THE REVISION OF TAIWAN'S COMPANY LAW: THE STRUGGLE TOWARD A SHAREHOLDER-ORIENTED MODEL IN ONE CORNER OF EAST ASIA

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ABSTRACT

Proponents of the theory of global convergence of corporate governance argue that corporate governance regimes around the world are converging toward one system—the dispersed-ownership/capital market model with a corporate governance system emphasizing the interests of shareholders. This article suggests that actual global convergence may be an unachievable myth, but the process toward greater protection of shareholder interests and a more efficient dispersed-ownership system in a particular jurisdiction should be an observable phenomenon.

This article proposes that if Taiwan were in transition toward a shareholder-oriented and/or dispersed-ownership model, we would expect it to be reflected in the recent revisions to Taiwan's Company Law. This article argues that the recent revisions indeed show that Taiwan is addressing controlling shareholder expropriation, which is essential to protecting shareholder interests in a concentrated-ownership system like Taiwan. In addition, the increased importance that the revisions place on the role and accountability of the professional manager indicate that dispersion of ownership is already factoring into the corporate governance of the Taiwanese firm. Whether Taiwan continues down this path of shareholder protection and dispersed ownership remains to be seen.

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I. INTRODUCTION

It is appropriate to begin an article on corporate governance with a definition of corporate governance: "[The] rules and market practices which determine how companies, especially listed companies, make decisions, the transparency of their decision-making processes, the accountability of their directors, managers and employees, the information they disclose to investors, and the protection of minority shareholders."[1] This definition could generally apply to corporate governance in most countries around the world, but only because it is a broad definition. As soon as one goes deeper into the study of comparative corporate governance, one discovers that our broad definition only raises more questions: What role should the board play in reducing potential abuse by large shareholders or powerful managers? What role should institutional investors, labor unions, creditors, or the state play in corporate governance? When should formal legal rules control and when should market practices and other norms define a corporate governance regime? The answer to each of these questions may vary from country to country and from firm to firm depending on a host of factors.

Once we have accepted the idea that specific corporate governance concerns may vary from country to country, we are confronted with additional questions: Is there a superior system of corporate governance? If there is, why are there so many variations around the world? Are the different corporate governance regimes in the world all converging toward one common system? If so, what system is it? How will convergence happen and is it happening now?

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[1]Bernard S. Black et al., *Introduction* to *Corporate Governance in Korea at the Millennium: Enhancing International Competitiveness—Final Report and Legal Reform Recommendations to the Ministry of Justice of the Republic of Korea*, 26 J. CORP. L. 546, 547-48 (2001).

The convergence theory, simply stated, suggests that globalization will create competition between companies governed by various corporate governance regimes.[2] The companies with access to strong securities markets will have a significant competitive advantage over companies that do not. Generally speaking, strong securities markets are characteristic of dispersed-ownership systems, where a diffuse body of public investors owns the shares of large companies.[3] For securities markets to operate at maximum efficiency, corporate governance rules must adequately protect shareholders. In short, countries must enable their companies to take advantage of the global securities market by providing them a legal regime that adequately protects the interests of shareholders.[4]

This article does not attempt to argue whether market forces will require all corporate governance regimes to converge toward a shareholder-oriented/dispersed-ownership model; rather, this article examines one specific jurisdiction, Taiwan, and analyzes whether it is making a transition toward a shareholder-oriented model of corporate governance and/or dispersed-ownership model. If a jurisdiction is making a transition toward a shareholder-oriented and/or dispersed-ownership model, formal legal change and private ordering should reflect this transition. More specifically, we would expect any major reform to a country's corporate law regime to reflect its transition toward a shareholder-oriented and/or dispersed-ownership model. Because Taiwan undertook a large-scale revision to its Company Law in 2001, the time is ripe to study whether Taiwan is transitioning toward a shareholder-oriented model of corporate governance and/or dispersed-ownership model.

Part II of this article presents a cursory review and a summary of the debate on global convergence of corporate governance.

Part III attempts to develop a model with which we can determine whether Taiwan is making a transition toward a shareholder-oriented model of corporate governance and/or a dispersed-ownership system. This article proposes that if Taiwan were transitioning toward a shareholder-oriented model of corporate governance, then recent revisions to its Company Law would address the issue of controlling shareholder expropriation of minority shareholders. In addition, if Taiwan were transitioning toward a

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[2]*See* John C. Coffee, Jr., *The Future as History: The Prospects for Global Convergence in Corporate Governance and its Implications*, 93 NW. U. L. REV. 641, 642 (1999); Ronald J. Gilson, *Globalizing Corporate Governance: Convergence of Form or Function*, 49 AM. J. COMP. L. 329, 336 (2001).

[3]Coffee, *supra* note 2.

[4]*See* John C. Coffee, Jr., *The Rise of Dispersed Ownership: The Roles of Law and the State in Separation of Ownership and Control*, 111 YALE L.J. 1, 24 (2001) (stating most scholars agree efficient securities markets are predicated on adequate protection of minority shareholders).

dispersed-ownership system, the recent revisions to its Company Law should reflect a growing concern regarding the role of the professional manager in the Taiwanese company and her ability to abuse her increasing power.

Part IV of this article, using the model developed in Part III, analyzes the recent revisions to the Company Law that address the independence of the board of directors, the independence of the supervisor and her ability to monitor the board, shareholders' rights, and the role of the professional manager. This article suggests that revisions in these areas of the Company Law indicate Taiwan has begun a transition toward a shareholder-oriented model of corporate governance and possibly toward a dispersed-ownership system.

Part V takes a broader look at the recent revisions to the Company Law, which were designed to create a more enabling corporate law regime. The revisions suggest that lawmakers were unwilling to change rigid provisions that provided even minimal protection to the interests of shareholders. This phenomenon lends support to the theory that Taiwan is transitioning toward a shareholder-oriented model of corporate governance.

This article concludes in Part VI that the November 2001 revisions to Taiwan's Company Law indicate Taiwan has indeed begun a transition toward a shareholder-oriented model of corporate governance. In summary, although one cannot declare that Taiwan has achieved a corporate governance regime that provides optimal protection for shareholders, certain indicia support the proposition that Taiwan has either begun to experience or is anticipating the corporate governance issues that manifest themselves in dispersed-ownership systems: the struggle with the relevant issues pertaining to controlling shareholder expropriation of minority shareholders; the reluctance of lawmakers to revise disabling Company Law provisions that provide even minimal protection to shareholders; and the increased importance the revisions place on the role of the professional manager and her ability to abuse her power.

II. TOWARD WHAT MODEL OF CORPORATE GOVERNANCE ARE WE CONVERGING?

A major question presented in the academic literature of both economics and law is whether corporate governance regimes around the world are converging toward one system of corporate governance. Proponents of global convergence of corporate governance advance the theory that a dispersed-ownership/capital market model with a corporate governance system emphasizing the interests of shareholders will ultimately become the predominant model of corporate governance around

the globe—market forces will require it. Thus, the two core concepts in the convergence literature are the dispersed-ownership model of corporate ownership and the shareholder-oriented model of corporate governance. The debate over convergence centers on whether these models are more efficient than other models of corporate ownership and governance and whether market forces would result in the eventual dominance of these models around the world.

A. *The Ultimate Global Dominance of the Dispersed-Ownership/Shareholder-Oriented Model of Corporate Ownership and Governance*

There are two basic corporate ownership models in the world: the dispersed-ownership model and the concentrated-ownership model.[5] The dispersed-ownership model is characterized by a strong securities market and substantial dispersion of ownership among the public. Securities markets play a major role in providing firms with capital in the dispersed-ownership model. The concentrated-ownership model, on the other hand, is characterized by strong banks and a weak securities market.[6] A sizeable percentage of a company's shares is held in large blocks, with a smaller portion of shares held by a dispersed group of public shareholders.[7] Banks generally play a greater role in providing firms with necessary capital in the concentrated-ownership model.[8]

The convergence theory in its simplest form states that globalization will create competition between the dispersed-ownership model and the concentrated-ownership model.[9] The dispersed-ownership model will emerge victorious because large corporations need capital to grow and compete in their product markets, and a strong securities market gives these

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[5]*See* Rafael La Porta et al., *Corporate Ownership Around the World*, 54 J. FIN. 471, 471-72 (1999) (surveying concentrated ownership and dispersed-ownership countries); *see also* Lucian Arye Bebchuk & Mark J. Roe, *A Theory of Path Dependence in Corporate Ownership and Governance*, 52 STAN. L. REV. 127, 129 (1999) (stating that some countries have diffuse ownership and some have concentrated ownership); Amir N. Licht, *The Mother of All Path Dependencies: Toward a Cross-Cultural Theory of Corporate Governance Systems*, 26 DEL. J. CORP. L. 147, 149 (2001) (questioning why companies in some countries have dispersed ownership and in other countries concentrated ownership).

[6]*See* Coffee, *supra* note 2, at 642-43.

[7]*See* La Porta et al., *supra* note 5, at 491-500.

[8]*See* Coffee, *supra* note 2, at 643.

[9]*Id.* at 641-42.

corporations more efficient access to capital.[10] Furthermore, a strong securities market better supports innovation through venture capital markets.[11] In short, companies that have access to a strong securities market will have a significant competitive advantage over companies that do not. This global competition means that a country must enable companies within its jurisdiction to take advantage of the global securities market.[12]

A country can enable its companies to better compete in the global stock market by providing them a corporate governance regime conducive to dispersed-ownership. Corporate governance may help reduce a company's cost of capital if it serves to maximize share value because when share values are at a maximum, a company can raise capital more efficiently. Generally speaking, the shareholder-oriented model, i.e., a legal regime that adequately protects the interests of shareholders, is most conducive to dispersed-ownership.[13] Share values will increase when a firm's priority is the interests of its shareholders, rather than the interests of labor, political agendas, management, or the private benefits of controlling shareholders. Therefore, a firm's success in raising capital on the securities market depends, at least in part, on whether it adequately protects the interests of its shareholders, especially minority shareholders. By adopting a shareholder-oriented model of corporate governance, a country can enable (and require) its companies to adequately protect the interests of minority shareholders.[14]

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[10]*See* Coffee, *supra* note 2, at 641 (discussing Berle & Means's assumption that dispersion was necessary to raise capital needed for large scale industry); *id.* at 649 (describing the theory that strong legal protections mean higher stock prices, which enables a company to more efficiently use its stock for acquisitions).

[11]*See* Ronald J. Gilson & Bernard S. Black, *Venture Capital and the Structure of Capital Markets: Banks Versus Stock Markets*, 47 J. FIN. ECON. 47, 47 (1998).

[12]*See* Bebchuk & Roe, *supra* note 5, at 152 (discussing the argument that a global capital market encourages companies to adopt more efficient ownership structures); Coffee, *supra* note 2, at 646 (characterizing the theory as "choose the wrong form, and if it is important, you will suffer at the hands of competitors who choose a superior form").

[13]*See* Coffee, *supra* note 2; La Porta et al., *supra* note 5, at 511 (concluding that "equity markets are both broader and more valuable in countries with good legal protection of minority shareholders").

[14]*See* La Porta et al., *supra* note 5, at 512 (suggesting that improving the legal environment to protect minority shareholders will create a preferable condition for dispersion of ownership).

B. *Counter Voices in the Debate on Global Convergence*

Of course, for every proposition there are contrary views, and the debate on global convergence of corporate governance is no exception. Some scholars have largely dismissed the theory of global convergence of corporate governance as U.S.-centric chauvinism and question whether globalization is really promoting convergence.[15] Other critics of the global convergence theory deny that the dispersed-ownership model is the most efficient model—they point to shortcomings of the dispersed-ownership model, such as encouraging management to place too much emphasis on short-term gains.[16] Scholars have also noted that the dispersed-ownership model may be inferior to the concentrated-ownership model with respect to monitoring the performance of managers and gaining access to information about the company.[17] They also suggest that a concentrated-ownership model may better support innovation through its institution-oriented system.[18] In addition, there are those who feel that corporate governance in each of the models of corporate ownership has advantages and disadvantages, and that a country may try to exploit the advantages of both systems.[19]

It has also been suggested that market forces were not solely responsible for the predominance of the dispersed-ownership model in the United States and Great Britain. Professor Mark Roe argues that the rise of dispersed ownership in the United States was not purely the result of market forces pushing firms toward the most efficient way to raise capital.[20] Instead, there were political and historical path dependent reasons that led the United States down the road of dispersed ownership.[21] He argues that

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[15]*See* Douglas M. Branson, *The Very Uncertain Prospect of "Global" Convergence in Corporate Governance*, 34 CORNELL INT'L L.J. 321, 350 (2001).

[16]*See* Jeremy C. Stein, *Takeover Threats and Managerial Myopia*, 96 J. POL. ECON. 61, 62 (1988) (discussing the theory of managerial myopia, which argues that the takeover market puts pressure on management and leads them to focus more on short-term profits); *see also* David Charny, *The German Corporate Governance System*, 1998 COLUM. BUS. L. REV. 145, 152-57 (discussing the monitoring role of banks in German corporations).

[17]*See* JEREMY EDWARDS & KLAUS FISCHER, BANKS, FINANCE, AND INVESTMENT IN GERMANY (1994); *see also* Coffee, *supra* note 2, at 661 (discussing the argument that blockholders are superior monitors).

[18]*See* Charny, *supra* note 16, at 163.

[19]*Id.* at 164-65.

[20]MARK J. ROE, STRONG MANAGERS, WEAK OWNERS: THE POLITICAL ROOTS OF AMERICAN CORPORATE FINANCE 285 (1994). *But see* La Porta et al., *supra* note 5, at 511-12 (questioning Mark Roe's "strong manager, weak owners" theory).

