable development measures for businesses, thereby contributing to the sound development of the capital market. Major activities include the evaluation of corporate governance and CSR of companies, research into corporate governance and CSR, identification and awarding of best practices for CSR, ranking of CSR (corporate governance, environmental, and social areas),

guidance on CSR and Sustainably Responsible Investment (SRI), elaboration of corporate CSR reports (sustainability report), guidance on voting rights exercised by institutional investors, and publication of CSR and SRI documents. To support KCGS, the Korea Exchange, Korea Financial Investment Association, Korea Listed Companies Association, and KOSDAQ Association are included as member organizations.

B. ESG Best Practices and ESG Evaluation Model Development of KCGS

Before the official establishment of KCGS, the Corporate Governance Reform Committee consisted of specialist groups from different sectors, which first began activities in their respective fields. This Committee, funded by the Korea Exchange, established “Corporate Governance Best Practices” in September 1999, which then served as a reference guide for listed companies in Korea for voluntarily improving their corporate governance, and helped them to implement sound corporate governance practices. In 2002, the Korea Corporate Governance Service (KCGS) was established by succeeding all the rights and roles of its predecessor.

Since its establishment, KCGS has been committed to developing evaluation models to assess the corporate governance of listed companies based on the Corporate Governance Best Practice guidelines, and has carried out annual evaluations. These evaluation models have evolved in line with the changing market and regulatory environment. The evaluation results from such evaluation models have then been utilized for policy development, new product development, index calculation, and academic research, and used as reference data for voluntary corporate improvement. Furthermore, the market also appreciates the values that such highly credible evaluations generate.

To the meet both the global trend of corporate social responsibility (CSR)⁴ and the diverse interests of the environment, consumers, and the local community, KCGS incorporated the Best Practice and Evaluation Model from the Environmental (E) and Social (S) areas into the corporate Governance (G)

⁴ On November 1, 2010, the International Standard Organization (ISO) officially published and confirmed ISO 26000 as the international standard for Corporate Social Responsibility (CSR), thereby drawing the attention of international organizations to CSR.

Measures for Improving the Corporate Governance of Listed Companies in Korea

evaluation model, thereby finalizing the “ESG Integrated Evaluation Model” in 2010. The development of such a best practice and integrated evaluation model first began in 2009, and from the outset, experts from environment and social areas were committed to perfecting the best practice and evaluation models by forming an advisory committee. The ESG Integrated Evaluation Model and Best Practices finalized by KCGS was expected to serve as a guide for the voluntary participation and improvement of CSR activities for businesses and as useful information on CSR management practice principles and norms for relevant stakeholders.

What is more, while developing the ESG Integrated Evaluation Model, KCGS tried to preserve the unique characteristics of each model while maintaining the consistency and the harmonization of evaluation methods and indicators within the integrated model. Therefore, the evaluation model used in this study to calculate the SRI score can be considered as a consistent, integrated evaluation model that harmonizes all ESG elements. Moreover, this corporate governance evaluation model is the only official governance evaluation model in Korea, and its findings have been deemed highly credible in the market over the past 10 years. Note that information on the model harmonization is available in the section on the evaluation model composition.

C. Characteristics and Uptake of ESG Evaluation Model of KCGS

The ESG Integrated Evaluation Model and Best Practices developed by KCGS apply global standards such as ISO26000, which will become the global norm for CSR. Moreover, a key characteristic of this model is that it is a Korean evaluation model that accommodates local needs by adapting the questionnaire to a Korea-specific business environment.

Currently, KCGS provides Governance (G) evaluation results to the Korea Corporate Governance Stock Price Index (KOGI) of the Korea Exchange, as well as the SRI Index and SRI Eco Index based on the new ESG Integrated Evaluation Model. Furthermore, these evaluation results facilitate the promotion of ESG activities in listed companies, awards and ranking of successful companies in corporate governance, ESG related studies, the development of new SRI-related products, and academic research and policy development for CSR and SRI development, among others.

D. ESG Evaluation Process at KCGS

In the first half of each year, KCGS researchers use data that includes disclosed business reports, sustainability reports, press information, government institutional data, and websites to directly evaluate the level of CSR activities led by businesses. Then, an auto-verification process takes place, and the results of the verification are uploaded to a website that was developed for this purpose. Before confirming the evaluation results, companies can look at the data, which is one of the greatest strengths of the KCGS evaluation in ensuring the fairness and credibility of the evaluation outcome, while encouraging corporate engagement. The corporate feedback process allows each company to confirm and print the questionnaires and results when needed, and also to provide detailed feedback for each question of the survey. The evaluation content can then be revised based on the feedback, thereby enabling a mutual consensus to be reached by both KCGS and companies regarding the evaluation results.

After the evaluation, results are confirmed and KCGS selects and awards successful companies for each ESG element, assigns a ranking, and provides basic data to calculate the KRX Index. The most important aspect of this process is that the analysis report is provided free-of-charge to all companies subject to the evaluation. This provision encourages companies to voluntarily improve their CSR activities, and furthermore to seek sound development of the capital market – which is in accord with the founding vision of KCGS. Moreover, all annual evaluations are stored and managed in a database to be used for academic research and policy development purposes in order to facilitate CSR and SRI practices.

E. Introduction to ESG Evaluation Model of KCGS

As corporate sustainable growth has become such an important buzzword in today's business sector, various evaluation models have emerged in attempts to identify sustainable companies and evaluate their sustainability. Evaluation models such as SAM, EIRIS, and MSCI (Riskmetrix Group merger) have been introduced to assess the sustainability level of Korean businesses. SAM and EIRIS evaluation results are respectively included in DJSI and FTSE4Good for evaluation, thus attracting considerable interest from Korean businesses.

Measures for Improving the Corporate Governance of Listed Companies in Korea

However, global evaluation models commonly fail to consider the corporate culture or regulatory environment specific to Korea, and hence have limitations for providing an accurate evaluation. In the SAM evaluation model, once the quantitative evaluation is performed for the economic, social, and environmental contexts, industry-specific characteristics are then considered. Therefore, it is only possible to evaluate the level within the industry group, and the industry classification is somehow inconsistent with the reality in Korea. Similarly, the EIRIS evaluation model focuses on the investment efforts of businesses regarding social responsibility in terms of environmental and social contexts, stakeholders, and human rights; thus, is designed to assist the decision making of investors. The MSCI evaluation model assesses the governance, human resources management, stakeholders, products, services, and environmental business practice. However, as it is designed to assess the intangible value of businesses, in the form of a qualitative evaluation, only a cross-industry comparison is possible.

The above evaluation models are generally used for a qualitative evaluation and take into account industry-specific characteristics, making it difficult to ensure the quantification of corporate sustainability and further assess the extent of sustainability covering all businesses. Moreover, the evaluation indicators that are commonly applied to global firms may include some that are not fully consistent with the Korean context, possibly creating a risk of under-evaluating the sustainability performance of Korean companies. As a result, KCGS has developed new evaluation models for the Environmental (E) and Social (S) contexts while combining the existing corporate Governance (G) evaluation model to finalize the “Korea-specific Model of Integrated ESG Evaluation.” This integrated model effectively accommodates all key characteristics of each model while maintaining the harmonization and consistency of model composition, evaluation indicators, and evaluation method. For example, the corporate governance evaluation model is Korea’s only governance evaluation model and has gained extensive credibility from the market during the past decade. The elements and the scores for each model are as indicated in the three tables below⁵.

⁵ Examples of corporate governance evaluation model, environmental evaluation model, and social evaluation model are based on the 2013 ESG evaluation models of Korea Corporate Governance Service.

Table 1: Environmental Evaluation Model of KCGS

Category (Number of Questions)	Subcategory	Score	Ratio
I. Environmental Strategy (7)	1. CEO Commitment	65	22%
I. Environmental Strategy (7)	2. Environmental Strategy and Policy	65	22%
II. Environmental Organization (7)	3. Environmental Organization Culture	35	12%
II. Environmental Organization (7)	4. Environmental Organization Structure	35	12%
III. Environmental Management (43)	5. Goal Setting & Planning	110	36%
III. Environmental Management (43)	6. Supply Chain Management	110	36%
III. Environmental Management (43)	7. Clean Production System	110	36%
III. Environmental Management (43)	8. Environmental Risk Management	110	36%
III. Environmental Management (43)	9. Environmental Accounting	110	36%
III. Environmental Management (43)	10. Environmental Performance Management	110	36%
III. Environmental Management (43)	11. Environmental Audit	110	36%
IV. Environmental Performance (28)	12. Resources	65	22%
IV. Environmental Performance (28)	13. Climate Change	65	22%
IV. Environmental Performance (28)	14. Environmental Laws & Regulations	65	22%
IV. Environmental Performance (28)	15. Green Product and Service	65	22%
V. Stakeholder Response (6)	16. Environmental Reporting	25	8%
V. Stakeholder Response(6)	17. Stakeholder Response Activity	25	8%
Total (91 questions)		300	100%

Measures for Improving the Corporate Governance of Listed Companies in Korea

Table 2: Social Evaluation Model of KCGS

Category (Number of Questions)	Subcategory	Score	Ratio
I. Employee (27)	1. Employment and Working Condition	140	47%
I. Employee (27)	2. Labor-Management Relations	140	47%
I. Employee (27)	3. Health and Safety at Work	140	47%
I. Employee (27)	4. Manpower Development & Assistance	140	47%
I. Employee (27)	5. Basic Rights at Work	140	47%
II. Partner and Competitor (17)	6. Fair Trade	64	21%
II. Partner and Competitor (17)	7. Anti-Corruption	64	21%
II. Partner and Competitor (17)	8. CSR Facilitation	64	21%
III. Consumer (14)	9. Fair Trade vis-a-vis Consumer	66	22%
III. Consumer (14)	10. Consumer Safety and Health	66	22%
III. Consumer (14)	11. Consumer Privacy Protection	66	22%
III. Consumer (14)	12. Communication with Consumer	66	22%
IV. Local Community (8)	13. Community Engagement and CSR	30	10%
IV. Local Community (8)	14. Economic Development of Community	30	10%
IV. Local Community (8)	15. Communication with Local Community	30	10%
Total (66 questions)		300	100%

Table 3: Corporate Governance Evaluation Model of KCGS

Category (Number of Questions)	Subcategory	Score	Ratio
I. Shareholder Protection (29)	1. Protection and Exercise of Shareholder Rights	90	30%
I. Shareholder Protection (29)	2. Ownership	90	30%
I. Shareholder Protection (29)	3. Dealing with Affiliated Persons	90	30%
II. Board of Directors (25)	4. Composition of Board of Directors	80	27%
II. Board of Directors (25)	5. Operation, Evaluation and Compensation of Board of Directors	80	27%
III. Disclosure: Business Transparency (27)	6. Disclosure-General	70	23%
III. Disclosure Business Transparency (27)	7. Disclosure-Website	70	23%
IV. Audit Body (13)		50	17%
V. Distribution of Profit (3)		10	3%
Total (97 questions)		300	100%

As indicated in Table 1, the environmental evaluation model consists of 5 categories and 17 subcategories, including a total of 91 evaluation indicators, for a total score of 300. The social evaluation model, as seen in Table 2, consists of 4 categories and 15 subcategories, including a total of 66 evaluation indicators, for a total score of 300. The governance evaluation model shown in Table 3 is a well-known model, and has been in the market for the past 10 years; it consists of 5 categories and 9 subcategories, including a total of 97 evaluation indicators, for a total score of 300.

The following section will present highlights of the 2013 results of the evaluation that was conducted among listed companies, which will serve as an important precondition to draw measures for improving corporate governance.

Measures for Improving the Corporate Governance of Listed Companies in Korea

2. Governance Evaluation Result of Listed Companies in Korea in 2013⁶

The 2013 corporate governance evaluation conducted by the Korea Corporate Governance Service included 693 companies listed on the KOSPI Market and 908 companies listed on the KOSDAQ Market. The 2012 evaluation was conducted among 710 KOSPI-listed companies and 890 KOSDAQ-listed companies. The evaluation outcomes below are based on the evaluation analysis⁷.

A. Current Status by Market

The average governance score of the KOSPI Market was 35.44 out of 100, similar to that of 2012 (35.43), and the average KOSDAQ governance score was 30.57, which is very low compared to KOSPI. This is probably because 215 venture firms, which are not subject to regulations that should be applied to companies with over a certain asset size, are included. However, the highest score for the KOSPI Market and the KOSDAQ Market were 74.67 and, 60.00 respectively, and KOSPI saw a 2.66-point drop compared to the previous year, whereas KOSDAQ saw a slight increase. In particular, the highest score for KOSDAQ was slightly higher than 2012, but still showed big gap compared to the KOSPI's highest score, leaving much room for improvement.

Table 4: Corporate Governance Evaluation Scores by Market

Category	KOSPI Market		KOSDAQ Market	
	2012	2013	2012	2013
Shareholder Protection	53.74 (78.89)	53.77 (75.56)	55.41 (78.89)	53.97 (75.56)
Board of Directors	19.01 (76.25)	19.72 (83.75)	13.37 (53.75)	13.38 (53.75)
Disclosure	24.99 (77.14)	24.40 (74.29)	19.33 (55.71)	20.31 (61.43)
Audit Body	47.59 (100.00)	47.96 (92.00)	33.68 (82.00)	34.72 (82.00)
Distribution of Profits	24.51 (100.00)	23.70 (100.00)	15.82 (90.00)	14.90 (100.00)
Total Score	35.43 (77.33)	35.44 (74.67)	30.78 (59.67)	30.57 (60.00)

※ () denotes highest possible score

⁶ Governance evaluation results of listed companies in Korea seen below are based on the internal analysis data of the Korea Corporate Governance Service and are not yet disclosed through any publication.

⁷ For the analysis of the 2011 evaluation findings, refer to Oh Duk-Gyo, "Governance Status of the KOSPI Market and KOSDAQ Market", Corporate Governance Review, vol. 59, Korea Corporate Governance Service, 2011. Reference.

Both markets show relatively higher scores in terms of “Shareholder Protection” and “Audit Body” compared to other sections. This difference is because “Shareholder Protection”, contrary to the other sections, has numerous questions asking for the existence of an institutional framework or system in violation of shareholder rights, and if such an instrumental framework or system does not exist, additional points were given. The “Audit Institution” section has many questions pertaining to internal control systems, and since the regulatory environment surrounding internal controls has recently become more stringent, higher scores were given based on the degree of conformity with regulations.

As for the “Board of Directors” and “Disclosure”, average scores were low but the highest scores were high, which indicates that only few companies were actively involved in relevant activities. The “Board of Directors” section evaluates both systems and activities, and “Disclosure” evaluates mostly activities; therefore, low scores in both areas imply a lack of activity taking place in relevant areas. As for the average score by section in each market, the KOSPI Market showed higher scores in all section, except for “Shareholder Protection,” compared to KOSDAQ. The average KOSDAQ score was 0.2 higher than KOSPI, which is a large decrease from the 1.67 gap from the previous year, and this is probably because KOSDAQ-listed companies have fewer affiliates and a simpler equity composition, whereas KOSPI-listed companies have a greater number of affiliates with intricately linked ownership structures.

B. Current Status by Asset Size⁸

By dividing the groups into business groups having assets worth at least KRW 2 trillion, and those with under KRW 2 trillion, it was possible to distinguish the level of governance improvement through regulatory means or through voluntary commitment. Major governance-related regulations under the Commercial Code are applied to listed companies having a total asset worth at

⁸ Companies were divided into an asset size of “at least KRW 2 trillion” and “under KRW 2 trillion” as of the ends of 2011 and 2012. The number of companies having at least KRW 2 trillion increased by 1 from 143 in 2012 to 144 in 2013, and those having under KRW 2 trillion decreased from 567 in 2012 to 549 in 2013.

