

International Jurisdictional Competition under Globalization: From the U.S. Regulation of Foreign Private Issuers to Taiwan’s Restrictions on Outward Investment in Mainland China

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Abstract

Drawing lessons from the story that the Sarbanes-Oxley Act drives away foreign issuers, this article takes as another case study the phenomenon that Taiwanese firms list shares overseas, to further test how usual law market demand and supply forces (or underlying exit and voice rights) interplay under international jurisdictional competition. Put simply, both cases of the U.S. and Taiwan significantly elaborate that law market forces underlying international jurisdictional competition are similarly at work even on both sides of the Pacific Ocean. Specifically, globalization strengthens the mobility of international production factors, and thus lowers firms’ costs of exiting from a given jurisdiction, which also fuels international jurisdictional competition for mobile firms or capital. Therefore, on the demand side of the international law market, if a regulating jurisdiction ignores business demands and imposes excessive regulation, firms would exit physically or threaten to exit in response. This means that the buyer side of the law market starts to operate and then sparks the seller side. On the international supply side, other jurisdictions as sellers would compete for these exiting firms’ corporate charters, listings and other related economic transactions by providing cost-effective regulatory products, to secure greater benefits to the local economy. Such economic exits send out signals to those in the political marketplace within the regulating jurisdiction, and thus activate interest group competition, or the domestic supply side. In consequence, firms, via these law market forces, exert pressure on the regulatory government to engage in a quest for more legal flexibility, or to liberalize unnecessarily excessive regulation.

Table of Content

I. INTRODUCTION	1
II. INTERNATIONAL JURISDICTIONAL COMPETITION UNDER GLOBALIZATION	6

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A.	The Law Market Dynamics	6
B.	Law Market Forces Underlying International Jurisdictional Competition	8
C.	International Jurisdictional Competition in Securities Regulation: The Case of the Sarbanes-Oxley Act of 2002	10
III.	JURISDICTIONAL COMPETITION AMONG LISTING MARKETS IN THE GREATER CHINESE ECONOMY: HONG KONG AS AN EXAMPLE OF COMPETITORS AGAINST TAIWAN	14
A.	The Demand Side of the Law Market	15
1.	The Restrictions on Outward Investment in Mainland China	15
1.1	The Background of the Capital Controls	15
1.2	The Legal Basis of the Constraints	17
2.	Problems of the Restrictions: Strong Intention but Weak Capability of Enforcement	19
2.1	Ignoring Economic Globalization and Business Demands	19
2.2	High Enforcement Costs of the Restrictions	24
2.2.1	Pervasive Evasion of the Restrictions	24
2.2.2	Regulatory Failure of the Restrictions	28
3.	Common Evasive Tactics to List Shares Overseas	37
B.	The Supply Side of the Law Market	41
1.	Mainly Selling Legal Flexibility, Rather than Legal Bonding	41
2.	Interest Group Competition to Seek Deregulation	51
3.	Ensuing Liberalization	60
C.	Summary	65
IV.	COMPARISONS BETWEEN THE PHENOMENA OF THE U.S. AND TAIWAN	68
A.	Differences	68
B.	Similarities	73
V.	CONCLUSION	75

I. INTRODUCTION

There are strong arguments favoring extending jurisdictional competition from the American competition between states for corporate charters¹ into international competition between securities regulators. This normative concept of issuer choice has been in a fierce debate among scholars. Some commentators propose permitting issuers to choose their disclosure regime. Specifically, proponents of issuer choice argue that when foreign firms enter U.S. capital markets, they should be permitted to obey the securities laws of the jurisdiction that they choose rather than the regulations provided by the Securities and Exchanges Commission (“SEC”). The proposal of issuer choice, by taking regulatory monopolies away from regulatory agencies such as the SEC, would force the agencies to make improvement on the quality of their respective local regulations.² In the meantime, opponents of issuer choice argue that it’s inevitable that jurisdictional competition in securities regulation would result in a race to the bottom where issuers would find jurisdictions with the least strict legal rules and the lowest degree of investor protection, which might drive the overall quality of securities regulation to decline.³ As a matter of fact, “[p]artial competition exists already, through firms’ choices of where to list and issue their shares.”⁴ Furthermore, “[d]espite some commentators’ fears of a race-to-the-bottom in

¹ For a detailed discussion of the state competition for corporate law and its policy implications of contractual choice-of-law, see Larry E. Ribstein & Erin Ann O’Hara, *Corporations and the Market for Law*, 2008 U. ILL. L. REV. 661 (2008).

² See, e.g., Stephen J. Choi & Andrew T. Guzman, *Portable Reciprocity: Rethinking the International Reach of Securities Regulation*, 71 S. CAL. L. REV. 903 (1998); Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L. J. 2359 (1998); Roberta Romano, *The Need for Competition in International Securities Regulation*, 2 THEORETICAL INQ. L. 387 (2001).

³ See, e.g., Merritt B. Fox, *The Securities Globalization Disclosure Debate*, 78 WASH. U. L. Q. 567 (2000); Merritt B. Fox, *Retaining Mandatory Securities Disclosure: Why Issuer Choice Is Not Investor Empowerment*, 85 VA. L. REV. 1335 (1999); Merritt B. Fox, *The Issuer Choice Debate*, 2 THEORETICAL INQ. L. 563 (2001).

⁴ Bernard S. Black, *The Legal and Institutional Preconditions for Strong Securities Markets*, 48 UCLA L. REV. 781, 843 (2001).

securities regulation, there is substantial evidence that issuers have chosen to bond their integrity by deliberately choosing regimes with more rigorous regulation.”⁵ In another word, foreign firms actually can choose to “bond” their insiders by cross-listing in the United States or other improved jurisdictions, thereby rendering themselves subject to these stricter legal rules in addition to the regulations in their home countries. Considerable evidence lends support to this bonding explanation of cross-listing.⁶ Nevertheless, with the Sarbanes-Oxley Act of 2002 (“SOX”), “full-fledged international competition is currently hobbled by the fact that the United States insists on regulating all trading within its borders regardless of where the firms are based.”⁷ In contrast to the normative debate on issuer choice, this article will in the following text seek to elaborate on a positive statement that law market forces underlying international jurisdictional competition have provoked partial exemptions and relaxation of mandatory rules in SOX as the U.S. aims at encouraging foreign issuers to raise capital there.

On the other side of the Pacific Ocean, even if Taiwan and China (hereinafter also referred to as the “PRC,”⁸ “Mainland China” or the “Mainland”) are highly economically interdependent on each other, there is some political antagonism between them.⁹ Therefore, facing its flourishing economic relationship with Mainland China since the late 1980s, Taiwan’s government is in a dilemma of whether and how to regulate the investments of the Taiwanese business community in China. But with Taiwan’s government attempting unsuccessfully to hinder further investment across the Taiwan Strait (the “Strait”), many Taiwanese corporations

⁵ Larry E. Ribstein, *Market vs. Regulatory Responses to Corporate Fraud: A Critique of the Sarbanes-Oxley Act of 2002*, 28 J. CORP. L. 1, 60 (2002) (footnote omitted).

⁶ Larry E. Ribstein, *Cross-Listing and Regulatory Competition*, REV. L. & ECON. Vol. 1, Issue 1, Art. 7, 97, 104, 112 (2005), available at <http://www.bepress.com/rle/vol1/iss1/art7>.

⁷ HENRY N. BUTLER & LARRY E. RIBSTEIN, *THE SARBANES-OXLEY DEBACLE: WHAT WE’VE LEARNED; HOW TO FIX IT* 35 (2006).

⁸ The People’s Republic of China is commonly known as China.

⁹ Chien-Min Chao, *Will Economic Integration between Mainland China and Taiwan Lead to a Congenial Political Culture?*, 43 ASIAN SURV. 280, 280 (2003).

have weaved their ways through these bans in order to hand over needed funds to their affiliates or subsidiaries in Mainland China. This Taiwan phenomenon seems also to exemplify international jurisdictional competition among global legal centers, pointing especially to Hong Kong and other Offshore Financial Centers (“OFC”s) in British Central America (e.g. the Cayman Islands). In effect much evidence to date reveals that this jurisdictional competition provoked by Taiwanese companies’ exit to elude the investment restrictions prompts substantial ease of capital limits placed by Taiwan’s government.

More importantly, this article is different from others concerning regulatory competition on the international dimension in that drawing lessons from the negative impact of SOX on the U.S. cross-listing market, this article takes the Taiwan phenomenon as another case study to further test how basic law market demand and supply forces (or underlying exit and voice rights) interplay under international jurisdictional competition. This article would first draw a positive lesson from the SOX story that law market forces underlying jurisdictional competition would constrain a regulating jurisdiction from disregarding business demands and from imposing excessive regulation, and then apply this implication to prove the positive thesis that in the Taiwan case the output of these market interactions underlying international jurisdictional competition among global legal centers is that Taiwan’s excessive regulation on outward investment in Mainland China (“China-Investment”) is nudged in the direction of relaxation.

As for the structure of this article, Section II first discusses underlying factors spurring the law market in a global setting. The increase of international factor mobility brought about by globalization lowers firms’ exit costs and then intensifies the international jurisdictional competition for mobile resources. Out-flowing capital and emigrating labor would then compel

regulatory jurisdictions to improve on the quality of their regulations. In other words, the international movement of production factors, delivered through domestic interest groups to political policy makers within a regulating jurisdiction, could galvanize the liberalization of excessive regulation. Section II then draws an implication from the SOX story that constraints on over-stringent SOX to foreign issuers would be imposed by international jurisdictional competition among global cross-listing markets fuelled by capital mobility. Specifically, SOX impacted non-U.S. firms so negatively that many foreign issuers were driven to list shares in other comparable markets, such as the London Stock Exchange (“LSE”). Foreign firms’ mobility fed the demand side of this law market, which subsequently spurred the supply side within the United States. Therefore, the U.S. responded to criticisms from German and other foreign companies by issuing rules that partially exempt foreign firms from some SOX requirements.

Section III further apply lessons as discussed above to illustrate the jurisdictional competition among global legal centers in which the above OFCs participated by elaborating on the law market for listings in the Greater Chinese Economy¹⁰ mainly led by Hong Kong Stock Exchange (“HKSE”) as a competitor against Taiwan. In concrete terms, Section III.A “The Demand Side of the Law Market” introduces the historical background and legal structures of the upper limits on outward investment in Mainland China (the “Capital Controls”) and related

¹⁰ Kevin Zhang points out:

In the two decades since 1979, China, Taiwan, and Hong Kong have become one integrated economic region, driving the dramatic growth of investment, production, and trade in East Asia. Often referred to as “the Greater Chinese Economy,” this region represents in certain respects the triumph of economics over politics, in the sense that the three very different political entities have today become an economic trading, investing, and producing region, despite political and military conflict and long-standing, deep-seated suspicion and mistrust. FDI has been the engine driving these three entities into an increasingly intimate relationship.

Kevin H. Zhang, *China’s Inward FDI Boom and the Greater Chinese Economy*, in FINANCIAL MARKETS AND FOREIGN DIRECT INVESTMENT IN GREATER CHINA 165, 165 (Hung-gay Fung & Kevin H. Zhang eds., 2002) (citation omitted).

constraints on use of capital raised in Taiwanese stock markets towards investment in China (the “Constraints”) (the above two restrictions altogether hereinafter also referred to as the “Restrictions”). The Restrictions, on the one hand, ignore trends of economic globalization and concomitant business demands for increasing investments in Mainland China. On the other hand, the predicament of enforcing the Restrictions brings to light the core problem of the Restrictions—even if a jurisdiction acts with strong intentions to regulate economic transactions beyond its borders, it would be restrained from doing so as globalization weakens its regulatory capacity. In order to raise capital allowed to be used for investments in China, fugitive Taiwanese firms cannot but circumvent the Restrictions through common evasive tactics to list shares overseas.

This fact is further corroborated in Section III.B “The Supply Side of the Law Market” that these Taiwanese firms spurn exchanges at home and choose to go public in other stock markets in the Greater Chinese Economy, not least Hong Kong, not primarily in order to opt into the laws thereof and to bond their insiders given the “bonding” effect, but rather mainly to “avoid” the Restrictions. In turn these Taiwanese firms’ physical exits and threats of exit motivate anti-regulatory and exit-affected interest groups in Taiwan to action. Subsequent to political competition with pro-regulatory interest groups, anti-regulatory interest groups combined with exit-affected ones successfully voiced their petition for legal flexibility especially through a critical political process in 2008—the presidential election in March. President Ma of the Nationalists (“Kuomintang” or “KMT,” which is the current ruling party in Taiwan whereas Democratic Progressive Party (“DPP”) was the former ruling party before the 2008 presidential election), advocating the pro-China and anti-regulatory policy, won the presidential election. In turn the Restrictions have been largely relaxed in a timely manner.

