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Financial Law Developments in Taiwan 2005/2006—Corporate Governance, Offshore Fund Regulation and Tax Law Reforms

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This article provides a brief account on, from the beginning of 2005 to the first quarter of 2006, five major pieces of new enactments/regulations that are of particular relevance to the operation of Taiwan public companies and capital markets. They are the 2005 Amendment to Company Law and 2006 Amendment to Securities Exchange Act, Rules of Supervision for Offshore Funds, and, in the tax-law category, the Safe Harbor Rule, which formed part of the transfer pricing regulation, and the Income Basic Tax Act, which governed alternative minimum tax issues.

Corporate governance reform

The 2005 Amendment to Company Law and 2006 Amendment to Securities Exchange Act (coming into effect in June 2005 and January 2006 respectively; collectively, the 2005-06 Reforms) represent a major foothold gained in Taiwan's ongoing corporate governance reform. They have significantly changed Taiwan public corporations' activities both within the boardroom and beyond. Four sets of new corporate governance measures were introduced by the 2005-06 Reforms, which can be divided according to their underlying policy objectives.

Upholding shareholder activism

The Company Law Amendment introduced two new types of shareholder rights—the rights to propose and to nominate directors. Alongside the board, minority shareholders (holding 1% or more of the outstanding shares) are now eligible to initiate proposals to be addressed at regular shareholder meetings and to nominate directors in their own right. Further, to exercise their voting rights, the shareholder's personal presence is no longer required, and they could now vote by sending a written notice or by way of electronic transmission.

Promoting independent boards

In terms of board composition, one major change brought by the new securities law to Taiwan's publicly traded corporations is the mandatory requirement for independent directors. From January 1 2007 onwards, publicly traded corporations with paid-in capital of NT\$50 billion or more, all financial holding companies, and other

specified financial firms have to appoint to their boards at least two (or more if by two the ratio is less than one-fifth of the total board members) independent directors. On the individual basis, the independent director's mandate goes no further than "making enquiries" about certain major corporate policies and executive director's self-interest deals. On the collective basis, however, the new securities law prescribes a more concrete mandate that only upon an audit committee (to be comprised entirely of all independent directors) approving the corporation's annual and semi-annual financial reports could they reach the board level for approval.

Streamlining board's responsibilities

On a functional note, the new securities law added a monitoring overtone (over the senior managers) to the board's general managerial undertakings by establishing a division of responsibility between the board and the senior managers. The law prohibits the board from delegating certain major corporate decisions, but restricts them to being decided at the board level. These decisions include adoption and amendment of internal control systems, handling procedures for major financial activities (such as asset acquisition/disposal, derivatives trading and extension of loans), and appointment/discharge of attesting CPA and chief internal auditor officer.

Enhancing integrity of financial statements

The misrepresentation/nondisclosure liability clause of the new securities law pertaining to financial reports/documents is probably the single amendment wielding the strongest deterrent effect on corporate insiders. It provides that, when the essential content of financial reports or relevant financial documents that has been publicly disclosed or filed with the competent authority contains misrepresentations or nondisclosures, the chairman and general manager of the issuing corporation shall bear liability for damages suffered by the *bona fide* purchasers, sellers, or holders of securities. It is notable that this liability will be sustained even if the chairman/general manager can demonstrate that they have exercised all due diligence and had legitimate cause to believe that the reports or documents contained no such misrepresentations or nondisclosures.

Offshore funds regulation

In 2004, the passage of the Securities Investment Trust and Consulting Law (SITCL) for the first time gave offshore funds a statutory basis to conduct public offering or private placement of securities in Taiwan. Authorized by the SITCL and built on its framework, Taiwan's Financial Supervisory Commission, the economy's financial industry/market watchdog, adopted in August 2005 the Rules of Supervision for Offshore Funds (the RSOF), stipulating the operating rules for offshore funds and their local partners.