Measures for Improving the Corporate Governance of Listed Companies in Korea

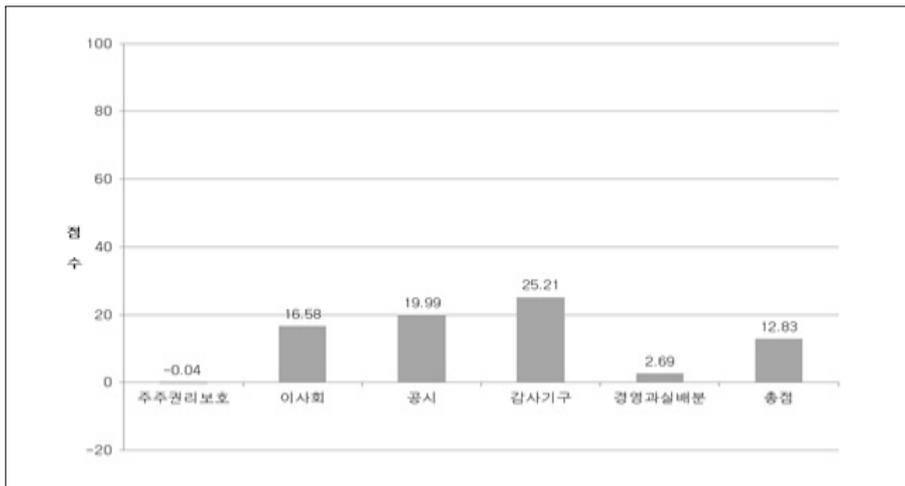
least 2 trillion won as end of the previous fiscal year. The average governance score for KOSPI-listed companies with at least 2 trillion won (45.62) was much higher than those under 2 trillion won (32.79), and in 2013, the score gap between the two groups was 12.83, which was a slight decrease compared to 2012 (13.33). Both groups also showed a large score gap in areas such as “Board of Directors,” “Audit Body,” and “Disclosure.” Such differences can be explained by the fact that, in the areas of “Board of Directors” and “Audit Body” it is mandatory for listed companies to establish an outside director nomination and Audit committees and to elect outside directors whose number is not less than a majority of the total number of its directors.

Regarding “Disclosure,” it has been found that companies having assets of at least KRW 2 trillion provide a great deal of information regarding their corporate governance practices through their websites and are more active in disclosing IR information, financial result forecasts, and data in English.

Table 5: Comparison of Governance Scores by Asset Size (KOSPI Market)

Category	at least KRW 2 trillion		under KRW 2 trillion	
Category	2012	2013	2012	2013
Shareholder Protection	54.69	53.74	53.50	53.78
Board of Directors	31.19	32.88	15.94	16.30
Disclosure	40.14	40.26	21.17	20.27
Audit Body	67.36	67.97	42.61	42.76
Distribution of Profits	26.85	25.80	23.92	23.11
Total Score	46.08	45.62	32.75	32.79

Image 1: Score Difference in Governance Evaluation by Asset Size (KOSPI Market)



점수:score
 주주권리보호 (Shareholder Protection), 이사회 (Board of Directors), 공시 (Disclosure), 감사기구 (Audit Body),
 경영과실배분 (Distribution of Profits), 총점 (Total Score).

C. Current Status by Business Group⁹

In 2012 and 2013, the governance scores for business groups having no leader was higher than those having a leader, with the former group showing higher scores in all areas except for “Shareholder Protection” and “Audit Body.” Both comparative groups had lower scores compared to 2012; however, as for the business group having no leader, the score dropped by 1.06 points, which is greater than for the “with leader group”(0.06 points). In “Shareholder Protection,” the average scores of both groups were lower than the KOSPI Market average (53.77), which means that regardless of whether a leader was present, large business groups displayed a higher percentage of investing in their affiliates and making frequent transactions with their affiliates.

⁹ Among 62 business groups subject to the limitations on mutual investment, announced by the Korea Fair Trade Commission in April 2013, 48 groups (excluding 21 public corporation groups and 3 business groups with no listed companies) as well as 243 listed companies under business group, were analyzed and in 2012, 48 out of 62 business groups (excluding 11 public corporations group and 3 business groups without listed companies) as well as 252 listed companies under business group were analyzed.

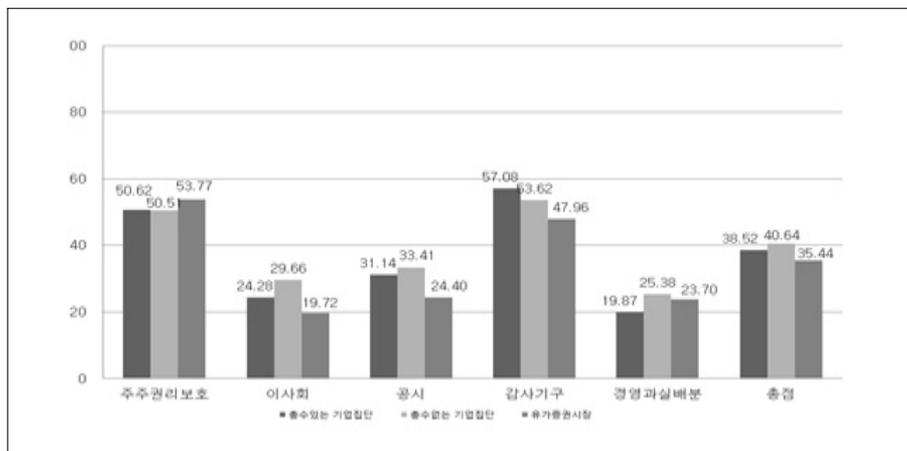
Measures for Improving the Corporate Governance of Listed Companies in Korea

The “without leader business group” received higher scores in “Board of Directors,” “Disclosure,” and “Distribution of Profits” compared to its counterpart, probably because a business group that has no leader has a more democratic decision making process than the autocratic management common by leaders’ families, ensuring a greater chance for a relatively fair distribution of profits.

Table 6: Governance Score Trend by Business Group

Category	Business Group w/ Leader		Business Group w/o Leader	
Category	2012	2013	2012	2013
Shareholder Protection	50.87	50.62	53.22	50.51
Board of Directors	23.07	24.28	28.88	29.66
Disclosure	31.35	31.14	34.86	33.41
Audit Body	56.49	57.08	55.30	53.62
Distribution of Profits	19.73	19.87	20.50	25.38
Total Score	38.58	38.52	41.70	40.64

Image 2: Comparison of Governance Scores by Business Groups in 2013



주주권리보호 (Shareholder Protection), 이사회 (Board of Directors), 공시 (Disclosure), 감사기구 (Audit Body), 경영과실배분 (Distribution of Profits), 총점 (Total Score), 총수있는기업집단 (Business Group with Leader), 총수없는 기업집단 (Business Group without Leader), 유가증권시장 (KOSPI).

D. Current Status of Major Issues¹⁰

(1) Written Ballot, Electronic Voting, and Cumulative Voting Systems

72 KOSPI-listed companies adopted a system for exercising voting rights by written ballot (10.39%), reflecting the lack of convenience for investors to exercise their voting rights. There were no (0%) of KOSPI-listed companies having introduced the system for exercising voting rights via electronic means, confirming a complete lack of adoption for electronic voting. Moreover, 662 companies (95.53%) were found to be undermining the exercise of minority shareholder rights by excluding cumulative voting for protecting minority shareholders from their by-laws. As such, written ballots, electronic voting and cumulative voting systems that were introduced to protect minority shareholders are bearing not much fruit.

Table 7: Status of Written Ballots, Electronic Voting, and Cumulative Voting Systems

Category	2012	2013
Implementation of Written Ballots	67 (9.44%)	72 (10.39%)
Implementation of Electronic Voting	0 (0%)	0 (0%)
Implementation of Cumulative Voting	41 (5.77%)	34 (4.91%)

(2) Exercise of Minority Shareholder Rights

The number of listed companies whose minority shareholder rights were exercised before the shareholders' meeting in 2013 were 17, representing 3 more companies than in 2012; however, the percentage of minority shareholder rights being exercised still remains low at 2.45%.

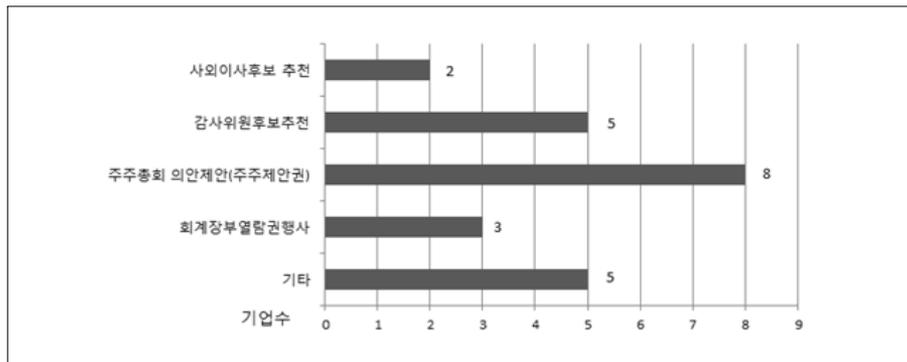
Table 8: Status of Exercise of Minority Shareholder Rights

Description	2012	2013
Exercise of Minority Shareholder Rights	14 (1.97%)	17 (2.45%)

¹⁰ The analysis below included 693 KOSPI-listed companies, 908 KOSDAQ-listed companies for 2013, 710 KOSPI-listed companies and 890 KOSDAQ-listed companies for 2012.

Measures for Improving the Corporate Governance of Listed Companies in Korea

Image 3: Status of Exercise of Minority Shareholder Rights by Type in 2013



사외이사후보추천 (Outside Director Nomination), 감사위원후보추천 (Audit Committee Member Nomination), 주주총회 의안제안 (주주제안권) (Shareholder Proposal Rights), 회계장부열람권행사 (Rights of Inspection of Books and Records), 기타 (Others), 기업수 (Number of Companies).

(3) Separation of CEO and Chairman of Board of Directors

It has been identified that 39 companies elect CEOs and the Board Chair separately, which is a 1/3 decrease from 61 in 2012, with 17 of these companies electing an outside director as the Board Chair. Most companies (94.37%) appointed their CEO as Board Chair, which undermines the independence of Board operations.

Table 9: Status of Separate Elections for CEO and Chairman of Board of Directors

Description	2012	2013
Separation of CEO and Chairman of Board of Directors (Outside Director serves as Board Chair)	61 (19)	39 (17)

(4) Establishment and Organization of Audit Committee

In 2013, a total of 254 companies have established an Audit committee, which is an increase of 18 companies compared to 2012. Among the companies having Audit committees, the number of companies subject to mandatory establishment increased by 14, whereas voluntary establishment increased by 4. The number of companies having established an Audit committee in 2013 increased as a whole, though the number of companies having elected a standing auditor decreased by 24 compared to 2012.

Table 10: Overview of Audit Bodies

Description	2012	2013
Standing Auditor	395	371
Establishment of Audit Body (mandatory establishment)	236 (127)	254 (141)

Among 254 companies having established an Audit committee, 221 companies (87.01%) elected one or more financial experts, and the average percentage of outside directors within the Audit committee is 91.04%, accounting for a higher percentage of outside directors compared to other Board committees.

Table 11: Organization of Audit Committees

Description	2012	2013
With at least one number of financial expert	210	221
Percentage of outside directors	90.93%	91.04%

3. Sub-conclusions

As such, the level of governance improvement among listed companies in Korea remains unsatisfactory, as revealed by the evaluation results, despite the multi-faceted efforts initiated by the government and capital market participants. Although some progress has been made, such as the introduction of institutional frameworks for improving corporate governance, many questions are being raised as to whether these measures are being implemented as originally intended. Moreover, despite the fact that an extensive list of disqualification criteria for outside directors has been defined, doubts regarding the independence of these appointed directors have been constantly expressed. There is also an issue of whether the mandatorily established Audit committees for listed companies having assets worth at least KRW 2 trillion are effectively performing their roles, compared to previous audit systems.

Moreover, major signs for corporate governance improvement, such as written ballot systems, electronic voting systems, and cumulative voting systems are either being introduced and implemented out of formality or are not being

Measures for Improving the Corporate Governance of Listed Companies in Korea

considered at all. Aware of such problems, the Korean government has proposed a progressive bill to reform the Commercial Code, aiming to improve corporate governance. However, at present, the future of this reform bill is in limbo, facing fierce opposition from the business sector.

Against this backdrop, the following section will provide some implications, issues and improvement proposals regarding the mandatory introduction of cumulative voting systems, electronic voting systems, and the separate election of directors serving on the Audit committee, which are particularly controversial issues regarding the pending Commercial Code reform bill. In addition, considerations and recommendations for strengthening qualifications of auditors and rationalization of shareholders' meetings will be presented, which are not at present included in the reform bill, and yet are potential areas of improvement.

III. Major Tasks for Improving Governance of Listed Companies in Korea

1. Partial Mandatory Adoption of Cumulative Voting System

A. Current Status

Cumulative voting was first introduced into the Commercial Code in 1998, with the aim to protect the rights of minority shareholders and to improve corporate governance following the financial crisis in 1997. The concept of cumulative voting originated in 1870, when it was first introduced in order to elect members of the House of Representatives in the State of Illinois, United States. The theoretical ground for cumulative voting is that it complements weaknesses of the current majority voting rule. For example, if a controlling shareholder with a 51% stake and another shareholder with a 49% stake exist, under the current election system, all directors are elected according to the preference of the controlling shareholder, such that the shareholder with the 49% stake cannot elect a director who can speak on their behalf in the Boards. In particular, in places like Korea, where the controlling shareholder not only monitors business activities but is also involved in the day-to-day operations and uses business resources for personal benefit, if the Board is dominated by the controlling shareholder, no measures can be taken by the other minority

shareholder to proposed a counter check and balance.

Yet, despite the introduction of the cumulative voting system, most listed companies in Korea fail to include this system in their by-laws, and such a trend is gaining momentum. Companies incorporating cumulative voting in their by-laws continue to decrease in number, proving that the cumulative voting system has *de facto* become a useless system¹¹. As a result, since July 2013, the Ministry of Justice announced its plan to legislate a partially mandatory introduction of cumulative voting as a means to protect not the majority but the minority shareholders and to monitor the activities of the majority shareholders and senior management. However, the amendment provision on cumulative voting, contrary to what had been announced during the 1st public hearing, reduces the scope of companies subject to this mandatory introduction from “all listed companies” to “listed companies with at least a certain asset size.”

B. Major Issues

First, opponents argue that the mandatory provision of cumulative voting in the Commercial Code violates the shareholder equality rule and majority rule in the stock company system, in which the rights are proportionately assigned based on the “one share one vote” principle¹². However, as mentioned above, the reason why “one share one vote” is believed to be rational is because without this system, the controlling shareholder can secure all managerial rights with minimum financial burden, thereby enabling an incompetent and immoral manager to secure or maintain managerial rights, which is quite problematic for the company. On the other hand, cumulative voting is a system designed to act in the interests of other shareholders, who can then add checks and balances to the business management leader when electing members of the Board. Indeed, in today’s corporate world, the role of supervising managerial practices is becoming all the more critical. In this regard, however, the objective of “one share one vote” system does not apply to cumulative voting. In most

¹¹ Among listed companies in Korea, the number of companies maintaining cumulative voting was 52 (90) in 2007, 52 (91) in 2008, 45 (47) in 2009, 40 (34) in 2010, 38 (31) in 2011, and 34 (27) in 2010 for the KOSPI (KOSDAQ) Market.

¹² Bae Sang-Geun, “Commercial Code Reform Public Hearing on Corporate Governance” discussion text, Ministry of Justice, 25 June 2013.

Measures for Improving the Corporate Governance of Listed Companies in Korea

Korean companies having an individual controlling shareholder, the controlling shareholder already enjoys excessive control of voting rights through friendly shares, including the equity of affiliates. It is therefore necessary to strengthen the voting rights of minority shareholders.