[21]*See* ROE, *supra* note 20, at 48-49 (summarizing the public sentiment and political reasons that led to the regulation of financial institutions and the rise of professional managers). Similarly, Professor Roe has also argued that the social democratic political systems of many

politically motivated regulation of financial institutions in the United States fragmented institutional capital,[22] effectively preventing financial institutions from becoming large blockholders in public corporations.[23] The implication of his theory is that if banks had been less restricted by government regulation in the United States during certain formative years, the typical U.S. public firm may have been characterized by power sharing between managers and financial institution blockholders.[24]

C. *Forces That May Serve as Obstacles to Convergence—Path Dependencies*

Even if we assume a shareholder-oriented/dispersed-ownership model is the most efficient system because it reduces capital costs, scholars continue to argue that there are certain path dependent forces that may prevent a country from developing a dispersed-ownership model despite market pressure.[25] They argue that not only have path dependent forces led countries to develop concentrated-ownership systems, but those countries' legal and extra-legal institutions would have also developed around and adapted in response to these systems.[26] In effect, these institutions, on both a national level and a firm level, would reinforce the existing concentrated-ownership system. Thus, changing to a shareholder-oriented/dispersed-ownership corporate governance regime is not as simple as deciding to create a securities exchange or transplanting the shareholder protections laws from a dispersed-ownership system like that of the United States. Simply copying another system's institutions would lead to inefficiencies

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European countries and Japan serve to "stymie" dispersion of ownership and encourage concentrated ownership as a defense against the costs imposed by the political system, namely, the pressure to use corporate funds for social welfare. *See generally* Mark J. Roe, *Political Preconditions to Separate Ownership from Corporate Control*, 53 STAN. L. REV. 539, 541 (2000) (arguing that "shareholders' core problems in the public firm cannot be readily resolved in a strong social democracy"). *But see* Coffee, *supra* note 4, at 6-7 (disagreeing with Mark Roe's theory that a country must first resolve the issue of pressures social democracy imposes on the firm before dispersion of ownership can occur).

[22]*See* ROE, *supra* note 20, at 48-49.

[23]*See id.* at 5.

[24]*See id.* Professor Mark Roe has also argued that social democracies may "stymie" dispersion of ownership and that political change may need to take place before dispersion can truly set in. *See* Roe, *supra* note 21, at 210-12.

[25]*See* Bebchuk & Roe, *supra* note 5, at 131-32 (stating that market pressures cannot eliminate path dependencies).

[26]*See id.* at 137-42 (discussing corporate structures and efficiencies gained by development around these structures); *id.* at 153-57 (discussing corporate rules and efficiencies gained by development around these rules).

because it would disturb the existing synergies and interdependencies within the system.[27]

In addition to path dependencies regarding efficiency concerns, there are also path dependencies related to rent-protection. In any corporate governance system, there will be rent-seekers—those who benefit from the status quo because they are able to extract private benefits at the expense of others.[28] Generally, rent-seekers will also possess political power and influence, which they can use to prevent legal reform.[29] In concentrated-ownership systems, controlling shareholders often enjoy a private benefit of control because they are in a position to extract benefits at the expense of minority shareholders.[30] Because protection of minority shareholders is an integral part of a shareholder-oriented model, controlling shareholders would be resistant to any significant move toward a shareholder-oriented legal regime.[31] Enacting laws that significantly change the balance of power between minority and controlling shareholders would reduce the ability of controlling shareholders to expropriate the minority, which, in turn, would reduce the value of the controlling shareholders' control premiums.[32] In contrast, the shares of the minority would increase in value as investor protection improves because there would be less risk of expropriation. This shift in the balance of power between controlling shareholders and minority shareholders would result in a redistribution of wealth—minority shareholders gain at the expense of the controlling shareholder.[33] Theoretically, there should be a point where the controlling shareholder will not resist reform because the benefits of reduced capital costs (reduced because share values have been maximized by adequate protection of shareholder interests) will exceed her private benefits of control.[34]

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[27]*See id.* at 137-42, 153-57.

[28]*See id.* at 142.

[29]*See* Bebchuk & Roe, *supra* note 5, at 142; Coffee, *supra* note 2, at 654.

[30]*See* Bebchuk & Roe, *supra* note 5, at 130.

[31]*See* Henry Hansmann & Reiner Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439, 442 (2001) ("The shareholder-oriented model does more than assert the primacy of shareholder interests, however. It asserts the interests of all shareholders, including minority shareholders."); La Porta et al., *supra* note 5, at 512 (stating authors' skepticism of the prospects of global convergence because of resistance from controlling shareholders).

[32]*See* Bebchuk & Roe, *supra* note 5, at 143-47 (discussing controlling shareholder resistance to diffusion because she would lose her rent and not capture the gain created by the efficiency).

[33]*See* La Porta et al., *supra* note 5, at 512-13.

[34]*See* Bebchuk & Roe, *supra* note 5, at 130 (discussing how powerful groups will resist change if they do not bear the full cost of current system or capture the full benefit of change); Hansmann & Kraakman, *supra* note 31, at 460-61(arguing that controlling shareholders may

In contrast, in dispersed-ownership systems, professional managers have opportunities to extract private benefits at the expense of shareholders. The dispersion of ownership creates problems for these owners in monitoring the faithfulness and competence of the firm's managers.[35] Because of the difficulties and costs associated with the monitoring of management, managers are in a position to benefit themselves at the expense of the shareholders.[36] Professional managers would resist any reform adopting a shareholder-oriented model because it would adversely affect their ability to benefit themselves.[37]

D. *Getting Around the Path Dependencies—Functional Convergence*

As discussed above, path dependencies based in intra-system efficiencies would be an obstacle for transition to a new system.[38] In response to this problem, scholars have suggested that convergence would most likely take place on a functional, rather than formal, level.[39] Instead of wholesale (or piecemeal) transplant of the shareholder protection regime of a dispersed-ownership jurisdiction, a country may develop equivalent protections around its already existing institutions.[40] Of course, this scenario assumes that the existing institutions, formal legal rules, and extra-legal norms are conducive to this type of functional convergence.[41] Although the theory of functional convergence has merit, as a practical matter it is difficult to determine when one mechanism or group of mechanisms in one country is functionally equivalent to those of another

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relinquish control to reap economic benefits of a shareholder-oriented system).

[35]*See* ROE, *supra* note 20, at 23 (discussing the agency costs of bonding, monitoring and residual losses).

[36]*See* Bebchuk & Roe, *supra* note 5, at 148 (discussing internal rent-seeking of incumbent managers).

[37]*See id.*

[38]*See supra* text accompanying notes 25-27.

[39]*See* Coffee, *supra* note 2, at 650; Gilson, *supra* note 2, at 332.

[40]*See* Gilson, *supra* note 2, at 338 (stating that functional convergence will be crucial where formal convergence is too costly).

[41]*See* Gilson, *supra* note 2, at 340-42 (suggesting that path dependencies reinforced by formal legal rules may prevent functional convergence); Curtis J. Milhaupt, *Creative Norm Destruction: The Evolution of Nonlegal Rules in Japanese Corporate Governance*, U. PA. L. REV. 2083, 2084-85 (2001) (discussing social norms that affect the corporate governance of Japanese firms).

country. Each system will have unique costs and benefits that may be difficult to identify and quantify.[42]

E. *Getting Around the Path Dependencies—Private Ordering*

If either formal or functional change to protect shareholders on the national level is stymied by path dependencies, a firm may still be able to make itself more competitive in the market for capital through private ordering.[43] Through private ordering, a company can effectively signal to potential investors that it will not expropriate the interests of minority shareholders. This private ordering may take the form of amending the company's articles of incorporation to provide better protections for minority shareholders, listing on a domestic securities exchange that has rules protecting minority shareholders, or cross listing on a foreign exchange (e.g., the New York Stock Exchange).[44] This serves as a way for the firm to bond itself to stricter corporate governance rules. It also signals to investors that the firm will protect shareholders' interests.[45] Even a private shareholders' agreement between the controlling shareholder and a large blockholder that is not in the controlling shareholder's camp may send a message to investors that the controllers will not benefit themselves at the expense of the minority.[46] The drawback of private ordering mechanisms, however, is the associated transaction costs that increase the firm's cost of

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[42]As an example, there had been support for the proposition that the Japanese main bank system was the functional equivalent of the U.S. takeover market. *See* Paul Sheard, *The Main Bank System and Corporate Monitoring and Control in Japan*, 11 J. ECON. BEHAV. & ORG. 399, 409 (1989) ("[T]he main bank performs a role that closely parallels in its effects the external takeover market . . . ."). Later scholarship raised doubt as to whether these two mechanisms were functional equivalents. *See* Ronald J. Gilson, *Reflections in a Distant Mirror: Japanese Corporate Governance Through American Eyes*, 1998 COLUM. BUS. L. REV. 203, 217 (1998) ("[T]he main bank system is not a substitute for external monitoring by the market for corporate control.").

[43]*See* Gilson, *supra* note 2, at 346-56 (discussing convergence by contract, terms of securities, a stock exchange listing, incorporation in another jurisdiction).

[44]*See id.*

[45]For a more detailed discussion on private ordering through listing on securities exchanges with favorable shareholder protection rules, see John C. Coffee, Jr., *The Impact of Cross-Listings and Stock Market Competition on International Corporate Governance*, *in* GLOBAL MARKETS, DOMESTIC INSTITUTIONS: CORPORATE LAW AND GOVERNANCE IN A NEW ERA OF CROSS-BORDER DEALS (New York: Columbia University Press, Curtis J. Milhaupt ed. forthcoming 2003).

[46]*See* La Porta et al., *supra* note 5, at 504-05 (discussing how having a large shareholder that is not part of the controlling shareholder group may prevent controlling shareholder expropriation).

raising capital.[47] Because of increased capital costs, the firm that must rely on private ordering as a signal to investors will ultimately suffer a competitive disadvantage in the market for capital.

F. *Does the Dispersion of Ownership Necessarily Require the Shareholder-Oriented Model—Does Law Matter?*

Scholars have debated how much law, rather than social and market forces, actually affects corporate governance and ownership structures.[48] Several prominent economists have become leading voices for the proposition that corporate law is important in the development of corporate ownership structures. In a series of articles examining corporate governance and ownership around the world, they concluded that there is a correlation among good legal protection of shareholders, dispersion of ownership, and strong securities markets.[49]

In contrast, it has been argued that strong legal protection for minority shareholders is not necessarily a prerequisite for dispersion of ownership. Professor John Coffee has presented evidence that private ordering played a major role in the dispersion of ownership in the absence of formal legal rules protecting minority shareholders.[50] Similarly, Professor Brian Cheffins has argued that the law was an insignificant factor in early ownership dispersion in Great Britain[51] and credits "self-regulation" for the beginning of dispersed ownership.[52]

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[47]*See* Bebchuk & Roe, *supra* note 5, at 141 (stating that network externalities may disadvantage a firm that gives greater protection to shareholders than other firms in its jurisdiction); Gilson, *supra* note 2, at 350-51 (discussing legal barriers to incorporating in another jurisdiction).

[48]*See* Brian R. Cheffins, *Does Law Matter? The Separation of Ownership and Control in the United Kingdom*, 30 J. LEGAL STUD. 459, 459 (2001) (characterizing the debate as "intense").

[49]*See* La Porta et al., *supra* note 5, at 511-13; Rafael La Porta et al., *Legal Determinants of External Finance*, 52 J. FIN. 1131, 1149 (1997); Rafael La Porta et al., *Law and Finance*, 106 J. POL. ECON. 1113, 1152 (1998).

[50]*See* Coffee, *supra* note 4, at 29-31. Coffee argues that dispersion developed in common law countries not because they provided better legal protections for shareholders, but because they were more conducive to private law-making. *See id.* at 8-9.

[51]*See* Cheffins, *supra* note 48, at 483 ("The law deserves little of the credit for [dispersion of ownership] since the legal system offered minority shareholders little protection against opportunism by insiders.").

[52]*See id.* at 484.

Professor Coffee does note, however, that formal legal protections are necessary to maximize share value.[53] Thus, eventually a minority shareholder constituency will grow to create a lobbying force for formal legal protections,[54] and a company in a jurisdiction adopting optimal legal protections for shareholders will be more competitive in the market for capital.[55] The U.S. experience as presented by Professor Coffee may echo the general sentiment of scholars—dispersion can occur to a certain extent before formal protections of minority shareholders are in place, but law does in fact play a significant role in the dispersion of ownership, in addition to market and social norms.[56]

G. *Does the Shareholder-Oriented Model Necessarily Result in Dispersion of Ownership?*

Although the initial stages of ownership dispersion may occur in the absence of formalized legal rules protecting minority shareholder interests, once a country has adequate legal protections for shareholders, it seems to follow that dispersed ownership will gradually grow. Legal rules protecting minority investors will limit the ability of controlling shareholders to extract private benefits at the expense of the minority, thus reducing their private benefit of control.[57] Therefore, the controlling shareholders will be less resistant to relinquishing control for two reasons: (1) gain from reduced capital costs will exceed private benefits of control (once formal legal rules have reduced the private benefit of control),[58] and (2) the

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[53]*See* Coffee, *supra* note 4, at 66 (reinterpreting earlier studies, author states that dispersion of ownership can occur without a strong legal framework, but will not function optimally).

[54]*See id.* at 7 (discussing how there must be a constituency of shareholders before legal change will occur).

[55]"[E]quity markets are both broader and more valuable in countries with good legal protection of minority shareholders." La Porta et al., *supra* note 5 , at 511.

[56]*See, e.g.*, Bernard S. Black, *The Legal and Institutional Preconditions for Strong Securities Markets*, 48 U.C.L.A. L. REV. 781, 782-83 (2001) ("Investor protective laws are important, but not nearly enough to sustain strong securities markets."); John C. Coffee, Jr., *Do Norms Matter? A Cross Country Evaluation*, 149 U. PA. L. REV. 2151, 2155 (2001) (calling the "law matters" thesis "highly plausible even in the absence of strong statistical correlations between minority legal protections and ownership dispersion[,]" but also discussing the importance of "legally nonenforceable norms"). *But see* Cheffins, *supra* note 48, at 484 ("The British experience therefore puts those who argue that the law has a pivotal influence on the development of strong securities markets under an onus to refine their analysis."). For a discussion of the interrelation between corporate law and social norms, see generally Melvin A. Eisenberg, *Corporate Law and Social Norms*, 99 COLUM. L. REV. 1253 (1999).

[57]*See supra* text accompanying notes 13-14.

