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Financial Developments and Foreign Investment Strategies in Taiwan—A Legal and Policy Perspective**

I. The Many Changing Faces of Taiwan

In recent years Taiwan's social, political, and economic developments and the resulting changes in this island republic have attracted increasing global attention.¹ Since its recovery from fifty years of Japanese occupation in 1945, Taiwan has been controlled by the Nationalist Republic of China (ROC). The 20 million Taiwan Chinese now enjoy a per capita GNP of about U.S. \$8,000, and their government has accumulated about U.S. \$70 billion of foreign exchange reserves. How best to tap this financial capital has become a new policy issue. This article thus examines three milestones of financial reform in Taiwan: the foreign exchange liberalization since mid-1987, the transformation of its securities mar-

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1. See, e.g., B. BALASSA & J. WILLIAMSON, ADJUSTING TO SUCCESS: BALANCE OF PAYMENTS POLICY IN THE EAST ASIAN NICs 71 (1987); K. LI, THE EXPERIENCE OF DYNAMIC ECONOMIC GROWTH ON TAIWAN 164 (1976); C. SHIVE, THE FOREIGN FACTOR: THE MULTINATIONAL CORPORATION'S CONTRIBUTION TO THE ECONOMIC MODERNIZATION OF THE REPUBLIC OF CHINA (1990); M. TODARO, ECONOMIC DEVELOPMENT IN THE THIRD WORLD 14 (4th ed. 1989); J. WHEELER & P. WOOD, BEYOND RECRIMINATION: PERSPECTIVES ON U.S.-TAIWAN TRADE TENSIONS 1 (1987); Evans & Pang, *Implications of the Taiwanese Case for Newly Industrializing Countries*, in TAIWAN, A NEW INDUSTRIALIZED STATE 3 (H. Hsiao, W. Cheng & H. Chan eds. 1989); Hsu & Liu, *The Transformation of the Securities Market in Taiwan, the Republic of China*, 27 COLUM. J. TRANSNAT'L L. 169 (1988); Liu, *Brave New World of Financial Reform in Taiwan, the Republic of China—Three Waves of Internationalization and Liberalization and Beyond*, 8 CHINESE Y.B. INT'L L. & AFF. 134 (1988–89); Liu, *Legal and Policy Perspectives on United States Trade Initiatives and Economic Liberalization in the Republic of China*, 11 MICH. J. INT'L L. 326 (1990); Winckler, *Institutionalization and Participation on Taiwan: from Hard to Soft Authoritarianism?*, 99 THE CHINA Q. 481–99 (1984).

ket since early 1988, and its banking reform since mid-1989. This article also attempts to develop strategies for foreign firms interested in this exciting market.

II. Liberalization of Taiwan's Foreign Exchange Control

A. PRE-1987 FOREIGN EXCHANGE CONTROL

Taiwan's principal foreign exchange statute has been the Statute for the Administration of Foreign Exchange (SAFE).² Foreign exchange authority lies primarily with the Foreign Exchange Bureau of the Central Bank of China (CBC) and secondarily with the Ministry of Finance (MOF), while the Ministry of Economic Affairs (MOEA) regulates imports and exports.

Prior to 1987, SAFE required that foreign exchange earnings resulting from exports of goods and services generally had to be sold to the CBC or to "appointed banks"—banks authorized by the CBC to engage in foreign exchange business. While this surrender system gave the CBC substantial discretion in channelling economic activities, the basic premise of the SAFE—shortage of foreign exchange—changed after the early 1970s, and the system became too rigid despite such discretion. Indeed, foreign exchange control had to be relaxed because of Taiwan's substantial trade surplus, the accumulation of foreign exchange reserves, and the expectation of the New Taiwan (N.T.) dollar's appreciation.

B. AMENDMENT TO THE SAFE

To liberalize foreign exchange control, the ROC's Legislative Yuan (the Parliament) passed a bill in June 1987, adding article 26-1 to the SAFE, which authorizes the Executive Yuan (the Cabinet) to suspend the application of core provisions of the SAFE in whole or in part when the ROC experiences a long-term international trade surplus or accumulates substantial foreign exchange reserves, or when the international economy experiences major changes.³ In July 1987, the CBC suspended the SAFE's core provisions and implemented eight regulations under article 26-1 to usher in a new era. Of these regulations, the most important are the Regulations for Nongovernmental Inward Remittance (Inward Regulations) and the Regulations for Nongovernmental Outward Remittance (Outward Regulations).

Under the Inward Regulations, any adult individual holding a national identification card or an alien residency certificate now may accept remittances up to

2. That this statute should have an acronym like "SAFE" is only fitting as Taiwan's foreign exchange policy has always been safety-oriented. For studies of the fiscal and monetary policies of Taiwan, see Lundberg, *Fiscal and Monetary Policies*, in *ECONOMIC GROWTH AND STRUCTURAL CHANGE IN TAIWAN, THE POSTWAR EXPERIENCE OF THE REPUBLIC OF CHINA* 263 (W. Galenson ed. 1979).

3. See Liu, *Republic of China's Deregulation of Foreign Exchange Control*, 6 CHINESE Y.B. INT'L L. & AFF. 298 (1986-87).

U.S. \$2 million each year for conversion into N.T. dollars. Furthermore, inward remittance for the repatriation of capital and profits from an offshore investment or from a foreign investor's investment in Taiwan has to be approved by the CBC.⁴ Under the Outward Regulations, Taiwan entities and adult individuals holding a national identification card or an alien residency certificate may make outward remittances in foreign exchange of up to U.S. \$5 million per year, except that each outward remittance exceeding U.S. \$1 million is subject to a ten-day waiting period. Remittances exceeding the U.S. \$5 million or U.S. \$1 million limit require a special approval by the CBC.⁵

C. IMPACT ON FOREIGN DIRECT INVESTMENT

Foreign investment in Taiwan is administered under the Statute for Investment by Foreign Nationals (SIFN) enacted in 1954. It is centered around the privilege of an investor with foreign investment approval (FIA) status, granted by the Investment Commission (IC) of the MOEA, to repatriate the original capital (whether in the form of equity investment or loan investment), investment yield (whether in the form of dividend or repayment of interest on loan investment), and return on investment (capital gains).⁶ However, the SIFN is not an all-inclusive statute on foreign investment in Taiwan; foreign banks, insurance companies, and other foreign companies can set up branches in Taiwan without undergoing the FIA process.⁷ The SAFE liberalization led to an amendment of the SIFN in 1989 and to relaxation of the administrative policy of the IC, which had even begun to grant FIA status more liberally since the early 1980s. The most recent example is evidenced by the IC's permitting FIA holding companies to be foreign-owned after 1988 in order to allow foreign investors more leeway in selecting proper opportunities in Taiwan. As amended, the SIFN now sets forth a negative listing policy by listing industries and businesses in which foreign investment is prohibited or restricted.⁸

The SIFN does provide for some advantages over, say, a non-FIA foreign-owned company. An FIA company is exempt from some cumbersome company law requirements on nationality and residence of the chairman and rules governing mandatory public offerings and employee stock subscription rights. Another reason for applying for the FIA status is that the Statute for Encouragement of Investment (SEI) provides for a more favorable rate for the withholding tax on dividends payable to FIA investors; the FIA withholding rate is 20 percent,

4. Regulations for Nongovernmental Inward Remittance art. 4. The quota has been increased several times from the original amount of U.S. \$50,000.