Subsequently, Section IV compares both the U.S. and Taiwan cases and argues that while there are some differences between them, these two cases demonstrate the similar operation of law market forces underlying international jurisdictional competition. Section V concludes from both case studies that if political jurisdictions refuse to recognize business needs and respect market demand, firms have incentives and ability to seek out more cost-justified or flexible laws in other jurisdictions, and that international jurisdictional competition stimulated by business demands and fueled by firm or capital mobility would drive governments to moderate excessive regulation.

II. INTERNATIONAL JURISDICTIONAL COMPETITION UNDER GLOBALIZATION

A. The Law Market Dynamics

Building on Tiebout's theory¹¹ and Hirschman's typology¹², O'Hara and Ribstein bring up the theory of the law market:

A market for law may have significant implications for political theory. Under the traditional view of politics, people who do not like their leaders elect new ones. In other words, they exercise what Albert O. Hirschman has referred to as "voice." However, coordinating the electorate is cumbersome and costly. Moreover, the political marketplace is often dominated by interest groups that can influence politicians with money and votes to act in ways that might not serve the public interest. Voting is not the only source of political

¹¹ Charles M. Tiebout, *A Pure Theory of Local Expenditures*, 64 J. POL. ECON. 416 (1956) (suggesting that different state governments compete with each other in the supply of public goods to consumers who on their side can choose between the public goods offered according to their preferences). The genesis of the jurisdictional competition theory can trace back to this article.

¹² Albert Hirschman argues that as members of a society such as a corporation or a country find that the quality of or the benefit provided by the human group is going down, they are fundamentally armed with two ways to respond: they might exit (break off the relation); or, they might voice (make an effort to mend or restore the relation by lodging their complaints or proposing some change). *See generally* ALBERT O. HIRSCHMAN, *EXIT, VOICE, AND LOYALTY: RESPONSES TO DECLINE IN FIRMS, ORGANIZATIONS, AND STATES* (1970).

power. People can choose the applicable law by deciding where to live—part of what Hirschman called “exit.” . . . Tiebout explicitly recognized a kind of consumer market in governments. There is no reason in principle this market would not embrace laws which, after all, are an important type of government-provided goods.¹³

As O’Hara and Ribstein further argue, the law market is referred to as the process in which “governing laws can be chosen by people and firms rather than mandated by states. This choice is created by the mobility of at least some people, firms, and assets and the incentives of at least some states to compete for people, firms, and their assets by creating desired laws.”¹⁴ The term “Market” here does not indicate “particular sets of idealized conditions of exchange, but rather simply to buyers demanding a commodity (law) and sellers being willing to provide it for a benefit;” this type of exchange is contrasted with “the view that law is decreed by government and forced on parties subject to its jurisdiction.”¹⁵ As for the demand or “buyer” side of the market, “parties ‘shopping’ for law have created their own market by using several mechanisms such as exit options for avoiding costly regulation.”¹⁶ As for the supply or “seller” side of the market, shopping generates incentives for some interest groups to favor contracting or legal flexibility (anti-regulatory interest groups), and thus to oppose those that prefer regulation (pro-regulatory interest groups). The interest group competition “involves not only the groups directly affected by the regulation, but also exit-affected interest groups, which have a stake in the parties’ decisions whether to locate, invest, or litigate in the state.”¹⁷ In a word, the basic law market demand and supply forces specify the operations of this market.¹⁸

¹³ ERIN A. O’HARA & LARRY E. RIBSTEIN, *THE LAW MARKET* 13-14 (2009).

¹⁴ *Id.* at 65.

¹⁵ *Id.* at 66.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.* at 121.

B. Law Market Forces Underlying International Jurisdictional Competition

In general, “[t]he reduction in barriers to trade and the liberalization of financial markets, transportation and telecommunications have created the basis for the increase in flows of factors of production between jurisdictions.”¹⁹ The above phenomenon is “globalization,” which is essentially “the phenomenon of increased international factor mobility.”²⁰ Kasper further argues that “government administration is a production factor, since good government is an ingredient in production, raises the productivity of all the other production factors, and enhances a country’s attractiveness to mobile production factors.”²¹ Moreover, Geradin and McCahery also find:

As countries move to a more liberalized domestic economy, questions of competition between jurisdictions abound. With the prospect of increased capital mobility, it is becoming conventional wisdom that national governments are forced to perform their economic policy functions more efficiently since governments that yield optimal levels of public goods may be more successful in the competition between jurisdictions for attracting mobile resources. The concern to attract mobile resources has shaped entire areas of governmental policy and plays a determinative role for firms locating new plants.²²

Since national laws and institutions are an important type of government-provided goods, globalization has galvanized international jurisdictional competition, by offering better laws and institutions, for mobile production factors as well.

Furthermore, globalization, or the worldwide intensified movement of capital, know-how

¹⁹ Damien Geradin & Joseph A. McCahery, *Regulatory Co-opetition: Transcending the Regulatory Competition Debate* 1 (Amsterdam Center for Law & Econ. Working Paper No. 2005-06, 2005), available at <http://ssrn.com/abstract=821087> (citation omitted).

²⁰ WOLFGANG KASPER, GLOBAL COMPETITION, INSTITUTIONS, AND THE EAST-ASIAN ASCENDANCY 4 (1994).

²¹ *Id.* at 11. In the second half of the 20th century, “[i]ncreasingly, local and national institutions are becoming a key cost factor that determines what is produced where—not surprisingly, because coordination costs account often for half of all costs and because these are greatly influenced by prevailing institutions.” WOLFGANG KASPER & MANFRED E. STREIT, INSTITUTIONAL ECONOMICS: SOCIAL ORDER AND PUBLIC POLICY 345 (1998).

²² Geradin & McCahery, *supra* note 19, at 1.

and firms across national borders, strengthens the exit option for the subjects of national jurisdictions. This phenomenon “weakens the power of governments. . . . It is therefore useful to constrain the scope for opportunistic national interventions in international exchanges.”²³ For example, as Andrews argues, “the degree of international capital mobility systematically constrains state behavior by rewarding some actions and punishing others.”²⁴

Following the insight of the law market as well as the dissection of globalization and jurisdictional competition, we can realize how law market forces are working in international jurisdictional competition. First of all, since globalization lowers exit costs across borders and enhances firm and capital mobility, globalization leads to international jurisdictional competition for worldwide mobile factors of production by offering better laws and institutions. We in turn come to the interactions between the economic process in the international environment and the political process within a jurisdiction when this jurisdiction engages in jurisdictional competition through changes in the provision of laws and institutions. Let’s suppose that the jurisdiction propose an excessive law favored by pro-regulatory interest groups, which create firms’ demand for legal flexibility and their incentive to leave. In the international economic process, firms, as “economic agents,” have some ability to manipulate jurisdictional choice. That is to say, this mobility, in the first place, can feed the demand side of the law market which firms’ exit rights underlie, and then spark competition for the supply of law by other jurisdictions. Exit and entry by firms seeking to avoid regulation creates costs and benefits for other interest groups in the jurisdiction. This mobility can thus activate the domestic interest group competition on the supply side. In particular, the exit or mobility may provide an indirect voice to outsiders and a

²³ KASPER & STREIT, *supra* note 21, at 342. *See also id.* at 381.

²⁴ David M. Andrews, *Capital Mobility and State Autonomy: Toward a Structural Theory of International Monetary Relations*, 38 INT’L STUD. Q. 193, 193 (1994). *See also id.* at 194, 197.

stronger voice to insiders who will be burdened by the proposed law.

In the domestical political process, these “exit-affected” interest groups join with the groups that are directly burdened by the regulation to promote legal flexibility even if the latter anti-regulatory groups could not alone defeat the regulation proposed by the pro-regulatory interest groups. This in turn pressures politicians or lawmakers within the regulating jurisdiction, as “political agents,” to appreciate the significance of the economic exit signals, to discover that they need to supply laws and institutions which constitute “an attractive locational factor,”²⁵ and to enable the relaxation of the excessive law. Hence, where regulation might be excessive, the jurisdictional competition could push the regulating jurisdiction to improve the substantive content of local laws.²⁶ What’s more, “[l]egal changes would be provoked by firms’ increasing need for legal flexibility.”²⁷ In other words, as Prof. Ribstein argues, “the mobility of firms, people and money across borders, transmitted through interest groups to political decision-makers, can produce long-run legal changes.”²⁸ That is, the feedback mechanisms, options of exit (choice of location) and voice (political action), might be translated into the regulatory evolution, or the liberalization of excessive regulation.

C. International Jurisdictional Competition in Securities Regulation: The Case of the Sarbanes-Oxley Act of 2002

To begin with, “the past two decades have witnessed the large-scale process of internationalization. . . . The U.S. loosened disclosure regulation for foreign issuers throughout the period of internationalization to maintain a competitive advantage in attracting participants

²⁵ KASPER & STREIT, *supra* note 21, at 403.

²⁶ See O’HARA & RIBSTEIN, *supra* note 13, at 191, 199.

²⁷ *Id.* at 110.

²⁸ Ribstein, *supra* note 6, at 99.

from the emerging markets.”²⁹ After corporate catastrophes like Enron’s, Congress wrote SOX to strengthen the scope of federal regulation from disclosure to corporate internal governance while SOX was applied to domestic issuers and non-U.S. issuers, otherwise known as foreign private issuers (“FPI”s), equally. Prof. Ribstein, however, notes:

[R]egulation may be perverse because markets do not always react to regulation the way regulators predict they will. For example, rather than pursuing the same activities more carefully, regulated parties may simply switch to safer activities that are less likely to lead to the sort of bad outcomes that attract regulatory scrutiny. A specific example of how markets can react to regulation concerns the risk that a party will simply move out of reach. Though federal regulation like SOX is harder for firms to avoid than state law, even the federal securities laws have limited reach. While it is unlikely that U.S.-based firms will move their activities offshore, stricter U.S. law might keep non-U.S.-based firms out of U.S. markets.³⁰

Consequently, in order to attract back or retain non-U.S. issuers in the U.S. stock markets, the U.S. government released exemptions for FPIs from excessive regulation in SOX. SOX’s effect on the cross-listing market not only suggests that the higher costs of regulation within jurisdictions are imposed on firms, domestic or foreign, the more likely firms exit and flee to where regulation is more flexible, but also illustrates the competitive constraints on federal law.³¹

Moreover, the negative effect of SOX on FPIs has triggered a political dynamic that may have far-reaching consequences. In the beginning, “[a]voidance by non-U.S. firms of the U.S.

²⁹ Erin Marks, *The Sarbanes-Oxley Act: Costs and Trade offs Relating to International Application and Convergence*, 17 RES. ACCT. REG. 233, 254 (2004).

³⁰ Larry E. Ribstein, *Sarbox: The Road to Nirvana*, 2004 MICH. ST. L. REV. 279, 292 (2004).