[58]*See supra* text accompanying notes 29-33.

controlling shareholder can be confident she will not be expropriated if she becomes a minority shareholder.[59]

In more recent scholarship, however, Professor Mark Roe has suggested that strong legal protections for minority shareholders will not necessarily result in greater dispersion of ownership if a legal regime does not adequately deal with the issues of management competence.[60] He argues that corporate law generally addresses the problem of expropriation of shareholders, either through direct diversion of funds or through interested party transactions.[61] Corporate law, however, provides shareholders with little or no protection against management incom-petence.[62] Because large blockholders in concentrated-ownership systems are better able to monitor management performance, a concentrated-ownership jurisdiction with strong protections against expropriation of minority shareholders may not see significant ownership dispersion (i.e., the breaking up of these large blocks) unless they also adequately deal with monitoring management performance.[63]

H. *Summary of the Convergence Debate*

In summary, scholars are debating whether there will be a global convergence of corporate ownership to a dispersed-ownership model because it provides firms with the most efficient access to capital. The dispersed-ownership model requires sufficient protection of shareholders from those who would extract private benefits at the expense of the shareholders.[64] On the firm level, companies may enter into private ordering mechanisms that signal to investors that the company adequately protects the interests of shareholders. Private ordering, however, is fraught with transaction costs. Furthermore, maximization of share value, which reduces a firm's cost of capital, may only be attainable through formal legal protection of shareholders.[65]

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[59]*See* Coffee, *supra* note 4, at 30-31 (discussing how investment bankers were able to protect shareholders from incoming controlling shareholders); *id.* at 33 (discussing how mergers of large corporations raised capitalization beyond the means of corporate raiders and, thus, created more stable dispersed ownership).

[60]Mark J. Roe, *Corporate Law's Limits*, 31 J. LEGAL STUD. 233 (2002).

[61]*See id.* at 235, 239-40.

[62]*See id.* at 235, 239-40; *see also* Coffee, *supra* note 4, at 6-7 (discussing the extent private lawmaking will allow dispersion in the absence of adequate legal mechanisms).

[63]*See* Roe, *supra* note 60, at 270-71.

[64]*See supra* text accompanying notes 13-14.

[65]*See supra* text accompanying notes 43-47.

Formal legal protections for shareholders in current dispersed-ownership jurisdictions (namely, the United States and Great Britain) guide our conception of corporate law, but there are certain path dependencies standing in the way of transplantation of these legal rules to other countries.[66] To the extent that path dependencies are based on efficiencies developed within the incumbent system, a country may be able to develop functional equivalents that operate efficiently within its system. It is difficult, however, to determine exactly what constitutes a functional equivalent.[67]

To the extent that rent-seekers stand in the way of convergence because it threatens their ability to extract private benefits from the company, convergence must be preceded by a change in political will (i.e., a rise in shareholders as a class) and/or a change in economic conditions that cause the gain from reduced capital costs to offset any loss from relinquishing private benefits. The existence of a shareholder-oriented model may not necessarily indicate or result in a dispersed-ownership system, but it may encourage dispersion by limiting the private benefits of large blockholders.[68]

III. HOW CAN WE TELL WHETHER TAIWAN IS MAKING A TRANSITION TOWARD A SHAREHOLDER-ORIENTED MODEL OF CORPORATE GOVERNANCE AND/OR A DISPERSED-OWNERSHIP MODEL?

The debate on whether and to what extent market forces will cause national regimes to converge toward one standard model of corporate ownership and governance, namely, a shareholder-oriented/dispersed-ownership system, will likely continue for quite some time. There are several reasons why we may never see closure to this debate. First, we can only declare convergence has occurred when all countries (or some subset of all countries, such as all developed economies, all Western economies, etc., depending on the particular research interests of scholars) have reached an optimal level of shareholder protection for dispersed-ownership models. As a practical matter, however, optimality is an illusive standard—impossible to achieve and impossible to recognize. Second, it is difficult to measure functional convergence.[69] It is relatively simple to

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[66] *See supra* text accompanying notes 25-27.

[67] *See supra* text accompanying notes 41-42.

[68] *See supra* text accompanying notes 28-34.

[69] *See supra* text accompanying notes 41-42 (discussing the difficulty of determining when functional convergence has occurred).

determine whether various countries have adopted the same legal provisions, the same extra-legal private ordering mechanisms, and the same legal and extra-legal corporate governance institutions; however, considering there is a "spectrum of acceptable corporate governance goals" common to all systems achievable in numerous ways,[70] how can we determine whether countries have modified and revised their respective legal and extra-legal forces to a point where we can declare they are functionally equivalent to one another? Although we are capable of presenting coherent arguments on the matter, the main issue, nonetheless, is whether shareholder protections in a particular jurisdiction are sufficient. Thus, actual global convergence may be an unachievable myth, but the process toward greater protection of shareholder interests and a more efficient dispersed-ownership system in a particular jurisdiction should be an observable phenomenon.

While the debate on global convergence continues, it may be helpful to examine Taiwan's transition toward a shareholder-oriented model of corporate governance and/or a dispersed-ownership system and the struggles associated with such a transition. Taiwan has recently made large-scale revisions to its Company Law.[71] These recent revisions affected 235 articles,[72] including changes to the language of 156 articles, the addition of twenty-four new articles, and the deletion of fifty-five articles.[73] Many of the revisions address corporate governance issues. If Taiwan were in transition toward a shareholder-oriented model and/or a dispersed-ownership model, we would expect a large-scale revision of the Company Law to reflect this transition. Thus, by examining the recent changes to Taiwan's Company Law and private ordering mechanisms that have developed, at least in part, in response to the revisions, we get a glimpse into Taiwan's struggle to provide better protection for shareholders.

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[70] *See* Milhaupt, *supra* note 41, at 2127-28 (suggesting that although corporate governance practices will probably continue to diverge, they will "operate within a spectrum of acceptable corporate governance goals").

[71] The revised Company Law was promulgated on November 12, 2001. *See Foreword* to XIN XIU ZHENG GONG SI FA JIE XI [AN ANALYSIS OF THE REVISED COMPANY LAW] (Yuan Zhao Publishing [Angle Publishing Co. Ltd.] ed. 2002).

[72] *See id.*

[73] This means the revisions affected almost half of the Company Law provisions. *See* Wang Ren-Hong, *Wo Dui Shi Ci Gong Si Fa Xiu Zheng Zhi Pi Pan* [*My Critique on This Revision to the Company Law*], *in* AN ANALYSIS OF THE REVISED COMPANY LAW, *supra* note 71, at 7.

A. *General—How Can We Tell Whether a Country is Making a Transition Toward a Shareholder-Oriented/Dispersed-Ownership Model?*

The "total package" of a country's corporate law comprises formal legal rules as well as social and market norms.[74] The intent of this article is not to downplay the importance of extralegal norms on corporate governance. When a country overcomes political costs and responds to corporate governance issues by reform of legal rules, however, these rules become significant indicators of the country's commitment to protecting shareholders.

To gauge whether formal legal changes in a particular country indicate a transition toward a shareholder-oriented system, we need to assess these reforms in light of the nature of the country's incumbent ownership and corporate governance models. Different corporate governance and ownership systems create somewhat different threats to shareholder interests. In concentrated-ownership systems, the main threat to minority shareholders comes from the majority's ability to expropriate.[75] In dispersed-ownership systems, the main threat to shareholders comes from the management's ability to expropriate and the costs associated with monitoring the performance of management.[76] Of course, in both systems, firms will have boards of directors that make the major business decisions and monitor the managers responsible for the day-to-day operations of the company. In addition, shareholders will elect the members of the board and vote on issues important to the operation of the company; thus, to the extent controlling shareholders or management (whichever the case may be depending on the ownership model) can control the board of directors and the agenda for the shareholder meetings, they can control the company and serve their own interests. Any legal reform or private ordering that protects shareholder interests in a particular jurisdiction will naturally respond to threats to shareholder interests that are specific to its individual circumstances.[77]

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[74]*See supra* note 41 and accompanying text.

[75]*See supra* text accompanying notes 13-14 (discussing controlling shareholder expropriation of minority shareholders).

[76]*See supra* text accompanying note 35 (discussing management expropriation of shareholders); *see also supra* text accompanying note 36 (discussing dispersion of ownership and the agency costs associated therewith).

[77]Assuming they respond at all. It is conceivable that firms can remain competitive on the product market without adequate shareholder protections. *See* Bebchuk & Roe, *supra* note 5, at 151-52. This may be especially true for firms that do not rely on capital markets. *See id.* at 152 (stating that many companies do not use capital markets for finance; rather they rely on bank loans

A transition to a shareholder-oriented model in a country may encourage further dispersion of ownership by reducing or eliminating the controlling shareholder's private benefits of control and by providing assurances to the controlling shareholder that its interests will not be expropriated if it allows its ownership stake to be diluted.[78] However, if a concentrated-ownership system develops shareholder protections that deal exclusively with protection from controlling shareholder expropriation, then there will be risks of expropriation at the hands of management as ownership becomes more disperse and agency costs related to the monitoring of management increase.[79] Thus, as part of a jurisdiction's transition from a concentrated-ownership system to a dispersed-ownership model, we should not only witness shareholder protections addressing controlling shareholder expropriation, we should also see mechanisms protecting shareholders from potential management expropriation.[80]

We must keep in mind that any transition toward a dispersed-ownership model in a particular country will not happen immediately; rather, there will be gradual change. If we were to examine a concentrated-ownership system in the early stages of transition, we could predict that legal reform would emphasize more concentrated-ownership-centered protections for shareholders, i.e., protection of the minority shareholders from possible controlling shareholder abuse and expropriation. Similarly, we could predict that legal reform in a concentrated-ownership system in the later stages of transition would address more dispersed-ownership-centered protections, i.e., protection of the shareholders from potential management abuse, expropriation and incompetence.

B. *Taiwan—How Can We Tell Whether Taiwan is Making a Transition Toward a Shareholder-Oriented/Dispersed-Ownership Model?*

As suggested above, the manifestation of a particular jurisdiction's transition toward a shareholder model will depend upon the nature of the existing threats to shareholder interests. It is therefore necessary to first understand Taiwan's current corporate ownership and corporate governance systems to better assess whether recent revisions to its Company Law

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or retained earnings).

[78] *See supra* text accompanying notes 13-14.

[79] *See supra* text accompanying note 56 (discussing dispersion of ownership and the agency costs associated therewith); *supra* text accompanying notes 35-36 (discussing Mark Roe's theory regarding whether the shareholder-oriented model will lead to dispersion without adequate mechanisms to monitor the competence of management).

[80] They should also ideally deal with the issue of management competence. *See supra* text accompanying notes 13-17.

adequately address the protection of shareholder interests or specifically address potential management expropriation and incompetence.

1. Taiwan—A Brief Introduction to Corporate Ownership and Corporate Governance

The Company Law establishes the fundamentals for Taiwan's corporate governance legal regime. The Company Law provides for a board of directors and a supervisor.[81] The role of the supervisory board, in general, is to monitor the board of directors, especially director self-interested transactions, and to review the financial reporting process, internal controls, and auditing of the company.[82] The supervisor in Taiwan, in contrast to supervisory boards in certain European countries, does not have representation of other stakeholders, such as labor representatives.

Taiwan's Securities & Exchange Law regulates the disclosure and transparency of public companies.[83] The Securities & Exchange Law provides for the establishment of the Securities and Futures Commission, which has jurisdiction over Taiwan's two major securities exchanges, the Taiwan Stock Exchange and the Taiwan Over-the-Counter Trading Center (also called the Taiwan GreTai Securities Market (GTSM)).

Like most countries around the world, ownership of public companies in Taiwan is dominated by family groups.[84] A recent study of 141 companies listed on the Taiwan Stock Exchange shows that forty-eight percent are controlled by such groups.[85] These family groups have a great deal of control over the boards of directors, often holding more than half of the board seats,[86] and typically control the agenda for shareholder

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[81] *See* GONG SI FA [COMPANY LAW], art. 192 (providing for the board of directors); *id.* art. 216 (providing for the supervisor).

[82] Securities and Futures Institute, *Corporate Governance in Taiwan*, Dec. 2001 (manuscript at 7, *available at* http://www.sfi.org.tw/download/resh_ftp/cgiten.pdf) [hereinafter SFI Paper].

[83] *Id.* at 2.

[84] *See* La Porta et al., *supra* note 5, at 502 (stating that family-controlled corporations are very common).

[85] Stijn Claessens et al., *The Separation of Ownership and Control in East Asian Corporations* (manuscript at 43, *available at* http://papers.ssrn.com/sol3/papers. cfm?abstract_ id=206448).

[86] *See* Chen-en Ko et al., *Corporate Governance in Chinese Taipei* (paper presented at the Organization for Economic Cooperation and Development Conference on Corporate Governance in Asia: A Comparative Perspective, Seoul, Mar. 3-5, 1999) (manuscript at 5, *available at* http://www.oecd.org/pdf/M000015000/M00015815.pdf); SFI Paper, *supra* note 82, at 5.

meetings.[87] This control over the board and the shareholder meeting agenda creates the potential for abuse.

Taiwan's publicly listed companies obtain financing through both bank loans and the capital markets,[88] but capital markets have become an increasingly important source of capital.[89] Between 1991 and 2001, the number of companies listed on the Taiwan Stock Exchange increased from 221 to 584.[90] During the same time period, the number of firms listed on the Taiwan Over-the-Counter Trading Center increased from 9 to 333.[91] This reliance on capital markets may make Taiwan more prone to a transition toward a shareholder-oriented model.[92] The increasing importance of securities markets has also led to greater dispersion of ownership among the public, especially with respect to Taiwan's largest listed companies.[93] In addition, there are signs that Taiwan is beginning to experience, or at least gaining greater awareness of, the corporate governance issues associated with such dispersion.[94]

Banks do not play a significant role in corporate governance in Taiwan because relevant regulations limit the amount of funds they can invest in other companies.[95] Similarly, institutional investors do not play

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[87]Ko et al., *supra* note 86, at 5.

[88]*Id.* at 7.

[89]The debt-equity ratios of companies listed on the Taiwan Stock Exchange have dropped steadily since 1981. *Id.* at 44.

