
Taiwan

Negotiated M&A Guide 2022

Corporate and M&A Law Committee

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1. INTRODUCTION

1.1. Overview of Taiwan's M&A market and the impact of Covid-19

According to the *2021 Taiwan M&A White Paper* published by PwC Taiwan and the Taiwan Mergers & Acquisitions and Private Equity Council, the total number of notable M&A transactions in Taiwan dropped from 85 in 2019 to 76 in 2020, but the total dollar value of M&A transactions in Taiwan increased from US\$7.2bn in 2019 to US\$10.59bn in 2020. The paper shows that the M&A market in Taiwan was practically unaffected by the Covid-19 pandemic and there was an upward trend of domestic M&A transactions.

According to the information published by the Taiwan's Ministry of Economic Affairs, inbound investments reduced from US\$11.1bn in 2019 to US\$9.1bn in 2020, while outbound investments increased from US\$6.8bn in 2019 to US\$11.8bn in 2020. Taiwanese companies are actively looking for the opportunity to acquire foreign companies to enhance their market strength and increase their global exposure, while foreign investors are being more conservative in offshore M&A activities in 2020.

1.2. Taiwan's foreign investment policy

Taiwan has a long-standing welcoming attitude with foreign investments. With the prior approval from the Investment Commission of Ministry of Economic Affairs (MOEAIC), foreign investors are allowed to incorporate a new company or branch or acquire an existing company in Taiwan in most of the industries, except for those listed in a 'negative list' promulgated by MOEAIC. This includes certain military, telecommunications, electricity and transportation businesses which may impose certain restrictions on shareholding by foreigners. A foreign-owned company or branch office in Taiwan may enjoy almost the same rights and protection as a domestically owned company. The Taiwan government has proposed to amend the above regime from prior approval to post-investment reporting, but it is still unclear whether and when the amendment will be passed by the Congress.

In contrast, due to the special political relationship and tension between Taiwan and the People's Republic of China (PRC), the Taiwan government places strict scrutiny on direct and indirect investments from PRC, and a different set of regulations apply to such investments. Only industries that are listed in a 'positive list' promulgated by MOEAIC are allowed to be invested in by PRC investors with prior approval from MOEAIC.

A new law enacted on 30 December 2020 has expanded the investment types that PRC investors need to obtain MOEAIC's prior approval for. The term 'PRC investor' is broadly defined to include PRC individual and PRC-incorporated legal entities, and any entity that is incorporated outside of PRC but (1) more than 30 per cent of the shares or voting power of such entities is directly or indirectly owned by PRC individuals/legal entities, or (2) PRC individuals/legal entities have the ability to control, by any means. Thus, even though an M&A transaction occurs offshore, as long as the offshore target company will become a PRC investor upon closing, prior approval from MOEAIC is required if such target company has any investment in Taiwan. Failure to obtain MOEAIC prior approval will subject the offshore target company to an administrative fine, suspension of shareholders' rights and an order to divest the investment in Taiwan within a given period.

This policy and restriction on PRC investment also has great de facto impact on Taiwan's foreign investment practice, as a foreign investor must demonstrate that it is not a PRC investor as defined by MOEAIC's regulations before MOEAIC may grant its approval.

MOEAIC will normally request the foreign investor disclose its holding structure up to the ultimate beneficial owners and the board composition for the above-mentioned 30 per cent threshold check. This has become one of the key considerations for foreign investors when contemplating investment in, or an acquisition of, a Taiwanese company.

1.3 Taiwan's M&A regulatory landscape

In addition to the laws and regulations related to foreign investment and PRC investments, Taiwan's Company Act (Company Act) and the Business Mergers and Acquisitions Act (BMAA) are the most significant laws that govern M&A transactions in Taiwan. In addition, if the target company is a public company or listed company, the Securities and Exchange Act (SEA) and related regulations such as tender offer rules may apply. The Fair Trade Act (FTA) which governs merger control, and the Labor Standards Act (LSA) which sets forth the mandatory labour protections applicable to all employees in Taiwan, are also major considerations when conducting an M&A transaction in Taiwan.

2. M&A TRANSACTION STRUCTURES

2.1. Type of transaction structures

M&A transactions in Taiwan can be structured as mergers, spin-offs, share exchanges (share swaps), asset purchases and share purchases. In each of these structures, the consideration may be paid by either in cash, shares or other assets in general, but there may be some additional restrictions or requirements on non-cash consideration.