³¹ Chang-Hsien Tsai, *Law Market Forces Underlying International Jurisdictional Competition: The Case of Taiwan’s Regulatory Evolution on Outward Investment in Mainland China, 1997-2008* (forthcoming May 2010) (unpublished J.S.D. dissertation, University of Illinois) (manuscript at 54-58, on file with author) (discussing how the SEC, given physical exit and threats of exit by FPIs as well as voice for liberalization by interest groups related to FPIs, allowed accommodation of home country regulations that would create an audit committee equivalent in independence to that envisaged under the U.S. rules, and arguing that naturally, it was the international jurisdictional competition activated by FPIs’ exiting from U.S. stock markets that pushed the SEC to adopt a more flexible regime).

market may reduce U.S. investors' ability to diversify their portfolios. . . . [T]his avoidance may reduce the revenues of US securities firms [as well as other exit-affected parties], thereby provoking these firms to lobby for reducing the regulatory burden on cross-listing firms.”³² Thereafter, the U.S. responded to criticisms from German companies and other groups by issuing rules that partially exempt foreign firms from some SOX requirements. Perhaps more importantly, as Butler and Ribstein discuss,

[t]hese rules raise the question of how far the SEC can go in exempting foreign firms before triggering significant complaints from their U.S. competitors in the U.S. capital markets. The exemptions undoubtedly are attributable to some extent to the fact that foreign firms are much better able to exit [from] the U.S. market than U.S.-based firms. The latter may be subject to U.S. laws even if they trade overseas, and they have other business reasons for needing to trade in the United States. To the extent the exemptions are, or should be, based on the costs of compliance, they arguably should apply to any firm that is incorporated under and must comply with the corporate law of another country, regardless of where the corporation's operations are based. But any such exemption would invite U.S. firms to avoid U.S. law by incorporating elsewhere. To the extent that such competition forces U.S. regulators and legislators to reassess the damage they have done to American securities markets, such exits by U.S. firms could ultimately help correct the SOX mistake.³³

In other words, the SEC will face pressure from U.S.-based firms, who would use their “greater” voice in the U.S. political marketplace to lobby for exemptions similar to those granted to FPIs,

³² Larry E. Ribstein, *International Implications of Sarbanes-Oxley: Raising the Rent of US Law*, 3 J. CORP. L. STUD. 299, 323 (2003) (footnote omitted) (alteration in original).

³³ BUTLER & RIBSTEIN, *supra* note 7, at 74 (alteration in original).

to extend benefits of foreign exemptions to domestic firms.³⁴ In fact, “in the wake of [SOX], many of the reforms passed to [foreign] issuers have been ultimately shared by U.S.-domiciled companies or are in the process of being considered for extension to U.S. companies.”³⁵ That is, exit could lead to general deregulation.³⁶

In general, the phenomenon of SOX and the global cross-listing market discussed above demonstrates some dimensions of the law market:

First, it shows how even what would seem to be the most mandatory laws must compete in the law market given the increasingly global nature of competition. This competition can increase the level and quality of regulation, as shown by the rise of cross-listing firms. Second, SOX’s aftermath indicates that regulated firms may exit in the face of increased regulatory costs. Third, this history shows how the financial impact of exit on interest groups in regulating countries ultimately can cause states to make changes in their laws that reduce regulatory costs. Although these changes may be provoked by the most mobile firms, they have the potential of reducing costs for all firms, including those that have higher costs of exit.³⁷

In conclusion, in this law market for cross-listings we see “the usual law market forces could work for securities regulation, just as U.S. states ultimately came to apply the [Internal Affairs Doctrine] to tramp corporations.”³⁸ On the buy side of this law market, “regulation and

³⁴ See Ribstein, *supra* note 6, at 130-39. See also Donald C. Langevoort, *The SEC, Retail Investors, and the Institutionalization of the Securities Markets*, 95 VA. L. REV. 1025, 1077 (2009).

³⁵ Chris Brummer, *Corporate Law Preemption in an Age of Global Capital Markets*, 81 S. CAL. L. REV. 1067, 1105 (2008) (alteration in original).

³⁶ Ribstein, *supra* note 32, at 325-26.

³⁷ O’HARA & RIBSTEIN, *supra* note 13, at 31.

³⁸ *Id.* at 124 (footnote omitted).

non-enforcement of contractual choice of law create an incentive to leave,” and on the sell side “exit activates local industries that depend on the exiting firms; “[t]his, in turn, pressures politicians to enable jurisdictional choice, sometimes even for immobile locals.”³⁹ In other words, feedbacks of exit and voice rights are translated into the regulatory evolution, or for the SEC to moderate the over-burdensome regulation imposed by SOX. This SOX case thus implies not merely that “the elements of the law market story apply in the international context,”⁴⁰ but also that law market forces underlying international jurisdictional competition would provoke a change in excessive regulation to a more flexible regime.⁴¹

III. JURISDICTIONAL COMPETITION AMONG LISTING MARKETS IN THE GREATER CHINESE ECONOMY: HONG KONG AS AN EXAMPLE OF COMPETITORS AGAINST TAIWAN

General law market forces are also at work in the law market for listings in the Greater Chinese Economy as in the law market for cross-listings explained above. In concrete terms, on the demand side, the Restrictions create incentives of China-based Taiwanese businesses to exit from Taiwan stock markets and their demands to find a regulatory product of securities regulation without being subject to the Restrictions. On the international supply side, neighboring stock markets in the Greater Chinese Economy, not least HKSE, supply this product

³⁹ Ribstein & O’Hara, *supra* note 1, at 711-12.

⁴⁰ *Id.* at 712.

⁴¹ Alan Dignam and Michael Galanis also seem to confirm this conclusion:

One can further observe the continuing importance of macroeconomic pressures in the problems that the NYSE has had since the introduction of [SOX] in response to the Enron and WorldCom scandals. In a continuation of the regulatory competition created by capital mobility . . . since 2002 the NYSE has been losing out to the LSE for new listings because of the onerous nature of SOX. Because of capital mobility, companies around the world, including US companies, can simply choose to avoid the US regulatory regime when raising capital. As a result, the SEC in May 2007 produced new guidance on interpreting the most contentious aspects of SOX, with the intention of making it less burdensome.

Alan J. Dignam & Michael Galanis, *Corporate Governance and the Importance of Macroeconomic Context*, 28 OXFORD J. LEGAL STUD. 201, 242 (2008), available at <http://ssrn.com/abstract=1154412> (alteration in original) (footnote omitted).

of legal flexibility. On the domestical supply side, a torrent of physical exit by these fugitive companies activates local industries and interest groups that depend on the exiting firms. Subsequent to interest group competitions over whether or how to relax the related restrictions, anti-regulatory and exit-affected interest groups successfully voice their petition for liberalization. Therefore, the jurisdictional competition among listing markets in the Greater Chinese Economy, through Taiwanese firms' exit and voice, pressures politicians in Taiwan to satisfy business demands for legal flexibility, or to loosen the relevant bans on outwardly investing in Mainland China.

A. The Demand Side of the Law Market

1. The Restrictions on Outward Investment in Mainland China

1.1 The Background of the Capital Controls

Historically, since China started opening up during the 1980s, Taiwan-invested firms have been one of the first companies which invested a lot on the Mainland and have already made a fortune. As Bradsher reported in 2007, “[e]stimates of total Taiwan holdings on the mainland run as high as \$280 billion.”⁴² Taiwan’s local economy has in some sense benefited from China-investment in the past few years. Why have Taiwanese firms been increasingly investing in China during these years? A higher degree of political antagonism existed between Taiwan and China prior to 1979. There were all but no business connections between them. In 1979, however, the fact that China changed its mind from liberating Taiwan to calling for peaceful unification

⁴² Keith Bradsher, *Investors Look to Taiwan in Hopes of Cashing In on China Boom*, N.Y. TIMES, Oct. 20, 2007, available at <http://www.nytimes.com/2007/10/20/business/worldbusiness/20exchange.html?fta=y>.

made an important change. As Taiwan suddenly allowed its citizens to visit their relatives on the Mainland in October 1987, cross-Strait economic relations were further developed. More importantly, representatives of China's Association for Relations Across the Taiwan Strait ("ARATS") and Taiwan's Straits Exchange Foundation ("SEF") in April 1993 had a historic meeting in Singapore. In this meeting, "[a]lthough characterized as unofficial, both delegations were headed by former high level officials tied to the top leadership in each capital."⁴³

What follows summarizes what drove cross-Strait trade and investments from Taiwan to China to turn out to be a torrent. First of all, Taiwan's democratization drive was also responsible for this trend. Second, the financial liberalization followed substantial appreciation of the New Taiwan ("NT") dollar resulting from the Plaza Accord. The NT dollar's value increased, thus making manufacturing in Taiwan less competitive and lessening Taiwanese exporters' profits. Taiwanese firms, to remain internationally competitive, started to make large investments on the Mainland, which attracted much of the manufacturing and exporting activities originally based in Taiwan. Another crucial factor was the decrease of cross-Strait political tension as shown above. In addition, the justification for Taiwanese investment mainly rests on comparative advantages as well as economic complementarities. Taiwan's plentiful funds and improved technology match China's abundant natural resources and low production cost almost perfectly. These comparative advantages, combined with cultural and linguistic similarities as well as geographic closeness, primarily contribute to capital flow from Taiwan to China. Last but not least, Taiwanese firms would lose the market to rivals like South Korea, if not for relocating their factories to China.⁴⁴

Even though cross-Strait economic interactions have turned really intense, officials of

⁴³ Ping Deng, *Taiwan's Restriction of Investment in China in the 1990s: A Relative Gains Approach*, 40 ASIAN SURV. 958, 962 (2000).

⁴⁴ *Id.* at 962-64.

Taiwan's government kept struggling to impede the fast development of business connections. In September 1996, President Teng-Hui Lee stressed a "No Haste, Be Patient" investment policy (the "NHBP" policy) while requiring Taiwanese firms to brake their rapid expansion of Mainland operations. He emphasized that Taiwan would become susceptible to Chinese political pressure with greater cross-Strait economic interdependence. The Council for Economic Planning and Development ("CEPD"), the official think tank of Taiwan's government, at the same time withdrew a suggestion to lighten restrictions on China-investment.⁴⁵ The following July, the Ministry of Economic Affairs ("MOEA") released its revised Principles Governing the Review of Investment or Technical Cooperation in Mainland China (the "Principles"). What should be noted is that the cap amount of investment is specified in Article 3 of the Principles, which is enacted under the authorization by Paragraph 1 of Article 35 of the Act Governing Relations between Peoples of the Taiwan Area and the Mainland Area (the "Act"). The intention of the Principles was to protect Taiwan's economic growth and national security. The Principles broadened the scope of prohibited investments, prohibited major infrastructure projects, confined single-project investments in China to \$50 million, and imposed a general system to limit Taiwanese firms' investments in the PRC according to their overall financial exposure and ownership structure (the "Capital Controls").⁴⁶

1.2 The Legal Basis of the Constraints

Although Taiwan has turned to large-scale deregulation⁴⁷ since President Ma of KMT

⁴⁵ *Id.* at 965-66.

⁴⁶ See Fu-Lung Lee, *Tai Shang Zai Da Lu Shang Shi De Zheng Ce Yu Fa Lü Ji Qi Yin Ying Zhi Dao* [On Policy, Law and Suggestion of Taiwanese Enterprise to Go Public in the Mainland Area], 34 TAI WAN DA XUE FA XUE LUN CONG [NTU L. J.] 277, 279-80 (2005) (Taiwan).

⁴⁷ See, e.g., Shu-Fang Huang, *Deng Lu Tou Zi Shang Xian Fang Kuan Zhi Bai Fen Zhi Liu Shi Zong Bu Zai Tai Zhe Bu She Xian* [The Capital Cap on Investment in China Is Relaxed to 60 % while No Cap Is Applied if Administrative Centers Established], ZHONG YANG SHE JI SHI XIN WEN [CENTRAL NEWS AGENCY NEWS], July 15, 2008, <http://news.msn.com.tw/print.aspx?id=862620> (last visited July 15, 2008); Yi-Feng Lin & Gui-Xiang Wen, *Zong*

won the presidential election in March 2008, prior to this notable legal change MOEA maintained the Capital Controls that the total dollar amount of direct and indirect investment in Mainland China cannot exceed the upper limits, generally 40% of a Taiwanese firm's net worth. In order to thoroughly implement the Capital Controls, Taiwan's government further imposed several constraints through administrative regulations to restrain Taiwanese and even foreign issuers from investing funds raised in Taiwan stock markets outwardly in Mainland China (the "Constraints"). First, according to Article 7 of Regulations Governing the Offering and Issuance of Securities by Securities Issuers, Taiwanese issuers were not allowed to directly or indirectly invest any capital raised in Taiwan stock markets in Mainland China. Second, the predecessor organization of the Financial Supervisory Commission ("FSC") in Taiwan, equivalent to the SEC in the U.S., also released an administrative regulation to prohibit public Taiwanese companies from investing capital raised through private placements, no matter in Taiwan or overseas, in Mainland China.⁴⁸ Third, Article 9 of Regulations Governing the Offering and Issuance of Overseas Securities provided that the fund raised from the issuance of securities in overseas stock markets was not allowed to be used for direct or indirect investments in Mainland China beyond the upper limit, 20-40% of the amount of the fund raised in each offering. Fourth, Regulations Governing the Offering and Issuance of Securities by Foreign Securities Issuers stipulated that neither could funds raised in Taiwan stock markets by foreign issuers be used for investments in Mainland China.