5. Regulations for Nongovernmental Outward Remittance art. 5.

6. Statute for Investment by Foreign Nationals [SIFN] art. 7.

7. Review by other competent ROC authorities, however, is still required.

8. See Liu, *Survey of Major Commercial Law Developments in the Republic of China: 1987-88*, 7 CHINESE Y.B. INT'L & AFF. 136, 152 (1987-88) for an analysis and translation of the negative list.

instead of the regular 35 percent.⁹ But the gradual removal of foreign exchange controls eventually could also obviate the need to seek the FIA status. In fact, as the Outward Regulations grant a *regulatory* repatriation privilege, some foreign investors have avoided the FIA application process with the IC by setting up, say, a non-FIA branch in Taiwan.

D. IMPACT ON DIRECT OUTWARD INVESTMENT

The 1987 Outward Regulations have facilitated direct investment abroad to secure raw materials, technology, and markets. The regulations should also enable the ROC to offset capital outflow against its trade surplus.¹⁰ For years, however, Taiwan companies have had to apply for an Outward Investment Approval (OIA) for investing directly abroad under the Regulations Governing the Review of Outward Investment and Outward Technical Cooperation (OIA Regulations). These regulations regulate companies, but do not relate to individuals investing abroad; before 1987 the policy was not to encourage individuals to invest abroad. After July 1987, these regulations became a hurdle, instead of a facilitating vehicle, to Taiwan companies wishing to invest. Individuals now simply may follow the less taxing requirements of the Outward Regulations to invest abroad, whereas Taiwan companies still have to undergo the OIA process.

To narrow this disparate treatment, an amendment adding a three-tier review test in the OIA Regulations was adopted in March 1989. An outward investment for less than U.S. \$1 million may be implemented prior to its being reported to the IC. To make an outward investment of between U.S. \$1 million and U.S. \$5 million, an OIA application has to be filed with the IC. After a thirty-day waiting period expires without the disapproval of the IC, the project is deemed to have been approved. An outward investment exceeding U.S. \$5 million will receive the full scrutiny of the IC.¹¹ As thus amended, the OIA Regulations now parallel the monetary limits of the Outward Regulations.

E. IMPACT ON ACQUISITIONS BY TAIWAN COMPANIES

The SAFE liberalization and the amendment to the OIA Regulations are not sufficient to foster an environment conducive to investment abroad; other changes are necessary. For example, until recently, under the Company Law a

9. See, e.g. SIFN art. 18; Statute for Encouragement of Investments [SEI] art. 16.

10. Small wonder, then, that 1989 was a boom crop year for outward investment by Taiwan companies, with a total approved amount of about U.S. \$930 million, representing a 300 percent increase in the total amount approved over the prior year and even surpassing the cumulative approved amount since 1959 by more than 50 percent. See INVESTMENT COMMISSION REPORT ON ANALYSIS OF OUTWARD INVESTMENT 5 (1989). Although lacking reliable statistics, individual investment abroad may be several times that of the corporate approved amount.

11. Regulations Governing the Review of Outward Investment and Outward Technical Cooperation art. 3.

Taiwan company's total investment in other companies in Taiwan and abroad could not exceed 40 percent of its own paid-in capital.¹² The tax law also discriminates against companies investing abroad; return on investment abroad that inures to a Taiwan individual investor does not constitute ROC-source income and is not subject to ROC income tax, whereas Taiwan companies' worldwide income is subject to corporate income tax.¹³

Such disadvantages do not inhibit outward investment; they only encumber the process. Foreign exchange liberalization certainly has enhanced the possibility of cross-border mergers and acquisitions.¹⁴ For example, for the first time in February 1990 a group of Taiwan investors, including a government-owned development fund, acquired Wyse Technology, Inc., a public company in San Jose, California, and a world leader in selling computer monitors. In December 1989, Yuen Foong Yu Paper Manufacturing Company, a leading public company in Taiwan, floated the first Eurobond ever by a Taiwan company for U.S. \$100 million at a low coupon rate of two percent per annum. The bond is "convertible" when and if foreign portfolio investment in Taiwan companies is permitted by the ROC Government.

The July 1987 liberalization, however, has also complicated the framework governing cross-border investment. There is now a dual regulatory scheme: the SIFN and the OIA Regulations form an internally coherent set of rules regulating foreign investment and investment abroad, but the CBC's Inward Regulations and Outward Regulations superimpose another regulatory layer on exactly the same regulatory framework.

F. IMPACT ON FOREIGNERS' PORTFOLIO INVESTMENT

For foreign portfolio investors interested in Taiwan's securities market, not much has changed since July 1987. In fact, measures were taken to enhance the control on inward remittance to prevent the influx of hot monies. Now that foreign exchange control is less useful in regulating investment, other measures such as the Securities Exchange Law (SEL) have become the more convenient regulatory substitutes. To this end, the Securities and Exchange Commission (SEC) instructed the Taiwan Stock Exchange (TSE) and Taiwan securities firms not to permit foreigners' applications to open brokerage accounts except for selling their holdings. Similarly, the MOF directed that ROC financial institutions may not take N.T. dollar deposits from nonresident aliens or foreign corporations. This containment policy has not worked very well, however. Hot

12. Company Law art. 13. A bill to relax this rule was enacted by the Legislative Yuan on October 24, 1990.

13. Income Tax Law arts. 2, 3, 8.

14. The term "mergers and acquisitions" is used descriptively, as the ROC's Company Law does not provide for mergers between foreign and Taiwan companies.

monies are believed to have come freely into Taiwan's financial system nonetheless and have made waves in the securities market.¹⁵

Pressures are mounting for foreign institutional investors' participation in Taiwan's securities market. Two examples are noteworthy. First is the new authorization under the 1988 SEL amendment to permit, under certain circumstances, foreign securities firms to establish joint-venture local subsidiaries (in which they initially will have to take a minority position) or branches to engage in underwriting, brokerage, and dealing business. The second is the recent attempt by foreign insurance companies operating through Taiwan branches to lobby for permission to invest their own funds and liability reserves in listed Taiwan securities.¹⁶ American insurance companies with licensed branches in Taiwan are now given national treatment to invest in listed securities in Taiwan through their head offices.¹⁷ Similarly, leading foreign securities houses are now permitted to set up branches to engage in the brokerage business in Taiwan. Following the lackluster performance of Taiwan's securities market in the first half of 1990, there are renewed speculations that foreign institutional firms will be permitted to invest in the securities market.¹⁸