Another opposing argument is that parties likely to be interested in the election of corporate directors are not the minority shareholders but main shareholders, including institutional investors, pension funds, hedge funds. And since their financial goal is to primarily increase the return on investment, they are not likely to act in a direction that would ultimately maximize the profits of minority shareholders¹³. However, theoretically speaking, directors have a duty to ensure the care and loyalty of their companies; therefore, it is a very biased argument that directors elected via cumulative voting would ignore the interest of the overall company and act in a factional manner, oblivious to the important roles and responsibilities that they should assume as directors. The maximized return on investment sought by institutional investors such as pension fund and hedge fund managers can be realized by enhancing the values of the companies they invest in. Therefore, it is difficult to accept the argument that they can impose management policies that are disadvantageous to the corporate value or other minority shareholders¹⁴. For example, some argue that foreign investors can ask for a too large a share of the dividends, and may in fact “eat and run” after receiving their dividends. However, it should be noted that foreign investors can only exercise voting rights based on their equity and do not have the final say on the dividend payments. Therefore, any so-called “excessive” dividend payout is ultimately subject to decisions made at the shareholders’ meeting. In the case a dividend payment is truly deemed “excessive,” it will lead to a cash and investment fund shortage for the company in question. Since this in turn will have a negative impact on the company’s stock prices, which will not only undermine the interests of the foreign investors but also the overall shareholders, appropriate decisions will be made during the shareholders’ meeting.

¹³ Choi Jun-Sun, *supra* note 11, 8-9.

¹⁴ Park Gyeong-Suh, *supra* note 8, 35-36.

Others argue that directors elected by cumulative voting may raise questions regarding the individual profiteering and opportunistic behaviors of specific minority shareholders, thereby undermining the efficiency of the Board operations¹⁵. A counter-argument would be that the bigger problem is that the Boards in Korean companies currently fail to adequately implement checks and balances and promote an exchange of ideas, but rather rush to adopt company proposals without much questioning. Even though the cumulative voting system has been in place for the past 10 years and that 3-40 listed companies have adopted this system, outside directors have rarely been elected through this system. Thus, even with the mandatory adoption of the cumulative system going forward, only companies having at least 2 outside directors on the Board will be affected, and even if the outside directors are elected via this method, such cases will be limited and will only represent a small percentage of all Board members. As such, if the item presented to the Board were reasonable, even if one or two outside directors oppose, the motion would be adopted in the Board meeting with the help of numerous other logically thinking directors. The current situation is that absolute majority of listed companies, which are run by funds invested by many investors, are refusing to implement the cumulative voting system. And this shows how distorted the views of the current senior management and controlling shareholder are, who even tend to avoid directors that represent the opinion of the minority shareholders.

Some also argue that among 20 countries having a cumulative voting system in place (i.e., the U.S., Japan, Russia, and Taiwan), only a few (i.e., Russia, Mexico, and Chile) have legislated the mandatory implementation of cumulative voting systems. However, these few cases of mandatory legislation of cumulative voting do not serve as a supporting argument to oppose its mandatory introduction. All countries have a unique history, traditions, economic structure, different levels of social awareness, and organizational culture, resulting in diverse forms of governance. For example, Germany with its strong social-democratic traditions, unlike other advanced countries, has legislation mandating that

¹⁵ Ju Jin-Yeol, "Review of Issues Regarding Indirect Mandatory Introduction of Cumulative Voting System", Major Issues and Evaluation of Commercial Code Reform Bill (Korea Economic Law Association Summer Academic Symposium, 2013. 8), 105-107.

Measures for Improving the Corporate Governance of Listed Companies in Korea

labor representatives serve on the (audit) committee. And yet, no one argues that corporate governance in Germany lags behind or is over-regulated because it is a form of governance selected by reflecting the economic and social conditions specific to Germany. On the other hand, in Korea, the controlling shareholder tends to dominate the managerial rights in business management, more so than in any other advanced country, with some engendering social problems due to their illegal and unethical behaviors. According to evaluations conducted by international institutions such as CLSA/ACGA over the past 10 years, Korea has been one of the lowest ranking countries in terms of governance among 11 Asian countries, which is increasingly becoming worse. Given the fact that, in reality, improving the governance efforts by providing best practices has not been overly successful, it may be more appropriate to adopt a legal requirement for cumulative voting system as a measure to protect the property rights of minority shareholders. For example, during the post-1997 financial crisis, the governance level of Korean companies was greatly improved through the legislation of requiring an outside director.

C. Sub-conclusions

It is quite reasonable to expect that companies required to implement cumulative voting system will be limited to corrupt and underperforming companies whose corporate value has decreased or are under-evaluated because the Board directors have failed to fulfill their roles. An entity who nominates an additional candidate to conduct cumulative voting must bear a great deal of the financial and non-financial burden, with associated costs including searching for the right candidate, executing shareholder proposal for nomination, and securing voting rights through a proxy contest. Therefore, there have been few shareholder proposals for nominating directors to date, which suggests that the chances of abusing cumulative voting are not very high, nor is the concern voiced by its opponents¹⁶. There were 8 shareholder proposals among Korean listed companies in 2012 and 19 in 2013; only 6 companies submitted a shareholder proposal for vote in 2012, and 9 in 2013,

¹⁶ Among S&P 500 companies, there were 585 shareholder proposals during the shareholders' meeting of the first half of 2012, which increased to 612 in the first half of 2013.

which indicates a relatively large participation of outside shareholders in management compared to other developed countries.

Instead of expecting that it is not the controlling shareholders but the shareholders-elected directors that will act opportunistically through cumulative voting, it is more reasonable to expect that the latter would monitor the management. And even if minority shareholders and institutional investors argue about ideas that would pursue immediate gains and potentially undermine corporate competitiveness in the long run, such irrational arguments will be amply countered by the directors who are elected by other shareholders. In fact, in today's Boards, the more pressing problem is the practice of just sitting by and watching a certain majority shareholder solely seek personal benefits, which consist of directors nominated and elected by the majority shareholder and management. Therefore, directors being elected not by the majority shareholder but by other shareholders serving on the Board means there will be an increased diversity of the Board make-up, which in turn will lead to more diverse proposals for the Board to vote on, leading to active discussions and a reasonable decision-making process.

Another important consideration is that under the "staggered term system" that has been introduced by most listed companies in Korea, the cumulative voting system's effectiveness will be weakened, thus reducing problems regarding the partial mandatory introduction of the cumulative voting system. In general, the average term of a director in a Korean listed company is 3 years; however, if there are fewer than 3 directors serving on a Board, due to the staggered term system, it is difficult to submit a proposal for electing 2 or more outside directors. In order to strengthen the effectiveness of cumulative voting, it is necessary to abolish the staggered term system; however, since there is currently no motivation for companies to voluntarily abolish the staggered term system, relevant institutional complementarity is required.

The requirement for claiming the exercise of cumulative voting rights must be reduced from the current 1% (listed companies with at least KRW 2 trillion in assets, other companies 3%) to 0.5% (listed companies with at least KRW 2 trillion in assets, other companies 1%). Furthermore, the new provisional requirement on holding the position for 6 consecutive months is still a strict

Measures for Improving the Corporate Governance of Listed Companies in Korea

condition compared to other developed countries, and therefore needs to be further improved¹⁷. Options may include adjusting an independent stockholder's rights, alleviating the equity share requirement, or defining a minimum equity value (for example KRW 10 million) as a requirement, as is the case in developed countries. It is also difficult to find a specific reason as to why the right to "claim" cumulative voting should be restricted to long-term investors, unlike in the shareholder proposal rule or right to claim the dismissal of directors or auditors, which require shareholders to be relatively long-term investors. Thus, deleting the requirement for 6 consecutive month holding needs to be reviewed.

As the cumulative voting system aims to ensure proportionate director election rights by the non-controlling shareholder versus the controlling shareholder, in order for the reform bill to ultimately reap the intended benefits, it is necessary to analyze the advantageous and disadvantages of the relevant systems and seek improvements in parallel. The cumulative voting system is useless if the list of company-only nominated candidates is submitted for the agenda item for direct election during the shareholders' meeting, i.e., if there are no nominations for director proposed by the shareholders. Therefore, without improving the reality in which shareholder proposals rarely take place regarding the election of directors, cumulative voting is highly likely to remain as a useless system, thus it is important to actively promote shareholder proposals¹⁸.

One example would be to promote the nomination of outside directors by institutional investors and expand relevant infrastructures such as the establishment of an outside director manpower bank. For the cumulative voting system to result in the election of candidates nominated by shareholders, it is crucial that minority shareholders including the institutional investors actively exercise their voting rights during the shareholders' meeting. Hence, it is

¹⁷ Jung Jae-Gyu, *supra* note 15, 39-40.

¹⁸ According to the KCGS survey of the KOSPI Market, of listed companies having held shareholders' meetings in the 1st quarter of 2013, shareholder proposals took place in only 9 companies (5 companies for outside director election, and 4 companies for inside director election), with nominations voted down in 8 companies, except for the 1 company whose proposal originated from the controlling shareholder.

important to actively consider ways to promote investors to exercise their voting rights in particular institutions. Concurrently, it is essential to revisit the systems relevant to shareholders' meetings. For example, it is customary for the majority of listed companies to submit nominees for both inside and outside directors as one proposal for a vote, making it difficult for investors to object to the election of a specific individual director. However, it is recommended that proposals for electing candidates be submitted for each and every candidate, putting an end to the abuse of current practices.

2. Partial Mandatory Introduction of Electronic Voting System

A. Background

Most listed companies in Korea hold annual shareholders' meetings on the third and fourth Friday of March, and these meetings are held in different locations across the country. According to the current Commercial Code, in companies without a written ballot and electronic voting system in place, only a person denoted the shareholder's proxy can attend these shareholders' meetings and exercise their voting rights. However, due to institutional constraints, a single shareholder is prohibited from attending the meetings of multiple companies on the same date; thus limiting their ability to exercise their voting rights. On May 28, 2009, following the introduction of Article 368.4 following the amendment of the Commercial Code, the foundation for having electronic shareholders' meetings was laid. However, even though it has been 4 years since its implementation, its uptake remains very low.

Indeed, it is in this context that the Commercial Code reform bill calling for mandatory electronic voting was proposed. According to the revision proposal, shareholders of listed companies prescribed under Presidential decree in consideration of the number of shareholders, can exercise their voting rights electronically without the need to attend the shareholders' meetings in person (Reform bill Article 542-14). Therefore, a listed company having a minimum number of shareholders must allow shareholders to exercise their voting rights via electronic means upon request.

Measures for Improving the Corporate Governance of Listed Companies in Korea

B. Major Issues

As it becomes easier for individual shareholders to cast their votes, the essence of shareholders' meetings will be improved. If electronic voting remains optional, as it is today, shareholders unable to attend the shareholders' meeting can be granted the opportunity to exercise their voting rights only when the company allows for them to do so. Therefore, the key to the reform bill was, unlike the current system, to allow shareholders to decide to vote electronically without requiring a special decision of the Board. That is, mandatory electronic voting can be interpreted as: "if the shareholders wish, the company must allow shareholders to vote electronically"¹⁹. Today, due to the separation of ownership-management, indifference of minority shareholders and increased costs due to time and geographical constraints, shareholders meetings have come to lose their essence. In this regard, electronic voting combined with written ballots and proxy solicitations will facilitate the exercise of voting rights by shareholders. Hence, the current reform bill fits perfectly the need to address the issue of shareholders' meetings losing their essence, and loss of momentum as being considered a mere dispersion of shares, since it is effective for overcoming diverse side effects such as technical errors resulting from electronic voting and by facilitating communication with minority shareholders.

C. Sub-conclusions

If a shareholders' meeting remains as a process of unilaterally realizing governance or management decisions, it cannot practically reflect the interests of all members of the company in question. As electronic voting becomes mandatory, and minority shareholders actively express their opinions on-line, and as companies promote communication with minority shareholders and send positive signals to the market, it can lead to a virtuous cycle of enhancing the market value of businesses.

¹⁹ Kwon Jong-Ho, "Necessity and Reason for Progressive Mandatory Implementation of Electronic Voting System", Major Issues and Assessment of Commercial Code Reform Bill (Korea Economic Law Association Summer Academic Symposium, August, 2013), 86.

Some have pointed out possible technical errors inherent in electronic voting systems; however, these systems have already been widely used in the U.S. and are neither highly sophisticated nor technically complex. Others are also concerned with the possible distortion of voting results through vicious rumors or politics in the media, though these issues can be regulated using current laws and be overcome by the benefits that electronic voting would bring.

3. Separate Election of Directors Serving on the Audit Committee

A. Background

The current law requires the implementation of an election “en bloc,” meaning that directors are first elected during the shareholders’ meeting, and the Audit committee are then elected. During the 1st step of electing directors en bloc, the 3% voting rights limitation rule of the majority shareholder does not apply during the decision-making process of the shareholders’ meeting. Therefore, it is natural that the Audit committee members are elected from among directors who are elected according to the preference of the controlling shareholder. During the 2nd step, the voting rights limitation rule does apply; however, it fails to attain the true objective of the 3% voting rights limitation rule of the majority shareholders, which is another issue.

Among the Commercial Code reform bill of the Ministry of Justice, pre-announced for legislation on July 17, 2013, the revised Article 542-12 stipulates the mandatory implementation of the separate election of Audit committee members for listed companies having assets worth at least KRW 2 trillion. Directors who will also serve on the Audit committee shall be elected separately from other directors, so that the 3% voting rights limitation rule remains applicable, even from the election stage^{20,21}.

²⁰ Some argue that applying the 3% rule for auditor election is unconstitutional. Ha Heon-Ju, “Problems and Solutions of Audit System of Stock Companies”, Property Law Study, Volume 25, 2nd Edition, 2008, 268.

²¹ 3% rule application when selecting auditors does not pose any problem in terms of purpose and method, therefore it is not unconstitutional. This perspective is according to Lee Chul-Song “Status of Auditor-Theory and Practice”, Listed Company Audit Committees Circular, No.123 (Korea Listed Companies Meeting, 2010. 3), 2010, 3; Jung

Measures for Improving the Corporate Governance of Listed Companies in Korea

B. Major Issues

The first issue to consider is whether the Board is a participatory type or a supervisory type. Under the Commercial Code, an Audit committee is a Board committee, which has the authority to substitute auditors and supervise the performance of duties of directors. However, a participatory Board member, as a Board member, becomes involved with decisions affecting the performance of Board duties, i.e., they audit the performance of their own duties, which presents limitations in preserving objectivity. Moreover, as for the current system of election en bloc, the rule limiting the voting rights of the controlling shareholder and affiliated persons does not apply, such that minority shareholders have insufficient equity shares to elect members to serve on the Audit committee.

Therefore, an Audit committee is only meaningful when it works as a supervisory Board, and in terms of organizational status, it is an institution under the Board and works as a participatory Board. The Audit committee is different from the Board and should remain an independent institution. Moreover, as for the status of its members, the members serving on the Audit committee are directors, and are therefore different from auditors. If a company has a supervisory type Board, one that includes executive officers, since the Audit committee is one of the committees on the Board, it is appropriate to assign them the authority to elect and dismiss members of the Audit committee to the Board. In this regard, a separate election system that ensures independence of the Audit committee from the controlling shareholder — even from the election stage — is very significant.

Opponents to this Reform Bill have raised concerns about the threats to managerial right coming from speculative foreign funds²². It is an unrealistic argument that the Boards of Korean companies will be dominated by foreign funds²³. The major examples cited by businesses regarding threats

Joon-Woo, “Review of Problems of the 2009 amended Commercial Code regarding Audit of Stock Companies”, *Comparative Private Law*, Vol. 17, No. 2 (Korea Association of Comparative Private Law), 2010, 347.

²² Choi Jun-Sun, “Review of Issues Regarding the Separate Election of Audit Committee Members”, Major Issues and Evaluation of Commercial Code Reform Bill (Korea Economic Law Association Summer Academic Symposium, 2013. 8), 7-11.