2.2. Advantages and disadvantages of each structure

Other than the tax considerations discussed below, there is no specific advantage or disadvantage between different kinds of transaction structures: each structure may be used to serve different kinds of acquisition purposes. In a private M&A transaction, the share purchase structure is more popular as there is more flexibility when negotiating a share purchase agreement; in a public M&A transaction, the merger/share exchange structure is more commonly used to squeeze out the minority shareholders. Spin-off/asset purchase structures are used when the purpose of transaction is only to acquire certain businesses or assets of the target company.

2.3. Tax considerations

Whether the transaction structure is a merger, asset purchase, share purchase or share exchange, when satisfying the requirements set forth in the BMAA, the parties to the transaction may enjoy certain tax incentives such as being exempted from stamp duty, deed tax and securities exchange tax, and the deferral of land value increment tax.

There are some differences in tax treatment between the different structures that should be considered. For example, in a simple merger structure, since the target company ceases to exist as a distinct legal entity, its carried losses would be assumed by the surviving company, while in a share exchange structure, since the target company survives and becomes a subsidiary of the acquirer, its carried losses may be preserved.

From the selling shareholders' perspective, the tax treatments under each transaction structure may be different as well. If the transaction is carried out through a share exchange, the proceeds

obtained by the shareholders of the target company from the sale of the target company's shares are treated as 'securities transactions income' under Taiwan tax laws. If the transaction structure is a merger and the proceeds obtained by the shareholders of the target company from the merger exceed their capital contribution to the target company, the exceeding portion of the proceeds is deemed as 'dividend income' under Taiwan tax laws. If the transaction is structured as an asset purchase and the target company is liquidated thereafter, the portion of the liquidation income that exceeds the share capital of the target company is 'securities transactions income' under Taiwan tax laws.

The taxation and applicable tax rate of 'dividend income' and 'securities transactions income' are treated differently between individuals and legal entities, and between domestic and foreign entities. The standard tax rate also may be reduced in accordance with the tax treaties entered into by Taiwan and other countries. Therefore, before selecting a specific transaction structure, it is crucial to conduct a tax evaluation beforehand.

2.4. Other considerations

When carrying out an M&A transaction in Taiwan, BMAA provides certain corporation action procedures (eg, a special committee must be established to review the fairness and reasonableness of the transaction, and a fairness opinion from an independent expert must be obtained if the target company is a public company). In addition, minimum voting thresholds, protective procedures for creditors, mandatory labour protection rules and protective procedures of dissenting shareholders that must be followed. These mandatory rules and regulations are applicable to almost all types of transaction structures.

3. PRE-AGREEMENT DOCUMENTATION

Typical pre-agreement documentation in Taiwan M&A transactions includes a confidentiality agreement, a memorandum of understanding/letter of intent and/or a term sheet. Basic commercial terms, closing conditions, representations and warranties, special covenants, employment matters, exclusivity/non-solicitation, and confidentiality clauses are all commonly seen in a pre-agreement term sheet, but normally only the confidentiality clause and exclusive rights clause are agreed by the parties to be binding. It is also common that parties go straight to the negotiation of transaction documents without entering into a formal pre-agreement documentation.

4. DILIGENCE STAGE

4.1 Scope and process of due diligence

The scope of legal due diligence in Taiwan M&A transactions usually includes the target company's shareholding structure and corporate governance, permits/licences/government documents, material contracts, financing documents, assets and intellectual property rights, related party transactions, labour, environmental and litigations. Most of the legal due diligence is now conducted through virtual data rooms and management interviews/Q&A sessions, which are commonly seen in Taiwan's M&A practice.

If the target company is a public company, it is more likely that the target company will not agree to disclose non-public information, primarily due to insider trading and corporate governance concerns.

4.2 Issues that are typically seen and how they are typically addressed

In conducting due diligence on Taiwan private companies, typical issues that may be discovered include:

- a) required permits/approvals for certain parts of the target company's business are not obtained;
- b) corporate documents or board resolution minutes are missing or incorrect;
- c) there are no formal agreements with trading counterparties;
- d) material contracts are undated or have expired;
- e) there are undocumented related party transactions;
- f) incorrect ownership of real estate;
- g) employment contracts (especially the termination and non-compete clauses) or work rules are in violation of the mandatory labour laws;
- h) protection of intellectual property rights; and
- i) factories or manufacturing sites have environmental pollution issues.