Tong Hui Wu Liu Kui Qiao Ding Deng Lu Tou Zi Shang Xian Song Bang [President Met Premier and Decided the Relaxation of the Capital Cap], ZHONG YANG SHE JI SHI XIN WEN [CENTRAL NEWS AGENCY NEWS], July 14, 2008, <http://news.msn.com.tw/print.aspx?id=862618> (last visited July 15, 2008).

⁴⁸ Order of Securities and Futures Commission, Ministry of Finance, Executive Yuan, Tai-Cai-Zheng-Yi Zi No. 09100168912 (passed Jan. 17, 2003). See also *Shang Shi Gong Si Si Mu Zi Jin Ke Yi Tou Zi Lu Gu Shang Xian Bai Fen Zhi Liu Shi* [Listing Corporations Can Invest Up to 60% of Capital Raised through Each Private Placement in Buying Chinese Stocks], FA YUAN FA LÜ XIN WEN [LAWBANK'S L. NEWS] (Taiwan), Oct. 9, 2008, <http://www.lawbank.com.tw/fnews/pnews.php?nid=64123.00> (hereinafter *Placements*) (last visited Oct. 9, 2008).

In addition, it should be noted that foreign issuers in Taiwan may be classified into two groups: one group, having not listed their shares on any other stock exchanges abroad, applies for listing shares in Taiwan stock markets (“Primary Listing Issuers”) while the other group, with securities being traded on stock exchanges abroad, applies for the listing of Taiwan Deposit Receipts (“TDR”)s in Taiwan stock markets (“Secondary Listing Issuers,” the equivalent of cross-listing issuers in the U.S. stock markets).

2. Problems of the Restrictions: Strong Intention but Weak Capability of Enforcement

2.1 Ignoring Economic Globalization and Business Demands

The Restrictions apparently ignore Taiwanese firms’ business demands created by economic globalization. Cross-Strait economic relations may have been treated as an issue of excessive politicization, with little economic reasoning, for policy making in Taiwan. From the perspective of economic statecraft⁴⁹ favored by the pro-regulatory interest groups, Taiwanese investment in Mainland China has a negative impact on Taiwan’s economic development; the primary one is the emptying out of Taiwan’s labor intensive industries as well as the flowing away of Taiwan’s industrial competitiveness to China. Taiwanese Direct Investment (“TDI”) in China “may increase Taiwan’s vulnerability and sensibility to the Mainland’s ‘economic warfare’.”⁵⁰ Put differently, “the main reasons behind Taiwan’s tough economic regulations are concerns over

⁴⁹ No matter in which form the economic regulation is imposed, economic statecraft is *per se* a kind of intervention in the law of comparative advantage of international economics and trade. That is, in order to reach expected political goals, the power of a state is wielded against market mechanisms. Tse-Kang Leng, *Cong Mei Guo Dui Nan Fei De Jing Mao Guan Zhi Tan Tao Wo Dui Da Lu De Jing Mao Zheng Ce* [Research on Taiwan’s Policy on Economic Relations with Mainland China in Light of U.S. Economic Regulation on South Africa], 41 ZHONG GUO DALU YAN JIU [MAINLAND CHINA STUDIES] 17, 17 (1998) (Taiwan).

⁵⁰ Tse-Kang Leng, *Securing Economic Relations Across the Taiwan Straits: New Challenges and Opportunities*, 11 J. CONTEMP. CHINA, 261, 262 (2002).

national security—that is, worries that China could use its economic power to make Taiwanese businessmen in China further the [PRC’s] policy aims.”⁵¹ Nonetheless, it is a natural trend of economic globalization that accounts for the gradual growth of investment by Taiwanese companies on the Mainland:⁵²

Growing Taiwanese Investment in the PRC and intensified trade across the Strait is [sic] part of larger East Asian and global economic trends. East Asian firms became increasingly tied to the dynamism of China in the 1990s. In its May 2001 *White Paper on Trade*, Japan’s Ministry of Economic Trade and Industry analyzed how China emerged as the center of growth in East Asia. China’s share of East Asian GDP grew from 25% in 1980 to 37% in 1999. This phenomenon was driven in large part by two key trends: PRC liberalization of tariffs and investment opportunities and a large influx of FDI. Competition intensified significantly in East Asia in the 1990s with the quadrupling of FDI into the region, further liberalization of trade and investment barriers, and the subsequent cross-border specialization occurring in the region as evidenced by the rapid growth in the trade of intermediate goods.⁵³

Accordingly, as Sutter further argues, “Taiwan’s growing commercial ties to China’s economy are part of a larger globalization trend that ultimately puts cross-Strait relations into a much larger scheme of regional and global economic interdependence.”⁵⁴ In a word, TDI in China “is a part of the global division of labor.”⁵⁵ Obviously, the phenomenon of economic globalization—the removal of barriers to free trade and the closer integration of national economies—plays a central role in why Taiwanese firms have massive business demands for increasingly investing in Mainland China.

⁵¹ Tain-Jy Chen & C.Y. Cyrus Chu, *Cross-Strait Economic Relations: Can They Ameliorate the Political Problem?*, in *TAIWAN’S PRESIDENTIAL POLITICS: DEMOCRATIZATION AND CROSS-STRAIT RELATIONS IN THE TWENTY-FIRST CENTURY* 215, 221 (Muthiah Aligappa ed., 2001) (alteration in original).

⁵² YAN-ZHI ZHU, LIANG AN JING MAO [CROSS-STRAIT ECONOMIC AND TRADE RELATIONSHIP] 31 (2006) (Taiwan).

⁵³ Karen M. Sutter, *Business Dynamism across the Taiwan Strait: The Implications for Cross-Strait Relations*, 42 *ASIAN SURV.* 522, 527 (2002) (footnote omitted).

⁵⁴ *Id.* at 534.

⁵⁵ Chen-Yuan Tung, *The Impact on Taiwan*, in *THE GLOBALIZATION OF THE CHINESE ECONOMY* 190, 201 (Shang-Jin Wei, Guanzhong James Wen & Huizhong Zhou eds., 2002).

To be concrete, first of all, as Stiglitz puts it, globalization can be understood as “the closer integration of countries and peoples of the world which has been brought about by the enormous reduction in the costs of transportation and communication, and the breaking down of artificial barriers to the flow of goods, services, capital, knowledge, and (to a lesser extent) people across borders.”⁵⁶ When it comes to globalization at work across the Strait, for instance, “exchange of human capital is the most intimate form of international commerce, and, despite political differences, economic globalization has added this dimension to cross-Strait relations.”⁵⁷ Discussing the causes and process of the mobility of advanced talent between Taiwan and China, as well as its impact on cross-Strait relations, Tse-Kang Leng argues that “[e]conomic globalization, demonstrated by new waves of Taiwanese investment and the formation of global Information Technology (IT) production networks with the U.S., is the major impetus behind talent flows between Taiwan and China,” that “cross-Strait talent interaction is boosted by Taiwanese investment in China’s metropolitan areas such as Shanghai and by financial instruments such as [venture capital],” and that “human capital flows across the Taiwan Strait are facilitated by the networking of production through international channels, especially through high-tech centers located in the U.S.”⁵⁸

Second, Chang & Goldstein note that “cross-Strait trade and investment were intimately linked,” that “[u]nderlying the dramatic growth of trade in the [period as early as prior to China’s and Taiwan’s accession to the WTO in 2002] was a related, and equally significant, evolving cross-Strait division of labor,” and that this international specialization “was driven by a parallel

⁵⁶ JOSEPH E. STIGLITZ, GLOBALIZATION AND ITS DISCONTENTS 9 (2002).

⁵⁷ Tse-Kang Leng, *Economic Globalization and IT Talent Flows across the Taiwan Strait: The Taipei/Shanghai/Silicon Valley Triangle*, 42 ASIAN SURV. 230, 230 (2002).

⁵⁸ *Id.* at 231 (alteration in original).

and similarly-rapid growth of investment by Taiwanese companies on the mainland, which began in the late 1980s.”⁵⁹ In addition, according to a study on TDI tendency, Taiwanese firms prefer investing in areas with similar business customs as well as cultural and linguistic affinity to Taiwan, in the sense that investment destinations with these characteristics show less investment risks (the “mental” factor). Moreover, Taiwanese firms’ international competitive edges rest on Taiwan’s networking with production through international channels (the “network” factor). These two factors contribute to Taiwanese firms’ investing in the PRC. When the international production network requests setting up bases of manufacturing in Mainland China, Taiwanese firms cannot resist this request in that if they are unable to interact well with the international production network, they will lose their position in this network.⁶⁰ For instance, many multi-national corporations (“MNC”), such as Dell Computers, outsource their manufacturing to Taiwanese firms while asking them to establish factories in the PRC given lower production costs and large consumer markets so as to directly ship products to customers in China and worldwide.⁶¹ In order to follow this international industrial specialization, Taiwanese firms have no other choice but to make large investments in China.

Third, subsequent to the entry into the WTO of both Taiwan and China, “growing business pressures and WTO commitments are converging in a way that would add pressure for . . . significant reductions in barriers to trade and investment in both the PRC and Taiwan.”⁶² The

⁵⁹ Julian Chang & Steven M. Goldstein, *Introduction: The WTO and Cross-Strait Economic Relations*, in *ECONOMIC REFORM AND CROSS-STRAIT RELATIONS: TAIWAN AND CHINA IN THE WTO* 1, 21 (Julian Chang & Steven M. Goldstein eds., 2007).

⁶⁰ Tain-Jy Chen & Yinh-Hua Ku, *Quan Qiu Hua Xia Tai Shang Dui Da Lu Tou Zi Ce Lue* [*Investment Strategies of Taiwanese Firms in China during Globalization*], in *JING JI QUAN QIU HUA YU TAI SHANG DA LU TOU ZI: CE LUE BU JU YU BI JIAO* [ECONOMIC GLOBALIZATION AND TAIWAN’S INVESTMENT STRATEGIES IN CHINA] 13, 13, 35 (Te-Sheng Chen ed., 2008) (Taiwan).

⁶¹ Xiao-Jia Qiu, *Song Bang Liang An Jing Mao Yi Li Taiwan Chan Ye Quan Qiu Bu Ju* [*Liberalizing Cross-Strait Economic Relations to Facilitate Taiwanese Enterprises’ Global Operation*], 1 *GUO JIA ZHENG CE LUN TAN* [NAT’L POL’Y F.] (ISSUE 8) 143, 143 (2001) (Taiwan).

⁶² Sutter, *supra* note 53, at 530.

gradual breaking down of trade and investment barriers means that Taiwan will and need to fit in with the international division of labor. Faced with the trend of globalization and international specialization, Taiwan is required to take into account the production resources and vast markets located in China, which drives Taiwanese firms to invest more in China.⁶³ Put differently, market incentives—economic globalization as well as China’s and Taiwan’s accession to the WTO—dominate cross-Strait economic interaction. Under economic globalization, in order to maintain their core competence, MNCs which confront more intense competition worldwide outsource other sectors not indentified as core business. This strategy results in more sophisticated international specialization. Since Mainland China has not only abundant resources such as labor and land but also a large potential domestic market, MNCs believe that China will play an increasingly important role in the international specialization. Especially after China’s entry into the WTO, MNCs will highlight China’s significance in global operation. As a result, economic globalization (in particular demonstrated by Taiwan’s removal of trade and investment barriers intended for the entry into the WTO) and market inducements offered by the accession to the WTO to engage in international division of labor have been boosting Taiwanese firms’ demands for active investment in China for the past few years.⁶⁴

In summary, under economic globalization, as Sutter points out,

[f]urther cross-Strait economic integration and specialization seem inevitable given the highly complementary nature of the economies of the PRC and Taiwan. Despite the

⁶³ See Bing-Zhong Lin, *WTO Quan Qiu Hua Yu Liang An Jing Mao Jing He* [WTO, Globalization and Cross-Strait Economic Co-opetition], 25 TAIWAN JING JI YAN JIU YUE KAN [TAIWAN ECON. RES. MONTHLY] (ISSUE 1) 64, 67 (2002) (Taiwan); also Horng-Ming Tsai & Koong-Lian Kao, *You Quan Qiu Jing Ji Zheng He Jing Yan Kan Liang An Jing Mao Hu Dong Xin Jia Gou* [The New Framework of Cross-Strait Economic Interaction in Light of the Experience in Global Economic Integration], 1 GUO JIA ZHENG CE LUN TAN [NAT’L POL’Y F.] (ISSUE 10) 39, 50 (2001) (Taiwan).