Public offering

The RSOF laid down a set of master-agent centered regulatory requirements for the offshore fund's public offering. Offshore funds are required to appoint a qualified master agent who has passed the regulator's scrutiny for eligibility and who will be in charge of the funds' public offering and sales in Taiwan. The master agent is then responsible for, among others, preparing and delivering the offering prospectus, serving as the litigious agent for the fund in Taiwan, coordinating with the fund to provide the necessary and updated disclosures to Taiwan investors, and coordinating execution orders of investors or executing settlement on behalf of the fund, as the case may be. The master agent may further retain firms such as securities brokers, banks or trust companies as their sales agents for sales of offshore funds. The master agent shall appoint a custodian bank with a certain credit rating to keep custody of the assets of its customers. The master agent's above-mentioned undertakings would then be subject to the regulator's ongoing supervision.

Private placement

The RSOF also outlines the procedure for offshore funds to conduct private placement. In principle, private placement may only be directed toward financial institutions, or no more than 35 high net-worth individuals and corporations who satisfy certain eligibility criteria. In addition, appointing an agent institution is optional in private placement as apposed to a mandatory regulatory requirement in public offering.

Tax-law initiatives*Transfer pricing regulation and accompanying safe harbour rule*

The adoption of the Assessment Rules for Non-Arm's Length Transactions by Profit-seeking Enterprises in December 2004 saw a full transfer pricing report that was required of Taiwan's profit-seeking enterprises from the tax authority to substantiate an arm's length transfer pricing of "controlled transaction", entered into between the enterprise and its related entity.

In response to the industry outcry for the full-report being overly burdensome, a major relief came in December 2005, when the Standards on Applicable Amounts for Supplanting Transfer Pricing Report with Supporting Documentation (the Safe Harbour Rule) was promulgated by Taiwan's Ministry of Finance under which presenting only supporting documentation, which is substantially less burdensome than the full report submission, would be satisfactory enough for the tax authority to accept the transfer price. The applicability criteria of such tax safe harbor consist, among other things, of the target enterprise's income level. For example, where a Taiwan company's operating income and non-operating income in total fall into the below NT\$ 100 Million category, that is, into the safe harbor, the full transfer-pricing report would than be replaced by the pricing supporting documentation for submission for the controlled transaction at question.

Alternative minimum tax system

As an integral part of the overall efforts in confronting Taiwan's multi-faceted tax concessions, in particular those capital-gain related, to enhance fair taxation, the newly enacted Income Basic Tax Act (coming into effect on 1 January 2006) introduced a comprehensive alternative minimum tax (AMT) system. With the introduction of AMT, gains realized from Taiwanese securities and/or futures transactions, which were normally tax exempt, may now be exposed to AMT calculations.

Under the Income Basic Tax Act, AMT's tax base is referred to

as alternative minimum taxable income; and the minimum tax liability is calculated by subtracting the AMT tax rate to arrive at the AMT. The AMT tax rate for corporate taxpayers shall be no less than 10 % and no more than 12 %. If regular tax is greater or equal to AMT, regular tax shall be paid. Conversely, if regular tax falls below this minimum, the taxpayers shall make up the difference by paying the AMT instead.

Banking and project finance**Recommended firms****Tier 1**

Baker & McKenzie
Lee and Li
Russin & Vecchi
Tsar & Tsai Law Firm

Tier 2

Jones Day
LCS & Partners

Tier 3

Formosa Transnational
Liang & Associates
Preston Gates & Ellis Taiwan Commercial Law Offices
Yangming Partners

Capital markets**Recommended firms****Tier 1**

Baker & McKenzie
Jones Day
Lee and Li

Tier 2

LCS & Partners
Tsar & Tsai Law Firm

Tier 3

Chen & Lin
Lexcel Partners
Preston Gates & Ellis Taiwan Commercial Law Offices
Russin & Vecchi

Insolvency and restructuring

Recommended firms

Tier 1

Baker & McKenzie
Lee and Li
Tsar & Tsai Law Firm

Tier 2

Formosa Transnational
Formosan Brothers
Jones Day
Russin & Vecchi

Tier 3

Huang & Partners
LCS & Partners
Liang & Associates
Preston Gates & Ellis Taiwan Commercial Law Offices
Yangming Partners