²³ Park Kyung-Suh, “Panel Discussion on Commercial Code Reform Bill for Improving

to managerial rights from foreign capital include SK Telecom in 1999 (Tiger Fund), SK Corp. Ltd. in 2003 (Sovereign), Samsung Corporation in 2006 (Hermes), and KT & G in 2006 (Carl Icahn), which only accounts for four cases in the 15 years since the 1997 financial crisis. Moreover, one should not forget that these cases involved companies whose market value failed to meet the potential book value and were exposed to governance problems. As for the argument that exponential costs are incurred in defending the managerial rights, these are not in fact actual costs but seem to be over evaluated in the investment context, and most are costs that are required to improve corporate governance. In particular, given the constraint of the current Fair Trade Act in which acquisition of at least 15% equity is subject to business merger assessment, the chances of multiple foreign capital investors uniting with one another remain very minimal.

Another issue is whether to apply the summed 3% rule or separate 3% rule for restricting the controlling shareholder voting rights. As for an Audit committee member who is neither an auditor nor an outside director, the voting rights are restricted to 3%, which is the sum of the stakes of only the majority shareholder and its affiliated persons (summed 3% rule), whereas for an Audit member serving as an outside director, the 3% voting rights limitation is applied to all individual shareholders (individual 3% rule), and such regulation needs to be improved.

The reason for applying the 3% rule as an exception of “one share one vote” is because the role of the Audit committee member is to restrict the unlimited intentions of the controlling shareholder and its affiliated persons by exercising the actual managerial rights. Therefore, we agree to the approach of limiting voting rights to 3% by summing the stakes of affiliated persons, including all shareholders without distinguishing auditors, Audit members not serving as outside director, Audit members serving as outside directors etc. In fact, the “one share one vote” system is commonly considered the most reasonable system, based on the concept that shareholder voting rights must be proportionate to their investment. And if there is a shift away from this system, the controlling

Corporate Governance” Discussion Text (jointly organized by Jeon Hae-Chul assemblyman office, Seo Ki-Ho assemblyman office, 2013.11), 30.

Measures for Improving the Corporate Governance of Listed Companies in Korea

shareholder may secure managerial rights with minimum financial burden, increasing the likelihood of an incompetent or immoral management leader securing or preserving managerial rights²⁴. On the other hand, even though Korean companies have constraints in issuing superior voting right stocks, the controlling shareholder can directly minimize the equity share while preserving managerial rights by issuing preferred stock equity to affiliates through recurring investments. Therefore, the fact that the controlling shareholder already enjoys excessive rights that are not proportionate to their investment compared to other shareholders can serve as rationale to limit the exercise of shareholder rights or to control shareholders and affiliated persons²⁵.

C. Sub-conclusions

In conjunction with the separate election process for Audit committee members, another consideration is that there is a need to handle Audit committee member election as an individual proposal such that each Audit member can vote in the shareholders' meeting²⁶. Even in the case of opposing a specific candidate among the individual Audit committee member candidates, if the election of all Audit committee members is proposed as a single motion for adoption, it is practically impossible for institutional investors and minority shareholders to vote down specific nominations. Therefore, for the practical application of shareholder rights during Audit committee member election, it is more reasonable to handle each individual Audit member candidate as a separate proposal to vote on.

4. *Enhanced Qualification Requirement of Directors and Auditors*

A. Current Regulations Under the Commercial Code

In order for the Board to operate in the best interests of all shareholders, it is not sufficient to merely strengthen the qualifications of outside directors and

²⁴ For example, the method of securing controlling rights using a small capital investment is by either owning shares of superior voting rights or by the concentrated purchase of common stocks when preferred stocks are issued.

²⁵ Park Kyung-Suh, *supra* note 12, 31-32.

²⁶ Jung Jae-Gyu, "Public Hearing for Commercial Code Reform on Corporate Governance", discussion text, Ministry of Justice, 2013. 6, 38-39.

improve the election process, but there is also a need enhance the qualification requirements of non-outside directors, executive officers, and auditors²⁷. Pursuant to Commercial Code 542-8, the outside director of a listed company refers to “a person for whom two years have not yet elapsed since their imprisonment without prison labor or a heavier punishment was completely executed or exempted” and “a person for whom two years have not yet elapsed since he was dismissed or removed from office after he/she violated an Act separately determined by Presidential Decree.” However, there are no similar qualification requirements for directors, executive officers, or auditors (Commercial Code Article 382, Article 408-2, Article 409, Article 542-5). As a result, even if a conglomerate leader or CEO is imprisoned due to malpractice and/or embezzlement, they can maintain the director position or even be newly elected as a director.

B. Regulatory Legislation by Sector

Some regulations limit the qualifications of executives; Article 18 of the Banking Act stipulates that “any person who has been sentenced to imprisonment without prison labor or heavier punishment and for whom five years have not elapsed since they completed the sentence or was exempted from the sentence” or “any person who has been sentenced to a fine or heavier punishment under finance-related Acts and for whom five years have not elapsed since he completed the sentence or was exempted from the sentence” is disqualified from selection as an executive. Moreover, pursuant to the Framework Act in the Construction Industry (Article 13) and Control of Firearms, Swords, Explosives, etc. Act (Article 5), if any person who has been sentenced to imprisonment, is elected as an executive within a certain period, the construction license registration shall be restricted or the manufacturing license shall not be approved. The Telecommunications Business Act Article 9 also limits the qualifications of executives.

²⁷ Kim Woo-Chan, “Panel Discussion on Commercial Code Reform for Improving Corporate Governance” presentation, (jointly organized by Jeon Hae-Chul assemblyman office, Seo Ki-Ho assemblyman office, 2013. 11), 19-20.

Measures for Improving the Corporate Governance of Listed Companies in Korea

C. Reinforcing Qualification Requirements of Directors and Auditors of Listed Companies

Some may say that it is practically impossible to enforce the qualification requirements of directors and auditors in all companies, pursuant to the above legislation. However, there seems to be no issue in applying such requirement to companies listed in the official capital market, allowing investors to freely trade stocks. Therefore, for listed companies, whether it be directors, executive officers, and auditors, and not outside directors, the following persons should not qualify to become corporate executives: an minor or person who is incompetent or quasi-incompetent; any person who has been declared bankrupt, and not yet reinstated; any person who has been sentenced to imprisonment without prison labor or heavier punishment and for whom two years have not elapsed since they completed or was exempted from the sentence; or any person who has been dismissed or removed from office in violation of the status prescribed under Presidential Decree and for whom two years have not elapsed since such dismissal or removal from office. Of course, it is also important to stipulate that any person to whom any of these cases applies — even after becoming director, executive officer or auditor — shall lose their position.

5. Rationalization of Shareholders' Meeting

A. Status on Organization of Shareholders' Meeting

The ineffectiveness of shareholder meetings of listed companies in Korea is not a recent problem. Since the notice for holding a shareholders' meeting should be made two weeks prior to the actual meeting date, pursuant to the Commercial Code²⁸, it is not easy for foreign investors or minority shareholders to fully deliberate on the agenda items and exercise their voting rights. In particular, foreign investors living abroad have difficulty exercising their voting rights based on these procedures, not to mention having time to deliberate on issues. Related to agenda items, questions also arise as to whether sufficient data are provided in advance of the shareholder meeting being held, especially with such short notice being given. What is worse, during the last

²⁸ See Article 363-1 of the Commercial Code.

few years, the shareholder meetings of listed companies have taken place on specific dates, such as the 2nd and 3rd Friday of March, the so-called “Super Shareholder Meeting Days”²⁹, and due to these overlapping dates if shareholders hold equity in many different companies they would be unable to attend all shareholders’ meetings and effectively exercise their voting rights. This current trend poses a serious threat for outside shareholders such as institutional investors and minority shareholders as they may be unable to attend shareholders’ meetings and exercise their voting rights. A few issues that need to be improved on are as follows.

B. Disclosure of Business Report Prior to Shareholders’ Meeting

The Capital Markets Act stipulates that the submitted business reports shall include financial statements and set forth dividends approved by the shareholders’ meetings. Moreover, when reporting the confirmation of corporate tax³⁰, the financial statement must be submitted. As a result, shareholders’ meetings must be held within 90 days following the end of the business year, which is also the deadline for the business report. For this reason, the shareholder meetings of listed companies having conducted annual closings in December are typically held in March. As a result, the schedule relevant to closing, auditing, and holding shareholders’ meeting must be expedited, placing a burden on businesses; thus considerably restricting the exercise of voting rights of institutional investors. Moreover, the auditor and outside auditor’s audit schedule is defined based on the shareholders’ meeting date, and thus the audit tasks and quality improvement may require more time, compared to the business report deadline. In order to mitigate these issues, it should be made possible to submit the financial statement, which is an attached document used for submitting the business report and reporting the confirmation of corporate tax, upon obtaining approval from the Board on the premise of the auditor’s qualified opinion. Even items that require approval by shareholders’ meetings as stated in the business report (financial statements, dividends, etc.),

²⁹ This year, the number of listed companies having held shareholders’ meeting on March 14 and 21 were 118 and 662 respectively; thus, 778 in total, representing 44% of all listed companies (1761).

³⁰ The relevant Act mandates that reports be made within 3 months following the last day of the month, which includes the closing date of each business year.

Measures for Improving the Corporate Governance of Listed Companies in Korea

should be allowed to be included upon approval by the Board, and in the case of requiring approval for revision during the shareholders' meeting, the revised version of the business report shall be disclosed. Moreover, it is also necessary to mandatorily disclose the business report before the decision and notice of holding a shareholders' meeting so that shareholders can verify and review the business reports and the business performance of competitors in advance, and then exercise their voting rights³¹. Moreover, if the deadline for audit-related tasks, including audit, audit report submittal, disclosure, and provision of financial statements, are based on the business report deadline, it will be possible to largely lessen the audit workload and contribute to enhancing the audit quality.

C. Extension of Notice Period of Convocation of Shareholder Meeting

As mentioned above, the deadline for providing notification of a shareholder meeting pursuant to the Commercial Code is two weeks prior to the actual meeting, which is very tight and seriously undermines the exercise of voting rights by shareholders, including institutional investors. According to the Korea Corporate Governance Service, as of the 1st half of 2014, 388 companies informed stakeholders of the convening of a shareholders' meeting 16.3 days prior to the actual meeting, on average; for the 2nd half of 2013, 53 major financial companies provided information 18.4 days in advance. If business reports have to be submitted and disclosed prior to providing notice of the convening of a shareholders' meeting, it is recommended that the deadline for providing notice of convocation must be increased to 4 weeks prior to the shareholders' meeting in order to give ample time for investors to analyze agenda items. Even if the shareholder meeting date is prior to the business report submittal, the deadline for giving notice of convocation for listed companies must be adjusted to 4 weeks prior to the shareholders' meeting so that at least the list of executive nominations can be disclosed in advance³².

³¹ Song Min-Kyung, "Reinforced Disclosure for Improving Fundamentals of shareholders' meeting", *CGS Report* Vol. 3 No. 10 (2013.5), Korea Corporate Governance Service, 2-7.

³² Song Min-Kyung, "Reinforced Disclosure for Improving Fundamentals of shareholders' meetings", *CGS Report* Vol. 2 No. 18 (2012.10), Korea Corporate Governance Service, 3-6.

D. Expansion of Disclosure Regarding Shareholders' Meeting Agenda Items

This section is focused on issues related to the election and remuneration of executives. Sometimes companies omit the profiles of directors, audit members, and auditor candidates from the notice of convocation, which increases the workload of institutional investors who need to fully exercise their voting rights. Therefore, it must be legislated that the detailed past 10-year career history of executive candidates of listed companies be included in the notice of convocation. In this way, shareholders can fully review the profiles and qualities of candidates and cast votes in favor of or against specific candidates. Following the amended Capital Markets Act in May 2013, "remuneration and its detailed calculation of criteria and method of individual executives" for executives receiving at least KRW 5 million was added as an item to be included in the business report. However, the actual disclosed data indicates that very few companies specified remuneration calculation criteria or the procedure used for corporate executives and the details of remuneration in conformity with the shareholders right to know³³.

E. Expansion of Disclosing Shareholder Meeting Outcomes

Currently, when disclosing the outcomes of shareholders' meetings, companies only mention whether the agenda item in question had been approved or not, without specifying the percentage of those in favor of the item. This means that there is no way to know how the opinions of attending shareholders were formed around the item, making it difficult for shareholders to consider the specific results and how to exercise their voting rights in the upcoming shareholders' meetings. This style of reporting undermines the rights of shareholders who must be able to exercise their voting rights based on ample information and an understanding of agenda items. In order to address this problem, when disclosing the shareholders' meeting results, the exact percentage of "in favor", "against" and "abstention" votes for each agenda item must be mandatorily disclosed. In this way, an accurate counting of "for" or "against" votes will be encouraged, which had been haphazard in the past, and which can further promote the use of electronic voting.

³³ Song Min-Kyung, Yoon Jin-Soo, Jung Jae-Gyu, "Analysis on the Specification of Remuneration of Individual Executives in Business Reports", *BFL* No. 65 (2014.5), Seoul National University Financial Law Center, 17-20.

IV. Conclusions

This paper focused on the current status and issues regarding significant issues that need to be reviewed in order to improve the corporate governance of listed companies in Korea. Of course, many other topics exist for further consideration; in particular, regarding the independence of outside directors, there are many criticisms as to whether outside directors are fully assuming their intended role of checking and balancing the management in an independent position. In today's Boards, the role of outside director is crucial for the successful implementation of the overall functions of the Board, and this is determined by the core qualities required of outside directors: independence, professionalism, and responsibility. Among such qualities, when focusing on the checks and balances role of the Board, independence is the most important element. Yet, it seems difficult to find the right answer for securing such independence. The aforementioned partial mandatory introduction of a cumulative voting system and the separate election of Audit committee members are useful for securing the independence of outside directors.

The enhanced qualification requirement regarding the independence of outside directors, additional measures to secure independence from the election process and the procedure for selecting outside directors, and reinforced roles of institutional investors in electing independent outside directors are other options that can be explored. A comprehensive study and concrete measures for improvement regarding these matters was not included in this paper, and are subject to further study.

It is also important to once again reflect upon the ultimate goal of improving corporate governance: Why should corporate governance be improved, and why are some business groups collectively opposing the Commercial Code reform bill? As many are aware, improving corporate governance also promotes corporate transparency and induces responsible management, thereby enhancing corporate value while ensuring that the fruits are distributed fairly to all shareholders. This in turn encourages sustainable companies, which in a larger framework ultimately contribute to promoting sustainable national economic and social development. Today, some controlling shareholder management practices oppose the improvement of corporate governance,

because they are accustomed to the existing practice of managing businesses and using corporate resources for their personal benefit, which is deeply mired in opportunism. At times, changes may also seem awkward, and may subsequently incur huge costs and unexpected difficulties, while the newly introduced systems take root.

Moreover, some companies may continue to prosper while maintaining their status quo without having to improve their corporate governance. However, how much and until when would such companies continue to flourish? In today's world, seeking immediate, external growth is no longer supremely important; increasing in importance is for companies to seek sustainable development and achieve "good growth." Good growth, which not only embraces shareholders, management, and employees of a company but also its consumers, competitors, partners, local community, and global environment, is needed. The first step and cornerstone in this journey is to improve corporate governance.