Normally these issues may be addressed by asking the target company to sign, re-sign, revise, amend or cancel the relevant contracts or documents, and including such action items as part of the closing conditions or to reserve a portion of the purchase price for the correction of environmental pollution issues. The acquirer may also request for an adjustment of the purchase price, to include more representations and warranties, to agree on a guarantee or escrow arrangement, or to divest or exclude a certain business/liability in the transaction documents.

5. MAIN TRANSACTION AGREEMENT

5.1 Formal requirement of transaction agreement

The BMAA requires that certain items must be included in a merger or share exchange agreement: the consideration, number of newly issued shares, share exchange ratio, change in the company's articles of incorporation, etc. There is no specific requirement applicable to the language of the transaction agreement.

5.2 Typical key clauses in the transaction documents

In Taiwan's M&A transactions, typical key clauses include the consideration (its calculation and its adjustment, if any), the closing conditions and closing mechanism, representations and warranties, pre-closing and post-closing covenants, indemnification, termination and other miscellaneous terms.

The key representations and warranties commonly seen in Taiwan's transactions mainly include: legitimate incorporation and good standing, authority, capital structure, accuracy of the financial statements and no non-disclosed liability, ownership of tangible and intangible properties, effectiveness of material contracts, compliance and no violations, no undisclosed litigation, labour laws compliance, etc.

6. TYPICAL CONDITIONS TO CLOSING/RELEVANT REGULATORY REGIME

6.1 Typical conditions to closing

In Taiwan's M&A transactions, typical closing conditions mainly include:

- a) all relevant approvals from government authorities having been obtained;
- b) the required corporate approvals having been duly obtained;
- c) all the representations and warranties made by the parties being accurate and correct;
- d) all covenants and obligations having been performed;
- e) no material adverse changes to the target company;
- f) consents from third parties having been obtained (if applicable); and
- g) legal opinion and/or officer certificates have been provided.

6.2 Relevant regulatory requirements

If an M&A transaction involves foreign investors, typical regulatory approvals include foreign investment approval and, as applicable, merger control clearance. If the target company is a listed company and if the target company will be delisted after the transaction or a mandatory tender offer is required, approval from the Financial Supervisory Commission and stock exchange that the company is listed on may be required. If the target company is operated with a special licence or permit (such as financial institutions), approval from the relevant regulatory body may be required. In addition, the Taiwan Central Bank's approval is also required in currency exchange if the consideration exceeds a certain threshold.

As stated above, Taiwan government has great concerns about PRC investors. When reviewing foreign investment approval, MOEAIC tends to require shareholder information up to the ultimate beneficial owners to see whether the foreign investors fall within the definition of a PRC investor under Taiwanese laws.

7. CLOSING ACTIONS

Typical steps to be undertaken for consummation of an M&A transaction in Taiwan mainly include paying consideration, paying securities exchange tax (if applicable), endorsement and handing over of physical share certificates (if applicable), exchange of other deliverables (such as company seals, bank books, permits, deeds, etc.), change of shareholders register and file for amendment of corporate registration.

In a cross-border transaction, the timing required for cross-border wire transfer and currency exchange should be considered in advance, especially when there is a financing arrangement involved.

8. POST-CLOSING

After closing, typical actions to be taken include re-electing the directors and supervisors of the company (and applying for amendment of corporate registration for change of directors and supervisors within 15 days), changing authorised signatories of bank accounts and other documents, and filing for verification of foreign investment within six months after closing.

According to the Company Act, all Taiwanese companies are now required to report annually the names, nationalities, birthdays or the dates of their incorporation, identification numbers, number of shareholdings or capital contributions, and other items as required of its directors, supervisors, managerial officers and shareholders holding more than 10 per cent of the total shares of a company to the information platform established by the competent authority by way of electronic transmission.

If there is any change in any of the above items, the company is required to report this to the information platform within 15 days. If the company is a public company or listed company,

more disclosure, reporting and compliance requirements are applicable pursuant to the relevant securities laws and regulations.