G. IMPACT ON OUTWARD PORTFOLIO INVESTMENT

Outward portfolio investment is now substantially liberalized because of the U.S. \$5 million annual quota for investment abroad provided for under the 1987 Outward Regulations. Since then, foreign financial firms have been frequenting this newly discovered market or have been setting up operations in Taiwan to promote portfolio investment abroad. Unfortunately, the definition of "foreign exchange" in the SAFE still includes foreign securities. Failure of the SEL and its enforcement rules to define the parameters of a private placement and some ambiguous rulings and interpretive letters of the MOF and the SEC further complicate this matter. In addition, the different regulatory standards for the "foreign exchange investment trust" program regulated by the MOF and the CBC, on the one hand, and the SEC programs on securities investment consulting enterprises (SICE) to purchase foreign securities including mutual funds, on the other hand, also add unnecessary confusion to this issue.¹⁹ Thus, for both would-be investors and avid promoters, the state of regulating outbound portfolio investment leaves much to be desired.

15. See Hsu & Liu, *supra* note 1, at 179-80.

16. See Liu, *supra* note 8, at 153.

17. For limitations, see Insurance Law art. 146. For a study on the trade pressure gradually leading to this result, see Liu, *supra* note 1, at 344-45.

18. See Ting, *Special Treatment for Foreign Institutional Investors in the Market*, COM. TIMES, July 22, 1990, at 1, quoting the Governor of the CBC as agreeing to grant these firms an exemption from the inward and outward remittance restrictions.

19. See Hsu & Liu, *supra* note 1, at 187-88.

III. Transformation of Taiwan's Securities Market

A. SECURITIES MARKET AND REGULATORY FRAMEWORK

The second wave of financial reform in Taiwan has been the transformation of its securities market since 1988. Under the Land to the Tillers program in the 1950s, the ROC Government secured land from landowners for distribution to the tenant farmers; in return, the landowners received from the government its holdings in four major companies and land bonds.²⁰ This exchange fostered an amorphous and primitive over-the-counter (OTC) securities market all over the island.

Following the recommendation by the Task Force to Study the Establishment of a Securities Market, the SEC was established in 1960. The TSE was established in November 1961, and in April 1968 the SEL was enacted. The framework for securities regulation in Taiwan was thus formally established.²¹ The SEL provides a comprehensive regulatory framework patterned after the American securities laws with the exception of the SEL's adoption of a merit review system.²² The TSE is the most active market while there is also a small OTC debt market and an emerging OTC market for equities. About 190 companies' securities now are listed on the TSE.

Before the 1988 SEL amendment, securities firms were classified into underwriters, brokers, and dealers. A securities firm engaging in any one of such businesses could not expand its activities into other lines of securities business. One exception was made for financial institutions, which could, for example, engage in the underwriting business if they were a trust company or the trust or savings department of a bank, and if they also chose to engage in either the dealer business or the brokerage business. At the time, only twenty-two underwriters (of which only five or six were active), ten dealers, and twenty-eight brokers (fourteen of which were private companies and the other fourteen the trust or savings departments of government-owned financial institutions) were licensed by the SEC.²³ These licenses had been "frozen" by the government for many years. Indeed, until six years ago the securities business in Taiwan was not profitable; with a small number of listed companies and inadequate depth in the market, many securities houses folded. The SEC has regulated brokerage com-

20. See Amsden, *Taiwan's Economic History: A Case of Etatism and a Challenge to Dependency Theory*, in *TOWARD A POLITICAL ECONOMY OF DEVELOPMENT, A RATIONAL CHOICE PERSPECTIVE* 142, 152 (R. Bates ed. 1988).

21. See SEC, 1986 ANNUAL REPORT 3, 4 (1987).

22. See, e.g., Securities Exchange Law [SEL] arts. 20 (antifraud), 22 (registration requirement), 30 (statutory prospectus), 31 (prospectus delivery requirement), 32 (prospectus accuracy requirement), 155 (prohibition of wash sales and other market manipulations), 157 (short swing profit disgorgement) & 157-1 (insider trading sanctions).

23. Such statistics were cumulative. Several different lines of the securities businesses could be engaged in by the same entity. See SEC, 1986 ANNUAL REPORT 17 (1987).

missions and has set the rate at 0.1425 percent of the transfer price.²⁴ Commission rebates are nevertheless frequent, reflecting keen competition.

Internationalization of Taiwan's securities market began in the mid-1980s. Prior to the 1988 SEL amendment, however, the government also did not consider permitting foreign ownership in securities firms.²⁵

There is an oligopoly of four mutual fund management companies, all of which are international joint ventures licensed by the SEC as securities investment trust enterprises (SITE). Total foreign ownership in each SITE company is restricted to no more than 49 percent.²⁶ The entire mutual fund industry was created as a result of the policy of the Executive Yuan of the ROC, adopted in 1982, to permit the three-stage internationalization of Taiwan's securities market.²⁷ The four management companies are authorized to establish mutual funds based upon securities investment trust contracts among them, the custodian banks, and the beneficial owners of units in the funds.

That this arrangement has been accomplished under a framework covered only by a single statutory provision, article 18-1 of the SEL, is amazing. As a civil law country, Taiwan does not have a comprehensive trust law, and the SEC drafted the detailed regulations from scratch. Each SITE company now sponsors a "foreign fund" traded abroad, as well as other funds. Despite the participation of new institutional investors such as the funds, the TSE is still overwhelmingly dominated by individual investors, whose herd mentality partially explains the volatility of the market. Until September 1990, pension funds could not invest in the Taiwan securities market because of the Basic Labor Standards Law and because of conservative government policies on the safety of such funds.

There are about three dozen SEC-licensed SICE companies. The ROC Government has always permitted complete foreign ownership in such SICE companies. However, this business was unprofitable until the SEC promulgated the Guidelines Governing the Operations of Securities Investment Consulting Enterprises in Providing Foreign Securities-Related Advice (Foreign Securities Advice Regulations) in late 1987 to permit SICE companies to advise on foreign

24. For a comparison of the securities transaction tax in other countries and a critique on the United States' proposal on such a tax, see Grundfest, *Transaction Tax Asks for Trouble*, Asian Wall St. J., July 24, 1990, at 8.

25. The only "exception" at that time was Citibank, which had a 40 percent holding in Taiwan First Investment Trust Co., Ltd., a local trust company authorized to engage in securities business under art. 101 of the Banking Law and art. 45 of the SEL.