Mergers and acquisitions

Recommended firms

Tier 1

Baker & McKenzie
Jones Day
Lee and Li
Lexcel Partners

Tier 2

LCS & Partners
Tsar & Tsai Law Firm

Tier 3

Chen & Lin
Formosa Transnational
Preston Gates & Ellis Taiwan Commercial Law Offices
Yangming Partners

Baker & McKenzie

Baker & McKenzie's Taipei office continues to be one of the most successful members of Baker & McKenzie's regional network. The banking and finance group is strong on lender representation, and more often than not can be found working on the more sizeable and complicated financings that come to the market. For example, the team helped Chinatrust Commercial Bank to arrange a complex NT\$8.3 billion (\$255 million) corporate bond and guarantee facility for Uni-President Enterprise, and also advised the International Commercial Bank of China on NT2 billion-worth of construction financing in relation to a private sector-operated public school dormitory. Mandates from borrowers, meanwhile, included representing EVA Airways on its \$233 million export credit agency-backed financing in the second half of 2005.

Capital markets highlights included acting as Taiwanese counsel to the issuer in connection with the \$538 million Nasdaq listing of Himax Technologies, and advising Powertech Technology on its \$115.7 million global depositary share offering made under Regulation S. The team showcased its securitization expertise this year on E-Sun's dual-tranche collateralized bond offering,

which adopted a master trust structure. E-Sun also turned to Baker & McKenzie for guidance on the issue of \$400 million-worth of European convertible bonds to Temasek.

The pickup in M&A activity has also benefited the firm. In one standout deal, Alex Chiang advised Nomura on its NT\$4 billion investment in Taishin Financial made via common shares and convertible preferred stock. At the time of writing the corporate team was busy advising on significant cross-border deals in the insurance and media sectors, scheduled to complete in late 2006.

The firm's best known-lawyer is Lindy Chern, a well-respected and prominent figure in the market. Banking partner Justin Liang and corporate expert Michael Wong also receive strong market recommendation.

Leading lawyers

Lindy Chern
Justin Liang
Michael Wong

Key contact partners

Justin Liang
Kevin Wang
Michael Wong

Chen & Lin

Since its establishment in 1992, Chen & Lin has carved out a well-developed niche advising technology companies in connection with their corporate finance transactions. Convertible bond issues have kept the firm busy in the past 12 months, the largest being United Microelectronics' issue of \$381.4 million convertible bonds. Chien-Chih Liu and his team also advised Epitech on a domestic convertible bond issue in January 2006, which was valued at NT\$1 billion (\$31 million).

The firm's capital markets expertise extends to local and cross-border equity offerings. Recent highlights include advising Pixart Imaging on its NT639 million listing on the Taiwan stock exchange, and being retained as Taiwanese adviser on Yorkey's Hong Kong initial public offering (IPO). Liu's team added to its international deal expertise this year by advising Goldman Sachs on AU Optronics' offering of American depositary shares on the New York Stock Exchange.

M&A activity has been similarly focused in the technology sector, with the firm advising XGI Technology on the sale of its alliance company Macrosynergy to ATI Technologies. At the time of writing, Chen & Lin was retained as lead counsel on a number of transactions set to close in late 2006, including the NT\$724 billion merger between AU Optronics and Quanta Display, Infineon's spin-off of its Dram division to Qimonda Technologies, and Sysware's NT\$8 billion merger with Systex.

Many corporate clients also retain the firm to advise on their credit facilities, but the banking practice is balanced out by lender-side clients such as the Taiwan Industrial Bank and Chinatrust Commercial Bank.

Key contact partners

Shelly Chen
Chien-Chih Liu

Jones Day

Among the most international firms operating in Taiwan, Jones Day remains a top choice for cross-border work. The firm benefits from the formidable combination of Jack Huang, who leads the M&A side, and William Bryson, who provides banking and debt expertise.