References

- Kwon Jong-Ho, "Necessity and Reason for Progressive Mandatory Implementation of Electronic Voting System", Major Issues and Assessment of Commercial Code Reform Bill (Korea Economic Law Association Summer Academic Symposium. August, 2013).
- Park Kyung-Suh, "Panel Discussion on Commercial Code Reform Bill for Improving Corporate Governance" Discussion Paper (jointly organized by Jeon Hae-Chul assemblyman office, Seo Ki-Ho assemblyman office, 2013.11), 30.
- Bae Sang-Geun, "Commercial Code Reform Public Hearing on Corporate Governance" Discussion Paper (Ministry of Justice, 2013. 6).
- Song Min-Kyung, "Measures for Legislative Improvement for Improving Fundamentals of Shareholder Meetings", *CGS Report*, Volume 3. Edition 10(2013.5), Korea Corporate Governance Service.
- Song Min-Kyung, "Reinforced Disclosure for Improving Fundamentals of shareholders' meeting", *CGS Report*, Volume 2 No.18(2012.10), Korea Corporate Governance Service
- Song Min-Kyung, Yoon Jin-Soo, Jung Jae-Gyu, "Analysis on Specification of Remuneration of Individual Executives in Business Report", BFL No. 65(2014.5), Seoul National University Financial Law Center.
- Oh Duk-Gyo, "Governance Status of the KOSPI Market and KOSDAQ Market", *Corporate Governance Review*, vol. 59 (Korea Corporate Governance Service, 2011)
- Lee Chul-Song, "Status of Auditor-Theory and Practice", Listed Company Audit Committees Circular, No. 123 (Korea Listed Companies Meeting, 2010.3).
- Jung Jae-Gyu, "Public Hearing of Commercial Code Reform on Corporate Governance" Discussion paper (Ministry of Justice, 2013. 6).
- Jung Joon-Woo, "Review of Problems of the 2009 amended Commercial Code regarding Audit of Stock Companies", *Comparative Private Law*, Vol. 17, No.2 (Korea Association of Comparative Private Law, 2010).
- Ju Jin-Yeol, "Review of Issues regarding Indirect Mandatory Introduction of Cumulative Voting System", Major Issues and Evaluation of Commercial Code Reform Bill (Korea Economic Law Association Summer Academic Symposium, 2013.8).
- Choi Jun-Sun, "Review of Issues regarding the Separate Election of Audit Committee Members", Major Issues and Evaluation of Commercial Code Reform

Bill (Korea Economic Law Association Summer Academic Symposium, 2013.8).
Ha Hun-Joo, “Problems and Solutions of Audit System of Stock Companies”,
The Journal of Property Law, Vol. 25, No. 2 (The Association for Korean Law of
Property, 2008) CLSA/ACCG, CG Watch 2012, Asia Corporate Governance
Association (10 September 2012).
OECD, Corporate Governance - A SURVEY OF OECD COUNTRIES,
2004.



ESG disclosure: Legal requirement to facilitate CSR implementation by Korean companies

Kwak Kwan-Hoon

I . Introduction

The concept of Corporate Social Responsibility (CSR) is gaining growing attention across the world, with CSR becoming a commonly used, familiar term. However, it is not easy to adopt a single definition of CSR, as it literally refers to the responsibility of a corporation vis-a-vis the society that it belongs to. Since social conditions differ between countries and periods, corporate responsibilities required by the society also take different forms, making it very difficult to ascertain what the actual definition of CSR is. However, when combining different conceptual definitions currently under discussion, CSR tends to refer to an act of considering not only financial performance but also diverse aspects linked to environment, human rights, and social, geographical and ethical aspects in business operations. For this reason, differences may exist between countries and regions since some may place more focus on human rights or environmental issues, or value donations more than others.

Demand for CSR management has recently entered a new phase; with ISO 26000, there are now on-going global efforts to standardize CSR practices. Although most guidelines are legally non-binding, it is important to note that there is an increasing trend to evaluate firms based on such guidelines, which have subsequently become de facto criteria for corporate evaluation. In other words, as firms with no CSR engagement are not appreciated in the market, CSR is no longer an option but is becoming a critical factor for ensuring business survival and sustainable growth.

Following this international trend, there are also increasing efforts to legislate CSR in Korea. To date, there has been legislation passed requiring businesses to consider environmental and social aspects to ensure sustainable growth,

ESG disclosure: Legal requirement to facilitate CSR implementation by Korean companies

although without explicit mention of CSR. And although this legislation was not enacted for the purpose of CSR management, it did require that CSR-related elements such as environmental factors be taken into account.

More recently, the enactment and amendment of laws directly requiring CSR business management is taking place. For example, the “Small and Medium Enterprises Promotion Act” was amended in 2012 to define socially responsible business operation requirements for small and medium enterprises. However, the Act holds limitations in that it only covers SMEs, though it is meaningful for being the first legislation to directly define CSR practice by law. Furthermore, reform bills including the National Pension Act and Capital Market Act are being discussed, with the goal to further develop CSR management.

II . Background on CSR Legislation

Discussions on both CSR and Socially Responsible Investing (SRI) are gaining momentum in Korea due to: (i) increasing social demand; (ii) increasing need for businesses risk management; and (iii) a paradigm shift in business regulations.

1. Increasing Social Demand for CSR

Traditionally, the primary focus of a good firm was to manufacture inexpensive quality products, offer them to the market, and distribute profits to its stakeholders and shareholders. However, the growing perception today is that no matter how good the quality of a product, if environmental or human rights concerns are involved in the manufacturing process, the product will not benefit society as a whole. With mankind enjoying ever greater prosperity in the 21st century, the stakeholder’s expectations of firms have also expanded to include both financial as well as social and environmental values. Firms that merely pursue financial values and neglect social and environmental values will fail to earn social trust and will subsequently find its existence threatened.

International norms and guidelines on CSR management have been proposed in attempts to meet such evolving demands for businesses, with major examples including “ISO 26000,” “UN PRI Principles,” and “UN Guiding Principles

on Business and Human Rights.” As more businesses are evaluated based on these criteria, the need for CSR implementation will also further increase.

2. Increasing Need for Business Risk Management

As there is an ongoing change in how society tends to view firms, there is a corresponding need for CSR management, from a business risk management perspective. A business stakeholder not only asks firms to generate more financial profits but also to assume social responsibility, and tends to proactively respond to companies who fail to do so. IT development plays a key role in this sense. IT technologies such as the Internet enable rapid sharing of information and helps international groups take a collective action through websites and social media. Today, firms in breach of regulations at times can find their existence threatened due to social criticism and boycotts from civil groups, even before facing any criminal or administrative sanctions.

When stakeholders including consumers and civic groups take proactive measures to respond to firms, they may call for a higher standard of social requirements than legal ones. For example, when the level of harmful substances in a product is below a legal threshold, it does not pose any legal problems. However, consumers may complain about the fact the harmful substance was included into the product in the first place, and in this case, the company may face social criticism as well as financial loss. This explains the growing need to fully incorporate environmental concerns, human rights, and social elements at the corporate risk management level. Thus, in today’s world, CSR is holding an ever greater significance since it no longer simply concerns corporate philanthropy at a moral or ethical level but as a risk management concern for sustainable corporate growth.

3. Paradigm Shift in Business Regulations

Administrative bodies impose diverse legal obligations on companies to attain their stated goals. However, when companies fail to voluntarily perform their obligations, these administrative goals cannot be achieved. As a result, the administrative body arranges a wide-range of sanctions as a means to secure the

ESG disclosure: Legal requirement to facilitate CSR implementation by Korean companies

effectiveness of its administrative intentions to have the obligations fulfilled or realize the same state of duties being performed. Sanctions on businesses include (i) administrative sanctions; (ii) criminal sanctions; and (iii) civil sanctions.

These sanctions primarily aim to restrain the non-compliance of firms. Imposing strong sanctions on companies engaged in malpractice helps prevent the same malpractice from recurring both in the current firm as well as others. However, there are limitations to deterring malpractice through stringent sanctions when the firm is not committed to complying with the law.

For example, the most powerful regulatory means such as administrative punishment has limitations in restraining business malpractice. Administrative punishments have the greatest impact because the disadvantages are the greatest (e.g., the non-complying firm faces administrative punishment and is left with a criminal record), thereby maximizing the psychological effect. This explains why administrative punishment is the preferred sanction despite the subsidiary principles stipulated in criminal law. However, one limitation is that it is difficult to expect the same kind of psychological effect in corporate entities, as is the case for individuals. In particular, if an employee's malpractice was for corporate profit, even though the actor faces criminal punishment, the company is likely to name his successor and continue to commit the same malpractice. In this case, there is often no criticism or sanction taking place within the organization, making it more difficult to restrain such malpractice from recurring by leveraging the psychological effect.

For this reason, since current sanctions are structured such that they are relatively ineffective for restraining corporate malpractice, a fundamental paradigm shift in business regulations is needed. The implementation of CSR by business is thus very important as a regulatory paradigm shift. That is, when businesses are encouraged to implement CSR, they will also build on their own system and either prevent or avoid potential legal misconduct. In this way, it will be possible to engage businesses to initiate voluntary compliance of laws and prevention of malpractice. In other words, CSR implementation is an advanced regulatory paradigm compared to the existing reactive sanction-centered regulations.

III. Development of Legislation Relevant to CSR

1. *Overview of Current Legislation*

Current legislation that directly regulates CSR is the “Small and Medium Enterprises Promotion Act.” Other legislation does not directly regulate CSR, but tends to indirectly regulate CSR’s individual elements, such as environmental and social aspects.

(1) Small and Medium Enterprises Promotion Act

Following its amendment in 2012, the Small and Medium Enterprises Promotion Act stipulates requirements with regards to the “corporate social responsibility of small and medium enterprises.” This Act states that SMEs shall make efforts to undertake socially responsible business operations vis-a-vis its employees, suppliers, customers and the local community (Article 62.4.1). Furthermore, it also stipulates that the government and local self-governing bodies can provide necessary support for the socially responsible business operations of SMEs (Article 62.4.2).

This Act targets SMEs and requires the Small and Medium Business Administration (SMBA) to take necessary measures and provide support for facilitating CSR implementation. In particular, the SMBA Administrator shall establish and implement a basic plan to promote CSR-implementing SMEs every five years with a goal to facilitate CSR implementation by SMEs and provide systematic support (Article 62.5.1). The basic plan shall include: 1) the basic policy goals and objectives for facilitating the promotion of CSR implementation by SMEs; 2) an action plan for promoting CSR management by SMEs; 3) assistance programs for CSR implementing SMEs; 4) the current status of CSR implementing SMEs; and 5) other items prescribed by the Presidential Decree for facilitating and supporting CSR implementing SMEs (Article 62.5.2). In this case, the items under the Presidential Decree refer to: a) the training and development of CSR professionals; b) CSR business management training for SME employees; c) the development and diffusion of implementation indicators for CSR management by SMEs; and d) other major initiatives relevant to facilitating CSR implementing SMEs (enforcement ordinance Article 54.3).

ESG disclosure: Legal requirement to facilitate CSR implementation by Korean companies

Furthermore, an annual execution plan built on the basic plan must be implemented (Article 62.5.3), and the requirements of this plan must be determined under the Presidential Decree (Article 62.5.4).

Moreover, the SMBA Administrator can designate an SME support agency or group to effectively assist the socially responsible business management by SMEs (Article 62.6.1). Pursuant to this regulation, the SMBA designated the “Korea Productivity Center” as the “CSR Small and Medium Business Center,” which first began activities in April 2014. A center or group must fulfill the following requirements to be designated as a CSR Small and Medium Business Center: 1) be a non-profit organization; 2) have a specialized team dedicated to supporting the CSR practice of SMEs; 3) include consulting or a training program in the scope of the institution or group’s activities; and 4) the total space of the training facilities shall be above 150 m², with one or more training and consulting rooms (enforcement ordinance Article 54.5.1). A center or group fulfilling such requirements should attach supporting documents and submit its application to the SMBA Administrator (Article 54.5.2).

The CSR Small and Medium Business Center must 1) provide guidelines regarding CSR implementation by SMEs; 2) nurture a professional workforce in terms of CSR implementation by SMEs; 3) provide training and education to raise awareness of CSR; and 4) provide necessary information and consulting assistance regarding CSR (Article 62.6.2). The SMBA Administrator may invest in or grant a loan to support the costs required for the operation of the Center (Article 62.6.4), and in the case that the legal requirements for designation are not met, the designation can be canceled (Article 62.6.5).

(2) Other Legislation Indirectly Regulating CSR

A. Industrial Development Act

The “Industrial Development Act” was enacted in 1999 and aims to facilitate the modernization of industrial structures, such as strengthening industrial competitiveness, enhancing the efficiency of industrial organization, and facilitating corporate restructuring. This Act is meaningful for being the first to introduce the concept of “sustainable development” in Korean legislation.

Sustainable development, first introduced in the environmental sector, has now expanded to include social and political aspects. Thus, the concept of “sustainable development” was presented under the view that it is no longer possible for businesses to ensure sustainable growth while neglecting environmental or social issues. Although this Act does not directly regulate CSR, it clearly underscores the importance of environmental and social aspects in CSR implementation for businesses, and defines the roles and responsibilities to be assumed by the government or local self-governing bodies to this end.

B. Sustainable Development Act

Furthering the concept of sustainable Development that was introduced in the Industrial Development Act (1999), the “Sustainable Development Act” was legislated in 2007 to put this concept into more concrete terms. This Act defines sustainable development as “development based on sustainability that is implemented simultaneously in the pursuit of economic growth, social stability, integration, and the preservation of the environment” (Article 2.2).

This Act provides the basic attitude and strategy to be adopted by the government and local self-governing bodies to ensure sustainable development from an environmental perspective (from Article 7 to Article 11), and includes a sustainability evaluation (Article 13) and sustainable reporting requirements (Article 14). Sustainability reporting refers to disclosing data on the efforts made by a firm to protect the environment, and it is deemed to have encouraged businesses to fully consider the environmental aspect.

C. Framework Act on Low Carbon, Green Growth

Among the environmental aspects of corporations, the “Framework Act on Low Carbon, Green Growth” was enacted in 2008 with the goal to lay the foundation for low carbon green growth by reducing greenhouse gas emissions. The term “low carbon” refers to the intent to lower the dependence on fossil fuels, expand the use and distribution of clean energy, and reduce greenhouse gases to an appropriate or lower level by expanding carbon sinks (Article 2.1). Moreover, “green growth” refers to growth achieved by saving and using energy and resources efficiently to reduce climate change and damage to the environment, secure new growth engines through research and development of green technology, create new job opportunities, and achieve harmony between the economy and environment (Article 2.2).

ESG disclosure: Legal requirement to facilitate CSR implementation by Korean companies

This Act defines the roles and responsibilities of the government and local self-governing bodies to ensure low carbon green growth while assigning certain duties for businesses. The government shall endeavor to promote the basic principles of low carbon discharge and green growth to be reflected in every aspect of government affairs (Article 4.1), and local self-governing bodies shall fully cooperate in the State's measures (Article 5.1). In particular, each business entity, shall, in all its activities, observe green management, reduce emissions of greenhouse gasses and pollutants, and expand investment and employment in the research and development of green technologies and green industries to fulfill its social and ethical responsibilities for the environment (Article 6.1). Moreover, each business entity shall actively participate and cooperate in policies enforced by the government and each local self-governing body that promote low carbon discharge and green growth (Article 6.2).

In addition, the government is also required to arrange policies to facilitate and support the green economy and green industries. It especially needs to make a plan and green management promotion measures to transform existing industries into green industries (Article 23). To facilitate the green management of enterprises, the government shall establish and enforce measures that support and enforce measurers to provide technical support for conversion into environment-friendly management or disclosing the achievements of green management (Article 25).

As such, this Act defines the efforts for low carbon green growth as an important social responsibility of firms and proposes support measures for its implementation.

D. Social Enterprise Promotion Act

A social enterprise aims to achieve the social goal of the organization. It does not operate business to maximize profits for the shareholders but uses its proceeds to achieve a social cause. Such social enterprises are now seeking a new paradigm shift, from pursuing social programs dependent on government subsidies or donations to a genuine social enterprise that seeks profits. The interest in social enterprises, which first began to grow in Europe, is now gaining momentum worldwide, and this interest continues to grow in Korea as well.

The “Korea Social Enterprise Promotion Act” was enacted in 2006, and according to this Act, an enterprise fulfilling specific qualifications is certified as being a social enterprise. A person who intends to operate a social enterprise shall satisfy the certification requirements and obtain certification from the Minister of Employment and Labor (Article 7).