[90]*See* Securities and Futures Commission, Major Indicators of Securities and Futures Market, Statistics of Publicly Issued Companies (Aug. 15, 2002), *available at* http://www.sfc.gov.tw/ensfcindex.htm.

[91]*See id.*

[92]*See supra* text accompanying notes 75-77 (discussing how reliance on other sources of finance may discourage a firm from improving protection of minority shareholder interests).

[93]Relatively recent studies indicate that only 15% of Taiwan's largest 20 companies are controlled by a family group, in contrast with 38% for the 50 medium-sized firms companies and 80% for the 50 smallest public companies. *See* Claessens et al., *supra* note 85, at 43.

[94]*See* Lawrence S. Liu, Chinese Characteristics Compared: A Legal and Policy Perspective of Corporate Finance and Governance in Taiwan and China (June 1, 2001) (manuscript at 6, *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=273174) ("Such gradual ownership de-centralization should reduce expropriation concerns over time. But the same trend will intensify agency concerns when firms increasingly rely on professional managers.") (cited with permission); Chen Quan-Shan, *Gong Si Dong Shi De Shi Ming, Yi Wu Yu Ze Ren—Gou Jian Qi Ye Jian Quan Jing Ying Zhi Gui Ze (Shang) [The Mission, Duties and Responsibilities of Company Directors]* 51:8 FA LING YUE KAN 21, 22 (1999) (stating that there is a trend toward greater diffusion of ownership in firms listed on the Taiwan Stock Exchange and the Over-the-Counter Trading Center); SFI Paper, *supra* note 82, at 5 (stating that the challenge to corporate governance in Taiwan is the need to reduce self-dealing of the professional manager).

[95]*See* Ko et al., *supra* note 86, at 8.

a significant role in corporate governance.[96] This diminished responsibility is due, at least in part, to regulations that limit the amount of shares they can own in any one company or other regulations that may limit the time they may hold certain stocks.[97] Because of the limited role banks and institutional investors play in corporate governance,[98] minority shareholders in Taiwan do not benefit from the activism of institutional investor minority block-holders, which creates an even greater need for reform of shareholder protection laws.

The history of corporate law in Taiwan has a strong flavor of state control and monitoring. At the center of the Taiwanese political machine is the highly developed bureaucracy. This bureaucracy has utilized state licensing, minimum capital requirements, foreign exchange restrictions, and rules governing business practices to promote governmental policies.[99] This mentality has played a part in creating a Company Law that restricts the operations and capital raising activities of the Taiwanese firm.[100]

2. The November 2001 Revisions to Taiwan's Company Law

The process to revise Taiwan's Company Law began when the Council of Economic Planning and Development (CEPD) commissioned a study on corporate law in Taiwan in 1999.[101] After fourteen months of work, the CEPD research team presented its draft report to the Ministry of Economic Affairs (MOEA)[102] who subsequently presented its own draft to the legislature. The revision process was finally concluded when the legislature passed the bill on October 25, 2001 and the president subsequently promulgated the new law on November 12, 2001. In all, the revision process resulted in the change, addition, or deletion of 235

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[96]There has been an overall increase in trading by value by institutional investors since 1990, see Securities and Futures Commission, *supra* note 90, Investor Composition by Trading Value, but they still are not playing a significant role in corporate governance. *See* SFI Paper, *supra* note 82, at 4; Liu, *supra* note 94, at 5 (stating the securities investment trust industry, i.e., the asset management/mutual fund industry, in Taiwan has been disappointing from a corporate governance perspective).

[97]SFI Paper, *supra* note 82, at 4.

[98]Ko et al., *supra* note 86, at 6.

[99]*See* Lawrence S. Liu, Global Markets and Local Institutions: Corporate Law System and Financial Reform Debates in Taiwan (Oct. 8, 2001) (manuscript at 6, *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=293082) (cited with permission).

[100]*Id.* at 10-11.

[101]*See id.* at 11.

[102]*See id.* at 13.

provisions the Company Law, affecting almost half of its articles,[103] including many of the Company Law's corporate governance provisions. The revisions provide abundant evidence that the Taiwanese corporation is undergoing a major transition. A careful assessment of these revisions will provide a better understanding of the exact nature and scope of this transition, especially as it pertains to the protection of shareholder interests and the dispersion of ownership.

C. *Taiwan's Transition, How Can We Tell?—Preliminary Conclusion*

The recent revisions to Taiwan's Company law should be examined in context. Taiwan is a concentrated-ownership jurisdiction with the potential for controlling shareholder expropriation due to the ability of large shareholders to control the board of directors and shareholder meetings.[104] In addition, because there is an absence of bank and institutional investor involvement in the corporate governance of the Taiwanese firm,[105] there is even less of a check on controlling shareholders. If Taiwan were moving toward a shareholder-oriented model of corporate governance, we would predict a large-scale revision of the Company Law to reflect this transition by addressing corporate governance issues particular to Taiwan—the problem of controlling shareholder expropriation of minority shareholders. In addition, to the extent that Taiwan is experiencing and/or anticipating the threat of potential management expropriation and agency costs that are concomitant with the dispersed-ownership model, we would expect to see revisions placing increased attention on the role of the professional manager in the Taiwanese corporation.

IV. RECENT REVISIONS TO TAIWAN'S COMPANY LAW— IS TAIWAN MAKING A TRANSITION TOWARD A SHAREHOLDER-ORIENTED MODEL AND/OR A DISPERSED-OWNERSHIP MODEL?

Recent revisions to Taiwan's Company Law indicate that Taiwan is in transition toward a shareholder-oriented model of corporate governance and a dispersed-ownership model. The revisions show that Taiwan is

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[103] *See Foreword*, AN ANALYSIS OF THE REVISED COMPANY LAW, *supra* note 71; Wang Ren-Hong, *in id.* at 7 (stating that the revisions affected nearly half of the provisions of the Company Law).

[104] *See supra* text accompanying notes 84-94.

[105] *See supra* text accompanying notes 95-99.

struggling to improve protection of minority shareholders against controlling shareholder expropriation. Furthermore, Taiwan is placing increased attention on the role of the professional manager in the Taiwanese corporation, anticipating a time in the future when further dispersion of ownership requires greater reliance on professional managers. Taiwan's struggle with these problems is demonstrated through recent Company Law revisions with respect to: (1) the independence of the board of directors; (2) the independence of the supervisor and her ability to effectively monitor the board; (3) the rights of shareholders and their ability to monitor the board of directors, the supervisor, and management; and (4) the role of managers.

A. *The Independence of the Board of Directors*

Director independence is a concern for shareholders in both dispersed-ownership and concentrated-ownership systems, but the problem manifests itself in different ways in each of the respective models. In concentrated-ownership systems, the concern with director independence focuses on the large blockholder's influence on the board and how she will use that influence to benefit herself at the expense of the minority shareholders.[106] In dispersed-ownership systems, the concern with director independence focuses on management's influence on the board and how this influence creates opportunities for management to benefit itself at the expense of the shareholders.[107] As proposed in Part III, above, a country transitioning from a concentrated-ownership model to a shareholder-oriented/dispersed-ownership model will have to address controlling shareholder influence on the board. As dispersion progresses and management gains more power, the law will have to address management influence on the board of directors. Thus, if Taiwan is making a transition from a concentrated-ownership model toward a shareholder-oriented/ dispersed-ownership model, the transition, ideally, should be evident through legal changes that attempt to address both large blockholder influence on the board and potential management influence on the board. Indeed, the recent revisions to the Company Law indicate that Taiwan lawmakers are attempting to address both controlling-shareholder and management influence on the board of directors.

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[106] *See supra* text accompanying notes 48-56 (discussing minority shareholder concerns in concentrated-ownership systems).

[107] *See* ROE, *supra* note 20, at 5-6 (discussing how management can control the board in dispersed-ownership companies); *supra* text accompanying notes 57-63 (discussing minority shareholder concerns in dispersed-ownership systems).

The Company Law creates a mechanism that enables a large shareholder to gain control of the board of directors by allowing the direct election of juridical persons, e.g., corporations, organizations, etc., to the board of directors.[108] The juridical person must appoint a natural person to participate in board meetings and act on its behalf in carrying out its various duties as director.[109] The juridical person also has the right to replace its appointed director at will.[110] Alternatively, a juridical person can designate natural persons to run for board seats as its appointed nominees. Although the shareholder meeting elects these natural persons as individuals, the juridical person can still replace them at will.[111] The effect this election regime has on board independence is obvious—the controlling shareholder can fill the board with its appointees and replace them at will as soon as they show any sign of independence.

This election regime, coupled with generally weak legal protections against self-interested transactions, creates conditions ripe for controlling shareholder expropriation in the Taiwanese firm. One would expect any major revisions to the Company Law to either directly or indirectly attempt to remedy this problem. Unfortunately, the recent revisions did not eliminate the juridical person-appointee director system,[112] but they did make progress toward improving board independence from controlling shareholder influence by allowing non-shareholder directors[113] and making it more difficult for a large blockholder to remove directors. The new revisions also address both large blockholder and potential management influence on the board by expressly imposing a duty of loyalty on directors.

1. Non-Shareholder Directors

The original Company Law required all directors to be shareholders of the company.[114] The revised Company Law now allows election of non-

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[108]COMPANY LAW, *supra* note 81, art. 27, ¶ 1.

[109]*Id.*

[110]*Id.* art. 27, ¶ 3.

[111]*Id.* art. 27, ¶ 2.

[112]It should be noted that the research team commissioned by the Council for Economic Planning and Development did, in fact, recommend changing this election regime. The MOEA, however, declined to include the research team's recommendation in its proposed draft of the revised Company Law. *See* Liu, *supra* note 99, at 25.

[113]*Id.* at 28.

[114]"The board of directors of a company shall have at least three directors, who shall be elected by the shareholder meeting from among *shareholders* having disposing capacity." COMPANY LAW, *supra* note 81, art. 192, ¶ 1 (version prior to November 2001 revisions) (emphasis added).

shareholders to the board of directors.[115] Some Taiwanese legal scholars consider this revision to be a step toward greater board independence, although they concede it is a minor one.[116] In fact, acquiring a few shares of a publicly listed firm was never a significant obstacle to qualify for election to the board of directors. Furthermore, the Securities & Exchange Law still requires the board of directors in public companies to own a certain amount of the company's shares.[117] Thus, the legal affect of allowing non-shareholder directors may be negligible, but its normative effect may be more significant. Presently, the boards of directors in Taiwanese firms are made up of and controlled by large shareholders.[118] Permitting non-shareholders to hold board seats may serve as a preliminary step toward undermining this norm of controlling shareholder dominance of the board.

It is worth noting that there has been a private ordering response to the issue of director independence in Taiwan. On the same day the revised Company Law was promulgated, the Taiwan Stock Exchange and the Taiwan Over-the-Counter Trading Center announced they would require new listing applicants to have independent directors and supervisors.[119]

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[115]"The board of directors of a company shall have at least three directors, who shall be elected by the shareholder meeting from among the *persons* having disposing capacity." COMPANY LAW, *supra* note 81, art. 192, ¶ 1 (emphasis added). Most scholars consider that requiring directors to be elected from among the shareholders served to provide some protection for shareholders by aligning the interests of the directors and shareholders. *See* WANG WEN-YU, GONG SI YU QI YE FA ZHI [THE LEGAL SYSTEM OF COMPANIES AND ENTERPRISES] 6 (Yuan Zhao Publishing [Angle Publishing Co. Ltd.] 2000). Yet, requiring directors to be shareholders had come to be considered meaningless. *See id.* (stating that it was not a major obstacle to acquire one share to qualify for a seat on board). The official legislative reason for the revision stated that by requiring directors to be shareholders, one could better expect the board to serve the company's interests in the exercise of their duties, but that it no longer fit in with the global trend toward separation of ownership and control. *See* Yu Xue-Ming, *Dong Shi Ji Dong Shi Hui* [*The Directors and the Board*], *in* AN ANALYSIS OF THE REVISED COMPANY LAW, *supra* note 71, at 257, 262.

[116]*See* Yu, *supra* note 115, at 262; *see also* Liu, *supra* note 99, at 32 (stating that repealing the requirement of shareholder directors was a "modest first step toward" a board not dominated by founders).

[117]The Securities and Futures Commission has the power to establish the exact number. ZHENG QUAN JIAO YI FA [SECURITIES & EXCHANGE LAW] art. 26. The Securities and Futures Commission imposed a fine for violation of this provision 62 times in the year 2000 and 40 times in the year 2001. *See* Securities and Futures Commission, 2001 Annual Report, Supervision of Secondary Market, Table 5 *Analysis of Penalties*, *available at* http://www.sfc.gov.tw/ensfcindex.htm; Securities and Futures Commission, 2000 Annual Report, Supervision of Secondary Market, Table 5 *Analysis of Penalties*, *available at* http://www.sfc.gov.tw/ensfcindex.htm.

[118]*See* Liu, *supra* note 99, at 32.

[119]*See* Huang Ming-Jie, *Jian Cha Ren* [*The Supervisor*], *in* AN ANALYSIS OF THE REVISED COMPANY LAW, *supra* note 71, at 285, 288; *see also* Lawrence S. Liu, Global Markets and Parochial Institutions: Transformation of Taiwan's Corporate Law, paper presented at Columbia Law School Conference on Global Markets and Domestic Institutions: Corporate Law and

The new rules, as approved by the Securities and Futures Commission, require listing applicants to have at least two independent directors on the board and one independent supervisor.[120]

The securities exchanges' responses demonstrate how private ordering can provide certain protections for shareholders when formal legal rules fail to do so. Firms can bond themselves to a stricter corporate governance regime by listing with the exchanges, thereby signaling to investors that they will not expropriate minority shareholders.[121] Nevertheless, the signal that these new listing rules give to investors will be confusing at best. First, the rules only apply to new applicants, so there will be no continuity among existing listed firms with respect to independent directors. Second, the rules do not expressly require a company to maintain independent directors once its application has been accepted and its shares have been listed with the exchange. In the past, the exchanges have had difficulty trying to enforce independent director and supervisor rules once a firm has been listed,[122] and the new rules do not address this problem. Finally, the securities exchanges have traditionally viewed director independence in terms of kinship,[123] which is evidence that Taiwan is still mostly concerned with family-group controlling shareholder influence on the board, and not management influence. The new listing rules do not place any significant emphasis on management influence on the board.