⁶⁴ See Charng Kao, *Zong Tong Da Xuan Hou Liang An Jing Mao Guan Xi Zhan Wang* [The Prospect of Cross-Strait Economic Relations after the Presidential Election], 2 ZHAN WANG YU TAN SUO [PROSPECT & EXPLORATION] (ISSUE 5) 13, 16-17 (2004) (Taiwan).

tendency to see relations as zero-sum, both the PRC and Taiwan share a convergence of economic interests. For example, both are highly dependent on an open U.S. market, especially for jointly developed PRC-Taiwan exports. A large percentage of PRC exports to the U.S. (both via the PRC directly and Hong Kong indirectly) are exported by Taiwan-invested firms. While statistically Taiwan's exports appear to depend less on the U.S. market, in fact they depend on the health and openness of the U.S. market more than ever via their investments in the PRC. Many products that the U.S. used to import directly from Taiwan are now imported indirectly via Taiwan-invested firms in the PRC.⁶⁵

In other words, in spite of the Restrictions, market forces—economic globalization and cross-Strait specialization—drive the surge of TDI in China. Taiwan's regulation of TDI in China seems incapable of thwarting the operation of market incentives. At best, the Restrictions delay or force underground TDI in China. As discussed above, Taiwanese firms do have their strong demands for investing in China and further for legal flexibility of the regulation on outward investment in China. Nonetheless, due to the Restrictions, on the one hand, Taiwan is incapable of being properly integrated into the system of international specialization. In this case, Taiwan cannot exploit its competitive advantage and might thus be trapped in a bottleneck in economic development.⁶⁶ On the other hand, as elaborated below, “the political foundation [and legitimacy] for a coherent and feasible policy [of the Restrictions] is eroding, and commercial interests are digressing from the Taiwan government's policy goals” by exit to evade the Restrictions.⁶⁷

2.2 High Enforcement Costs of the Restrictions

2.2.1 Pervasive Evasion of the Restrictions

Many Taiwan-invested firms have funneled funds to China through their affiliates or

⁶⁵ Sutter, *supra* note 53, at 538.

⁶⁶ Lin, *supra* note 63, at 70.

⁶⁷ Szu-Yin Ho & Tse-Kang Leng, *Accounting for Taiwan's Economic Policy toward China*, 13 J. CONTEMP. CHINA 733, 733 (2004) (alteration in original).

subsidiaries incorporated in third countries like the Cayman Islands in order to skirt the investment restrictions, laid down by Taiwan's government in 1997 subsequent to a wave of investment in China.⁶⁸ To be concrete, regardless these obstacles, Taiwanese capital, goods, and know-how kept flowing across the Strait, in many cases indirectly via Hong Kong. Obviously, the investment restrictions urged Taiwanese firms to incorporate overseas in Hong Kong or other OFCs in British Central America such as the Cayman Islands and the British Virgin Islands ("BVI"). As Sutter finds,

[t]o skirt equity caps, companies have formed international consortiums of several players and phased in major investments over time. Ironic situations can result: As Taiwan's Grace Semiconductor Manufacturing Co. was breaking ground on its new integrated circuit facility in the Pudong district of Shanghai in 2000, legislators in Taipei were still debating whether to ease restrictions on semiconductor investments in the PRC.⁶⁹

In sum, to evade the Restrictions, evasive tactics through international channels that Taiwanese firms employ not only turn TDI in China underground but also lead to physical exit of their operation from Taiwan.

We can observe from the illustrations below how underground outward investment in Mainland China becomes. Even in the face of stringent government regulations, TDI in China remained vibrant. Table 1 shows the disparate statistics of TDI in China. Two sets of statistics are shown: one recorded by Taiwan's government and the other by Chinese government, both on a prior approval basis. A large disparity exists between these two statistics. According to Taiwanese statistics, by June 2000 there were a total of 22,475 projects approved to invest in

⁶⁸ Chyan Yang & Shiu-Wan Hung, *Taiwan's Dilemma across the Strait: Lifting the Ban on Semiconductor Investment in China*, 43 ASIAN SURV. 681, 682 (2003).

⁶⁹ Karen M. Sutter, *WTO and the Taiwan Strait: New Considerations for Business*, 29 THE CHINA BUS. REV. 28, 29 (2002).

China and a total investment reached \$15,598 million. In the same period 44,915 investment projects were recorded in Chinese statistics while a total amount of investment arrived at \$45,758 million. This suggests that about a half of Taiwanese investment projects did not obtain the prior-approval from Taiwan's government as the law requires. In other words, about half of investments in China by Taiwanese entrepreneurs have evaded Taiwan's Capital Controls. Moreover, a tendency appeared here, showing that even if Taiwan-invested firms did register with Taiwan's government, they mostly underreported their investment amounts. For instance, the amount of investment registered by Taiwan's government is about one-third of the amount registered by Chinese government. This suggests that the investment amounts that Taiwanese firms reported to their government are also under-stated. Although some of the approved projects have never materialized, the investment figures recorded by the Chinese government are believed to be closer to the reality.⁷⁰ Why do the two statistical sources (the official data both from Taiwan and China) differ that substantially? As Hou and Zhang argue, the dominant reason for the discrepancy is that the Capital Controls placed by Taiwan's government "forced many Taiwanese investors to avoid documenting their cases to their government."⁷¹

Table 1 TDI in China

Year	Taiwan's Statistics		China's Statistics	
	Cases	Amount (\$ million)	Cases	Amount (\$ million)
1991 and before	237	174	3,446	2,783
1992	264	247	6,430	5,543
1993	1,262 (8,067) ⁷²	1,140 (2,028)	10,948	9,965

⁷⁰ Chen & Chu, *supra* note 51, at 218.

⁷¹ Jack W. Hou & Kevin H. Zhang, *Taiwan's Outward Investment in Mainland China*, in FINANCIAL MARKETS AND FOREIGN DIRECT INVESTMENT IN GREATER CHINA 182, 186 (Hung-gay Fung & Kevin H. Zhang eds., 2002).

⁷² Numbers in parentheses are investment projects recorded through make-up registration, as discussed below in Section III.A.2.2.2; they were not approved by MOEA in advance.

1994	934	962	6,247	5,395
1995	490	1,093	4,778	5,777
1996	383	1,229	3,184	5,141
1997	728 (7,997)	1,615 (2,720)	3,014	2,814
1998	641 (643)	1,519 (515)	2,970	2,982
1999	488	1,253	2,499	3,374
2000	341	1,102	1,399	1,984
Total	22,475	15,598	44,915	45,758

Source: Chen & Chu, *supra* note 51, at 219.

Note: Statistics are up to June 2000 only.

Similar to the above view, Ho and Leng note:

The huge Taiwanese exports to mainland China are driven by the investment activities of Taiwanese business people. However, a huge gap exists between official estimation and real investment value to China. According to official statistics from Taiwan's [MOEA] released in July 2002, the Taiwanese have invested 22.1 billion US dollar in China since 1992. The mainland Chinese authorities estimate that the “negotiated value” of Taiwanese investments has reached US\$59.9 billion. According to Huai-Nan Peng, Chairman of the Central Bank of Taiwan, the accumulated Taiwanese investments to China in the past decade may be around US\$104.5 billion. Peng's estimation reconfirms the huge gap existing between official data and business activities across the Taiwan Straits. In other words, the real economic dynamics across the Taiwan Straits come from autonomous actions from the business community.⁷³

We could thus conclude that “most Taiwanese investments projects on Mainland China are not screened by the Taiwan government,”⁷⁴ and that “[g]overnmental interventions from Taiwan play only a marginal role in regulating this unique economic relationship.”⁷⁵ Overall, the rampant evasion might demonstrate high enforcement costs of and the regulatory failure of the

⁷³ Ho & Leng, *supra* note 67, at 738 (alteration in original) (footnote omitted).

⁷⁴ Tse-Kang Leng, *Dynamics of Taiwan-Mainland China Economic Relations: The Role of Private Firms*, 38 ASIAN SURV. 494, 501 (1998).

⁷⁵ Ho & Leng, *supra* note 67, at 738.

Restrictions.

2.2.2 Regulatory Failure of the Restrictions

To enforce the Capital Controls, Paragraph 1 of Article 35 of the Act states: “Any individual, juristic person, organization, or other institution of the Taiwan Area *permitted by the Ministry of Economic Affairs* may make any investment or have any technology cooperation in the Mainland Area . . .(emphasis added).” According to Article 86 of the Act, any person who makes an investment or has technology cooperation in violation of the provisions of Paragraph 1 of Article 35 (i.e. without MOEA’s ex-ante approval) shall be punished with an administrative fine of not less than NT\$50,000 but not more than NT\$25 million. To clarify and identify what would be “investment in the Mainland Area” in the above provisions, MOEA reenacted the Regulations Governing the Approval of Investment or Technical Cooperation in Mainland China (the “Regulations”) on July 31, 2002. Article 4 of the Regulations stated:

For the purposes of these Regulations, the term “investment in the Mainland Area” shall denote any of the following activities by any nationals, legal entity, organization or other institution in Taiwan Area: 1. Establishing a company or business entity; 2. Increasing the capital of an existing local company or business entity; 3. Acquiring the equity of, and operating, an existing local company or business entity, but excluding the purchase of stock of a listed company; or 4. Establishing or expanding the business of a branch company or business entity. (Paragraph 1) These Regulations shall be applicable to those investments mentioned above made by any company in a third area in which any national, legal entity, organization or other institution in Taiwan Area invested while owning a controlling interest of that company.(Paragraph 2)

Given that Taiwanese parent companies are not permitted to freely shift funds located in Taiwan to satisfy their branches’ and subsidiaries’ demand in Mainland China, many Taiwanese companies or individuals would thus decide to organize a company in a third area like the

Cayman Islands while owning a controlling interest in that company, or to delegate investment on the Mainland to a company in the same third area.⁷⁶ Then those companies established or delegated would directly set up a company in Mainland China and transfer capital to that company or have that company list shares in Shenzhen or Shanghai stock market on the Mainland, or would indirectly head for stock exchanges in the neighboring areas in the Greater Chinese Economy (sometimes also encompassing Singapore)⁷⁷, HKSE mostly, so as to raise capital there which the parent company in Taiwan could freely invest in Mainland China.⁷⁸ Several cases are introduced here to exemplify how these Taiwanese companies find their investment avenues into Mainland China and how Taiwan's judicial authority treats these tactics.

The First case is Taipei Gaodeng Xingzheng Fayuan [Taipei High Admin. Ct.], 95 Su Zi No. 4266 (2006) (Taiwan). In this case, the defendant MOEA argued that the plaintiff United Microelectronics Corporation (“UMC”), founded in 1980 as Taiwan's first semiconductor company and a foundry technology leader and industry leader, by organizing a holding company in BVI (the “Holding Co.”) and through a succession of transactions between its subsidiaries, incorporated HeJian Technology (Suzhou) Ltd. (“HJTC”) in Mainland China, and that UMC then supplied HJTC with necessary skills and resources to help HJTC smoothly pass through the start-up stage, for which UMC received 15 % of the Holding Co.’s share capital in exchange.

⁷⁶ Under the two judgments made by Taiwan’s Supreme Administrative Court—Zuigao Xingzheng Fayuan [Sup. Admin. Ct.], 92 Pan Zi No. 1463 (2005) (Taiwan) and Zuigao Xingzheng Fayuan [Sup. Admin. Ct.], 95 Pan Zi No. 1065 (2006) (Taiwan)—the above two routes were held to be in violation of Article 4 of the Regulations.

⁷⁷ Mainland Affairs Council, The Executive Yuan, The Republic of China (Taiwan), http://www.mac.gov.tw/big5/rpir/2nd7_2.htm (last visited Oct. 8, 2008).