More specifically, a social enterprise is required to: 1) take the form of a corporation or an association under Civil Law; 2) employ paid workers; 3) primarily aim to realize social objectives; 4) have a decision-making structure that includes the participation of stakeholders; 5) have a certain level of revenue from operating activities; 6) have articles of incorporation, rules, etc.; 7) spend at least two thirds of its revenue on social objectives; and 8) satisfy all other matters prescribed by the Presidential Decree (Article 8). Certified social enterprises pursuant to such criteria will benefit from a wide-range of support (from Articles 10 to 13).

Since the main goal of a social enterprise is to achieve a social cause, it essentially differs from the CSR management of a typical for-profit enterprise. However, it is significant that it presents a new model in which enterprises may move away from the conventional approach of solely pursuing profit and move towards pursuing both profit and public good. Moreover, some large corporations have begun to directly run social enterprises or implement corporate social responsibility by sponsoring social enterprises. Since these social enterprises can become a model for enabling CSR management by businesses, social enterprises and CSR management are closely related with one another.

2. Reform Bills under Discussion

(1) National Pension Act Reform Bill

In August 2013, a “Reform Bill on the Partial Amendment to the National Pension Act” was submitted to the National Assembly (proposed by parliamentarian Lee Mok-Hee). This bill calls for the National Pension Fund to consider Environment, Social, and Governance (ESG) elements when selecting a firm to invest in. This yet-to-be passed bill is still under discussion in the National Assembly,

ESG disclosure: Legal requirement to facilitate CSR implementation by Korean companies

though it is significant in that it aims to legislate SRI to indirectly facilitate CSR implementation by businesses.

The National Pension Fund of Korea is the world's third largest pension fund, with a total asset of KRW 391.9677 trillion as of the end of 2012. Moreover, the investment-to-market capitalization ratio stands at 5.4%, making it the largest shareholder in the Korean Exchange; it plans to expand its investment ratio to 30% by 2017. If this trend continues, by 2020, the National Pension is expected to dominate 15% of the Korean Exchange Market. As such, the National Pension with its huge size has a considerable impact on the Korean exchange market as well as the companies it has invested in. Some believe that as a public fund pursuing the public good, the Fund needs to proactively pursue socially responsible investing (SRI). This reform bill therefore aims to establish an institutional framework that allows the National Pension to incorporate such social needs and opt for more socially responsible investing in order to promote CSR implementation by businesses.

In this reform bill, as the Minister of Health and Welfare is to manage and administer the National Pension Fund, social responsibility elements such as ESG elements must be considered. When making decisions based on ESG elements, the National Pension Fund Commission is required to disclose data regarding the consideration of each element and its extent. Moreover, in the case when ESG elements are not considered, the reason for non-consideration shall also be disclosed (Reform Bill Article 102.4).

The reform bill does not directly mandate SRI in the National Pension management; rather, it takes an indirect disclosure approach. This approach is in line with the "Comply or Explain" scheme in the U.S. and Europe, which is often used as a means to regulate corporate governance. Since the biggest goal of the National Pension Fund is to secure the income for subscribers' old age, its first and foremost priority should be to improve profitability. Therefore, it may seem inappropriate to make SRI mandatory at the expense of profit-generation. Against this backdrop, SRI must be fully considered when making investment decisions; however, when deemed to undermine the investment return, the reason for non-consideration must be disclosed to ensure the autonomous management of the Fund. It should also be noted that the SRI of the National Pension Fund may come as a short-term burden to businesses.

(2) Capital Market Act Reform Bill

In July 2013, the “Reform Bill on the Partial Amendment to Financial Investment Services and Capital Market Act” (hereinafter, “Capital Market Act”) was proposed (by parliamentarian Lee Eon-Joo). This bill is to include data relevant to CSR implementation efforts of businesses in the business reports that listed companies are required to submit. A similar reform bill had been proposed (by parliamentarian Park Sun-Sook) during the 18th National Assembly in 2010; however, this bill failed to pass, and it was revised and proposed again during the 19th National Assembly.

This reform bill mandates business reporting firms to include corporate social responsibly implementation efforts in their business reports in order to assist investors in their decision-making process and facilitate voluntary CSR implementation efforts by business, thereby creating a win-win social environment. The additional information required in the business report is as follows:

1. Working conditions (wage, working hours).
2. Labor-management relations (agreement with the labor union based on collective bargaining rights).
3. Number of senior managers and employees (including part-time, temporary workers), training hours per employee, and representation of women in senior management).
4. Support for family and work balance of employees (in-house nursery, maternity leave, and reduced working hours for child rearing).
5. Working environment including safety conditions and safety regulations.
6. Environment-friendly business practices to reduce environment pollution and environmental damage caused by business activities.
7. CSR implementation vis-a-vis companies deemed to be de facto dominating the legal, contractual, and transactional relations.
8. Planning and implementation efforts with regards to consumer safety and data protection, consumer complaints, and dispute settlement procedures.
9. Ethical management (whistle blower protection for in-house malpractice, and anti-bribery and corruption measures).
10. History of administrative measures or criminal punishment due to non-compliance of laws prescribed by the Presidential Decree relevant to fair

ESG disclosure: Legal requirement to facilitate CSR implementation by Korean companies

trade, finance, labor, environment, and anti-corruption laws.

11. Community participation and development (social philanthropy and employment of local workforce).

There are numerous examples of legislation that require listed companies to disclose CSR data. In countries like the U.K., France, and Germany, it is legally required that companies disclose non-financial data regarding environment, working conditions, benefits, and profitable activities with the community together with the financial data. Such disclosure is meaningful in that it lays the institutional framework to help investors make informed decisions and provide transparent data for stakeholders. Moreover, this reform bill is also important from a business perspective because while preparing for the disclosure of data, companies themselves may become more motivated to adopt CSR business practices.

(3) Government Procurement Act Reform Bill

Besides the aforementioned National Pension Act and Capital Market Act reform bills proposed to the National Assembly, there is a growing need to reform the “Government Procurement Act.” Although the bill is yet to be submitted to the National Assembly, a detailed amendment of the bill is under preparation, and is likely to be submitted to the National Assembly soon.

This Act requires the government to purchase with priority the products manufactured by companies fully engaging in ESG elements in order to facilitate voluntary CSR implementation by businesses. For example, the “Government Procurement Act Reform Bill” currently under discussion proposes, in part, to create a new provision that incorporates social and environmental values such as the environment, human rights, employment, fair trade, and consumer protection in the government procurement process. Moreover, measures are being sought to give priority to businesses who amply consider ESG elements in the “Act on Contracts to Which the State is a Party” and the “Act on Contracts to Which a Local Governments is a Party.”

The approach of giving priority or incentives to businesses meeting certain requirements is also commonly found in other existing laws. For example, the

“Framework Act on Low Carbon, Green Growth” mandates public institutions to purchase green products to facilitate the development of green technology and green industries (Article 32.2). Moreover, the “Act on the Facilitation of the Purchase of Small and Medium Enterprise-Manufactured Products and Support for Development of Their Markets” stipulates that for the government procurement process, the government must sign procurement deals first with small and medium enterprises in order to facilitate SME protections (Article 4.2). The Act uses the government procurement system as a means to attract the voluntary participation of businesses in a way that would benefit the nation as a whole.

The reform bill currently under discussion also can be understood from such a perspective. If the government takes the initiative to make it a priority to use the products and services of businesses implementing CSR management, businesses will more voluntarily commit to CSR implementation.

IV. Business Environment Changes and Response Following Law Amendment

1. Change in Business Environment

The National Pension Act and the Capital Market Act reform bills have had the greatest impact of all the aforementioned Korean laws in terms of CSR. Both Acts mandate businesses to actively disclose CSR related data. This disclosure of information is a preventive regulatory paradigm in that firms actively notify their situation to investors or stakeholders, and in the process work to identify problems and to take preventive measures to avoid potential problems. The following section will deal with the expected outcomes of these legislation reforms.

(1) National Pension Fund Reform

When the National Pension Fund is amended, the Fund will allow the National Pension Fund to consider ESG elements when selecting firms for investment. Moreover, if the Fund factors in ESG elements, it should disclose the details for consideration; if it does not consider ESG elements, it should also disclose

ESG disclosure: Legal requirement to facilitate CSR implementation by Korean companies

the reason for non-consideration. Therefore, the National Pension Fund, when selecting firms for investment, must not only analyze and review their financial data but also the non-financial data pertaining to environmental, social, and human rights issues.

Given the importance of the National Pension Fund in Korea's exchange market, it is expected that such change will have a huge impact on businesses as a whole. Going forward, businesses should not only consider operating profits but also make sure that legal malpractice during the Fund management does not happen. Moreover, businesses should also work to mitigate potential environmental, human rights, or labor issues. In this way, businesses will actively lead CSR management on their own.

As mentioned above, it is very difficult to eliminate business malpractice, even by applying very stringent reactive sanctions. In particular, in large firms with tens of thousands of employees, reactive sanctions are far from effective; it is more important to ensure that companies build and manage an internal control system on their own to avoid potential problems. As such, if the National Pension Fund evaluates firms while considering ESG elements, companies must work to ensure the effective functioning of the internal control system. In other words, a company without an effective internal control system or without full engagement of ESG factors is likely to be eliminated from the market when such information is disclosed.

(2) Capital Market Act Reform

When a firm's ESG information becomes available in a business report following the Capital Market Act Reform, the expected changes are: 1) the adjustment of the enterprise market evaluation criteria, and 2) the increased legal risks of enterprises.

Information disclosed on business reports has long been an important criterion for investors when evaluating a company. The focus of existing reports has been on the disclosure of financial data, with most investors evaluating companies based solely on this data. However, when ESG elements are disclosed together with the legal amendment, investors can also make investment decisions by taking non-financial elements into account.

In particular, recent cases have reported that investors not only consider investment return but also pursue investments and public good through “crowd funding.” There is also a growing number of consumers who are willing to make “good consumption” by purchasing eco-friendly, human rights-friendly products at higher prices. Moreover, businesses are learning by experience that if they decide to only care about investment return, though short-term gains may be great the long-term losses may be greater. Therefore, an increasing number of investors no longer merely consider the financial data when choosing an investment option. In this respect, when enterprises’ ESG information is fully disclosed, the decision-making criteria for investors will change accordingly.

The second expected outcome pertains to increased business management and legal risks. In the past, firms faced no particular issue when meeting the minimum legal requirements. For example, in the case an environment law bans the use of pollutants higher than a certain level, firms only had to meet the minimum requirement provided in the law and would face no problem. However, with the Capital Market Act reform and the reinforced disclosure of ESG, firms are likely to set and practice a higher level of requirements than set by law in order to enhance their corporate image.

With ever fiercer business competition, firms that fail to run its business as eco-friendly as their competitors will eventually be eliminated from the market. As a result, since a higher level of environment requirements are needed than exists by law, the legal risks of businesses are also likely to grow. That is, the level of ESG considered by businesses will also become an important criterion for corporate evaluations.

(3) Government Procurement Act Reform

When incorporating ESG factors into government procurement processes, it is expected that business ESG considerations will directly correlate with their operating profit. In particular, the fact that a firm supplied its product to the government can also greatly impact consumer trust, thus serving as a matter of survival for the firm in question. It also allows for more direct regulation rather than indirect regulation through information disclosure; if the reform

ESG disclosure: Legal requirement to facilitate CSR implementation by Korean companies

bill is passed, ESG consideration and CSR implementation by businesses will become inevitable.

2. Corporate Response Measures

(1) Management Decisions Considering Stakeholders

In most cases, senior management takes priority in maximizing profits for its shareholders. This is how a company is typically structured, and how commercial laws are generally set forth obligations vis-a-vis shareholders. However, society demands that the interests of both the shareholders and stakeholders such as consumers, employees, suppliers, the local community be considered. For example, the National Pension Fund, due to its nature of pursuing public good, tends to exercise its voting rights by considering the interests of various stakeholders together with the shareholders. That is, when corporate management makes shareholder-centered decisions, these decisions can be in conflict with the perspectives of institutional investors such as the National Pension Fund, which takes the interests of different stakeholders into account. In this aspect, once the National Pension Fund or the Capital Market Act reform bills are passed, it is highly likely that not only the National Pension Fund but also many other institutional investors will consider CSR management as important criteria for management decisions.

In order to respond to such a changing environment, when management makes business decisions, it should consider the interests of its shareholders as well as other stakeholders. That is, it should prevent unnecessary conflicts with not only the major and minor shareholders but also stakeholders including consumers, the local community, employees, and partner companies and also seek collaborative ways to promote synergy between all.

(2) Strengthening the Internal Control System

As mentioned above, when the National Pension Fund Act and the Capital Market Act are amended, it will be mandatory to disclose the ESG information of a firm to the market. Therefore, when a company faces a certain problem, it will be disclosed to the market without delay, thus impacting the company. In this environment, both investors and shareholders are expected to take

proactive measures to respond to such problems. Therefore, going forward, problem prevention will be viewed as having primary imp, and as a concrete measure, the adequate establishment and management of an international control system is required.

To prevent the occurrence of problems during business management, an internal control system is needed. To run businesses that fully engage ESG factors, companies are required to look for environment issues or risks, or social or human rights problems in advance. Moreover, it is necessary to build a system capable of confirming the full compliance of ESG elements at each management step. In this regard, building an internal control system is indeed of crucial importance.



Does South Korea need Corporate Social Responsibility? The Impact of CSR on National Competitiveness

Simon Childs

In recent years, the concept of Corporate Social Responsibility (CSR) has enjoyed increased attention by managers, academics, consumers, NGOs, and policymakers alike, thereby reflecting the advent of a new business paradigm that highlights the need to develop frameworks for ensuring socially and environmentally sustainable growth¹. In this vein, Bhattacharya and Sen report that more than 80% of the Fortune 500 companies already address CSR issues and regularly communicate the extent of their social engagement.² This development may indicate that the concept of CSR has become not only an ethical but also an economic standard in today's business practice.³ ⁴ From a managerial perspective, the basic assumption is that investment in CSR engagements serves to attain a company's economic goals.⁵ ⁶ ⁷ ⁸ The underlying rationale suggests that there

¹ Van Marrewijk, M. (2003). Concepts and Definitions of CSR and Corporate Sustainability: Between Agency and Communion. *Journal of Business Ethics*, 44, 95-103.

² Bhattacharya, C.B., & Sen, S. (2004). Doing Better at Doing Good: When, why, and how consumers respond to corporate social initiatives. *California Management Review*, 47(1), 9-24.

³ Carroll, A.B. (1999). Corporate Social Responsibility Evolution of a Definitional Construct. *Business & Society*, 38(3), 268-295.

⁴ Freeman, R.E. (1988). A Stakeholder Theory of the Modern Corporation. Perspectives in Business Ethics, 144.

⁵ Aupperle, K.E., Carroll, A. B., & Hatfield, J.D. (1985). An Empirical Examination of the Relationship between Corporate Social Responsibility and Profitability. *Academy of Management Journal*, 28(2), 446-463.

⁶ Luo, X., & Bhattacharya, C.B. (2009). The Debate over Doing Good: Corporate Social Performance, Strategic Marketing Levers, and Firm-Idiosyncratic Risk. *Journal of Marketing*, 73, 198-213.

⁷ McGuire, J.B., Sundgren, A., & Schneeweis, T. (1988). Corporate Social Responsibility and Firm Financial Performance. *Academy of Management Journal*, 31(4), 854-872.