In November 2005 Huang advised Yuanta Core Pacific Securities as financial advisor to World Peace Industrial on its \$351 million stock-for-stock merger with Silicon Application, notable for being Taiwan's first share-swap transaction involving two listed companies to result in a single holding company. This was followed up by China Development Financial's NT\$3.7 billion (\$113 million) tender offer for Taiwan International Securities, which received publicity for being a rare hostile takeover. In another major finance-sector deal, Jones Day played a key role as acquiror's counsel on Shinsei Bank's \$350 million purchase of a 35% stake in Jih Sun Financial. Marianne Chao and Thomas Chen were promoted to the partnership in January 2006 and a further two associates were added to the M&A team, signalling the firm's expansion mode. Chen in particular received market recognition as a rising star.

Jones Day also remained active in the financial markets. Bryson advised Ambac Assurance as guarantor on the country's first cross-border and first wrapped securitization of mortgage receivables, originated by Hsinchu International Bank. Another deal saw the finance practice act for the arrangers on a novel securitization plan involving commercial paper backed by the account receivables of an LCD manufacturer. Key structured finance clients include the Industrial Bank of Taiwan, HSBC and ABN Amro.

The banking team, meanwhile, has been active in the non-performing loans (NPL) field, with the team completing a number of structured NPL acquisitions and related financings for Shinsei Bank and GMac Commercial Mortgage. In capital markets, Julian Lin completed two deals in December 2005 – first, advising Action Semiconductor on its global offering of American depository receipts, and secondly, acting for Morgan Stanley as underwriter of a \$250 million convertible bond issue under Regulation S by Shin Kong Financial.

Leading lawyers

William Bryson
Jack Huang

Key contact partners

William Bryson
Jack Huang

LCS & Partners

LCS & Partners is relatively young compared to many of its competitors, and is seen as a firm to watch in the coming years, especially as its practice has been strengthened by the addition of eight associates over the past year. The firm's profile is set to benefit further with the return of Amy Chin, who had left for a high-ranking post in the Financial Supervisory Commission.

US-qualified Mark Harty heads the banking team, which has been busy as lender's counsel on a respectable volume of domestic syndicated lending transactions this year. The capital markets team, led by Brian Yu, has strong relationships with local underwriters such as Fubon Financial, Taiwan Securities and KGI Securities, and is particularly active in the equity-linked space, recently completing convertible bond offerings by Cheng Vei Precision, Coretronic, Catcher Technology and Taiwan Kolin. LCS & Partners is also experienced in GDR issues by Taiwan corporates.

The market rates securitization as one of the firm's strongest suits, and David Chuang as "without doubt the firm's leading light" in this area. This is evidenced by its recent deal portfolio, most notable being its roles advising Taishin International Bank on its asset-backed commercial paper project, valued at NT\$42.72 billion (\$1.3 billion), and a separate Reits project for the same client. Among other deals, the firm has been busy advising the

Industrial Bank of Taiwan on its proposed collateralized bond obligation (CBO) programme and acting for ICBC as arranger on Calyon's pioneering NT\$10 billion CBO, which was one of the first to be backed by US-dollar denominated assets.

LCS & Partners also saw some action in the insolvency field, representing the state-owned Taiwan Life Insurance Institute on the receivership of Kuo Hua Insurance, resulting in Taiwan Life acquiring the distressed assets. M&A work has been plentiful, the most significant deal being the \$2 billion acquisition of Agilent's semiconductor business by Kohlberg Kravis Roberts and Silver Lake Partners, in which Rich Lin's team advised the purchasers. Lin also advised Taiwan Securities Central Depository on its NT\$2 billion merger with DIDC.

At the time of writing the firm continues to be busy on a number of M&A deals involving technology players. Clients single out Pijan Wu as an emerging talent in the market.

Leading lawyers

David Chuang
Rich Lin

Key contact partners

David Chuang
Mark Harty
Brian Yu

Lee and Li

Another excellent year sees Lee and Li retain first tier rankings in every category, a feat matched by no other firm. By hiring a total of 11 associates in the past year, the firm has also indicated its plans to continue onward and upward.