⁷⁸ During these years, more than 53 Taiwanese companies through these tactics listed on HKSE and 23 on Singapore Stock Exchange. Chin-Ho Hsieh, *Wan Dian Zai Wang Tai Wan Xin Cai Fu Zao Shan Yun Dong* [Approaching 10,000 points of Taiwan’s Bourse: Taiwan’s New Orogeny of Wealth], JIN ZHOU KAN [BUS. TODAY] (Taiwan), July 16, 2007, at 138. Additionally, some Taiwanese companies also directly incorporated in Mainland China and in turn listed on the Shenzhen Stock Exchange or the Shanghai Stock Exchange. Chong Chen [Sean Chen], *Tai Min Jin Rong He Zuo Hu Meng Qi Li* [The Financial Cooperation between Taiwan and FuJian Province, PRC Benefits Each Other], MIN ZHONG RI BAO [THE COMMONS DAILY] (Taiwan), Nov. 4, 2006, www.ettoday.com/2006/11/04/141-2011380.htm (last visited Mar. 23, 2008).

MOEA deemed that without its *ex ante* approval, UMC's above conduct was in violation of Paragraph 1 of Article 4 of the Regulations, which stipulates: "For the purposes of these Regulations, the term 'investment in the Mainland Area' shall denote any of the following activities by any nationals, legal entity, organization or other institution in Taiwan Area: 1. Establishing a company or business entity" Consequently, MOEA punished UMC with an administrative fine of NT\$5 million. UMC appealed MOEA's decision to the Taipei High Administrative Court. This court of appeals held for UMC that by relying only on documentation provided by the prosecutor indicting UMC's board chairman and other two executive employees,⁷⁹ MOEA did not meet its burden of proving that UMC did make an "investment in the Mainland Area" in violation of Paragraph 1 of Article 4 of the Regulations.

The second case is Taipei Gaodeng Xingzheng Fayuan [Taipei High Admin. Ct.], 95 Su Zi No. 3566 (2006) (Taiwan). In this case, the defendant MOEA argued that the plaintiff An-Hai Ling, a national of Taiwan, by first organizing Cando Investment Limited ("Cando") in BVI and then through Cando incorporated ARROW in Shanghai, PRC, a company specializing in manufacturing TFT-LCD, and that the plaintiff's above activities were tantamount to the term "investment in the Mainland Area" in violation of Paragraph 2 of Article 4 of the Regulations, which provides: "These Regulations shall be applicable to those investments mentioned above

⁷⁹ See also Taiwan HsinChu Difang Fayuan [Taiwan HsinChu Dist. Ct.], 95 Zhu Su Zi No. 1 (2006) (Taiwan). In this criminal judgment, the district court held that the three defendants, who were the executive management of UMC, were not guilty owing to lack of evidence that HJTC was given human capital, customer base, management skills and trade secrets by UMC. Taiwan's high-tech industry indicated that this case made salient illegitimacy of the government's re-tightening the Capital Controls announced in the beginning of 2006. See, e.g., *Lian Dian Sheng Su Zhu Ke Ye Jie Ren Dui Chan Ye Da Lu Zheng Ce Ju Zhi Biao Zuo Yong* [UMC Wins— High Tech Industry Deems It a Leading Case against the Government's Anti-China-Investment Policy], ZHONG GUANG XIN WEN WANG [BCC NEWS NETWORK] (Taiwan), Oct. 27, 2007, <http://news.msn.com.tw/print.aspx?id=45087> (last visited Oct. 27, 2007). Although the prosecutors appealed this case, Taiwan High Court, the court of appeals, still overruled this appeal and held that the prosecutors met no burden of proof of the defendants' criminal conduct. See, e.g. Guo-Ren Zhang, *Han Jian An Er Shen Cao Xing Cheng Pan Wu Zui* [UMC's Former Chairman of the Board Was Found Not Guilty by the Court of Appeals], GONG SHANG SHI BAO [INDUSTRY & BUS. TIMES] (Taiwan), Jan. 1, 2009, available at <http://news.chinatimes.com/CMoney/News/News-Page/0,4733,contentx122009010100365,00.html>.

made by any company in a third area in which any national, legal entity, organization or other institution in Taiwan Area invested while owning a controlling interest of that company.” In consequence, MOEA punished the plaintiff with an administrative fine of NT\$2 million. The plaintiff appealed MOEA’s decision to the Taipei High Administrative Court. This court of appeals held against MOEA that failing to submit ARROW’s stock ledger or record but merely relying on reports bought from private detective agencies expert in acquiring corporate internal information, MOEA did not meet the burden of proof.⁸⁰

As discussed above, MOEA struggled to enforce the Capital Controls, especially Paragraph 2 of Article 4 of the Regulations. Nonetheless, at least according to these cases, we could find that MOEA often failed to submit documentation with sufficient evidentiary weight, like stock ledgers or records of companies incorporated in a third area such as the Cayman Islands, but punish those arguably in violation merely by reports bought from private detective agencies expert in acquiring corporate internal information. The courts thus hold against MOEA on the ground of their failure to meet the burden of proof. In other words, the failure of MOEA’s enforcement conspicuously reveals that the enforcement cost might be too high in that MOEA does not have the necessary skills and resources to collect required evidence. Therefore, administrative courts often hold in favor of fleeing corporations which adopt evasive tactics, due to the government’s failure to meet the burden of proof to establish “investment in the Mainland Area.” This fact also implies that it is not so difficult for Taiwanese companies, especially closely-held corporations usually adopted by Taiwan’s small- and medium-sized enterprises, to

⁸⁰ Also in other two cases, Taipei Gaodeng Xingzheng Fayuan [Taipei High Admin. Ct.], 95 Su Zi No. 1507 (2006) (Taiwan) and Taipei Gaodeng Xingzheng Fayuan [Taipei High Admin. Ct.], 93 Su Zi No. 1063 (2004) (Taiwan), the defendant MOEA could only submit reports bought from these private detective agencies as evidence to show that the plaintiff individual did “invest in the Mainland Area.” As explained below, this fact reveals that MOEA, the authority concerned in Taiwanese government’s executive branch, lacks the required skills and resources to enforce these restrictions on investing in Mainland China. Apparently, the enforcement cost of the Capital Controls may be too high.

circumvent the Capital Controls if those companies so doing are not required to report all material activities within their enterprise group under Taiwan’s securities and company laws.⁸¹

As a matter of fact, Taiwan’s government to an extent cannot help but acknowledge China-investment projects that are already underway via underground channels. As shown in Table 2, numbers in parentheses are investment projects recorded through make-up registration rather than prior approval. Any jump in official Taiwan investment figures should thus be considered against unofficial estimates of what has been moving into the PRC market via offshore structures. For example, in 2002 MOEA issued a six-month grace period for firms that have illegally invested or entered into technology cooperation in the PRC, during which they can register with MOEA with no or merely a trifling fine.⁸² In March 2008 before the Presidential election, MOEA announced a new round of make-up registration and attracted considerable registrations by substantially lowering administrative fines.⁸³ As these outliers in 1993, 1997, 1998, 2002, 2003, and 2008 demonstrate, on the one hand, Taiwan’s government through these “amnesties” intends to make Taiwanese firms’ exit to the PRC emerge from underground; on the other hand, Taiwan’s government, in a sense, recognizes its regulatory failure of Taiwanese firms’ outward investment in Mainland China.

Table 2 TDI in China

Year	Taiwan’s Statistics
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⁸¹ See Cheng-Kai Chou, Fang Kuan Dui Zhong Guo Da Lu Tou Zi Jin E Shang Xian Zheng Ce Zhi Yan Jiu [Research on the Policy of Lifting the Amount Ceiling for China-bound Investment from Taiwan] 123 (Jan. 2008) (unpublished master thesis, Tamkang University) (on file with author) (Taiwan).

⁸² Yi-Fu Lin, Bu Zhang Zhi Tai Shang Gong Kai Xin [Public Letter from Minister of MOEA to China-based Taiwanese Firms] (June 26, 2002) (on file with author) (calling on Taiwanese firms to conduct make-up registration).

⁸³ *Deng Lu Tou Zi Shang Xian Ke Wang Tan Xing Song Bang Zheng Yuan Da She Tai Shang [The Investment Caps Are Expected to be Relaxed; the Executive Yuan Will Pardon China-Based Taiwanese Firms]*, FA YUAN FA LU XIN WEN [LAWBANK’S L. NEWS] (Taiwan), Mar. 6, 2008, <http://www.lawbank.com.tw/fnews/pnews.php?nid=57870.00> (last visited Mar. 6, 2008).

	Cases	Amount (\$ million)
1991	237	174
1992	264	247
1993	1,262 (8,067) ⁸⁴	1,140 (2,028,046)
1994	934	962
1995	490	1,092
1996	383	1,229
1997	728 (7,997)	1,615 (2,720)
1998	641 (643)	1,519 (515)
1999	488	1,253
2000	840	2,607
2001	1,186	2,784
2002	1490 (1,626)	3,859 (2,864)
2003	1,837 (2,038)	4,595 (3,104)
2004	2,004	6,941
2005	1,297	6007
2006	1,090	7,642
2007	996	9,971
2008	482 (161)	9,843 (848)
From 1991 to Dec. 2008 ⁸⁵	37,181	75,560

Source: INVESTMENT COMMISSION, MINISTRY OF ECONOMIC AFFAIRS, MONTHLY STATISTIC REPORT ON OVERSEAS CHINESE & FOREIGN INVESTMENT, OUTWARD INVESTMENT, MAINLAND CHINA INVESTMENT (Feb. 2009), <http://www.moeaic.gov.tw/> (last visited Mar. 15, 2009).

Note: Statistics are up to December 2008.

Moreover, since 1991 Taiwan's outward investment has initially been concentrating on countries of the Association of Southeast Asian Nations ("ASEAN"). In 1995 the investment in ASEAN increased to 62.29% of Taiwan's overall outward investment. Afterwards, Taiwan's investment in China increases gradually while the investment in ASEAN decreases year by year.

⁸⁴ Numbers in parentheses are investment projects recorded through make-up registration rather than prior approval.

⁸⁵ The number of cases and amount in this row include those of previously unregistered investments which are recorded through make-up registration.

In 1995 the investment in China remains only 17.34% of Taiwan's overall outward investment.⁸⁶ Nevertheless, as shown in Table 3, in April 2008 the accumulative total of investment in Mainland China turns out to be the largest proportion of Taiwan's overall outward investment, that is, 55.64%. The second largest goes to British Central America with 16.91%. In fact, British Central America refers to tax havens mainly involving BVI and the Cayman Islands. Via these OFCs, Taiwanese firms indirectly make large investment in Mainland China largely in order to evade the Capital Controls imposed from 1997.⁸⁷ Therefore, the real total of investment in Mainland China would exceed 70% of Taiwan's overall outward investment if the percentage of British Central America is added. This fact further illuminates that Taiwan's government possesses poor knowledge of the realities regarding Taiwanese firms' investment in Mainland

⁸⁶ TAIWAN JING JI YAN JIU YUAN [TAIWAN INSTITUTE OF ECONOMIC RESEARCH], LIANG AN MAO YI YU TOU ZI YING XIANG PING GU BAO GAO [ASSESSMENT REPORT ON THE INFLUENCE OF CROSS-STRAIT TRADE AND INVESTMENT] 20-21 (2007) (Taiwan).