In summary, permitting non-shareholder directors addresses the issue of large shareholder control of the board. Although the legal affect of this revision may not be significant, it may serve to help undermine the current

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Governance in a New Era at Cross-Border Deals, Apr. 5-6, 2002 (manuscript at 28, on file with author) (cited with permission) (indicating that these new exchange rules supplement earlier rules for director independence in listing companies that were largely ineffective).

[120](91) Tai Cai Zheng (1) Zi No. 172439 (letter from Securities and Futures Commission authorizing the Taiwan Stock Exchange to change it rules to require applicants to have at least two independent directors and one independent supervisor); (91) Tai Cai Zheng (1) Zi No. 172370 (letter from Securities and Futures Commission authorizing the Taiwan Over-the Counter Trading Center to change it rules to require applicants to have at least two independent directors and one independent supervisor).

[121]*See supra* text accompanying notes 43-50 (discussing private ordering responses to corporate governance issues).

[122]*See* Liu, *supra* note 119, at 28.

[123]Article 17 of the Supplementary Provisions to the Taiwan Stock Exchange Corporation Criteria for Review of Securities Listing define director independence in terms of the following relational statuses: (1) spouse, (2) linear relatives by blood within the third degree of relationship, (3) collateral relatives within the fourth degree of relationship, (4) representatives of the same juridical person, and (5) affiliates. *See* Supplementary Provisions to the Taiwan Stock Exchange Corporation Criteria for Review of Securities Listing, art 17, ¶ 1, item 1 (English translation based on SFI Paper, *supra* note 82, at 8).

norm of controlling shareholder domination of the board. In addition, the securities exchanges have taken preliminary steps toward improving the problem of controlling shareholder dominance of the board by requiring new applicants to have independent directors. These new rules, however, may send an ambiguous message to investors regarding whether listed companies protect the interests of minority shareholders.

2. Removal of Directors

The revised Company Law requires an extraordinary shareholder resolution to remove a director,[124] thus making it more difficult for a large shareholder to oust an independent director. Such a provision, however, may also have the negative effect of making it virtually impossible for the minority to remove a director it feels is not serving the best interests of the company. It logically follows, then, that the efficacy of this provision depends upon on the ability of the minority shareholders to elect at least one director who will represent their interests. Unfortunately, the revised Company Law no longer makes cumulative voting mandatory, which makes it more difficult for minority shareholders to elect a director without the cooperation of the controlling shareholder. More specifically, the new law provides that there will be no cumulative voting for directors unless the company's articles of incorporation expressly provide otherwise.[125] The articles of incorporation for most companies in Taiwan simply parallel the language of the Company Law, especially with respect to mandatory provisions and will, therefore, expressly provide for cumulative voting to reflect the mandatory requirements of the pre-revision Company Law. Because of this norm, the vast majority of companies will maintain cumulative voting for the immediate future until shareholders amend their respective articles of incorporation.[126] In any event, the listing rules of the securities exchanges that require independent directors and supervisors

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[124]COMPANY LAW, *supra* note 81, art. 199, ¶ 2 (requiring a quorum of shareholders representing two-thirds of the issued shares and a vote of a majority of the shares in attendance); *id.* ¶ 3 (allowing public issuing companies a quorum of shareholders representing a majority of the issued shares and a vote of two-thirds of the shares in attendance). This is true unless the director is the appointed representative of a juridical person. The juridical person will still be able to remove its appointed director at will. *See supra* text accompanying notes 108-11 (discussing the appointment and removal of directors by juridical persons).

[125]The articles of incorporation cannot be amended without approval of the shareholders. See COMPANY LAW, *supra* note 81, art. 277, ¶ 1.

[126]It will be interesting to see how minority shareholders will react if the board proposes amending the articles to eliminate cumulative voting.

could somewhat mitigate any negative effect the elimination of cumulative voting may have on the election of independent directors to the board.

3. Directors' Duty of Loyalty

One of the more notable recent changes to the Company law was the addition of an express duty of loyalty for directors.[127] The Company Law and the Civil Code had already expressly imposed a duty of care that, in theory, held directors to a higher standard than United States law,[128] but there had never been an express duty of loyalty. Despite the fact there was no express provision in the law before the November 2001 revisions, Taiwanese legal scholars had disagreed whether directors nonetheless owed a duty of loyalty.[129] This debate, however, appears to have been an academic one, with no significant development in the courts.[130] An express duty of loyalty provision in the Company Law should promote the development of director responsibility beyond pure academic discourse. Further, there is hope that the new duty of loyalty will supplement existing legal rules governing self-dealing, which are generally considered to be weak and insufficient.[131]

The first wave of Taiwanese legal scholarship responding to the revisions, however, has been somewhat critical of the new duty of loyalty.[132] One criticism of the new provision is that it is too abstract—it simply adds the words "duty of loyalty" to the Company Law, without any

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[127]*See* COMPANY LAW, *supra* note 81, art. 23, ¶ 1 (stating that "responsible persons" owe a duty of loyalty in the exercise of their duties); *id.* art. 8, ¶ 1 (stating that directors are "responsible persons").

[128]The legal relationship between the director and the company is based on a contract of mandate. *See* COMPANY LAW, *supra* note 81, art. 192, ¶ 4. The director, therefore, has a duty of to act as a good administrator. *See* MIN FA [CIVIL CODE] art. 528, 540-542; *see also* COMPANY LAW, *supra* note 81, art. 23, ¶ 1. The duty to act as a good administrator means the director will be liable for his ordinary negligence, which is a higher standard of liability than the deferential business judgment rule in the United States. *See* Liu, *supra* note 119, at 26. For a discussion of why the contract of mandate is a poor theoretical basis for the relationship between company and director, see WANG, *supra* note 115, at 4-5.

[129]Chen, *supra* note 94, at 24. The legislative reason for this revision was "to clearly provide that responsible persons owe a duty of loyalty to the company." Wang Tai-Quan, *Zong Ze* [*General Principles*], *in* AN ANALYSIS OF THE REVISED COMPANY LAW, *supra* note 71, at 17, 75-76. This reasoning may imply that the duty of loyalty is nothing new, just an express clarification of duty that already existed.

[130]*See* Chen, *supra* note 94, at 24.

[131]WANG, *supra* note 115, at 4-5, 22–23 (discussing and criticizing the loopholes in the Company Law's director self-dealing rules).

[132]*See* Liu, *supra* note 119, at 27 (criticizing the fact that the director owes a fiduciary duty to the company, not the shareholders); Yu, *supra* note 115, at 262 (stating that the revision adding "fiduciary duty" is too abstract and does not apply to shadow directors).

further elaboration.[133] Although the Company Law failed to define "duty of loyalty," the vague standard may actually open doors for U.S.-style duty of loyalty standards to permeate Taiwan law, hopefully improving upon existing rules. Many Taiwanese legal scholars writing on corporate governance are influenced by U.S. scholarship and case law addressing the duty of loyalty.[134] In fact, now that the law has provided the legal basis for a "duty of loyalty," the opinions of eminent scholars will play a significant role in the development of this concept.[135]

Critics have also argued that the new duty of loyalty did not go far enough to protect shareholders because it applies to directors and other responsible persons, not to those who actually control the directors from behind the scenes.[136] This problem of "shadow directors" is especially acute in Taiwan where juridical persons can gain election to the board and remove their appointee-directors at will.[137] In fact, one can easily see how the duty of loyalty would directly clash with the appointee-director system. The appointee-director who places the interests of the minority shareholders over the interests of the large shareholder who appointed her will be subject to removal at the will of that large shareholder.

Despite the criticisms, however, Taiwanese legal scholars generally recognize the new express duty of loyalty as an important step toward increased director responsibility and independence.[138] Of course, because

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[133]*See* Yu, *supra* note 115, at 260 (stating that the revision merely adding "fiduciary duty" is too abstract without further procedural regulations on related-party transactions); *see also* WANG, *supra* note 115, at 16 (arguing that simply adding the words "duty of loyalty" to the Company Law would not be sufficient).

[134]*See, e.g.*, WANG, *supra* note 115, at 3–29 (citing to U.S. sources in nn.5, 21, 26, & 32); Chen, *supra* note 94, at 22-30 (relying heavily on U.S. sources to define a director's fiduciary duty).

[135]Taiwan is a civil law jurisdiction. In general, the work of scholars in civil law countries plays a more active and formal role in lawmaking. For a brief and general discussion of the role of scholars in civil law jurisdictions, see Vivian Grosswald Currant, *Romantic Common Law, Enlightened Civil Law: Legal Uniformity and the Homogenization of the European Union*, 7 COLUM. J. EUR. L. 63, 67 n.12 (2001). There is, however, a growing body of scholarship that debates whether countries can successfully transplant U.S. style fiduciary duties. *See, e.g.*, Katharina Pistor & Chenggang Xu, *Fiduciary Duty in Transitional Civil Law Jurisdictions: Lessons from Incomplete Law Theory*, *in* GLOBAL MARKETS, *supra* note 45; Lynn A. Stout, *On the Export of U.S.-Style Fiduciary Duties to Other Cultures: Can a Transplant Take?*, *in* GLOBAL MARKETS, *supra* note 45.

[136]*See* Yu, *supra* note 115, at 260 (stating that adding an express fiduciary duty was an improvement but leaves a large loophole because it does not apply to shadow directors).

[137]*See supra* text accompanying notes 108-11 (discussing the appointment and removal of directors by juridical persons).

[138]*See* Liu, *supra* note 119, at 27 ("It is good that all directors (and supervisors) now owe a fiduciary duty."); Yu, *supra* note 115, at 260 (stating that adding an express fiduciary duty to the Company was a major improvement).

large shareholders are predominant in Taiwanese public companies, the problem of director independence is most often conceived in terms of independence from controlling shareholder influence. The new express duty of loyalty, however, addresses director independence from management influence as well—as long as you are a director, your loyalties lie with the company, not with any other influence, be it management or controlling shareholders. In fact, U.S.-style fiduciary duties have largely developed around the dispersed-ownership model and the problem of management control of the board. Because of the influence of U.S. scholarship on the Taiwan debate of fiduciary duties, the U.S. experience may ultimately guide the development of the duty of loyalty in Taiwan with respect to management control of the board.

4. Director Independence—Preliminary Conclusion

Understandably, because of the predominance of controlling shareholder/family groups in Taiwan, the new revisions to the Company Law place heavy emphasis on controlling shareholder influence.[139] The new revisions demonstrate, however, that Taiwan is addressing both controlling shareholder dominance of the board as well as potential management influence on the board. The revised Company Law mitigates large shareholder dominance over the board by allowing the election of directors who are not shareholders, which may have more significant normative effect than legal effect.[140] Another check on controlling shareholder influence on the board is the revision making it more difficult for a large blockholder to remove directors.[141] There is still a need, however, to better ensure the election of independent directors, possibly through more aggressive revisions to the listing rules.[142] Finally, expressly imposing a duty of loyalty on directors addresses both large blockholder influence and potential management influence on the board. The ultimate effectiveness of the duty of loyalty on directors, however, largely depends on how Taiwan courts and scholars develop the specific nature and scope of the duty.

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[139]*See supra* text accompanying notes 115-26.

[140]*See supra* text accompanying notes 115-18.

[141]*See supra* text accompanying note 124.

[142]Until recently, neither the United States nor Great Britain (the paradigms for the shareholder-oriented model) have had legal rules addressing director independence. *See* Coffee, *supra* note 56, at 2155-56. But the Sarbanes-Oxley Act of 2002 now requires issuers subject to the Securities Act of 1934 to have independent directors. *See* 15 U.S.C.A. § 78j1(m)(3) (Supp. 2002) (requiring the members of the board's audit committee to be independent).

B. *The Independence of the Supervisor and Her Ability to Monitor the Board*

Because the Company Law charges the supervisor with monitoring the operations of the company, reviewing the company's books, and monitoring director loyalty and performance, supervisor independence is a critical issue in the corporate governance of the Taiwanese firm. The supervisor represents the company in transactions with a director,[143] serves as the primary conduit for derivative lawsuits against directors,[144] and has a duty to notify the board to stop or refrain from any act that violates relevant laws or the articles of incorporation.[145] Moreover, because institutional investors and financial intermediaries do not play a significant role in Taiwanese corporate governance[146] and because impediments to shareholder derivative suits make such suits an ineffective check on director misconduct,[147] the supervisor is an even more crucial institution for protecting minority shareholder interests in Taiwan.

Unfortunately, the supervisor has been an ineffective corporate governance institution in Taiwanese firms. The supervisor is elected through the same process as directors, which means a juridical person can gain election to the position of supervisor and appoint and remove representatives at will.[148] The ramifications are obvious—a controlling shareholder can dominate both the board and the supervisor through this method of election, which results in the supervisor acting as a "rubber stamp" for board action.[149]

Although the lack of supervisor independence has been a major failure in corporate governance of Taiwanese companies, the recent revisions to the Company Law failed to remove the root of the rubber stamp supervisory—the juridical person election system. There was, however,

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[143]COMPANY LAW, *supra* note 81, art. 223.

[144]The Company Law requires a shareholder wishing to sue a director to make a written request asking the supervisor to bring suit. A shareholder may only directly initiate legal action against a director if the supervisor does not bring an action within thirty days of the shareholder's written request. *Id.* art. 214.

[145]*Id.* art. 218-2.

[146]*See* Ko et al., *supra* note 86, at 5; SFI Paper, *supra* note 82, at 4.

[147]*See* WANG, *supra* note 115, at 25-27 (discussing and criticizing substantive and procedural obstacles to shareholder derivative suits in Taiwan); *see also* Lawrence S. Liu, *Simulating Securities Class Actions: The Case in Taiwan*, 3 CORP. GOVERNANCE INT'L 4 [issue 4] (2001) (discussing informal efforts to promote shareholder suits in Taiwan).

[148]COMPANY LAW, *supra* note 81, art. 27. *See supra* text accompanying notes 109-11 (discussing the appointment and removal of directors by juridical persons).