26. Rules for the Administration of Securities Investment Trust Enterprises art. 4.

27. The first step, which entailed permitting foreign investors to invest indirectly in Taiwan's securities market through such "foreign funds," has been accomplished. The second stage contemplated a plan giving access to foreign institutional investors to invest directly in Taiwan's securities market. The ROC Government had begun to draft the regulations in 1986 for the second-stage liberalization, but put a halt to it because of concerns with the foreign exchange effect of the second stage. The foreign exchange reserves of the ROC were already at a staggering amount at that time. The third stage, which is yet to be accomplished, envisions complete access to any foreign investor to invest directly in Taiwan's securities market.

securities, particularly foreign mutual funds.²⁸ In fact, such permission amounts to permitting such SICE companies to promote and distribute foreign securities. The SICE, however, still may not handle discretionary investments for their clients. Hence, there is now a strong lobby by the association of SICE companies for this authorization.

B. GROWTH OF TAIWAN'S SECURITIES MARKET

The TSE has undergone a major transformation in recent years. Trading has multiplied at least fifty times since 1972, and on a high day the trading volume now can surpass U.S. \$7.5 billion, roughly one-tenth of Taiwan's total foreign exchange reserves. It is widely suspected that much of this active trading is fueled by "hot monies" from abroad and the activities of underground "investment companies." This increase in activity of the TSE has brought about changes in work ethics and the value system.²⁹ With entrenched positions in the market until mid-1988, brokers earned oligopolistic profits, to the order of several times their paid-in capital during 1986–1987.

Before 1985, few would have surmised that the TSE weighted stock index could ever exceed 1,000 points. But it went up to 4,673 points shortly before the October 1987 global crash and rebounded to 8,000 points by September 1988. The market, however, lost about 3,000 points in a month's time after an MOF capital gains tax announcement. Then, again the market rallied, and by early 1990 the TSE index exceeded 12,000 points. Adverse economic performance in 1990 and uncertainties in the development of several political reform measures once more brought it down to 3,500 points. Since 1972 the number of shareholders of record in TSE-listed companies has increased by five times. The number of brokerage accounts is already approaching five million as of May 1990, an exponential growth.³⁰

C. TRANSFORMATION OF TAIWAN'S SECURITIES MARKET

The 1988 SEL amendment and ensuing regulatory changes have transformed Taiwan's securities market.³¹ To foreign observers the most important revision in the amendment clearly has been the liberalization of the securities industry. The

28. There are requirements on the rating, listing, size, and track record of the fund or fund management companies. Guidelines Governing the Operations of Securities Investment Consulting Enterprises in Providing Foreign Securities-Related Advice arts. 2, 3, 4, 6, 7.

29. Also, one recent governmental study suggested that gaps in income distribution in Taiwan for 1988 continued to widen after seven consecutive years of increasing discrepancies. As of the end of 1988 the top 20 percent of earners in Taiwan as a group earned 4.85 times the income of the lowest earners as a group. See Econ. Daily News, Aug. 31, 1989, at 2.

30. Many investors maintain multiple brokerage accounts. One estimate suggests that there are actually only about 1.2 million investors, still a significant percentage. Lin, *Myths about Taiwan's Money Game*, China Times, July 30, 1990, at 4.

31. See Hsu & Liu, *supra* note 1, at 169.

amendment has permitted foreign securities firms to have limited access to Taiwan's securities market and has created integrated securities houses (ISH). These are securities firms that can hold underwriter, broker, and dealer licenses simultaneously.

Following the 1988 SEL amendment, the Criteria for the Establishment of Securities Firms (Establishment Criteria) were adopted quickly, and the SEC began accepting applications. The result is a Taiwan version of the "Big Bang": the number of brokerage firms in Taiwan has increased to over 300 now, with about forty ISH operations. The securities market cannot sustain so many intermediaries; a shake-out will occur when the market undergoes a downturn. The minimum paid-in capital for the underwriting, dealing, and brokerage operations is N.T. \$400 million, N.T. \$400 million, and N.T. \$200 million, respectively. Therefore, an ISH operation will require a total paid-in capital of N.T. \$1 billion. Prior SEC approval is required for setting up such securities firms.³²

Foreign access to this new market was provided for in three alternative ways. First, any foreign investor may invest in a securities operation by joint-venturing with Taiwan investors. Second, foreign securities firms may set up a branch operation. Third, foreign banks' branches in Taiwan may set up a securities operation, now a closer reality because of the 1989 Banking Law Amendment. As of this writing, however, no such foreign bank branch has been licensed. The SEC has discretion to limit the number and the business scope of foreign securities firms setting up a branch operation or foreign banks' Taiwan branches setting up a securities operation. Foreign securities firms must meet certain requirements in order to set up a branch in Taiwan and, once set up, they will be subject to the same requirements as Taiwan securities firms, except that they have to choose to engage in only certain securities operations.

Foreign nationals may invest in a securities company to engage in securities operations, but prior approval of the SEC is required. Such investment also has to undergo the FIA review process pursuant to the SIFN. The total amount of foreign ownership in a securities business entity, however, may not exceed 40 percent of its paid-in capital, and each foreign investor may invest in not more than 10 percent of the total paid-in capital of the entity.³³ Moreover, once a foreign investor invests in a securities entity, it may not invest in any other securities entity.

In June 1989, the SEC issued Regulations for Foreign Securities Firms Establishing Brokerage Branches (Brokerage Branch Regulations) to permit foreign securities firms to set up a Taiwan brokerage branch. The home country of these foreign securities firms must grant reciprocity in order for them to set up this branch. However, initially only three foreign securities firms would be permitted

32. Criteria for the Establishment of Securities Firms arts. 3, 7.

33. *Id.* arts. 36, 37.

to set up the branch, and the number of these brokerage branches may increase over time, subject to the conditions of Taiwan's economy and its financial and securities markets. The paid-in capital of such foreign securities firms must exceed U.S. \$2 billion, and their total asset value must exceed U.S. \$20 billion. The foreign securities firm or one of its subsidiaries must be a member of the New York Stock Exchange, the Tokyo Stock Exchange, and the London Stock Exchange. In addition, it must have the necessary information transmission facilities linked up with these three stock exchanges.³⁴ Thus far, only Merrill Lynch and Shearson Lehman Hutton, both of which have since suffered adverse operating results in their home country, have indicated their interest in such a branch.