⁸⁷ In the light of China's statistics, from mid-1990s TDI remains the second largest FDI in the PRC. But from 1999 TDI falls to the fourth largest while OFCs in British Central America such as BVI become the second largest FDI inflows in China. As discussed above, at least since 1994 OFCs in British Central America have been priorities for destinations of Taiwan's outward investment aside from Mainland China. A study displays that Taiwanese firms transit their funds to these OFCs for later investments in China whereas these funds are not exhibited in China's statistics of TDI. David Ming Wei, *Tai Shang Yu Tai Shang Zheng Ce: Da Zao Liang An Guan Xi De Suo Yue* [*Taiwanese Businessmen in China: Key to Cross-Strait Relationship*], 460 DONG YA LUN TAN JI KAN [E. ASIA REV.] 37, 42-43 (2008) (Taiwan). See also Shao-Yun Fang, *Jing Wai Gong Si Ji Tuan Chong Zu De Yun Zuo* [*How the Restructuring of Offshore Corporate Groups Works*], SHI YONG YUE KAN [TAXES & BUS. MONTHLY SERVICES], Apr. 2002, at 54 (Taiwan); Shao-Yun Fang, Xuan Yong Wei *Jing Dao Gong Si Zuo Da Lu Tou Zi Kong Gu Gong Si De Zai Kao Liang* [*Reconsidering Whether to Adopt BVI Corporations as Holding Corporations for Investment in Mainland China*], SHI YONG YUE KAN [TAXES & BUS. MONTHLY SERVICES], June 2002, at 57 (Taiwan) (arguing that Taiwanese firms indirectly invest in China by incorporating investment holding corporations in BVI in order to evade the Capital Controls); Zi-Ping Huang, Cong Guan Xi Ren Jiao Yi Ji Cai Wu Bao Biao Xiang Mu Deng Gong Kai Zi Xun Tan Tao Tai Shang Jin Xing Da Lu Tou Zi Zhi Cai Wu Zi Xun [Research on Financial Information on Taiwanese Businesses' Investment in Mainland China in Light of Public Information such as Related Party Transactions and Items on Financial Statements], at 1 (June 2002) (unpublished master thesis, National Cheng Kung University) (on file with author) (arguing that Taiwanese firms indirectly invest in the PRC by incorporating holding companies in a third area such as BVI, Hong Kong, Singapore, and the Cayman Islands); JUNG-PAO KANG ET AL., WO QUO QI YE FU HAI WAI MU JI ZI JIN AN JIAN ZHI FA XING TIAO JIAN JI QI FA XING JIA GE HE LI XING ZHI YAN JIU [RESEARCH ON THE REASONABILITY REGARDING IPO CONDITIONS AND PRICE OF TAIWANESE FIRMS RAISING CAPITAL OVERSEAS] 2 (2004) (on file with author) (Taiwan) (arguing that restrictions on capital flow and caps on investment in Mainland China are among the reasons why Taiwanese firms invest in the PRC usually through a third country); Te-Shen Chen, *Jing Ji Quan Qiu Hua Yu Tai Shang Da Lu Tou Zi: Ce Lue Yu Bu Ju* [*Economic Globalization and Taiwan's Investment Strategies in China*], in JING JI QUAN QIU HUA YU TAI SHANG DA LU TOU ZI: CE LUE BU JU YU BI JIAO [ECONOMIC GLOBALIZATION AND TAIWAN'S INVESTMENT STRATEGIES IN CHINA] 127, 139 (Te-Sheng Chen ed., 2008) (Taiwan) (explaining that as demonstrated in Table 3 most of Taiwan's investments in British Central America and Hong Kong are transited for investments in China).

China,⁸⁸ and that Taiwan’s economic regulation hardly could completely stem the outflows of Taiwanese capital and firms. As a matter of fact, Po-Chih Chen, a former chairman of CEPD who helped President Chen’s administration to carry through the regulatory transition of relaxation from the NHBP policy to the “Proactive Liberalization with Effective Management” policy (the “PLEM” policy) in 2001, admitted that it was not easy to effectively enforce the Capital Controls given that Taiwanese firms were able to evade this regulation through third countries.⁸⁹ Furthermore, by the time President Chen replaced the NHBP with his own PLEM policy in September 2001, “many had already invested in the Chinese market, disregarding government regulations. To many in the business community [the PLEM policy] is nothing more than a rationalization of fait accompli, as it is an open secret that many investors could simply route their money to a third country, then transfer the fund to China.”⁹⁰

Table 3 Taiwan Approved Outward Investment by Country (Area)

Period	1991-2007			Jan.-Apr. 2008			Accumulative Total		
Area	Cases	Amount(\$ million)	Percentage by Amount (%)	Cases	Amount(\$ million)	Percentage by Amount (%)	Cases	Amount(\$ million)	Percentage by Amount (%)
Mainland China	36,538	64,869.07	55.40	257	2,946.26	61.44	36,795	67,815.32	55.64
British Central America	1,881	20,028.35	17.10	28	577.67	12.05	1,909	20,606.02	16.91
USA	4,583	8,975.51	7.67	19	135.34	2.82	4,602	9,110.85	7.47

⁸⁸ The current Taiwan’s SEF Secretary-General Koong-Lian Kao has expressed a similar opinion. See Koong-lian Kao, *Liang An Jing Mao Zheng He De Qi Dian—Zi You Mao Yi Qu [The Starting Point of Cross-Strait Economic Integration—Free Trade Area]*, 2 GUO JIA ZHENG CE LUN TAN [NAT’L POL’Y F.] (ISSUE 7) 26, 31 (2002) (Taiwan); also Xue-Yi Cai [William Tsai], *Quan Qiu Hua Yu Liang An Jing Ji Fa Zhan [The Dynamics and Analyses of Direct Trading Relationships between Taiwan and China]*, 2 ZHAN WANG YU TAN SUO [PROSPECT & EXPLORATION] 34, 43 (2004) (Taiwan).

⁸⁹ Po-Chih Chen, *Dui Zhong Guo Da Lu Tou Zi De Zheng Ti Ce Lue [The Integral Strategy of Investment in Mainland China]*, 25 TAIWAN JING JI YAN JIU YUE KAN [TAIWAN ECON. RES. MONTHLY] (ISSUE 4) 137, 141 (2002) (Taiwan).

⁹⁰ Ho & Leng, *supra* note 67, at 737-38 (alteration in original).

Singapore	400	4,671.50	3.99	4	629.73	13.13	404	5,301.24	4.35
Hong Kong	912	2,672.93	2.28	13	35.33	0.74	925	2,708.26	2.22
Vietnam	348	1,462.36	1.25	8	96.86	2.02	356	1,559.22	1.28
Panama	58	1,178.66	1.01	0	0.00	0.00	58	1,178.66	0.97
Japan	427	1,120.99	0.96	11	23.99	0.50	438	1,144.98	0.94
Thailand	274	1,703.98	1.46	1	3.61	0.08	275	1,707.58	1.40
Philippines	123	512.29	0.44	1	1.36	0.03	124	513.65	0.42
Korea	129	250.73	0.21	2	229.01	4.78	131	479.74	0.39
Germany	130	140.86	0.12	3	7.01	0.15	133	147.88	0.12
Others	1,827	9,506.49	8.11	34	109.36	2.26	1,861	9,615.85	7.89
Total	47,630	#####	100.00	381	4,795.54	100.00	48,011	121,889.25	100.00

Source: MAINLAND AFFAIRS COUNCIL, CROSS-STRAIT ECONOMIC STATISTICS MONTHLY NO.185, at 31 (May 2008), available at <http://www.mac.gov.tw/big5/statistic/em/185/13.pdf>.

To put it in a nutshell, the huge gap between Taiwan's official estimation and Taiwanese firms' real investment value to China, on the one hand, reveals that costs of enforcing the Capital Controls are so high that ineffective enforcement results. This, on the other hand, emphasizes that Taiwan's regulatory failure is a consequence of Taiwanese firms' internationalization.⁹¹ In particular, the first lesson we can learn is concerned with the changing role of nation states. The above discussion illustrates that even if Taiwan has the intention to enforce the Capital Controls as effectively as possible it is endowed with little capability for such enforcement. Therefore, despite the strictness of the Capital Controls, Taiwan's government possesses few required resources and skills to implement the regulations, which highlights Taiwan's predicament that laws alone cannot carry themselves into practice. For instance, although the huge gap existing between Taiwan's official data and business activities across the Strait clearly evidences that many Taiwanese firms circumvent the Capital Controls, MOEA and other authorities concerned

⁹¹ See Leng, *supra* note 49, at 34.

scarcely succeed in meeting their burden of proof to punish these illegal activities. That way, the regulatory authority of Taiwan's government suffers many a setback. Since Taiwanese firms progressively change into MNCs with the ability of international planning and management, the Taiwanese government's substantial intervention in market mechanisms of cross-Strait economic interaction naturally brings about the salient gap between private activities and government policies.⁹²

Coming up against the Capital Controls and Constraints, Taiwanese companies with mass investment in Mainland China would thus be unwilling to raise capital in Taiwan stock markets. Indeed, they need a huge amount of capital to meet financial demand of their subsidiaries or affiliates in Mainland China. Therefore, they cannot but through the following similar tactics list their shares in other stock markets in the Greater Chinese Economy, HKSE among others, so as to take the "exit" option to evade the Restrictions.

3. Common Evasive Tactics to List Shares Overseas

As Deng reports, "the total amount of Taiwanese capital flowing into China remains difficult to estimate. . . . By 1998, the amount of Taiwanese investment approved by China had reached a formidable \$41.11 billion going to 41,455 projects. In monetary value, Taiwanese investment in China ranked second after Hong Kong at that time."⁹³ What's more important is that "investment in China has shifted from labor-intensive, low value-added and short-term operations to more capital- and technology-intensive industries with longer investment horizons

⁹² *See id.* at 37.

⁹³ Deng, *supra* note 43, at 962.

such as computers, construction equipment, machinery, and petrochemicals.”⁹⁴ For instance, Taiwan’s biggest manufacturer of personal computers (“PC”), Acer Computer, Inc. (“Acer Computers”),⁹⁵ “has begun to manufacture a large number of advanced color monitors in China and half of its capital is valued as technology transfer.”⁹⁶ This example means that regardless of Chinese military intimidation, Taiwan’s Information Technology (“IT”) firms, “over the past two decades, have continued to sail across the strait for cheaper land and labor.”⁹⁷ Specifically, in order to enlarge their business or acquire necessary natural and labor resources in Mainland China, many Taiwanese companies that have listed in Taiwan stock markets might usually, through companies incorporated in a third area such as the Cayman Islands, invest in Mainland China indirectly. For fear of being subject to the Restrictions while avoiding MOEA’s oversight, most of these listed companies might through spin-offs split their China-based business into another company incorporated in some OFC, and subsequently have that company list shares in other neighboring stock markets, not least HKSE.⁹⁸ In this case, Taiwan lost many excellent companies which could have listed in Taiwan stock markets. Meanwhile Taiwan should have not lost relevant business, such as financial services, if these companies had maintained their head offices at home. This common type of evasive tactics may be regarded as a physical exit by many China-based Taiwanese companies.

For example, take Hon Hai Precision Industry Company Limited (“Hon Hai”), a renowned high-tech company incorporated in Taiwan, to elaborate on a type of these large companies’

⁹⁴ *Id.* at 963

⁹⁵ Founded in 1976, Acer Computers ranks as the world’s third-largest company for total PC shipments, is No. 2 for notebooks, and has a global workforce of more than 6,000 employees. *See* Acer Group, http://www.acer-group.com/public/The_Group/overview.htm (last visited May 19, 2009).

⁹⁶ Deng, *supra* note 43, at 964.

⁹⁷ Yang & Hung, *supra* note 68, at 681-82.

⁹⁸ Ming-Hsuan Lin, *Tai Shang Qi Ye Zhi Xiang Gang Shang Shi Zhi Xing Tai Mo Shi Fen Xi* [The Model Analysis of Listing Types in Hong Kong for Taiwan Enterprise] 94-95 (June 2007) (unpublished master thesis, TamKang University) (on file with author) (Taiwan).

similar routes into Mainland China. According to Global Offering Prospectus of Foxconn International Holdings Limited (the “Prospectus”), Hon Hai is “a company incorporated on February 20, 1970 under the laws of Taiwan and listed on Taiwan Stock Exchange,”⁹⁹ and has “a consolidated turnover of over \$11 billion in 2003.”¹⁰⁰ Since Hon Hai’s formation in 1974, it together with its subsidiaries (the “Hon Hai Group”), including the main actor in this story — Foxconn International Holdings Limited (“FIH”),

has become one of the largest global manufacturing services providers in the computer, communications and consumer electronics industries. The Hon Hai Group designs, manufactures and markets connectors and cable assemblies in the computer and computer peripherals, communications and consumer electronics industries. It engages in the design, manufacture and marketing of enclosures, principally for personal computers. Within the Hon Hai Group, [FIH] has specialized in manufacturing handsets.¹⁰¹

Nevertheless, the Hon Hai Group effectuated the “Restructuring” in early 2004. Subsequent to the Restructuring, FIH, having become an independent stand-alone company, owns 100% of the business of handset manufacturing services, which is mainly based in Mainland China but previously owned by Hon Hai. That is, since the Restructuring, FIH has separated its production and management from that of Hon Hai while developing client relationships independently of Hon Hai.¹⁰²

Moreover, the majority of FIH’s assets are located in the PRC, Hungary and Mexico while only a handful of its remaining assets are located in Taiwan.¹⁰³ In other words, before FIH was spun off from Hon Hai, Hon Hai had had a need to freely shift funds raised in Taiwan stock

⁹⁹ GLOBAL OFFERING PROSPECTUS OF FOXCONN INTERNATIONAL HOLDINGS LIMITED 15 (Jan. 24, 2005), <http://main.ednews.hk/listedco/listconews/sehk/20050124/LTN20050124000.htm> (on file with author).