[149]*See* WANG, *supra* note 115, at 14 (characterizing the supervisor as a "rubber stamp" for the board).

some progress toward increasing the independence of the supervisor and improving the ability of the supervisor to monitor the board of directors.

1. Non-Shareholder Supervisors

The revised Company Law allows non-shareholders to be elected as supervisors as well as directors.[150] As discussed above in the context of non-shareholder directors, allowing non-shareholder supervisors was not a major practical or legal breakthrough since shareholder status was never a significant obstacle to qualifying for the position of supervisor.[151] In addition, the Securities & Exchange Law still requires supervisors and directors in public companies to hold a certain amount of stock in the company.[152] Nonetheless, the new revision allowing non-shareholder supervisors may serve to undermine the norm of controlling shareholder domination of the supervisor.

2. Increase in the Number of Supervisors and Removal of Supervisors

The revised Company Law now requires a company to have at least two supervisors,[153] instead of one as was originally required. Strength in numbers could translate to a better ability to stand up to the board. Furthermore, more seats on the supervisory board improves the chances that minority shareholders will be able elect a supervisor who is not controlled by a dominant shareholder. The effectiveness of an increase in the number of supervisors, however, depends significantly on the ability of the minority to elect independent supervisors and keep them in office. Toward that end, the recent revisions make it more difficult for a controlling shareholder to remove a supervisor who protects the interest of minority shareholders by requiring an extraordinary shareholder resolution to remove a supervisor.[154] Unfortunately, however, the elimination of mandatory cumulative voting could play a significant role in undermining the minority's ability to elect an independent supervisor in the first place.[155]

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[150]COMPANY LAW, *supra* note 81, art. 216, ¶ 1.

[151]*See supra* text accompanying notes 115-16.

[152]SECURITIES & EXCHANGE LAW, *supra* note 117, art. 26.

[153]This applies to public issuing companies only. COMPANY LAW, *supra* note 81, art. 216 ¶ 2.

[154]*Id.* art. 199, ¶ 2 (applicable *mutatis mutandis* to supervisors pursuant to *id.* art. 227).

[155]*See supra* text accompanying notes 124-26 (discussing the removal of mandatory cumulative voting in the November 2001 revisions). An influential Company Law scholar in Taiwan, Professor Ke Fang-Zhi argues that cumulative voting for directors may not be necessary, but cumulative voting for supervisors is essential to effectuate the monitoring responsibilities of

As discussed above, the Taiwan Stock Exchange and the Taiwan Over-the-Counter Trading Center have responded to the issue of supervisor independence by requiring listing applicants to have at least one independent supervisor.[156] Once again, the securities exchanges have traditionally viewed independence in terms of kinship and not in terms of connections to management,[157] which speaks more to concern with controlling shareholder influence and not to management's influence on the supervisor.[158] Moreover, the rules do not expressly require a company to maintain independent supervisors once its application has been accepted and its shares have been listed with the exchange.[159]

3. Supervisor's Duty of Loyalty

The new express duty of loyalty extends to supervisors as well as directors.[160] Imposing a duty of loyalty on supervisors should serve to fill legislative loopholes that exist because self-dealing and corporate opportunity provisions in the Company Law do not apply to supervisors.[161]

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the supervisor. *See* KE FANG-ZHI, A DISCUSSION OF THE COMPANY LAW 368 n.290 (4th ed. 2001).

[156]*See* Zi No. 172439 Letter, *supra* note 120 (authorizing the Taiwan Stock Exchange to change its rules to require applicants to have at least two independent directors and one independent supervisor); Zi No. 172370 Letter, *supra* note 120 (authorizing the Taiwan Over-the Counter Trading Center to change its rules to require applicants to have at least two independent directors and one independent supervisor).

[157]Article 17 of the Supplementary Provisions to the Taiwan Stock Exchange Corporation Criteria for Review of Securities Listing interprets supervisor independence in terms of the following relational statuses: (1) spouse; (2) linear relatives by blood within the third degree of relationship; (3) collateral relatives within the fourth degree of relationship; (4) representatives of the same juridical person; and (5) affiliates. Supplementary Provisions, *supra* note 123, art 17, ¶ 1, item 2.

[158]The Company Law also somewhat mitigates outside influence on the supervisor by providing that "[a] supervisor shall not concurrently be a director, manager, or employee of the company." COMPANY LAW, *supra* note 81, art. 222 (no change was made to this provision in the November 2001 revisions).

[159]*See supra* text accompanying notes 119-20 (discussing the independent director requirements for listing on the securities exchanges).

[160]*See* COMPANY LAW, *supra* note 81, art. 23, ¶ 1 (stating that a responsible person owes a duty of loyalty in the exercise of her duties); *id.* art. 8, ¶ 2 (stating that supervisors are "responsible persons" within the scope of their duties).

[161]Article 223 provides that the supervisor will represent the company when one of its directors represents himself or another party in a transaction with the company. *Id.* art. 223. This provision does not apply to transactions between the company and one of its supervisors. *See id.* art. 227 (not providing for the application of Article 223 to apply to supervisors). Article 209 requires that when a director acts for himself or on the behalf of another person in a transaction within the scope of business of the company, the director must explain the contents of the transaction to a meeting of the shareholders for their approval. *Id.* art. 209. This provision does

In addition, imposing a duty of loyalty on supervisors should improve supervisor independence—it sends a strong signal to supervisors that their loyalties lie with the company and not the board or the controlling shareholder. Whether the rubber stamp supervisory becomes a thing of the past in Taiwan may depend, at least in part, on the development of the nature and scope of the duty of loyalty.[162]

4. Supervisor's Ability to Monitor Board Activities

The revised Company Law provides a more forceful directive to the supervisor. Prior to the November 2001 revisions, Article 218 began "[a] supervisor *may* at any time investigate the business and financial condition of the company."[163] After the revision, Article 218 begins with the charge: "The supervisor *must* oversee the operations of company."[164]

To better enable the supervisors to oversee the operations of the Company, several new revisions to the Company Law provide the supervisor with improved abilities to monitor the board of directors. First, an increase in the minimum number of supervisors from one to at least two[165] provides twice as many hands, eyes, ears, and gray matter to sift through information, attend board meetings, and perform other supervisory duties. Simply stated, more people can monitor more effectively.[166] The revisions also give the supervisor greater ability to obtain information by allowing her to bypass the board and go directly to the managers for information.[167] Finally, the Company Law now gives the supervisor an express right to attend board meetings and voice an opinion at those meetings.[168] The Company law also requires the board to notify the supervisor seven days prior to any board meeting.[169] Although these revisions provide a basis for improved supervisor monitoring of the board,

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not apply to supervisors that engage in transactions within the company's scope of business. *See id.* art. 227 (not providing for the application of Article 209 to apply to supervisors).

[162]*See supra* text accompanying notes 127-43 (discussing the potential development of the duty of loyalty in Taiwan).

[163]COMPANY LAW, *supra* note 81, art. 218 (language prior to November 2001 revisions) (emphasis added).

[164]*Id.* (November 2001 revised version) (emphasis added).

[165]This applies to public issuing companies only. *Id.* art. 216, ¶ 2.

[166]*See* Huang, *supra* note 119, at 287 (discussing how multiple supervisors can increase the effectiveness of the supervisory).

[167]COMPANY LAW, *supra* note 81, art. 218, ¶ 1.

[168]*Id.* art. 218-2, ¶ 1.

[169]*Id.* art. 204.

their effectiveness ultimately depends on the independence of the supervisor.

5. Supervisor Independence and Ability to Monitor the Board—Preliminary Conclusion

As one Taiwanese scholar aptly expressed, the revisions to the Company Law with respect to the supervisor were "a foundation for further change."[170] The revisions did, however, make some progress toward increasing the independence of the supervisor by allowing non-shareholder supervisors, increasing the minimum number of supervisors and expressly imposing a duty of loyalty on supervisors.[171] The revisions also improved the ability of the supervisors to monitor the board of directors by increasing their number,[172] giving them better access to information and greater access to board meetings.

C. *Shareholder Rights*

The revisions to the Company Law include only a few changes to shareholder rights, but these changes show that the shareholder voice is becoming more important in Taiwan. The revised Company Law now gives shareholders more notice of shareholder meetings, reinforces the importance of shareholder resolutions, and removes the voting discount for small blockholders. Although the revisions did not significantly improve shareholder access to derivative suits, other extra-legal efforts to provide shareholders with better access to courts show an increased awareness of the role shareholders can play in monitoring the board of directors.

1. Shareholder Voting

The revisions improve the ability of shareholders to participate in corporate governance. First, the new revisions provide shareholders of public companies with a longer notice period for shareholder meetings[173]

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[170]*See* Huang, *supra* note 119, at 291.

[171]*See supra* text accompanying notes 150-62.

[172]*See supra* text accompanying note 153.

[173]COMPANY LAW, *supra* note 81, art. 172, ¶ 3 (providing that public issuing companies must give 30 days notice to shareholders prior to the regular shareholder meeting and 15 days prior to an extraordinary shareholder meeting). *Compare id.* art. 172, ¶ 1 (providing that non-public issuing companies must give 20 days notice prior to the regular shareholder meeting) *with id.* art. 172, ¶ 2 (providing that non-public issuing companies must give 10 days notice for extraordinary shareholders meeting).

and limit what motions can be raised at a shareholder meeting without being included in the notice of the meeting.[174] These revisions provide better opportunity for dissenting views to be heard in shareholder meetings by providing more time for those who oppose management's proposals to organize and solicit proxies.

The revised Company Law also reinforces the notion that the board serves the interests of shareholders by expressly providing that directors cannot violate shareholder resolutions.[175] This provision may be less significant in a concentrated-ownership system where both board actions and shareholder resolutions generally reflect the will of the controlling shareholder, but it reinforces the directors' duty of loyalty as ownership in Taiwan becomes more diffuse and management gains greater control over the operations of the company and the board.

2. Shareholder Derivative Suits

Originally, the Company Law required a shareholder to hold five percent of the company's shares for one year before she could qualify to initiate a derivative suit against a director.[176] Minimum shareholding qualifications were not the only obstacles to shareholder derivative suits in Taiwan. The Company Law allows the court to require the shareholder-plaintiff to post a bond.[177] In addition, plaintiffs must advance court fees at each level of trial and appeal,[178] further discouraging shareholder derivative suits.

To provide shareholders better access to the courts, the revised Company Law lowered the minimum shareholding threshold to three percent.[179] Obviously this will have little effect on the ability of most minority shareholders to initiate derivative suits. More significantly, however, the Securities and Futures Commission in cooperation with a

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[174]The revised Company Law no longer allows new motions at shareholder meetings with respect to the major transactions listed in Article 185. *See id.* art. 172, ¶ 5.

[175]*Id.* art. 218-2, ¶ 2 ("When the board of directors or any director violates a law, regulation, the articles of incorporation, or *the resolutions of the shareholder meeting*, in the operation of the business of the company, the supervisor shall immediately notify the board or director to stop."). The original wording of Article 218-2 did not include reference to "resolutions of the shareholder meeting."

[176]*Id.* art. 214, ¶ 1 (prior to November 2001 revisions).

[177]COMPANY LAW, *supra* note 81, art. 214, ¶ 2.

[178]*See* Liu, *supra* note 147, at 5.

[179]COMPANY LAW, *supra* note 81, art. 214, ¶ 1.

private institution, the Securities and Futures Institute, have taken other measures designed to promote greater shareholder access to the courts.[180]

3. Elimination of the Blockholder Voting Discount

Originally, the Company Law required the company's articles of incorporation to discount the voting rights of shareholders holding three percent or more of the company's issued shares. The revised law removes this mandatory blockholder voting discount.[181] This revision may provide minority blockholders with a greater voice in shareholder meetings by eliminating the blockholder voting discount, but may have removed a deterrent to controlling shareholder expropriation in the same breath. Although the elimination of the blockholder voting discount was based on the egalitarian principle of "one share, one vote"[182] and will arguably provide minority blockholders with greater voice, it may have a negative overall effect. Recent studies indicate there is a greater potential for controlling shareholder expropriation when voting rights exceed cash flow rights.[183] To the extent the blockholder voting discount made it more difficult for a controlling shareholder's voting rights to exceed her cash flow rights, it may have actually discouraged a certain amount of controlling shareholder expropriation.[184]

The elimination of the blockholder voting discount may promote minority shareholder interests to the extent it gives more voting rights to small blockholders who are not dominated by the controlling shareholder. Yet, it may serve to harm minority interests to the extent it gives greater voting rights to the controlling shareholder, or removes a mechanism that

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[180]For a more thorough discussion of the role of the Securities and Futures Institute in encouraging shareholder suits, see Liu, *supra* note 119, at 31-32

[181]COMPANY LAW, *supra* note 81, art. 179, ¶ 1.

[182]*See* Lai Yuan-He, *Gu Dong Hui* [*The Shareholder Meeting*], *in* AN ANALYSIS OF THE REVISED COMPANY LAW, *supra* note 71, at 225, 242.

[183]*See* La Porta et al., *supra* note 5, at 511; *see also* Bernard Black & Reinier Kraakman, *A Self-Enforcing Model of Corporate Law*, 109 HARV. L. REV. 1911, 1945-46 (1996) ("The case for the one share, one vote rule turns primarily on its ability to match economic incentives with voting power and to preserve the market for corporate control as a check on bad management.").

[184]Voting rights may exceed cash flow rights through super-voting preferred shares, which the Taiwan Company Law does not allow. *See infra* text accompanying notes 238-41 (discussing preferred shares). In addition, the use of pyramid ownership structures can effectively increase a shareholder's voting rights without increasing her cash flow rights proportionately. *See* La Porta et al., *supra* note 5, at 502-04. In a study on the expropriation of minority shareholders in Asia, relatively little evidence of expropriation in Taiwan correlates with an insignificant difference between cash flow rights and voting rights. *See* Stijn Claessens et al., *On Expropriation of Minority Shareholders: Evidence from East Asia* (manuscript at 27, *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=20239).

made it less likely a controlling shareholder's voting rights will exceed her cash flow rights. Ultimately, the elimination of the blockholder discount may be appropriate when greater dispersion of ownership dominates Taiwanese companies; if no single shareholder (or group) dominates the vote, then there is little need to discount blockholder votes.