D. "NEW" INSTRUMENTS AND MARKET STABILITY

To enhance market stability and growth, Taiwan's SEC has to be receptive to developing "new" securities and other instruments. A case in point is the convertible bond, a new arrival in Taiwan's market. The SEC drafted a set of regulations as early as March 1983. No convertible bond could be issued at the time, however, because of some practical difficulties arising from the Company Law rigidity and share listing.³⁵ Then, in 1988, Yuen Foong Yu Paper Manufacturing Company, Ltd., issued a modified form of the convertible bond, Yuen Foong Yu Series No. 1 (Exchangeable) Bond, for N.T. \$1 billion at 3.01 percent per annum. Being the first "convertible" bond issued in Taiwan, it was quite unusual in that it was convertible into the shares of a company in which Yuen Foong Yu has a significant holding. Subsequent developments are also encouraging: Yuen Foong Yu and other companies have successfully floated convertible preferred shares to the public in Taiwan.

In August 1989, the SEC amended its 1983 convertible bond regulations to deal with the issues that had prevented such bonds from being issued. Again, Yueng Foong Yu issued another "convertible" bond at 2 percent coupon rate in late 1989 in the Eurobond market to finance the acquisition of offshore paper manufacturing facilities. Other public companies in Taiwan attempted to follow suit, but failed to launch such offerings in time for the bullish Eurobond and Taiwan markets in 1989. The Yuen Foong Yu pattern merits continued examination because an offshore convertible bond could finance Taiwan companies' mergers and acquisitions abroad at a much lower funding cost. And, importantly, it will increase the globalization of the TSE as foreign portfolio investors convert to become shareholders of TSE-listed companies.

34. Regulations for Foreign Securities Firms Establishing Brokerage Branches art. 3.

35. The main issue is the Company Law's requirement of registering paid-in capital, which is difficult to administer when there are continuing conversions.

Another governmental measure to increase the size of the TSE is to privatize and then to list state-owned enterprises.³⁶ Already a successful pattern has emerged. The first privatization program (also the largest underwriting in the TSE's history) was the secondary offering by Chinese Petroleum Corporation, a government-owned enterprise, of some of its holdings in China Steel Corporation, the government-owned steel corporation, in early 1989. A basic statute governing the privatization of government-owned enterprises will be amended to give the Executive Yuan freer hands in the privatization program. Close to twenty government-owned companies, with businesses ranging from petroleum, steel, electrical power, and utilities to banking and chemicals, have been identified for gradual privatization. But Taiwan's privatization program calls for, at least in the beginning, the government holdings to be maintained at a majority level to ensure control.

Other proposals also could increase the size of the securities market. The SEC has demonstrated a keen interest in allowing warrants and options to be issued, which would require another amendment to the SEL.³⁷ Following the market downturn since early 1990, domestic pension funds now are permitted to invest in the securities market to increase its stability.

E. NEW WAVE OF CROSS-BORDER MERGERS AND ACQUISITIONS

Some form of internationalization of the TSE is already happening as a result of a new wave of cross-border mergers and acquisitions of listed companies. A recent example is the acquisition of 25 percent of the shares of the Yue Loong Motors Company, Ltd., a TSE-listed automobile manufacturer, by Nissan Motors of Japan in 1985. Such acquisitions generally involve some form of management participation in order to receive the FIA. Therefore, they are almost always friendly takeovers or alliances. Since the Wyse Technology takeover by a Taiwan consortium, internationalization of Taiwan's securities market has also taken on a new meaning because of the long-term impact of cross-border mergers and acquisitions by Taiwan companies. Such acquisitions, which tend to be friendly transactions as well, certainly will make Taiwan companies more internationalized.

Mergers and acquisitions abroad would make sense for Taiwan companies for several reasons. First, the country and its people are now rich enough to invest abroad. Second, many Taiwan companies are diversifying or positioning themselves as the economy in Taiwan is being transformed. Third, the appreciation of the N.T. dollar has made foreign goods (including foreign companies) less ex-

36. Privatization has been suggested by the private sector in Taiwan for a long time. See, e.g., *Introspections on Breaking 5,000 Points: Privatizing Government-Owned Enterprises to Stabilize the Securities Market*, Econ. Daily News, June 10, 1988, at 2.

37. Currently there are only statutory subscription rights of employees and the public. See Company Law art. 267; SEL art. 28-1.

pensive. Fourth, mindful of dealing with trade protectionism, and in need of natural resources and new technologies, Taiwan companies have found that mergers and acquisitions abroad offer the expediency of leap-frogging if synergy exists. Fifth, in countries like the United States industry is going through a trend of divestment so that one-time conglomerates can concentrate on their main-line businesses. This breakup creates buying opportunities. For listed companies in Taiwan, or those that will become so in the short-term, this phenomenon even offers a key financial strategy: price earnings arbitrage.³⁸

The price earnings arbitrage assumes that the price earnings ratios of TSE-listed companies will be much higher than other listed companies in the world. On this assumption, public investors in Taiwan are willing to pay a premium for assets abroad, including foreign companies, which do not earn as much. Therefore, it would be financially sensible for Taiwan companies to take over foreign companies and, after having their value consolidated into their own, go public on the TSE. To introduce another financial consideration into this strategy, Taiwan companies could issue convertible bonds to finance more cheaply such mergers and acquisitions abroad. By the end of this century, one could expect to see more Taiwan-based multinational corporations whose growth presumably would be bankrolled by the less expensive equity capital in Taiwan.

IV. Banking Law Reform

A. BANKING INDUSTRY

The third wave of Taiwan's recent financial reform has been the banking sector reform since 1989. Again, the reasons and momentum for reform can be traced to a much earlier period. From the 1945 restoration of Taiwan to the loss of mainland China in 1949, banks in Taiwan were gradually transformed from the previous Japanese management. Most of them became state-owned banks and began to play a major role, because almost all banks originally operating in mainland China ceased operation. Not even the CBC was in operation when the ROC Government relocated to Taiwan. The 1933 Banking Law enacted in mainland China became out-of-date as the banking industry began to settle in Taiwan, and new banking legislation was finally enacted in 1975. Foreign banks were also permitted to set up branches in Taiwan, with Daichi Kangyo Bank taking the lead to set up a branch office in 1959, thus beginning the modest internationalization of Taiwan's banking industry.

There is a partial and one-sided regulatory dichotomy of commercial and investment banking in Taiwan. Some banking institutions may engage in certain kinds of securities business through their savings and trust departments; securi-

38. For a description of the price earning ratios of TSE companies, see Hsu & Liu, *supra* note 1, at 180.

ties firms, however, may not engage in any banking business.³⁹ For many years state-owned banks and financial institutions dominated the banking industry. Throughout the 1970s and 1980s foreign banks were increasingly attracted to this market by Taiwan's economic development.

