15 March 2022

Securities and Futures Bureau
No. 85, Section 1, Xinsheng South Road,
Da'an District
Taipei City
Taiwan

To Whom it May Concern,

Proposed Draft Amendments to Article 43-1, Article 178-1, and Article 183 of the Securities Exchange Act

We are writing in response to the call for public comment on the Proposed Draft Amendments to Article 43-1, Article 178-1, and Article 183 of the Securities Exchange Act issued by the Financial Supervisory Commission on 14 January 2022.

General comments

We welcome this proposed revision to regulations on the disclosure of substantial shareholdings, which has long been a topic of discussion between ACGA and regulators in Taiwan. We are pleased to see after many years of raising the issue that the proposed threshold for substantial shareholding disclosure is set to be lowered to 5%.

We also note with appreciation the wording of the press release for the call for comment, which highlights the original intention of the legislation: "The legislative intent of Article 43-1, Item 1 of the Securities and Exchange Law is it is expected that information about major changes in the company's equity can be disclosed in real time and fully, so that investors and competent authorities can know the reasons and trends of large changes in the company's equity, and then understand possible changes in the company's management rights and stock prices."

The draft amendment threshold of 5% brings Taiwan in line with most major international markets. However, despite this positive development, we remain concerned that the change to this single regulation will not be enough to achieve the stated legislative intent, which is to alert investors and regulators to possible changes in company management rights. The reason is that many unique characteristics of the Taiwan market mean that drastic changes in a company's management rights are possible with barely any changes in equity. We believe therefore that a more holistic approach to the issue is necessary.

We observe that the only proposed amendment to Article 43-1 of the Securities and Exchange Act is to change the existing 10% threshold for shareholding disclosure to 5%. We understand that changes to other regulations may be forthcoming, particularly to the

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Regulations Governing the Declaration of Acquisition of Shares in Accordance with Article 43-1, Paragraph 1 of the Securities and Exchange Act. We thus write this submission with the intention of highlighting concerns about the system of regulation as a whole and offering suggestions and comments to address them.

The system of regulation

As mentioned above, the legal intent of calling for 5% shareholding disclosure is to alert the market to the emergence of a significant shareholder on the company register which could try to exert influence over the board or lead to changes in management control at a later date. In most markets, such disclosure is enough to achieve this purpose because control is exercised through the holding of a sizeable or majority ownership stake. However, in the Taiwan context, this is not always so. As observed through a number of cases in recent years, such as Solar Applied Materials Technology (https://www.acga-asia.org/blog-detail.php?id=46), it is possible to gain control of a significant number or even a majority of board seats with disclosed holdings of much less than 5%. A number of characteristics of the Taiwan market contribute to this phenomenon:

- Shareholders with 1% holdings can nominate directors and independent directors;
- Cumulative voting makes it comparatively easy to get candidates elected, particularly if steps are taken to lock up the local proxy solicitation market;
- Independent directors may call EGMs and board elections and some independent directors may be firmly allied with particular factions.

While some of the mechanisms above were designed to empower minority shareholders to hold controlling shareholders and management accountable, in Taiwan they have sometimes been used as tools to seize control of companies despite small ownership stakes--a phenomenon that simply would not be possible in other developed markets.

A further concern is the prevalence of group structures and poorly disclosed networks of collaboration that can be deployed to surreptitiously gain control of a company without clear disclosure of the combined share ownership or even of the agreement to collaborate.

There is also the issue of “legal entity directors”. Again we refer to the Solar Tech case in which a legal entity changed its representative director and was able to affect the power balance on the board, nearly resulting in a change of both chair and management, and all with no notice at all to other shareholders until after the fact.

Given these factors, we believe that the legislative intent of Article 43-1 to allow “investors to understand possible changes in the listed company's management rights” is clearly not being met.

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Specific comments

To achieve the legislative intent – an objective we all share – we turn our attention to the Regulations Governing the Declaration of Acquisition of Shares in Accordance with Article 43-1, Paragraph 1 of the Securities and Exchange Act ("governing regulations"). As we understand, the governing regulations require that those who acquire, individually or jointly, 10% or more (5% after the amendment) of a listed entity to disclose this fact to the market and regulators within 10 days. This disclosure must also include information on the purpose of the acquisition and on any further plans, for example regarding additional share acquisitions, holding a special shareholders' meeting, running for board positions, disposing of assets, or changing the financial or operational condition of the acquiree company.

1. Timing

Our first concern, and perhaps the easiest to address, is the timing of disclosure. As written, the initial disclosure to the market of a substantial ownership position is required within 10 days (Article 6), while subsequent changes in ownership stakes must be made within two days (Article 7). We recommend that the initial disclosure be within five days, while the subsequent changes remain at two days.