4. Shareholder Rights—Preliminary Conclusion

The recent revisions to the Company Law show an increased awareness of the importance of minority shareholders in corporate governance. Most notable of these changes are the new rules providing better notice of shareholder meetings, which improves the ability of dissenting shareholders to rally support and solicit proxies.[185] The revisions, however, did little to improve shareholder access to derivative suits, although extra-legal developments show a trend, albeit a slow one, toward providing shareholders greater access to courts.[186]

Finally, the elimination of the blockholder voting discount may better promote minority shareholder interests to the extent it gives more voting rights to small blockholders who are not dominated by the controlling shareholder. The elimination of the voting discount may be more appropriate, however, when Taiwanese companies have more dispersed-ownership structures with no controlling shareholders.

D. *The Role of Managers in the Company Law*

The separation of ownership and control that occurs in dispersed-ownership systems gives rise to powerful managers.[187] The new revisions to the Company Law show that Taiwan is placing greater importance on the function of the professional manager in the Taiwanese corporation. Although no single revision definitively shows that managers are gaining power in Taiwanese corporations to the extent they pose as significant a threat to shareholder interests as controlling shareholders do, a look at several revisions demonstrates a trend toward a greater role, increased responsibility for managers in the Taiwanese firm, and concern with their accountability.

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[185] *See supra* text accompanying notes 173-74.

[186] *See supra* text accompanying notes 179-80.

[187] *See supra* text accompanying notes 17, 76-80.

1. The Greater Role and Responsibility of Managers

Several revisions show that the professional manager is playing a greater role in the Taiwanese corporation. First, new revisions provide a company with more flexibility to create whatever management position, structure, and hierarchy it may require. Originally, the Company law expressly provided that "when there is more than one manager, there shall be one general manager and one or several managers."[188] The revised Company Law removed this requirement and now allows companies to establish their own management systems in their articles of incorporation.[189]

Second, the revisions clarify the authority of managers to administer the affairs of the company and sign documents on behalf of the company if provided for in the articles of incorporation or by contract.[190] Although this revision basically restates what is already provided in the Civil Code,[191] its significance may be more evident in light of Taiwan's system of corporate representation. Because the law provides that the directors, usually the chairman of the board, are the default legal representatives of the company,[192] expressly allowing the manager to act as the company's legal representative shows a subtle shift toward increased authority and power for managers.

Third, as discussed above, imposing a duty of loyalty on directors and supervisors serves not only to limit controlling shareholder influence on directors and supervisors, but also management influence on directors and supervisors as dispersion of ownership increases and management becomes more powerful.[193]

Finally, the revised Company Law reinforces the binding effect of shareholder resolutions on the board,[194] which buttresses the director's duty of loyalty *vis-à-vis* management as ownership in Taiwan becomes more diffuse and management gains greater control over the board.

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[188]COMPANY LAW, *supra* note 81, art. 29, ¶ 1 (prior to November 2001 revisions).

[189]*Id.* art. 29, ¶ 1 (November 2001 revised version).

[190]*Id.* art. 31, ¶ 2.

[191]*See* CIVIL CODE, *supra* note 128, art. 553.

[192]*See id.* art. 27, ¶ 2 ("The director has the authority to represent the juridical person to the outside in all matters. Unless the articles of incorporation provide otherwise, when there is more than one director, all shall have the authority to represent the juridical person.").

[193]*See supra* text accompanying note 143 (discussing how imposing a duty of loyalty on directors and supervisors serves to limit management influence on the board).

[194]*See supra* text accompanying note 177 (discussing the revision reinforcing the binding affect of a shareholder resolution on the board).

2. The Manager's Duty of Loyalty

The express imposition of a duty of loyalty on all responsible persons was an important addition to the Company Law.[195] This article has already discussed the effect the new duty of loyalty may have on the conduct of directors and supervisors.[196] Importantly, however, the duty of loyalty also applies to managers because they too are "responsible persons."[197]

There is nothing in the official legislative purpose for this revision indicating the lawmakers specifically intended to impose a duty of loyalty upon managers; rather, it seems as if they were generally concerned with conflicts of interests for all who had opportunity to abuse their position in the company.[198] By imposing a duty of loyalty upon managers, the revised Company Law has provided the shareholders with some protection from management misconduct and expropriation as dispersion of ownership results in more power for management. In addition, creating a duty of loyalty for management is a fairly significant revision to the Company Law because the self-dealing rules apply only to directors, not to managers.[199] Before the revisions, the basis for a manager's liability to the company was limited to tort (his failure to act as a good administrator),[200] a violation of laws, regulations, the articles of incorporation,[201] a violation of the decisions of the shareholders or board of directors,[202] or a violation of the rule prohibiting a manager from competing with the company or acting as the manager of another company.[203] By imposing a duty of loyalty on the manager, the Company Law addresses the issues of increasing management

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[195]COMPANY LAW, *supra* note 81, art. 23, ¶ 1.

[196]*See supra* text accompanying notes 127-44 (discussing the director's duty of loyalty); *supra* text accompanying notes 160-62 (discussing the supervisor's duty of loyalty).

[197]*See* COMPANY LAW, *supra* note 81, art. 8, ¶ 2 (stating that managers are "responsible persons" within the scope of their duties).

[198]The legislative reason for this revision was "to clearly provide that responsible persons owe a duty of loyalty to the company." Wang, *supra* note 129, at 75-76.

[199]Article 223 provides that the supervisor will represent the company when one of its directors represents himself or another party in a transaction with the company. COMPANY LAW, *supra* note 81, art. 223. This provision does not apply to the self-dealing transactions of managers.

[200]Managers are usually appointed by the board of directors. The contract of mandate, therefore, also applies to managers, which means they have a duty to act as good administrators. *See supra* text accompanying note 128 (discussing the contract of mandate in the context of directors).

[201]COMPANY LAW, *supra* note 81, art. 34.

[202]*Id.* art. 33 (liability express in Article 34).

[203]*Id.* art. 32.

power and opportunity for expropriation, including self-dealing, as dispersion of ownership increases.

It should be noted, however, that the Company Law contains no mechanism for a shareholder derivative suit against a manager. Since the manager owes her duty of loyalty to the company, and not to the shareholders,[204] the absence of a provision allowing a shareholder derivative suit against management means shareholders must rely upon the board or the supervisor to initiate a suit against a manager. This issue may not seriously undermine the ability to monitor management while Taiwanese public companies remain dominated by family-controlled blockholders. As Taiwan moves away from the concentrated ownership system, management gains more power and influence over the board and supervisor. The lack of a shareholder derivative suit against managers will become a significant deficiency in Taiwan's corporate governance regime.

3. The Role of Managers—Preliminary Conclusion

The recent revisions to the Company Law demonstrate a subtle shift toward greater authority and power for professional managers. Along with this greater power comes more opportunity for abuse and misconduct. The new revisions take an important step toward regulating potential management expropriation by imposing a duty of loyalty on managers,[205] although there is no means by which a shareholder can initiate a derivative suit against a manager.[206] In addition, revisions that reinforce the binding effect of shareholder resolutions and impose an express duty of loyalty on directors and supervisors serve to limit management influence. This effect is key as dispersion of ownership increases and management stands to gain greater control over the operations of the company, the board, and supervisors.

E. *Taiwan's Revised Company Law and the Transition Toward a Shareholder-Oriented Model and Dispersed-Ownership Model—Preliminary Conclusion*

The recent revisions to the Company Law strongly indicate Taiwan is making a gradual transition toward a shareholder-oriented model of corporate governance. This transition does not necessarily manifest itself

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[204] *See supra* text accompanying notes 138-42, 197-99 (discussing how responsible persons owe their duties of loyalty to the company, not the shareholders).

[205] *See supra* text accompanying notes 195-203.

[206] *See supra* text accompanying notes 138-42, 197-99.

in an overall improvement to the rules protecting shareholder interests but is indeed evident in Taiwan's struggle with the issues crucial to the protection of minority shareholders. Arguably, every improvement in shareholder protection in the November 2001 revisions was offset by setbacks. Adding an express duty of loyalty served to increase director and supervisor independence, but was tempered by the elimination of mandatory cumulative voting and the failure to eliminate the appointee-director system. New revisions giving minority shareholders a better voice in shareholder meetings may have been somewhat mitigated by the elimination of the voting discount for the controlling shareholder. Furthermore, private ordering responses from the securities exchanges, addressing director and supervisor independence, sent a mixed signal at best and may have weakened the securities exchanges as a method for companies to bond themselves to a stricter corporate governance regime.

On the other hand, the recent revisions portray a country grappling with the problems of protecting minority shareholders from controlling shareholder expropriation, which is an essential aspect of protecting shareholder interests in a concentrated-ownership system. The November 2001 revisions demonstrate that Taiwan is struggling with issues that are critical to protecting minority shareholders: director independence from controlling shareholder influence; supervisor independence from board and controlling shareholder influence; the supervisor's ability to monitor the board; and the ability of the minority shareholders to voice their opinions. The struggle itself shows progress toward better protection of minority shareholder interests. Thus, even though Taiwan has not achieved an optimal level of minority shareholder protection, it has at least set a course toward a shareholder-oriented model of corporate governance. Whether Taiwan continues on this course depends on the regulators, the lawmakers, the courts, and whether the shareholders themselves are able to form a strong lobby for reform.

Finally, the increased importance that the revisions place on the role and accountability of the professional manager indicates that dispersion of ownership is already factoring into the corporate governance of the Taiwanese firm. This trend toward a dispersed-ownership model may be further encouraged by revisions addressing board independence from controlling shareholder dominance. To the extent the revisions reduce the controlling shareholder's private benefits of control, they will consequently reduce her incentive to maintain such a large block of shares. In addition, a board that is truly independent of controlling shareholder and manager dominance provides the controlling shareholder assurances that there will be little risk of expropriation of her investment if she relinquishes control through dilution of her shareholdings. Thus, the revisions to the Company

Law may not only be a preliminary response to the early stages of dispersion of ownership, they may in fact promote continued dispersion.

V. THE RELUCTANCE OF LAWMAKERS TO ELIMINATE DISABLING PROVISIONS THAT MAY PROTECT SHAREHOLDERS

The parameters of Taiwan's Company Law are rather restrictive. Its restrictive nature may in part reflect Taiwan's historical lack of emphasis on and understanding of corporate finance.[207] Some of the restrictive provisions may also reflect a distrust of corporate insiders[208] or reinforce the state's control over the firm through a corporate registration system.[209] The aggregate result is a somewhat disabling Company Law.[210]

The November 2001 revisions to the Company Law made great strides toward providing companies with more flexibility.[211] This article suggests, however, that the bureaucracy and legislature were reluctant to make changes to provisions of the Company Law that provided even minimal protection for shareholders, even where change would have provided significantly increased flexibility for companies. This phenomenon further lends support to the proposition that Taiwan is in transition toward a shareholder-oriented model of corporate governance.

A. *Revisions to the Company Law That Provide More Flexibility*

Many revisions to the Company Law serve to create a more enabling legal regime by easing restrictions on the formation and operation of companies. For example, the pre-revision Company Law required a

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[207]*See* Liu, *supra* note 119, at 5 (discussing Taiwan's traditional emphasis on the manufacturing industry and the view that the role of the financial sector is to support manufacturing).

[208]*See* Liu, *supra* note 99, at 13 ("Another implicit message lies behind these rigid rules: Taiwan has not been able to deal with the corporate governance issues effectively."); Liu, *supra* note 119, at 14 (stating the Company Law's affiliated company rules controlled abuse by parent companies when the real issue was the role of the director).

[209]*See* Liu, *supra* note 119, at 15 (discussing how registration of a company's business scope allowed the government to promote and implement its policies); *see also id.* at 3-4 (discussing how Taiwan's relation with the People's Republic of China affected Taiwan's corporate law system).

[210]*See* Liu, *supra* note 119, at 9 (characterizing Taiwan's corporate law system as "rigid and archaic").

[211]*See* Lai Yuan-He, *Cong Fa Gui Song Bang Yu Gong Si Jian Kong Lun Gong Si Fa Zhi Xiu Zheng Dong Xiang* [*Discussing the Direction of the Revisions from the Perspective of Loosening Restrictions and Corporate Governance*], *in* AN ANALYSIS OF THE REVISED COMPANY LAW, *supra* note 71, at 1-2.

corporation to have at least seven shareholders.[212] The rhetoric justifying this rule was the traditional civil law classification of a company as a "societal association."[213] "Society," of course, implied more than one person. The spirit of the seven-shareholder minimum, however, was easily circumvented by issuing virtually all of the company's shares to one shareholder and one share to each of six nominee shareholders. This nominee system created transaction costs, including potential corporate governance issues.[214]

The law after the November 2001 revisions now allows single shareholder companies when the one shareholder is a juridical person or the government.[215] Curiously enough, the revised Company Law still requires at least two shareholders when the shareholders are natural persons[216] due to concerns that single shareholder companies could be mere corporate shells used to defraud creditors.[217]

Furthermore, the revisions provide more flexibility by eliminating the requirement that a closely-held company must issue shares to the public once it reached a certain level of paid-in capitalization.[218] This rule had created perverse incentives for companies to limit their growth to keep their capitalization from reaching the regulatory threshold.[219] It probably also further exacerbated corporate governance issues because it essentially forced companies to create a class of minority shareholders.

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[212]*See* COMPANY LAW, art. 2, ¶ 1, item 4 (prior to November 2001 revisions). The revised Company Law also changed the shareholding structure for limited companies. Prior to the revisions, the Company Law required limited companies to have at least five shareholders, with twenty-one shareholders as a maximum. The revised Company Law now allows one-shareholder limited companies, regardless of whether that shareholder is a natural person, juridical person, or the government, and removes the maximum shareholder requirement. *Id.* art. 2, ¶ 1, item. 2.

[213]*See* KE, *supra* note 155, at 5 (describing the company as a societal association ("she tuan") and, thus, requiring at least two shareholders).