There are now twenty-four domestic banks in Taiwan, most of which are commercial banks. Thirty-four foreign banks maintain Taiwan branches, and more than a dozen foreign banks maintain representative offices. There are also eight trust and investment companies, some of which have foreign minority shareholders. But the Banking Law is not all-inclusive in regulating financial institutions. Outside the regulatory framework of the Banking Law are other banking institutions, such as credit cooperatives and credit departments of farmers' and fishermen's associations. In addition, a well-entrenched postal savings system, influenced by the Japanese system, also receives deposits through widely dispersed post offices.

B. BANKING LAW AMENDMENT

The 1989 Banking Law Amendment revised more than one-fourth of its provisions. The amendment's professed goals were to (1) permit privately held banks to be set up for the first time, (2) strengthen the banking system, (3) expedite liberalization of the banking sector, and (4) maintain disciplined, orderly, and responsible activities in the banking system. The MOF also obtained substantial discretion in implementing the amendment by detailed regulations, as in the case of liberalizing the capital and foreign exchange markets. Since the Big Bang of 1988 for the securities market, about 300 new securities firms have sprung up. But one should not anticipate a significant number of new commercial banks being set up after the 1989 Banking Law Amendment. Indeed, all indications thus far suggest that opening up the banking sector to private investment will take a much longer time to launch and that liberalization will be carefully planned and implemented. Nineteen groups applied to set up new commercial banks in October 1990, but there may be ten newly set-up private banks at the most, and even they probably will not be profitable in the beginning.

One of the keen governmental concerns in adopting banking sector reform is to ensure that new banks will not be controlled by wealthy groups of individuals and their affiliates.⁴⁰ Under the new Banking Law and Regulations Governing the Establishment of Commercial Banks (Commercial Banks Regulations), unless approved by the MOF, no person may own more than five percent of the total issued capital of a commercial bank. In addition, the total holdings of affiliated persons may not exceed fifteen percent of the total issued capital of such a bank.

39. See Banking Law arts. 78, 101; SEL art. 45.

40. For Taiwan's recent concerns with the concentration of economic power, see Liu, *Experimenting with Competition Law: A Preliminary Analysis of the Draft Fair Trade Law of Taiwan, the Republic of China*, 13 WORLD COMP. L. & ECON. REV. 1 (1989).

In addition to this requirement, the MOF's Commercial Banks Regulations also require 20 percent of new commercial banks' initial paid-in capital to be subscribed through public offerings. New commercial banks must have a minimum paid-in capital of N.T. \$10 billion (approximately U.S. \$370 million).⁴¹ This amount is substantially higher than even the banking industry average in the United States, Japan, and European countries, which are perceived to have a more sound and modernized banking system. Therefore, the banking sector liberalization is a stark contrast to the securities market liberalization.

C. REGULATION OF FOREIGN BANKS

Negative listing under the SIFN classifies foreign investment in banking institutions as a restricted activity. The Banking Law is silent as to foreign ownership of banking institutions in Taiwan; in the short-term future the likelihood of foreign-owned Taiwan banks is low. Rather, the Banking Law primarily contemplates foreign banks operating through Taiwan branches. It also authorizes the MOF to specify the branch locations of foreign banks based upon the need for international trade and industrial development.⁴² Foreign banks must allocate a separate operating capital in Taiwan.⁴³

Pursuant to the amended Banking Law, foreign banks' banking powers now are selected from the powers of not only commercial banks, but also savings banks or departments and trust banks or departments.⁴⁴ This expansion of the banking powers of Taiwan branches of foreign banks is the result of many years of lobbying efforts, particularly by American banking institutions operating in Taiwan, for national treatment. Such change has necessitated an amendment to the Guidelines for Screening and Approval of Establishment of Branches and Representative Offices by Foreign Banks (Foreign Banks Regulations).

The Foreign Banks Regulations have improved the national treatment of foreign banks, but complete open market access for foreign banks to participate in Taiwan's financial market is not likely in the foreseeable future.⁴⁵ The Foreign Banks Regulations clearly indicate that the MOF generally only invites the best and largest foreign banks to set up operations in Taiwan, knowing that allowing some level of foreign competition is the necessary trade-off for further internationalization of its financial sector. This limitation is to assist the MOF and the CBC in regulating foreign banks in Taiwan. Since they are the largest (and thus

41. See Banking Law art. 25; Regulations Governing the Establishment of Commercial Banks art. 3.

42. Banking Law art. 118.

43. *Id.* arts. 120, 121.

44. *Id.* art. 121.

45. There are, e.g., requirements on past business dealings with Taiwan banks and companies in order for foreign banks to be approved to set up branches or representative offices in Taiwan. There are also requirements such as those governing locations, banking powers, and deposit-to-capital ratios that are applicable to foreign banks' Taiwan branches. See also Liu, *supra* note 1, at 338-40.

presumed the best) foreign banks and are publicly traded in their home countries, they have an incentive to maintain their own reputation. Extensive regulation by the banking authorities in the foreign banks' home countries also alleviates the burden on ROC banking regulators.

V. Taiwan's Financial Developments for the New Decade

A. REMOVAL OF CAPITAL GAINS TAX

The rapidly transforming political, economic, and social environment in Taiwan requires that various laws and regulations be revamped. Tax measures are one of them. In 1988 highly volatile and speculative trading on the TSE fueled a well-politicized capital gains tax revolt. As a result, the government made a major compromise. The Income Tax Law was amended in late 1989 to eliminate entirely the income tax on gains from securities trading.⁴⁶ Instead, a higher rate was set, at 0.6 percent, for the securities transactions tax. Both measures became effective in 1990.

The removal of the securities-related capital gains tax will have a major impact for both domestic and foreign investors. If securities-related capital gains had been realized in 1989, Taiwan individuals and corporations would have been subject to an income tax on 50 percent or 25 percent, respectively, of the gains. A foreign investor's 1989 tax rate for capital gains was 25 percent as well. The new 0.6 percent securities transactions tax, as the only tax cost, compares favorably with the previous tax regime, so long as a transfer of securities realizes sufficient capital gains. In light of the high price-earning ratios of public companies and of those companies having the potential to go public in Taiwan, the shares of these companies often change hands at several times the cost basis of the original shareholders.⁴⁷ The removal of the capital gains income tax, therefore, could fuel more mergers and acquisitions in Taiwan, as the tax cost is now reduced to 0.6 percent of the gross selling price. The removal will also facilitate corporate reorganizations such as spin-offs by eliminating otherwise prohibitive tax costs. Taiwan's income tax legislation does not allow tax-free reorganizations except in the case of statutory mergers.

The new tax regime also takes on another significance: it applies to the transfer of both listed and unlisted securities. For most of the 1980s the capital gains income tax was suspended, but only with respect to listed shares. Therefore, the new tax regime since 1990 provides for adequate room in planning for tax-advantaged investment projects, particularly where they involve the transfer of unlisted shares of Taiwan companies before going public.