The firm boasts one of the most established and largest banking departments in the country, consisting of 13 partners and 33 associates. The team provides a wide range of transactional and regulatory advice, and recently picked up interesting asset financing work acting for export credit agency lenders on a \$233 million aircraft financing for EVA Airways. In March 2006, the firm advised Chinatrust Commercial Bank as agent on the \$325 million syndicated refinancing of Eastern Multimedia.

At 15 partners and 46 associates, the capital markets team is also sizeable. From among the team, Abe Sung comes highly recommended for his capital markets expertise. One recent highlight of a busy year was the firm's role advising on Himax Technologies' \$510 million ADR issue, which involved a complex offering of old and new shares due to a share migration to a Cayman Islands vehicle. The team has also been active in the real estate investment trust (Reit) arena, advising Fubon Securities as arranger of the Fubon No 2 Reit, the first Taiwanese Reit to make distributions twice a year.

In securitization, Lee and Li had the enviable position of advising on nearly all the major CBO deals over the past year, and in the process remaining at the forefront of legal developments in this growing area. Recent deals included the NT\$10 billion (\$308 million) CBO issue for Calyon in December 2005, one of the first pilot deals to involve asset-backed commercial paper. April 2006, meanwhile, saw the completion of the Polaris Securities and Bank of Overseas Chinese 2006-1 securitization special purpose trust, the first in Taiwan to involve two originators, as well as BNP Paribas' issue of synthetic collateralized debt obligations. In both deals, the firm acted as counsel to the arrangers.

The first quarter of 2006 was also a busy time for the M&A team, as the firm acted on a significant demerger in the insurance industry – the \$400 million spin-off of ING Life Insurance's Taiwan branch to a new subsidiary – as well as on Temasek's \$400

million investment in E.Sun Financial Holding through convertible bonds. The practice's stellar client list includes Morgan Stanley, Citigroup, UBS, Goldman Sachs and the Carlyle Group. From among the team, CT Chang is recognised for his extensive experience and Lilian Kou is a favourite among international clients.

Leading lawyers

CT Chang
Lilian Kou
Abe Sung

Key contact partners

Lilian Kou
Sherry Lin
Alex Liu

Lexcel Partners

Formed as a corporate boutique in 2004 by a group of ex-Lee and Li partners, Lexcel Partners has quickly become a formidable force in the Taiwanese legal market. The excellent reputation of its key lawyers has meant that the firm has easily established a favourable market position in its core areas of financial services and M&A, and increased work in these areas has enabled the firm expand its associate ranks to 13. The client roster is stocked with quality names such as Fidelity, Citigroup, Merrill Lynch, ING Asset Management and AIG. From among the team, Echo Yeh is consistently regarded as the firm's leading light.

The past year has seen the firm advise Fidelity in relation to offshore mutual fund regulations, and assist the Taiwanese operations of Fortis Bank and UBS Securities with their corporate restructurings.

However, it is in M&A where the firm shines brightest, scooping roles on several important finance-sector deals over the past year. The most significant in size was Taishin's \$1.2 billion investment in Chang Hua Commercial Bank. In the following months, Taishin appointed Yeh's team again to advise on a \$900 million investment by Newbridge, marking the world's largest private equity investment in Taiwan at the time. The corporate team also represented Mitsui Sumitomo Insurance, Japan's second-largest non-life insurer, on its acquisition of MingTai Fire and Marine Insurance for \$273 million.

Leading lawyer

Echo Yeh

Key contact partners

Echo Yeh
Mike Lu
Sue Su

Russin & Vecchi

Russin & Vecchi in Taiwan is a boutique practice of 16 fee-earners that is part of an international network of 11 independent firms. While the firm's coverage extends to corporate and other areas, it is best known for its strength in banking. Unsurprisingly, the firm has a high proportion of clients in the banking and financial services industry. The team is led by Thomas McGowan, who one peer described as "one of the top finance lawyers in the country," and the market also singled out Echo Hsu as a rising star.

Russin & Vecchi has been extremely busy over the past 12 months advising its clients on a variety of matters, ranging from transactional lending with cross-border elements and regulatory advice to foreign financial institutions operating in Taiwan.