[214]Some transaction costs were purely administrative, for example, finding six nominees, producing and executing nominee agreements, and keeping track of the nominee and her shares, etc. Other transaction costs involved the introduction of potential corporate governance issues for what should have been, and what was for all practical matters, a single shareholder company.

[215]COMPANY LAW, *supra* note 81, art. 2, ¶ 1, item 4 (revised version).

[216]*Id.* art. 2, ¶ 1, item 4 (revised version).

[217]*See* Liu, *supra* note 99, at 14.

[218]The Company Law originally provided: "Where the capital of a Company has reached or exceeded a specific amount fixed by the central competent authority, its shares shall be issued publicly, unless the central competent authority approves otherwise." COMPANY LAW, art. 156, ¶ 4 (prior to November 2001 revisions). The revised version provides: "A company may by resolution of the board of directors apply to the securities regulation authority to issue shares to the public." *Id.* art. 156, ¶ 4 (November 2001 revised version).

[219]*See* Liu, *supra* note 119, at 20 (stating that many mid-sized companies in Taiwan have chosen to keep their paid-in capital below the threshold).

Other major changes of the November 2001 revisions mark the beginning of a gradual relaxation of Taiwan's burdensome registration system.[220] For example, the Company Law originally provided that a corporation did not come into existence until it received its Company License. The revised version of the Company Law now provides that a corporation comes into existence upon the filing of its articles of incorporation,[221] and no longer requires a company to restrict itself to a particular scope of business in its articles of incorporation.[222]

There were numerous other examples of revisions that created increased flexibility for companies, including: no longer requiring the chairman of the board to be a citizen of Taiwan;[223] allowing directors to attend board meetings by teleconference;[224] further liberalizing a company's ability to issue shares in exchange for in-kind consideration;[225] establishing the legal authority for spin-offs;[226] establishing a regime for employee stock options;[227] allowing a company to maintain treasury stock for employee options;[228] and authorizing a company to issue options to the employees of its subsidiaries.[229] In summary, the November 2001 revisions to the Company Law create a more enabling and more flexible legal regime for companies.

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[220]For a more thorough treatment of the problems with the registration system and the revisions that address those problems, see Liu, *supra* note 119, at 15-16, and Liu, *supra* note 99, at 20-21.

[221]COMPANY LAW, *supra* note 81, art. 6. *But see id.* art. 17, ¶ 1 ("If the business of a company requires the special permission of the government in accordance with relevant laws or orders given under authority of law, such company may only apply for registration of incorporation after it has obtained permission.").

[222]The Company Law originally provided, "A company shall not engage in any business outside the scope of its registered business." *Id.* art. 15, ¶ 1 (prior to November 2001 revisions). This provision was deleted in the November 2001 revisions.

[223]The Company Law had provided, "The Chairman of the board and the vice chairman shall have Republic of China [i.e., Taiwan] citizenship and domicile; at least half of the members of the board managing committee shall be domiciled in Republic of China [i.e., Taiwan]." *Id.* art. 208, ¶ 5 (prior to November 2001 revisions). This provision was deleted by the November 2001 revisions.

[224]*Id.* art. 205, ¶ 2 (revised version).

[225]COMPANY LAW, *supra* note 81, art. 156, ¶ 5 (revised version).

[226]*Id.* art. 316 (revised version).

[227]*Id.* art. 167-2 (revised version).

[228]*Id.* art. 167-1 (revised version).

[229]COMPANY LAW, *supra* note 81, art. 235, ¶ 4 (revised version).

B. *Provisions in the Company Law That Lawmakers Were Reluctant to Change*

Despite the general effort to create a more enabling Company Law, the bureaucracy and the legislature were not willing to make significant changes in some areas—most notably, to rules that served to protect shareholder interests. Although these provisions were not the paradigmatic corporate governance rules, they were designed either to have some or complete influence on protecting shareholder interests. The unwillingness to change provisions that provided even minimal shareholder protection supports the theory that Taiwan is struggling toward a shareholder-oriented model of corporate governance.

1. Restrictions on Corporate Reinvestment

Article 13 of the Company Law allows a company to invest in other companies only to the extent its aggregate investment in other companies does not exceed forty percent of its own paid-in capital.[230] The company may exceed the forty percent limitation, however, if it receives approval from the shareholders.[231] Since the shareholders have the ultimate authority to decide whether the company can exceed the statutory limitation, it is relatively safe to assume that the purpose of this rule is to protect the interests of the shareholders. Although the CEPD research team recommended eliminating this reinvestment restriction, the MOEA rejected the recommendation and proposed no change to the legislature.[232]

2. Prohibition on Corporate Guaranties

The Company Law prohibits a company from acting as a guarantor unless its articles of incorporation or relevant laws expressly allow otherwise.[233] Although this provision obviously provides some protection for creditors, it is more likely that the intent of this rule is to protect the company's shareholders. First, the shareholders have the power to amend the articles of incorporation and allow the company to act as a guarantor.[234]

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[230] *Id.* art. 13, ¶ 1; *id.* ¶ 1, item 3.

[231] *Id.* art. 13, ¶ 1; *id.* ¶ 1, item 3.

[232] *See* Liu, *supra* note 99, at 16.

[233] COMPANY LAW, *supra* note 81, art. 16.

[234] Creditors will benefit to the extent they know their non-priority creditor rights will not be compromised by liabilities the company incurs by acting as a guarantor unless, of course, the shareholders agree to amend the articles of incorporation.

In addition, the company is insulated from liability if one of its "responsible persons" violates the rule.[235] Consequently, the shareholders' investments are effectively insulated from liability if the company violates this provision. The CEPD research team recommended allowing a company to act as a guarantor or, as an alternative, holding the company civilly liable for any guarantees it makes in violation of this provision.[236] The MOEA, however, rejected these recommendations.[237]

3. Prohibition on Preferred Shares with Super Voting Rights

The Company Law allows a corporation to issue preferred shares.[238] Although the law does not expressly prohibit preferred shares with higher voting rights than common shares, the MOEA has interpreted this provision to prohibit a company from issuing preferred shares with super voting rights.[239] This rule creates problems for companies trying to raise capital through more innovative transactions. On the other hand, this rule may provide some protection to minority shareholders. There is evidence that when voting rights of a controlling shareholder exceed her cash flow rights, she may have more incentive to expropriate the minority shareholders.[240] Thus, the prohibition on super voting shares may ultimately protect minority shareholders, although it may hinder a company's ability to attract a large investor. The provisions in the Company Law governing the issue of preferred shares were not amended to expressly allow preferred shares with super voting rights.[241]

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[235]The Company Law provides: "The responsible person of a company acting in violation of [the prohibition on acting as guarantor] shall personally bear the responsibility of such guaranty and shall also be liable to the company for any injury that it may have sustained." *Id.* art. 16, ¶ 2.

[236]*See* Liu, *supra* note 99, at 17.

[237]*See id.*

[238]COMPANY LAW, *supra* note 81, art. 156, ¶ 1 (stating a company may issue preferred shares on terms as provided for in the articles of incorporation); *id.* art. 157 (stating that the company must provide for certain items in its articles of incorporation if it desires to issue preferred shares).

[239]Jing Ji Bu 73.03.23 Shang Zi 11159 [MOEA Mar. 23, 1983 No.11159].

[240]*See supra* note 184 and accompanying text (discussing cash flow rights and voting rights). *But see* Black & Kraakman, *supra* note 183, at 1946 (discussing the argument against the "one share, one vote" rule).

[241]The CEPD research team was aware of this issue and at least some of the members were critical of the status quo. *See* Liu, *supra* note 99, at 20.

4. Shareholders' Preemptive Rights

The Company Law gives preemptive rights to all shareholders when the company issues new shares.[242] The CEPD research team not only thought this provision hindered a company's ability to raise new capital, they also considered it especially unnecessary for shareholders of public companies who could buy more shares on the market if they so desired.[243] The CEPD research team, therefore, recommended eliminating shareholders' preemptive rights from the Company Law. The MOEA rejected the recommendation.[244]

5. One Price Rule

The Company Law provides that all shares issued at the same time and with the same terms, must be issued for the same price.[245] This rule protects shareholders from the possibility of insiders issuing shares to themselves or related parties for a more favorable price. The CEPD research team recommended eliminating this provision because it prevented "efficient price discrimination."[246] They suggested that fiduciary duties should address the problem of insider abuse of price discrimination.[247] This provision was modified somewhat during the recent revisions to allow increased flexibility for the underwriting industry.[248] The revised Company Law now allows price discrimination on shares issued by public companies, but only if the Securities and Futures Commission allows.[249]

6. Restrictions on Promoters' Transfer of Shares

The Company Law prohibits the promoters of a company from transferring their shareholdings within one year of incorporation.[250] Apparently, the legislative intent of this provision was to prevent promoter abuse of other shareholders.[251] The CEPD research team recommended

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[242]COMPANY LAW, *supra* note 81, art. 267, ¶ 3.

[243]*See* Liu, *supra* note 99, at 23-24.

[244]*See id.*

[245]COMPANY LAW, *supra* note 81, art. 156, ¶ 7.

[246]Liu, *supra* note 119, at 19.

[247]*See* Liu, *supra* note 99, at 19.

[248]*See* Wang Ren-Hong & Wang Wen-Yu, *Gu Fen* [*Shares*], *in* AN ANALYSIS OF THE REVISED COMPANY LAW, *supra* note 71, at 179, 190.

[249]*See* Liu, *supra* note 99, at 19.

[250]COMPANY LAW, *supra* note 81, art. 163, ¶ 2.

[251]*See* Liu, *supra* note 99, at 26.

eliminating this provision because it was easily circumvented and they doubted whether it actually served to protect shareholders.[252] In the end, this provision was slightly modified by a limited exception. Promoters are now allowed to transfer their shares within one year of incorporation only in the case of a merger or spin-off.[253]

7. Prohibition on Corporate Loans

The pre-revision Company Law prohibited a company from making loans to its shareholders or any other person, except in transactions where credit is provided to a trading partner.[254] The apparent purpose of this provision was to prevent insiders from siphoning the funds out of the company.[255] The CEPD research team recommended creating a general exception that would allow for the creation of finance companies.[256]

The MOEA rejected the team's recommendation because they feared finance companies would fall between regulatory cracks.[257] The MOEA made its own recommendation, which proposed allowing loans among affiliated companies.[258] Although the recommendation by the MOEA makes the provision somewhat less potent in light of its purpose—to discourage insiders from expropriating company funds—the provision was, nonetheless, revised accordingly by the legislature.[259]

C. *The Reluctance to Change Certain Provisions—Preliminary Conclusion*

During the large-scale revision process of the Taiwan Company Law, the reluctance to revise rigid Company Law provisions that provide even limited protection for shareholders demonstrates an increased awareness in Taiwan of the importance of protecting shareholder interests. Indeed, the

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[252]*See id.* at 26-27.

[253]COMPANY LAW, *supra* note 81, art. 163, ¶ 2.

[254]*Id.* art. 15, ¶ 2 (prior to November 2001 revisions).

[255]*See* Liu, *supra* note 99, at 17.

[256]The CEPD research team members were split on this issue and the recommendation was the result of a compromise. *See id.*

[257]*See id.* The Taiwanese regulators may have been influenced by the Japanese experience. For a discussion of how the Japanese home mortgage lending industry fell between regulatory cracks, see Curtis J. Milhaupt & Geoffrey P. Miller, *Cooperation, Conflict, and Convergence in Japanese Finance: Evidence from the "Jusen" Problem*, 29 LAW & POL'Y INT'L BUS. 1 (1997).

[258]*See* Liu, *supra* note 99, at 17.

[259]COMPANY LAW, *supra* note 81, art. 15, ¶ 1 (November 2001 revised version).

lawmakers must have been uncertain whether other revisions to the Company Law's corporate governance regime would serve as adequate substitutes.[260] The decision to not make significant revisions in these cases indicates that Taiwan is taking steps toward a shareholder-oriented model of corporate governance. Furthermore, the reluctance of lawmakers to change these rules coupled with the general need for a more enabling Company Law may, in fact, encourage further development and strengthening of the corporate governance rules in Taiwan—strengthening rules that deal directly with the issue of protecting shareholder interests would allow for elimination of the these restrictive provisions.

VI. CONCLUSION

The November 2001 revisions to Taiwan's Company Law indicate that Taiwan is transitioning toward a shareholder-oriented model of corporate governance and a dispersed-ownership system. Even though the Company Law may still need significant improvements with respect to protecting shareholder interests, the revisions to the Company Law demonstrate Taiwan is struggling with the issues crucial to protecting shareholders. This struggle strongly indicates Taiwan has already begun the gradual transition toward a shareholder-oriented model of corporate governance and a dispersed-ownership system.

This article has suggested that if Taiwan were transitioning toward a shareholder-oriented model of corporate governance, recent revisions to its Company Law would address the issue of controlling shareholder expropriation of minority shareholders. An analysis of the revised Company Law does indeed show that Taiwan is struggling with the problems of controlling shareholder expropriation of minority shareholders by addressing director independence from controlling shareholder influence, supervisor independence from board and controlling shareholder influence, the supervisor's ability to monitor the board, and the ability of minority shareholders to voice their opinions. In addition, the reluctance of lawmakers to revise disabling company law provisions that provide even minimal shareholder protections also supports the proposition that Taiwan is making the transition toward a shareholder-oriented model.

Moreover, this article has suggested that if Taiwan were transitioning toward a dispersed-ownership model, we would not only see new rules in

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[260]There were other instances during the revisions where sunk adaptive costs played a part in preventing more progressive reforms. *See* Liu, *supra* note 119, at 15 (discussing how reform of the onerous corporate registration system must be gradual because the administration and regulation of companies in Taiwan is geared toward it).

the revised Company Law addressing controlling shareholder expropriation, we would also see rules protecting shareholders from potential management expropriation. The revisions do indeed show the increased importance of the authority and accountability of the professional manager in the Company Law, which probably indicates dispersion of ownership is already affecting corporate governance of the Taiwanese company. Whether Taiwan's transition continues depends a great deal upon whether regulators, lawmakers, and judges continue to develop shareholder-oriented corporate governance rules and whether the shareholders themselves advocate further protection of their interests.