46. See Income Tax Law art. 4-1.

47. On the SEC's previous practice of regulating the underwriting price, thereby causing higher traded prices after the shares are listed, see Hsu & Liu, *supra* note 1, at 187.

B. NEW INVESTMENT INCENTIVE PROGRAM AND TAX REFORM

For many years Taiwan has used various tax and other incentives to encourage investment and foster economic growth. Enacted in the 1960s, the SEI has been the major embodiment of this incentive program. These incentives mainly take the form of an income tax holiday or an accelerated depreciation of machinery and equipment. They also include other measures such as investment tax credits, reduced customs duties or exemption of duties on the importation of machinery and equipment, reduced dividend withholding rate for approved FIA investors, and assistance in the acquisition of industrial land. Of late, the SEI has been criticized for distorting efficient allocation of resources and for creating an imbalance in sectoral growth in the economy. The SEI itself provides for its expiration by the end of 1990, which will have a major impact on investment decisions in Taiwan. The ROC Government has sponsored a bill to enact a replacement statute, the Statute for Upgrading Industries (SUI).⁴⁸

The SUI's professed cornerstone is neutrality of various measures to encourage investment, so as to avoid the misallocation of resources. To be sure, there will be fewer tax incentives. In addition, the focus of the legislation will shift from encouraging sectoral investments selectively to encouraging investment activities by their functions and their impact on the economy. The traditional preoccupation with the manufacturing sector will be rectified; instead, activities such as the purchase of machinery and equipment, marketing efforts to develop brand name recognition, and research and development programs will often be the test for providing investment incentives. Instead of providing for income tax holidays, the SUI is expected to rely more on investment tax credits.⁴⁹ To upgrade industries by fostering more capital-intensive investments, the proposed SUI bill also contains measures to liberalize restrictions on the amount of accumulated earnings companies may retain without such accumulated retained earnings being held to constitute deemed dividends to shareholders. The present incentive of the reduced dividend tax rate for FIA investors under the SEI is expected to remain as well.

Following the SAFE liberalization in 1987, the MOF impaneled a Tax Reform Commission to study various tax measures. It is expected that these tax reform measures will be guided by the same principles that have shaped the SUI bill. Thus far, the MOF has yet to act on these measures by adopting concrete bills to amend various existing tax measures. The long-term development of this tax reform, however, should be of interest to foreign investors examining investment opportunities in Taiwan. One possible recommendation of the tax measure may be the elimination of double income taxation on the same underlying corporate

48. As of the writing of this article, the SUI was being debated in the Legislative Yuan.

49. See Statute for Upgrading Industries [SUI] art. 7.

profits. There could be two alternatives. The first would grant a deduction to the distributing company, thereby treating dividends essentially as interest payments. The second alternative would call for granting a tax credit to the receiving shareholders. Both approaches are designed to streamline the taxation of corporate income streams and reduce the overall tax burden of corporations. Another tax measure may be not to recognize income when stock dividends are distributed.⁵⁰ Previously, the SEI provided for a tax deferment treatment for the distribution of stock dividends, but this exemption applied only to manufacturing companies declaring stock dividends in connection with a capital expansion, pollution control, or credit enhancement program.⁵¹

VI. Foreign Investors' Strategies for the Taiwan Market

A. LEVERAGE BY ON-SHORE PRESENCE

The discussions above should produce the following strategies for foreign companies interested in doing business in or with their counterparts in Taiwan. Foreign firms may wish to take advantage of the excess liquidity in Taiwan by, for example, attracting Taiwan individuals and enterprises to invest abroad. This is the business goal of many foreign firms. Experience has shown that these firms will be more successful if they set up some form of on-shore presence in Taiwan. On-shore presence suggests long-term commitment as well, a virtue for conducting business in a Chinese environment. This strategy also takes advantage of the liberalized investment environment of Taiwan in recent years. Even when the business goal of foreign firms is not to attract investment from Taiwan, but to trade with Taiwan, this strategy also applies. As indicated above, now there is no restriction on setting up wholly owned trading companies or branches with statutory or regulatory repatriation rights.

For those foreign investors interested in eventually providing liquidity and creating a public market for interest in their Taiwan operations, the on-shore presence is crucial. As discussed above, this strategy would entail having a company incorporated under the laws of the ROC and having the center of business activities for that company in Taiwan. These requirements are preconditions to taking such a company public in Taiwan.⁵²

B. TAKE ADVANTAGE OF THE SUI INCENTIVES

Foreign firms interested in engaging in manufacturing activities in Taiwan recently placed timing considerations above all other considerations because of the SEI expiration at the end of 1990. However, those who apply to set up investment operations after 1991 need not feel that they have necessarily missed

50. See Income Tax Law art. 76-1.

51. See SEI art. 13.

52. See SEL arts. 4, 22.

the boat. The SUI's investment tax credit could be a potentially useful incentive. Although a trend toward granting fewer incentives is clearly the long-term policy of the government in Taiwan, the incentives will not be withdrawn completely. Therefore, foreign investors keen on obtaining the marginal utility of their investment funds should take full advantage of the tax and other incentives available under the SUI.

C. INVEST IN THE SCIENCE PARK

Under the Statute for the Establishment of Science-Based Industrial Parks, a science park has been set up in Hsin Chu. The goal of the Hsin Chu Science Park is to create a mini-Silicon Valley in Taiwan to foster high-tech investment. Therefore, this statute also provides for a variety of investment incentives, including the five-year income tax holiday on initial establishment and the four-year income tax holiday on project expansions.⁵³ Importantly, however, unlike the SEI, which expired at the end of 1990, the science park statute does not have an expiration date. Indeed, a policy is being formulated to expand the science park concept and location islandwide. Therefore, foreign firms engaging in high-tech activities should consider the alternative of investing in the science park.

Timing should be an important consideration as the Hsin Chu Science Park already has shown some signs of saturation and difficulties in housing all investment projects. However, as scientific and technological research continues to be an important governmental policy, it is believed that the government will acquire additional space around the science park. Therefore, its long-term prospect as an ideal research, development, and manufacturing environment is still promising.

D. TAP THE SERVICE AND RETAIL MARKETS IN TAIWAN

The service sector of Taiwan's economy has been identified as the sector that will enjoy higher growth in the future. In 1988 and 1989 this sector represented the highest growth in Taiwan's domestic economy. Foreign firms should do well to penetrate this potentially lucrative market. As discussed above, the overall regulatory environment has been substantially liberalized. However, these firms should take heed of the negative listing policy discussed above and then structure their investment projects accordingly.