Securitization is an area in which the firm has remained at the cutting-edge, recently advising Lehman Brothers on structuring Taishin Bank's proposed asset-backed securitization, which involved the multiple issue of structured bonds, synthetic CDOs

and preferred shares. The firm also played a key role advising the originator, BNP Paribas, on its NT\$14 billion (\$429 million) securitization of NT\$- and US dollar-denominated bonds.

Leading lawyer

Thomas McGowan

Key contact partner

Thomas McGowan

Preston Gates & Ellis Taiwan Commercial Law Offices

As the Taiwan arm of Preston Gates & Ellis's global network, Preston Gates & Ellis Taiwan Commercial Law Offices is able to bring a useful international edge to its domestic capabilities. The firm's clients are comprised of a diverse range of local and international companies, while financial institutions, securities firms and insurance companies form a high proportion of the client mix because of the firm's strong finance credentials.

Among the year's highlights, the firm recently represented Chinatrust Commercial Bank on the provision of a NT\$6.5 billion (\$198.5 million) facility for King Yuan Electronics. In addition to advising on corporate, trade, project, asset and lease financing, the banking team handles capital raisings, debt restructurings and regulatory matters. Co-managing partner and banking expert Christina Yang is the firm's best-known personality. The M&A practice, led by co-managing partner James Chen, is part of the larger corporate, investments and taxation group.

Key contact partners

James Chen
Christina Yang

Tsar & Tsai Law Firm

Tsar & Tsai Law Firm has a well-developed track record and enjoys a good profile in the market. There are over 45 lawyers in this well-respected law firm, many of whom are multilingual and have been trained overseas. Of them, partners CY Huang and Jackie Lin were once again singled out by peers and clients alike for their "deep experience and legal skills".

The firm has an excellent banking and capital markets practice. Recent deal experience includes advising Asia Pacific Telecom on a structured financing transaction involving foreign lenders, and acting for Newbridge Capital and LCD maker CPT as borrowers on a number of domestic-led syndicated financings. Capital markets activity, meanwhile, has consisted mainly of advising Taiwanese issuers such as Powerchip, Wistron and CPT, as well as a number of underwriters, on euro convertible bond and GDR offerings.

M&A is another area in which the firm stands out. Last year saw Tsar & Tsai score key roles on important deals such as Newbridge Capital's \$844 million investment in Taishin Financial Holding and Lenovo's acquisition of IBM's Taiwanese PC operations. Among other deals, the firm also acted on several cash buyouts and tender offers involving overseas-listed Taiwanese technology companies.

Leading lawyers

CY Huang
Jackie Lin

Key contact partner

Jackie Lin

Yangming Partners

Yangming Partners is a full-service law firm that has developed a solid reputation for domestic and cross-border work. The firm is staffed by a total of seven partners and senior counsel, ably supported by 11 associates, who together practice across a broad range of areas including cross-border investments, joint ventures, mergers and acquisitions, projects, banking and securities regulation.

The capital markets team operates under the leadership of Richard Chuang, who was previously an adviser to the Securities and Futures Bureau and a member of the Taiwan stock exchange's listing committee. A headline deal in this area saw the firm represent Global Testing on a share swap with its Singaporean shareholder United Test and Assembly Centre, and its subsequent listing on the Singapore stock exchange.

The team has also been busy acting for underwriters and issuers in connection with international offerings of convertible bonds, exchangeable bonds, ADRs and GDRs. The firm also showcased its regulatory expertise this year by landing instructions from several US and Japanese securities firms on the securities licensing regime in Taiwan.

M&A is also an important area for Yangming Partners, having represented numerous foreign and local companies on their inbound and outbound investments. More recently the corporate team also added to its debt portfolio by advising on a number of disposals of non-performing loans and debt restructurings.

From among the team, corporate partner Paul Cassingham comes particularly highly recommended by the market for his overall strength.

Leading lawyer

Paul Cassingham

Key contact partner

Paul Cassingham