Does South Korea need Corporate Social Responsibility? The Impact of CSR on National Competitiveness

is a relationship between CSR engagement and the competitiveness of firms. For example, Turban and Greening argue that a reputation for a strong corporate social performance positively relates to an organization's ability to attract valuable human resources, which in turn constitutes a competitive advantage over competitors in the labor market.⁹ And Porter and Kramer posit that corporate philanthropy provides a competitive advantage because strategic donations help to improve the competitive context of a company, e.g., through the improved availability of natural resources or productivity due to the attraction of skilled workers.¹⁰

The bulk of these studies conceptualize the relationship between CSR and competitiveness at the microeconomic firm level. However, little understanding exists as to whether CSR has further implications for improving the competitiveness of a society and/or an entire nation at the macroeconomic level.^{11 12} This lack of data is surprising given the fact that politicians and policymakers increasingly turn to political measures to foster CSR deployment, such as the European Commission's late Europe 2020 strategy for smart, sustainable, and inclusive growth.¹³

Indeed, these proposals are seemingly put forth without a sound understanding of the relationship between CSR and the competitiveness of a nation; the European Commission admittedly states that "the principal focus is on how CSR might contribute to competitiveness at the level of the individual

⁸ Varadarajan, P. R., & Menon, A. (1988). Cause-Related Marketing: A Coalignment of Marketing Strategy and Corporate Philanthropy. *Journal of Marketing* (3), 55-78.

⁹ Turban, D.B., & Greening, D.W. (1997). Corporate Social Performance and Organizational Attractiveness to Prospective Employees. *Academy of Management Journal*, 40(3), 658-672.

¹⁰ Porter, M.E., & Kramer, M.R. (2002). The Competitive Advantage of Corporate Philanthropy. *Harvard Business Review*, 80(12), 56-69.

¹¹ Boulouta, I., & Pitelis, C.N. (2014). Who Needs CSR? The Impact of Corporate Social Responsibility on National Competitiveness. *Journal of Business Ethics*, 119(3), 349-364.

¹² MacGillivray, A., Begley, P., & Zadek, S. (2007). *The State of Responsible Competitiveness 2007*. London: AccountAbility.

¹³ EC. (2011). COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE COUNCIL, THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE AND THE COMMITTEE OF THE REGIONS: A renewed EU strategy 2011-14 for Corporate Social Responsibility COM(2011) 681 final.

enterprise. The links between CSR and macro-level competitiveness are also explored, although there has been comparatively little research at this level of analysis¹⁴. Therefore, in order to address the politically sensitive question as to whether firms should be politically, or even legally, *encouraged* to engage in CSR practices and thus direct political and bureaucratic resources to such endeavors, an empirically tested conceptualization of the relationship between the aggregated level of national CSR performance and national competitiveness appears to be urgently required. This is especially the case for South Korea: while there have been a few conceptual models derived from datasets focusing on European countries presented¹⁵, there is no similar study that reports on data obtained from a South Korean sample. This research gap, however, conflicts with recent developments in the political agenda of South Korea's economic policy debates: CSR has been widely discussed among Korean practitioners, policymakers, and NGOs. In addition, German political foundations, with the Konrad-Adenauer-Foundation (KAS) standing at the forefront, have made significant efforts to engage the involved parties in a scientifically and politically rigorous debate, one which may ultimately foster CSR in South Korea.¹⁶ This engagement by the KAS reflects the strong interest held by South Korean leaders in understanding the feasibility of implementing CSR-related standards into current economic policies.

Accordingly, this study seeks to answer the following question: does CSR affect the national competitiveness of South Korea? In order to answer this question, a conceptualized link between CSR and national competitiveness is proposed here based on literature in economics, strategic management, and CSR. Then, an empirical analysis is presented by drawing upon a sample of 20 leading South Korean companies in terms of their CSR engagements. This analysis subsequently contributes to the existing body of literature by proposing a conceptual model that links CSR and competitiveness by exclusively focusing on South Korean.

¹⁴ EC. (2008). European Competitiveness Report 2008, p.106. Luxembourg.

¹⁵ Boulouta, I., & Pitelis, C.N. (2014). Who Needs CSR? The Impact of Corporate Social Responsibility on National Competitiveness. *Journal of Business Ethics*, 119(3), 349-364.

¹⁶ The Korea Office of the Konrad-Adenauer-Foundation has been collaborating with academics, NGOs, and policymakers to bring forward the debate about CSR in South Korea for years. As a result, an extensive body of publications as and conference contributions exists today.

Does South Korea need Corporate Social Responsibility? The Impact of CSR on National Competitiveness

To conclude, the practical value offered by this study is then deemed relevant for those engaged in the numerous political and legal discussions pertaining to the question as to whether CSR is capable of contributing to South Korea's competitiveness by providing a feasible rationale to politically foster its enactment.

Conceptual Framework

Conceptualizing Corporate Social Responsibility

The concept of CSR has long been the object of academic discussions. An intense debate pertaining to the question whether a company's responsibilities stretch beyond profit making and maximizing shareholder value began when economist Howard Bowen, widely regarded as the first scholar to discuss a company's responsibilities, stated that the obligation of a businessman was "to pursue those policies, to make those decisions, or to follow those lines of action which are desirable in terms of the objectives and values of our society."¹⁷ A major critic of this claim was Milton Friedman, who prominently asserted that a firm's (social) responsibilities do not "go beyond serving the interest of their stockholders or their members."^{18 19} As a result of the process of discussing CSR, numerous definitions, concepts, and theories related to CSR thinking have emerged.²⁰ In this vein, Carroll stated that "for a definition of social responsibility to fully address the entire range of obligations business has to society, it must embody the economic, legal, ethical, and discretionary categories of business performance."²¹ In addition, by proclaiming that companies should accept their role as corporate citizens, Carroll further proposed a four-dimensional pyramid that incorporates economic responsibilities as a building block on which the other three layers are built, including: legal responsibilities

¹⁷ Bowen, H.R. (1953). *Social Responsibilities of the Businessman*, 6: Harper & Brothers.

¹⁸ Friedman, M. (1962). *Capitalism and Freedom*: University of Chicago Press.

¹⁹ Friedman, M., & Friedman, R. D. (2002). *Capitalism and freedom* (40th anniversary ed.), 133. Chicago: University of Chicago Press.

²⁰ Dahlsrud, Alexander. (2008). How corporate social responsibility is defined: an analysis of 37 definitions. *Corporate Social Responsibility and Environmental Management*, 15(1), 1-13.

²¹ Carroll, A.B. (1979). A Three-Dimensional Conceptual Model of Corporate Performance, 499. *Academy of Management Review*, 4, 497-505.

(“to obey the law”), ethical responsibilities (“do what is right, just, and fair, and to avoid or minimize harm to stakeholders”), and philanthropic responsibilities (“to contribute financial and human resources to the community and to improve the quality of life”).²²

A similar concept was introduced by Freeman, who embraced the main tenet of CSR thinking – that companies have responsibilities that go beyond the legal and economic argument to solely pursue the interests of its shareholders. Instead, he argued that socially responsible firms not only take into account their shareholders, but also consider their stakeholders. Accordingly, to answer the questions “in whose interest and for whose benefit the modern corporation should be governed”²³, Freeman laid out a conceptual framework that explicitly recognizes the importance of managing relationships both with a firm’s shareholders and with stakeholders including employees, financiers, customers, employees, and communities. As such, stakeholders have been defined as: “persons or groups with legitimate interests in procedural and/or substantive aspects of corporate activity (and) are identified by their interests in the corporation, whether the corporation has any corresponding functional interest in them”²⁴; “those groups who have a stake in or claim on the firm [···], including suppliers, customers, employees, stockholders, and the local community, as well as management in its role as agent for these”²⁵; “groups and individuals [···] each with (a) the power to affect the firm’s performance and/or (b) a stake in the firm’s performance”²⁶; and “persons or groups that have, or claim, ownership, rights, or interests in a corporation and its activities, past, present, or future”, where primary stakeholders continuously participate in the corporation’s operations and essential for its survival (e.g. shareholders, investors, or employees, or the public), and secondary stakeholders who

²² Carroll, A.B. (1991). The Pyramid of Corporate Social Responsibility: Toward the Moral Management of Organizational Stakeholders, 42. *Business Horizons*, 39-48.

²³ Freeman, R.E. (1988). A Stakeholder Theory of the Modern Corporation, 39. *Perspectives in Business Ethics*, 144.

²⁴ Donaldson, T., & Preston, L.E. (1995). The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications, 67. *Academy of Management Review*, 20(1), 65-91.

²⁵ Freeman, R.E. (1988). A Stakeholder Theory of the Modern Corporation, 39. *Perspectives in Business Ethics*, 144.

²⁶ Jones, T.M. (1995). Instrumental Stakeholder Theory: A Synthesis of Ethics and Economics, 407. *Academy of Management Review*, 20(2).

Does South Korea need Corporate Social Responsibility? The Impact of CSR on National Competitiveness

“influence, affect, or are influenced or affected, by the corporation”(e.g., media or special interest groups)²⁷. In order to advance stakeholder theory, Donaldson and Preston pointed out important distinctions of stakeholder concepts by formulating four central theses, reflecting distinct approaches towards stakeholder theory.²⁸ First, they posited that stakeholder theory is descriptive, serving to align models of a modern corporation and its actual state. Second, they argue that stakeholder theory is instrumental for establishing and examining relationships between stakeholder management practices and corporate performance. Third, they argue that stakeholder theory is normative, serving to align an ethical framework that seeks to reconcile various stakeholders with legitimate interests in the corporate activities. Fourth, they argue that stakeholder theory is managerial, as it serves to derive recommendations regarding attitudes, structures, and practices that originate from cause-effect relationship predictions. In line with the instrumental/strategic view of CSR, i.e., benefits for both business and society, Hopkins explicitly posits that the aim of CSR at the macro-level should be “to create higher and higher standards of living while preserving the profitability of the corporation, for people both within and outside the corporation.”²⁹

In addition to CSR definitions that emphasize the firm-view at the micro-level, there are definitions that emphasize the aim of CSR at the macro-level. The World Business Council for Sustainable Development defines CSR as “a continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large.”³⁰ The German Government follows the definition of the European Commission and defines CSR as a system of “companies, organizations and institutions that voluntarily assume social responsibility — above and beyond their legal obligations [...] whereby companies integrate social and environmental

²⁷ Clarkson, M.B.E. (1995). A Stakeholder Framework for Analyzing and Evaluating Corporate Social Performance, 106-107. *Academy of Management Review*, 20(1), 92-117.

²⁸ Donaldson, T., & Preston, L.E. (1995). The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications, 67. *Academy of Management Review*, 20(1), 65-91.

²⁹ Hopkins, M. (2003). *The Planetary Bargain - CSR matters*, 1. Earthscan: London

³⁰ <http://www.wbcsd.org/work-program/business-role/previous-work/corporate-social-responsibility.aspx> (06-01-2014)

concerns in their business operations and in their interaction with their stakeholders on a voluntary basis”³¹

All these definitions include the common suggestion that CSR refers to businesses assuming and fulfilling responsibilities that go beyond mere profit-making, with the aim to enhance social objectives, such as sustainable economic development, quality of life, and increasing the national standard of living, amongst many others. In this study, and in line with the above broad definition of CSR, the impact of CSR at the national level is tested.

Conceptualizing Competitiveness

The concept of competitiveness originates from the analysis of firms, and is used at the national level to evaluate the effectiveness of economic policies. The World Economic Forum (WEF) defines competitiveness as “the set of institutions, policies and factors that determine the level of productivity of a country”³². According to Krugman, the growth rate of domestic productivity equals the growth rate of national living standards.³³ Similarly, the European Commission has defined competitiveness at the macro-economic level as “a sustained rise in the standards of living”³⁴. Aiginger notices a convergence towards a core definition as “the ability of a country or location to create welfare”³⁵. This broad definition of competitiveness contains an “outcome evaluation” of competitiveness (e.g., welfare or social safety) that can be measured by indicators such as per capita income, Human Development Index, or happiness.

In line with the above definitions of competitiveness, this study focuses on

³¹ Federal-Ministry-of-Labour-and-Social-Affairs. (2014). CSR in Germany. Retrieved 13.06.2014, from <http://www.csr-in-deutschland.de/en/about-csr/what-is-csr.html>

³² Schwab, K. (Ed.). (2009). The global competitiveness report 2009-2010, p.4. Geneva: World Economic Forum.

³³ Krugman, P. (1994): Does third world growth hurt first world prosperity? *Harvard Business Review*.

³⁴ EC. (2008). European Competitiveness Report 2008, 15. Luxembourg.

³⁵ Aiginger, K. (2006). Competitiveness: From a dangerous obsession to a welfare creating ability with positive externalities, 161. *Journal of Industry, Competition and Trade*, 6, 161-177.

Does South Korea need Corporate Social Responsibility? The Impact of CSR on National Competitiveness

national living standards, as measured by per capita GDP at purchasing power parities. Despite the fact that this is only one among many possible measures of competitiveness, the ready availability of data pertaining to the GDP per capita (GDPC) has led us to use this measure as a proxy for national competitiveness. In addition, the GDPC reflects the aggregate productivity of a country, which constitutes a measure often deployed by prominent researchers such as Krugman³⁶ and Porter³⁷.

The relationship between CSR and Competitiveness

The majority of CSR-related studies have focused on the relationship between CSR and business competitiveness. Within this research stream it has been argued that firms engage in “strategic” CSR^{38 39}, which may result in higher levels of financial and social performance.⁴⁰ More specifically, it has been suggested that CSR has a positive effect on a firm’s competitiveness, as evidenced by factors such as by reduced costs⁴¹, value creation through new market entries^{42 43}, fostering human resource performance and helping attract new talent^{44 45}, building better relations with employees, customers, suppliers,

³⁶ Krugman, P. (1994). Competitiveness, a dangerous obsession. *Foreign Affairs*, 73, 28-44.

³⁷ Porter, M.E. (1990). *The competitive advantage of nations*. Basingstoke: Macmillan Press.

³⁸ Baron, D.P. (2001). Private politics, corporate social responsibility, and integrated strategy. *Journal of Economics & Management Strategy*, 10(1), 7-45.

³⁹ McWilliams, A., & Siegel, D. (2001). Corporate Social Responsibility: A Theory of the Firm Perspective. *Academy of Management Review*, 26(1), 117-127.

³⁹ McWilliams, A., & Siegel, D. (2001). Corporate Social Responsibility: A Theory of the Firm Perspective. *Academy of Management Review*, 26(1), 117-127.

⁴⁰ Husted, B., & de Jesus Salazar, J. (2006). Taking Friedman seriously: Maximising profit and social performance. *Journal of Management Studies*, 43, 75-91.

⁴¹ Jenkins, H. (2006). Small business champions for corporate social responsibility. *Journal of Business Ethics*, 67, 241-256.

⁴² Porter, M.E., & Kramer, M.R. (2002). The Competitive Advantage of Corporate Philanthropy. *Harvard Business Review*, 80(12), 56-69.

⁴³ Pralahad, C. K. (2004). *Fortune at the bottom of the pyramid: Eradicating poverty through profits*. Upper Saddle River, NJ: Wharton School Publishing.

⁴⁴ Cochran, P. L. (2007). The evolution of corporate social responsibility. *Business Horizons*, 50, 449-454.

⁴⁵ Turban, D.B., & Greening, D.W. (1997). Corporate Social Performance and Organizational

and communities⁴⁶, and lastly, by improving corporate reputation, which may be rewarded by stock market investors.⁴⁷

In order to scale the impact of CSR engagement from the firm- to the macro-level, it has been suggested to align CSR with national competitiveness goals, hence embedding it into the wider economy. For this purpose, MacGillivray et al. coined the term “responsible competitiveness,” which they define as “an economy’s productivity being enhanced by businesses taking explicit account of their social, economic, and environmental performance”.⁴⁸ The concept of embedding CSR into the wider economy was also supported by the European Union (EU). The European Commission has theoretically examined the impact of CSR on national competitiveness, and has subsequently suggested a positive link, mainly through to indirect impact on competitiveness factors such as social capital, innovation, and human capital.⁴⁹

Following this line of argument, the research hypothesis of this study can be formally stated as follows: the higher the levels of South Korea’s aggregate level of firm CSR, the higher South Korea’s national competitiveness.