The same consideration applies to Taiwan's emerging retail and leisure-related market.⁵⁴ Taiwan consumers' purchasing power has increased along with the accumulation of wealth. However, their willingness to spend and enjoy a higher living standard is not matched by the availability of inexpensive goods and

53. See Statute for the Establishment and Administration of the Science-Based Industrial Parks arts. 15-19.

54. To be sure, much of this has to do with Taiwan's massive import liberalization in recent years. See B. BALASSA & J. WILLIAMSON, *supra* note 1, at 83.

services, hence, the business opportunities for tackling this market. In any event, some Japanese, European, and American firms' success in this market (in such segments as department stores, supermarket and convenience stores, fast food restaurants, trading companies, and other retail outlets) already strongly suggests that there is no reason why other foreign firms cannot achieve the same result in this segment of the economy.

E. TAKE ADVANTAGE OF THE FIA HOLDING COMPANY STRUCTURE

As discussed above, foreign firms now may set up FIA holding companies in Taiwan with repatriation rights. Although the foreign investor does not yet have any clear idea of what sector of Taiwan's economy in which to invest, the FIA holding company enables him to deposit such funds pending investment in N.T. dollars in Taiwan. This structure thus offers the flexibility of a vehicle for holding investments in various sectors in Taiwan's economy within the limits of the negative listing. Where the foreign investor has a commitment toward Taiwan, but wishes to reduce the foreign exchange risk resulting from the N.T. dollar's further appreciation, the FIA holding structure also provides for this exchange risk protection.⁵⁵

An FIA holding company can invest in public companies in Taiwan, but it also may set up or invest in private companies that have a good potential of going public in Taiwan. Although double income taxation is a potential disadvantage, under the SUI, as shareholders in operating companies, such FIA holding companies can accumulate or capitalize retained earnings without triggering any income tax. When the opportunity is ripe for an acquisition or initial public offering, then offering investors may exit through realizing capital gains at a low overall tax cost.

F. PARTICIPATE IN MEZZANINE FINANCING OPPORTUNITIES

Many Taiwan companies are seeking to internationalize, yet they do not enjoy recognition in the international business community. Participation in the management of such Taiwan companies through the acquisition of some (often minority) equity interest is a viable strategy for foreign companies seeking to enter the Taiwan market. Such Taiwan companies often seek mezzanine financing to widen their shareholder base and to secure international recognition by obtaining the investment and support from world class companies or investor groups. At one time this strategy had become too costly because of the runaway price earning ratios during late 1989 and early 1990. Since then the market corrected itself, making the entry price for foreign investors in a round of mezzanine financing more affordable.⁵⁶

55. The initial capital of a Taiwan company has to be paid in before the promoters' meeting can be held. Company Law art. 143.

56. This strategy could be perceived as a variation of the venture capital investment. See Liu, *Case Study: Venture Capital Investment Enterprises in Taipei, China*, in ASIAN DEVELOPMENT BANK, VENTURE CAPITAL FINANCING IN THE ASIA-PACIFIC REGION 227 (1988).

Again, a good exit for such mezzanine financing participation is often the initial public offering of the investee companies. As discussed above, the more favorable tax regime since 1990, following the removal of the securities-related capital gains income tax, will also foster an environment conducive to such investment strategies.

G. SEEK JOINT VENTURE OPPORTUNITIES AND STRATEGIC ALLIANCES

Foreign firms should consider joint venture opportunities when contemplating investment projects in Taiwan. A multitude of reasons supports this strategy. First, there is a changing of the guard in Taiwan's leading corporate families. First-generation entrepreneurs are transferring control to second-generation, Western-trained family members, who are more receptive to joint ventures. Second, businesses targeting Taiwan's domestic market have become more profitable; for one thing, the currency appreciation and increased per capita GNP have made the domestic market more important. In penetrating the domestic market local partners can help a great deal. Third, Taiwan companies have gained much sophistication in production and management. They can truly contribute in a joint venture project. More importantly, international joint ventures are a good way for Taiwan companies to internationalize; strategically, sooner or later Taiwan companies need to increase their international activities outside Taiwan. They will become a new breed of multinational corporations. Such international joint ventures could pave the way for further global strategic alliances.⁵⁷

To be sure, such international joint ventures could take a variety of forms and select a number of sites. However, Taiwan partners in an international joint venture are always mindful of the possibility of the joint venture company going public in Taiwan, and rightly so. In recent years more international strategic alliances have been formulated on such a model. Many Taiwan companies have successfully acquired partial interest in existing foreign companies or have established new joint ventures to gain access to marketing and distribution channels, raw materials, and technologies.

VII. Conclusion

Financial reforms pose challenges and opportunities. Financial regulators and intermediaries in Taiwan alike will have to deal with the aftermaths of its three waves of financial reforms. Further development of Taiwan's economy has much to do with the success of such reforms, and there are reasons to be optimistic about such success because liberalization has increased the flexibility in arranging transactions and implementing investment strategies.

57. Except for more sensitive economic segments in the negative list such as securities, Taiwan does not require foreign investors to joint venture with local investors. Compare Salacuse, *Host Country Regulation of Joint Ventures and Foreign Investment*, in *JOINT VENTURING ABROAD: A CASE STUDY* 103 (D. Goldsweig ed. 1985).

Taiwan is in a deregulatory trend. Well-to-do middle class, western-trained technocrats and business leaders are more practical than their counterparts of the prior generation. More importantly, the government is beginning to realize and accept the change of its role from primarily a leader and active participant in the economy to a regulator whose task is to adopt fair and clear rules to be faithfully enforced in order to maintain an efficient, competitive environment.⁵⁸ Financial crises may still occur during this process, but should be addressed early enough to be nipped in the bud. That, of course, was the lesson of the 1980s for Taiwan; it was paying for the cost of a largely successful, but imbalanced, national development strategy of the 1970s.

Taiwan is not an isolated, island Chinese economy. Recent ties with Hong Kong and, for that matter, the overseas Chinese business community throughout Southeast Asia have increased substantially. There is much to the Taiwan-Hong Kong linkup of their market economies. The two most successful Chinese-oriented economies offer much hope for an aspiring mainland China. Assuming a gradually stabilized, enlightened, and liberalized China (or at least regionally within it), resources in Taiwan are also useful in developing the mainland Chinese market. That, to be sure, will also be the task of the 1990s for these two free Chinese communities.⁵⁹

Taiwan's transformation definitely will center around financial development strategies, and as argued above, therein lie business opportunities for astute foreign investors. For its part, Taiwan traditionally has had to rely on human capital alone, but now has tasted the power of financial capital. In the long run the capital and financial markets in Taiwan should gain more sophistication and respect and may indeed play a more significant role in the regional financial market. Foreign firms will do well to take advantage of the new strategy of tapping Taiwan's human and financial capital during the next round of its economic growth.

58. See Liu, *supra* note 1, at 358-60.

59. See J. WEISS, *THE ASIAN CENTURY* 155-56 (1989).