2. Disclosure location

We understand that disclosure will continue to be made via the Market Observation Post System (MOPS). If the acquirer is a public company, it will make the disclosure itself on MOPS. If the acquirer is not a public company, it must first notify the issuer who will then make a MOPS announcement to the market. We would like to confirm that disclosure in all cases will appear on the issuer's announcements within two days and in English. Our test of the MOPS system shows that disclosure of acquisition of 10% of shares under current regulations does appear in acquirer announcements, but does not reliably appear in searches of the acquiree's announcements.

3. Disclosure of significant controllers

Article 6 Item 1 of the governing regulations requires disclosure of the identity "of any shareholder holding 5 percent (sic) or more of the shares, or any person who directly or indirectly controls any shareholder holding 5 percent (sic) or more of the shares, of the company".

There are at least two problems with the structure of this wording. First, it allows shareholders who want to surreptitiously control a listed company to simply hide their shareholding or control in an unlisted company that is one level beyond the level that must

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be disclosed. Secondly, shareholders may circumvent this rule by arranging to control unlisted companies with holdings of less than 5%.

Hong Kong's approach to addressing this issue has been to implement a "Significant Controller Register" (https://www.cr.gov.hk/en/legislation/scr/overview.htm). This register applies only to unlisted companies, not listed companies. It makes it possible to identify who controls the unlisted companies that hold shares in listed companies. It applies to those who directly or indirectly hold:

- 25% or more of an unlisted company's shares
- 25% or more of an unlisted company's voting rights
- the right to appoint or remove a majority of the unlisted company's board
- the right to exercise, or who actually exercise, significant influence or control over the company
- the right to exercise, or who actually exercise, significant influence or control over the activities of a trust or firm

We suggest including such significant controller information in the existing Ministry of Economic Affairs, Department of Commerce, Industrial Services Portal.

A further suggestion is requiring a statement from acquirers that they do not have direct or indirect control over shares in the issuer other than those declared and enforcing firmly if that turns out not to be the case.

4. Disclosure of "joint" acquisition

As noted above, one characteristic of the Taiwan market is the prevalence of group structures and poorly disclosed networks of collaboration. Therefore, disclosure on "joint" acquisition is important and we note some apparent inconsistency in how "joint" acquisition is treated in the regulations.

Article 4 of the governing regulations states that "acquisition of shares by a person jointly with another person or persons means acquiring issued shares of a public company by means of contract, agreement, or any other form of mutual consent between that person and such other person or persons."

Article 6 states "If the acquirer is a financial holding company and the company whose shares are acquired ("acquiree company") is a financial institution, also indicate the shareholdings of the acquirer's subsidiaries and affiliated enterprises in the acquiree company." From the wording of these two articles, we conclude that aggregate shareholdings of any non-financial acquirer's parent, subsidiaries and affiliates would not be considered as a "joint" acquisition. We would appreciate further clarification on whether this is the case and if so why.

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We would also appreciate information on how "joint" acquisitions are tracked and assessed in practice. We suggest providing additional guidance in a separate supporting document based on actual cases. We also suggest requiring a statement from acquirers that they do not have a "joint" acquisition agreement in place other than those declared.

5. Disclosure of "plans"

Article 6 of the governing regulations require disclosure of "whether the acquirer has a plan to exercise any of the following share rights, and if so, specify details of the plan:

A. Plan to propose and facilitate, either individually or jointly with another person or persons, the holding of a special shareholders meeting.
B. Plan to run for, or to support another person to run for, director or supervisor.
C. Plan to dispose of assets, or to change the financial or operational condition, of the acquiree company."

Article 7 further simply states that changes to the "content of any plan to exercise share rights" must also be disclosed.

We would bring attention to the fact that these rules as written leave a lot of room for interpretation and manipulation. For example, it is not clear if item A would include efforts to influence or convince an independent director to call a special shareholders meeting. Item B evidently does not include a requirement to disclose the intent to become the representative of an existing legal entity director. Item C does not seem to include the intention to gain control of the board of directors. Furthermore, it is not clear what level of detail is required under Article 7. We suggest providing additional guidance in a separate supporting document based on actual cases.

6. Substantial shareholders vs insiders

In previous discussions, regulators have said that one challenge in changing the 5% disclosure rule has been that the definition of substantial shareholder is linked to the definition of "insider", which triggers the pre-disclosure of share transfers. It is not clear from the draft if or how that challenge has been resolved.

Enforcement

We would ask for greater transparency from the regulator on the enforcement of substantial ownership rules and their enforcement philosophy. We would be interested to see details of investigation and enforcement of failure to disclose "plans" and "joint" efforts. We would also be keen to know how the regulator enforces against individuals who have not honestly identified themselves as working jointly.

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In conclusion, although we still have many concerns about how the legislative intent of Article 43-1 will be achieved so that investors and regulators understand possible changes of company management rights, we appreciate and support the proposed amendment to a 5% threshold as a concrete step in bringing Taiwan's substantial shareholding disclosure further in line with international norms. We would be pleased to discuss any of the points in our letter further with you.

Yours sincerely,

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