Empirical Analysis

Sample

To measure CSR, performance data were obtained from RobecoSAM, S&P Dow Jones Indices, and the Korea Productivity Center, which in cooperation composed the Dow Jones Sustainability Index Korea (DJSIK) based on its annual Corporate Sustainability Assessment. The Index is based on economic,

Attractiveness to Prospective Employees. *Academy of Management Journal*, 40(3), 658-672.

⁴⁶ Sen, S., & Bhattacharya, C. B. (2001). Does doing good always lead to doing better? Consumer reactions to corporate social responsibility. *Journal of Marketing Research*, 38(2), 225-244.

⁴⁷ Brown, B. (1998). Do stock market investors reward companies with reputations for social performance? *Corporate Reputation Review*, 1(3), 271-280.

⁴⁸ MacGillivray, A., Begley, P., & Zadek, S. (2007). *The State of Responsible Competitiveness 2007*, 13. London: AccountAbility.

⁴⁹ EC. (2008). *European Competitiveness Report 2008*. Luxembourg.

Does South Korea need Corporate Social Responsibility? The Impact of CSR on National Competitiveness

environmental, and social components and includes the top 30% of the 200 largest South Korean Companies in the S&P Global Broad Market IndexSM. Macroeconomic data were obtained from various online databases (Table 1). Because the DJSIK was launched in 2009, the observations were analyzed on a quarterly basis from 2009 to 2013, resulting in a total of 20 observations.

Measures

National Competitiveness: The dependent variable, national competitiveness, was measured using GDP per capita (GDPC), which is a widely deployed measure used in economic performance analyses. However, because GDPC data were not available on a quarterly basis, this measure was constructed by dividing the quarterly GDP statistics by the annual population data obtained from databases provided by the Ministry of Strategy and Finance and Korea Statistics (KOSTAT).

Corporate Social Responsibility Performance: The independent variable, an aggregate of the national Corporate Social Responsibility Performance, was measured using the DJSIK. This metric is widely adopted in CSR-related studies and is thus considered a valid measure for the proposed model. The DJSIK seeks to capture the CSR performance of leading Korean companies in terms of their social, economic, and environmental performance. Because DJSIK scores were not available on a quarterly basis, averages were calculated for each quarter from Quarter 1 2009 through Quarter 4 2013, based on the daily DJSIK data.

Innovation and Cost Advantage: In order to control for extraneous effects, the control variables of Innovation and Cost Advantage were included in the model following the procedures established by Boulouta and Pitelis.⁵⁰ Innovation was measured in terms of the number of registered patents per quarter, using data obtained from the Korean Intellectual Property Service (KISPO). In turn, the control variable Cost Advantage was measured based

⁵⁰ Boulouta, I., & Pitelis, C.N. (2014). Who Needs CSR? The Impact of Corporate Social Responsibility on National Competitiveness. *Journal of Business Ethics*, 119(3), 349-364.

on the Unit Labor Cost Index, as published on a quarterly basis by the Bank of Korea. Both measures are considered robust, as they are frequently used in similar studies to measure Innovation and Unit Cost economies.

Methodology & Results

For the data analysis, the following regression model was applied:

$$Y_i = \beta_1 X_{i1} + \beta_2 X_{i2} + \beta_3 X_{i3} + \varepsilon, i=1, \dots, N$$

where Y_{it} is the dependent variable, measured in per capita GDP (Y_i), X_1 represents the independent variable CSR Performance, and β_1 its respective regression coefficient. The control variable Innovation is represented by X_2 , with β_2 as its respective regression coefficient. Likewise, X_3 and β_3 represent the control variable Cost advantage and its regression coefficient; the error term is represented by ε .

In order to test Hypothesis 1, the regression model was tested using tested using SPSS. The descriptive statistics and correlations are shown in Tables 1 and 2, respectively. As shown in Table 3, a positive and significant correlation between national the CSR Performance and National Competitiveness ($b = 0.005, p = 0.001$) was found, which in turn confirms the relationship predicted in the research hypothesis. In addition, only the control variable Innovation was found to be a significant predictor for National Competitiveness ($p = 0.001$), whereas Cost Advantage did not display a significant effect on the dependent variable.

Table 1: Descriptive Statistics

	Mean	Std. Deviation	N
National Competitiveness	2.9575	.90419	20
CSR Performance	1457.0655	192.58697	20
Innovation	22498.3500	7952.45621	20
Cost Advantage	99.1350	24.99678	20

Does South Korea need Corporate Social Responsibility? The Impact of CSR on National Competitiveness

Table 2: Correlations

		National Competitiveness	CSR Performance	Innovation	Cost Advantage
Pearson Correlation	National Competitiveness	1.000	.887	.252	-.118
	CSR Performance	.887	1.000	.582	-.184
	Innovation	.252	.582	1.000	-.150
	Cost Advantage	-.118	-.184	-.150	1.000
Sig. (1-tailed)	National Competitiveness	.	.000	.142	.311
	CSR Performance	.000	.	.004	.218
	Innovation	.142	.004	.	.264
	Cost Advantage	.311	.218	.264	.
N	National Competitiveness	20	20	20	20
	CSR Performance	20	20	20	20
	Innovation	20	20	20	20
	Cost Advantage	20	20	20	20

Table 3: Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B	
	B	Std. Error	Beta			Lower Bound	Upper Bound
1 (Constant)	-3.820	.706		-5.413	.000	-5.316	-2.324
CSR Performance	.005	.000	1.124	11.065	.000	.004	.006
Innovation	-4.520E-5	.000	-.398	-3.938	.001	.000	.000
Cost Advantage	.001	.003	.030	.359	.724	-.005	.007

a. Dependent Variable: National Competitiveness

Discussion and Limitations

The results suggest that the aggregated CSR performance of South Korean businesses can contribute to increased levels of national competitiveness. This finding is in line with studies that have previously conceptualized and tested the relationship between national CSR performance and national competitiveness, though which have mainly focused on Western countries.^{51 52}

In terms of practical implications, the positive relationship between the aggregated CSR performance of Korean businesses and the national competitiveness of South Korea may be important for policy makers and political interest groups alike; from a political perspective it may seem appropriate to provide voters, legislature bodies, and business managers with a sound justification for any step taken towards *coercive* policies aimed to foster CSR among Korean businesses. Despite the fact that there has been a rising interest among Korean politicians and other stakeholders in discussing representative CSR case studies on both business and political levels, questions may remain whether copying a blueprint from Western countries presents a feasible solution for the Korean case, or whether such an endeavor would merely squander available resources (e.g., time resources, political resources, political agenda-setting, etc.). The findings presented in this study, however, do not confirm this scenario. On the contrary, given the perspective that South Korea's national CSR performance positively impacts its national competitiveness, it appears feasible to take action towards implementing CSR-related economic policies to *encourage* firms to engage in CSR practices, thereby highlighting the importance to debate and learn about cases and experiences from countries that have a richer history of political CSR records. In line with the findings of this study, a political expansion of CSR concepts among and within South Korean firms may further increase Korea's national competitiveness in the future.

⁵¹ Boulouta, I., & Pitelis, C.N. (2014). Who Needs CSR? The Impact of Corporate Social Responsibility on National Competitiveness. *Journal of Business Ethics*, 119(3), 349-364.

⁵² MacGillivray, A., Begley, P., & Zadek, S. (2007). *The State of Responsible Competitiveness 2007*. London: AccountAbility.

Does South Korea need Corporate Social Responsibility? The Impact of CSR on National Competitiveness

Limitations of this study that may inspire further future research in order to improve validity, are as follows. First, the DJSIK data generally focus on the performance of a small sample of relatively big and profitable firms that already pursue sophisticated CSR. A larger sample of firms that include small- and medium-sized companies (SMEs) may increase the generalizability of results. In addition, the measure of national CSR performance does not reflect the level of CSR practices across the country. The results presented here are based on the impact of a few “CSR champions” in terms of national competitiveness. According to competitiveness literature, even the impact of single large companies on the economy as a whole can be significant. This is likely the case for South Korea, whose economy is dominated by only a handful of large conglomerates, locally referred to as *chaebol* (e.g., Samsung or Hyundai). Therefore, the impact of small-scale South Korean companies on national competitiveness as measured by GDP per capita could yield results different from those presented in this study.

In line with these limitations, additional research should focus on 1) obtaining a larger sample of firms, including SMEs, and 2) deploy measures for national competitiveness that would improve consistency. Despite these limitations, this study contributes towards the critical question whether CSR has an impact on the South Korean economy as a whole. It provides support for the strategic view of CSR towards delivering a shared value for improving both business and society.

Literature

- Aiginger, K. (2006). Competitiveness: From a dangerous obsession to a welfare creating ability with positive externalities. *Journal of Industry, Competition and Trade*, 6, 161-177.
- Baron, D. P. (2001). Private politics, corporate social responsibility, and integrated strategy. *Journal of Economics & Management Strategy*, 10(1), 7-45.
- Bhattacharya, C.B., & Sen, S. (2004). Doing Better at Doing Good: When, why, and how consumers respond to corporate social initiatives. *California Management Review*, 47(1), 9-24.
- Boulouta, I., & Pitelis, C.N. (2014). Who Needs CSR? The Impact of Corporate Social Responsibility on National Competitiveness. *Journal of Business Ethics*, 119(3), 349-364.
- Bowen, H.R. (1953). *Social Responsibilities of the Businessman*: Harper & Brothers.
- Brown, B. (1998). Do stock market investors reward companies with reputations for social performance? *Corporate Reputation Review*, 1(3), 271-280.
- Carroll, A.B. (1979). A Three-Dimensional Conceptual Model of Corporate Performance. *Academy of Management Review*, 4, 497-505.
- Carroll, A.B. (1991). The Pyramid of Corporate Social Responsibility: Toward the Moral Management of Organizational Stakeholders. *Business Horizons*, 39-48.
- Carroll, A.B. (1999). Corporate Social Responsibility Evolution of a Definitional Construct. *Business & Society*, 38(3), 268-295.
- Clarkson, M.B.E. (1995). A Stakeholder Framework for Analyzing and Evaluating Corporate Social Performance. *Academy of Management Review*, 20(1), 92-117.
- Cochran, P. L. (2007). The evolution of corporate social responsibility. *Business Horizons*, 50, 449-454.
- Dahlsrud, Alexander. (2008). How corporate social responsibility is defined: an analysis of 37 definitions. *Corporate Social Responsibility and Environmental Management*, 15(1), 1-13. doi: 10.1002/csr.132
- Donaldson, T., & Preston, L.E. (1995). The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications. *Academy of Management Review*, 20(1), 65-91.
- EC. (2008). *European Competitiveness Report 2008*. Luxembourg.
- EC. (2011). *Communication from the Commission to the European Parliament*,

Does South Korea need Corporate Social Responsibility? The Impact of CSR on National Competitiveness

the Council, the European Economic and Social Committee and the Committee of the Regions: A renewed EU strategy 2011-14 for Corporate Social Responsibility. *COM(2011) 681 final*.

Federal-Ministry-of-Labour-and-Social-Affairs. (2014). CSR in Germany. Retrieved 13.06.2014, from <http://www.csr-in-deutschland.de/en/about-csr/what-is-csr.html>

Freeman, R.E. (1988). A Stakeholder Theory of the Modern Corporation. *Perspectives in Business Ethics*, 144.

Friedman, M. (1962). *Capitalism and Freedom*. University of Chicago Press.

Friedman, M., & Friedman, R. D. (2002). *Capitalism and freedom* (40th anniversary ed.). Chicago: University of Chicago Press.

Hopkins, M. (2003). The planetary bargain: Corporate social responsibility matters. London: Earthscan.

Husted, B., & de Jesus Salazar, J. (2006). Taking Friedman seriously: Maximising profit and social performance. *Journal of Management Studies*, 43, 75-91.

Krugman, P. (1994). Competitiveness, a dangerous obsession. *Foreign Affairs*, 73, 28-44.

Jenkins, H. (2006). Small business champions for corporate social responsibility. *Journal of Business Ethics*, 67, 241-256.

Jones, T.M. (1995). Instrumental Stakeholder Theory: A Synthesis of Ethics and Economics. *Academy of Management Review*, 20(2).

MacGillivray, A., Begley, P., & Zadek, S. (2007). *The State of Responsible Competitiveness 2007*. London: AccountAbility.

Porter, M. E. (1990). *The competitive advantage of nations*. Basingstoke: Macmillan Press.

Porter, M.E., & Kramer, M.R. (2002). The Competitive Advantage of Corporate Philanthropy. *Harvard Business Review*, 80(12), 56-69.

Porter, M. E., & Kramer, M. R. (2006). Strategy and society: The link between competitive advantage and corporate social responsibility. *Harvard Business Review*, 84, 78-92.

Pralahad, C. K. (2004). *Fortune at the bottom of the pyramid: Eradicating poverty through profits*. Upper Saddle River, NJ: Wharton School Publishing.

Schwab, K. (Ed.). (2009). *The global competitiveness report 2009-2010*. Geneva: World Economic Forum.

Sen, S., & Bhattacharya, C. B. (2001). Does doing good always lead to doing better? Consumer reactions to corporate social responsibility. *Journal of*

Marketing Research, 38(2), 225-244

Turban, D.B., & Greening, D.W. (1997). Corporate Social Performance and Organizational Attractiveness to Prospective Employees. *Academy of Management Journal*, 40(3), 658-672.

Van Marrewijk, M. (2003). Concepts and Definitions of CSR and Corporate Sustainability: Between Agency and Communion. *Journal of Business Ethics*, 44, 95-103.

Williams, A., & Siegel, D. (2001). Corporate social responsibility: A theory of the firm perspective. *Academy of Management Review*, 26, 117-127.

Does South Korea need Corporate Social Responsibility? The Impact of CSR on National Competitiveness

Appendix

Table 1: Descriptive Statistics

	Mean	Std. Deviation	N
National Competitiveness	2.9575	.90419	20
CSR Performance	1457.0655	192.58697	20
Innovation	22498.3500	7952.45621	20
Cost Advantage	99.1350	24.99678	20

Table 2: Correlations

		National Competitiveness	CSR Performance	Innovation	Cost Advantage
Pearson Correlation	National Competitiveness	1.000	.887	.252	-.118
	CSR Performance	.887	1.000	.582	-.184
	Innovation	.252	.582	1.000	-.150
	Cost Advantage	-.118	-.184	-.150	1.000
Sig. (1-tailed)	National Competitiveness	.	.000	.142	.311
	CSR Performance	.000	.	.004	.218
	Innovation	.142	.004	.	.264
	Cost Advantage	.311	.218	.264	.
N	National Competitiveness	20	20	20	20
	CSR Performance	20	20	20	20
	Innovation	20	20	20	20
	Cost Advantage	20	20	20	20

Table 3: Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B	
	B	Std. Error	Beta			Lower Bound	Upper Bound
1 (Constant)	-3.820	.706		-5.413	.000	-5.316	-2.324
CSR Performance	.005	.000	1.124	11.065	.000	.004	.006
Innovation	-4.520E-5	.000	-.398	-3.938	.001	.000	.000
Cost Advantage	.001	.003	.030	.359	.724	-.005	.007

a. Dependent Variable: National Competitiveness



About the authors

Simon Childs

MSc (Hanyang University), currently pursuing his PhD degree; former Junior Researcher in the Korea Office of the Konrad Adenauer Foundation

Norbert Eschborn

Resident Representative to Korea, Konrad Adenauer Foundation

Jeong Jae-Kyu

Research Coordination Director, Senior Research Fellow, Korea Corporate Governance Service

Kwak Kwan-Hoon

Professor, Department of Police Administration and Law, Sunmoon University

Kwon Sung-Sik

Korean Standards Association

Sung Jin-Young

Research Consultant, Center for Sustainability Management, Korea Standards Association

Yang Chun-Seung

Standing Director, Korea Sustainability Investing Forum, Visiting Lecturer Seoul National University of Science & Technology