¹⁰⁰ *Id.* at 2.

¹⁰¹ *Id.* at 93 (alteration in original).

¹⁰² *Id.*

¹⁰³ *Id.* at 10, 41.

markets in order to satisfy FIH's financial demand in Mainland China but was not permitted so under the Constraints. Furthermore, it was not feasible for Hon Hai's overseas subsidiaries based in Mainland China to list their shares in Taiwan stock markets due to the Constraints. Therefore, for the expansion of the capacity of FIH's existing production facilities in Mainland China, Hon Hai cannot but opt, through a succession of transactions between its subsidiaries incorporated in the Cayman Islands, to incorporate FIH at the same place, to which Hon Hai transferred relevant production, management and clients with respect to the handset business while indirectly owning a controlling interest in FIH. Then FIH established its head office in Shenzhen, Guangdong, PRC¹⁰⁴ and headed for HKSE to raise capital which could freely be utilized in Mainland China. As commentators maintain, all of Hon Hai's tactics are arguably to evade Taiwan's Capital Controls and Constraints.¹⁰⁵ This, nonetheless, results in the physical exit of Hon Hai's *nearly entire* handset business from Taiwan. Accordingly, even if many China-based Taiwanese companies desire to keep their head offices in Taiwan while expanding their business in Mainland China, the Restrictions apparently discourage them from doing so. At the very least, a Taiwanese corporate group could, though, avoid the Capital Controls and Constraints by possessing an independent subsidiary incorporated offshore with the ability to freely raise funds overseas to satisfy financial need of expansion or operation in China.

Once waves of large Taiwanese companies list their shares on HKSE, the proportion of these issuers' aggregate value to that of all listed firms on HKSE will thus increase. What follows

¹⁰⁴ *Id.* at 58.

¹⁰⁵ See e.g., Lin, *supra* note 98, at 95; Chou, *supra* note 81, at 118; Jerry G. Fong, *Chu Zou Taiwan Yuan Li Mei Guo—Cong Ri Yue Guang An Kan Tai Shang Chu Zou Chao* [Exiting from Taiwan and Leaving the United States: On Trends of Taiwanese Firms' Exit in Light of the Incident of ASE Group], 611 NENG LI ZA ZHI [LEARNING & DEV.] 96, 99-100 (2007) (Taiwan); Zhao-Ming Wu, *Tai Zi Qi Ye Yu Da Lu Ji Xiang Gang Shang Shi De Yan Jiu—Yi Xiang Guan Ge An Yan Jiu Wei Li* [The Study of Public Listing on the China and Hong Kong Stock Exchanges for Taiwan-Based Companies—Related Case Study] 101 (July 2006) (unpublished master thesis, National Chengchi University) (on file with author) (Taiwan).

is that international investors would appreciate more and more highly the stocks of these Taiwan-invested firms which are incorporated in OFCs and based in China. For instance, investors started to classify China-based Taiwanese businesses listed on HKSE as “T-Share.” If T-Share group becomes bigger and bigger international investors intending to share China’s economic development will buy these T-Shares. In Hon Hai’s case, Hon-Hai spun off its handset business, which is one of its core competencies, into FIH, and had FIH list shares on HKSE. Since FIH is growing faster than Hon-Hai, foreign investors may purchase more FIH shares than those of Hon-Hai on Taiwan Stock Exchange (“TWSE”) instead. Because Hon Hai’s shares are TWSE’s value-weighted stocks, if Hon Hai’s stock price declines accordingly, TWSE stock index may be forced to run down as well. Supposing that more and more large Taiwanese listed companies, under the cluster effect, would through tactics similar to Hon Hai’s Restructuring have their China-based overseas subsidiaries listed on HKSE, because the stock price of Taiwanese parent companies might fall the outlook of the TWSE stock index would also be gloomy.¹⁰⁶

B. The Supply Side of the Law Market

1. Mainly Selling Legal Flexibility, Rather than Legal Bonding

As discussed above, substantial evidence supports the bonding explanation of cross-listing. Under this dominant explanation, cross-listing firms are seeking stronger laws.¹⁰⁷ To name a few, John Coffee presents the thesis that “although the cross-listing decision involves a complex

¹⁰⁶ See Chia-Chen Lee, *Tai Zi Qi Ye Zai Xiang Gang Shang Shi Wen Ti Zhi Yan Xi* [A Study on the Issue of Taiwanese Enterprises Listing in Hong Kong], 8 JING JI YAN JIU [ECON. RES.] 357, 371-73 (2008) (Taiwan).

¹⁰⁷ Ribstein, *supra* note 28, at 104.

interaction of bonding, signaling, self-selection, and reduced informational asymmetry, the overall evidence supports the ‘bonding hypothesis’ and suggests that U.S.’s greater emphasis on enforcement reduces informational asymmetry and gives it a lower cost of equity capital.”¹⁰⁸ He also asserts that “one legal variable—the level of enforcement—does distinguish jurisdictions in a manner that can explain national differences in the cost of capital (especially between common law and civil law countries)”¹⁰⁹ Nonetheless, in Taiwan’s case, it seems that China-based Taiwanese businesses spurn exchanges at home and choose to go public in other neighboring stock markets, especially HKSE, not mainly to opt into the laws thereof and to bond their insiders given the “bonding” hypothesis, but rather to “avoid” the Restrictions.

JP Morgan has made an assessment of listing merits among TWSE, HKSE, and the U.S. stock exchanges by 13 indices.¹¹⁰ Some may think this report appears to support a bonding hypothesis that Taiwanese firms flock to list on HKSE just because Investor Protection of HKSE is better than that of TWSE where Investor Protection in the former is evaluated as high whereas the latter is medium. Nevertheless, the differences between TWSE and HKSE do not appear to be that large: When it comes to the U.S., Listing Requirements and Disclosure Requirements are both “strict” while Investor Protection, Listing Cost and Expenditure, and Visibility in International Markets are “high.” Compared with the U.S., both TWSE and HKSE are inferior in a similar manner.¹¹¹

Table 4 Comparison and Evaluation regarding Listing Advantages among TWSE, HKSE

¹⁰⁸ John C. Coffee Jr., *Law and the Market: The Impact of Enforcement 3* (Columbia Law & Econ. Working. Paper No. 304, 2007), available at <http://ssrn.com/abstract=967482>.

¹⁰⁹ *Id.* at 6.

¹¹⁰ Table 4 is cited from: SHI JIE ZONG HE YAN JIU ZHONG XIN GU FEN YOU XIAN GONG SI [ACCUMIND RESEARCH, INC.], CONG TAI SHANG HAI WAI SHANG SHI KAN TAIWAN ZI BEN SHI CHANG GUO JI HUA ZHUAN TI YAN JIU BAO GAO [THE PROJECT REPORT ON THE INTERNALIZATION OF TAIWAN’S CAPITAL MARKETS IN LIGHT OF LISTING OVERSEAS BY TAIWANESE FIRMS] 28 (2007) [hereinafter *Internationalization*] (on file with author) (Taiwan).

¹¹¹ *Id.* at 27.

and the U.S. Stock Exchanges

Evaluation Indices	Taiwan	Hong Kong	The U.S.
Stock Exchange	TWSE	HKSE	NYSE and NASDAQ
Applicable Law	Taiwanese Law and Regulations	Hong Kong Law and Regulations	U.S. Securities Law and SEC regulations
Ease of Transferring Shares	Easy	Easy	Easy
Target Investors	Global Institutional Investors	Global Institutional Investors	Global Institutional Investors
Investor Protection	Medium	High	High
Forecast Institutional Liquidity	Medium	High	High
Forecast Retail Liquidity	High	High	Low
Scope of Research Coverage	Medium	High	High
Listing Requirements	Reasonable	Reasonable	Strict
Listing Cost and Expenditure	Medium	Medium	High
Disclosure Requirements	Reasonable	Reasonable	Strict
Visibility in International Markets	High	High	High
Options by Potential Investors	High	High	High

Source: JP MORGAN, EQUITY MARKETS OVERVIEW 21 (2005).

As Litvak notes, “cross-listing has important costs (compliance with stricter governance and accounting rules; exposure to the threat of shareholder litigation, which is common in the United

States and rare elsewhere, and so on).”¹¹² In comparing listing costs among TWSE, HKSE, the Singapore Stock Exchange and China’s two stock markets, a famous senior partner in Taiwan’s branch of KPMG (one of the top four global accounting firms) has said that the listing cost in Taiwan, including listing fees, underwriting fees, tax, attorney fees, accountant fees and time cost, is the lowest.¹¹³ Another research paper indicates that the listing cost of HKSE is four or five times that of TWSE.¹¹⁴

The fact that Taiwanese firms listed in Hong Kong despite higher costs, and surged to list back in Taiwan after the Capital Controls were considerably lightened in 2008 as discussed below in Section III.B.3 infers that the securities regulation in Hong Kong might not be meaningfully stricter or otherwise significantly different (except for the Capital Controls)¹¹⁵ than that in Taiwan when Taiwanese firms considered listing shares in Taiwan or Hong Kong prior to the relaxation in 2008. In concrete terms, according to Deloitte Touche Tohmatsu in Taiwan (one of the top four global accounting firms), since the relaxation of the Capital Controls occurring in the second half of 2008 through October 9, 2009, a record 34 Taiwan-invested offshore corporations have initiated or completed the procedures to list shares back in Taiwan. Among them, 29 firms intend to apply for doing IPOs (they would be Primary Listing Issuers).¹¹⁶ From

¹¹² Kate Litvak, *Sarbanes-Oxley and the Cross-Listing Premium*, 105 MICH. L. REV. 1857, 1862 (2007).

¹¹³ SONG-QI TSAI [EDWARD TSAI], SHANG SHI GUI ZHI TONG CHE: LIANG AN SAN DI JI XIN JIA PO SHANG SHI SHI YONG ZHI NAN [A THROUGH TRAIN TO GO PUBLIC: PRACTICE GUIDELINES FOR LISTING IN CHINA, HONG KONG, TAIWAN OR SINGAPORE] 264-65 (2008) (Taiwan). See also Chia-Chen Lee, *Tai Zi Qi Ye Zai Da Lu Shang Shi Wen Ti Zhi Tan Tao* [A Study on the Problems of Stock Market Listing by Taiwan-Invested Firms in Mainland China], 4 JING JI YAN JIU [ECON. RES.] 157, 173-74 (2003) (Taiwan); Li-Jun Hong, *Tai Zi Qi Ye Zai Da Lu Zheng Quan Shi Chang Fa Xing Shang Shi Zhi Tan Tao* [The Research on Listing in China’s Stock Markets by Taiwanese Firms] 164 (June 2007) (unpublished LL.M. thesis, National University of Kaohsiung) (on file with author) (Taiwan); *Internationalization*, *supra* note 110, at 74.

¹¹⁴ Lee, *supra* note 106, at 364.

¹¹⁵ See Tai-San Ciou & Jung-Pao Kang, *Hai Wai Tai Shang Ru He Zai Taiwan Shang Shi Gui?* [How Do Overseas Taiwanese Firms List Shares in Taiwan?], 349 GUAN LI ZA ZHI [MGMT. MAG.] 54, 54-55 (2003) (Taiwan) (arguing that compared with other stock exchanges in China, Hong Kong, Singapore, and Malaysia, Taiwan stock markets would be Taiwanese firms’ best option for listing shares if the Capital Controls and Constraints could be further liberalized in the future).

¹¹⁶ Xin-Ren Wang, *Qin Ye Qian Zheng Tai Shang Hui Tai Shang Shi Ju Di Yi* [Deloitte Stays Top in Granting

the relaxation in question until November 13, 2009, 10 Taiwanese offshore firms mostly listed in Hong Kong have applied for listing TDRs (they would be Secondary Listing Issuers); most of them are China-based.¹¹⁷ Among them, Taiwan Ting Hsing Group (whose Master Kang-brand instant noodles have been a great success in China) is the largest food and drinks manufacturer in the Greater Chinese Economy. It has had its overseas holding company, Tingyi (Cayman Islands) Holding Corp., list shares in Hong Kong since 1996 and has so far become the Taiwan-invested HKSE-listed company with the largest market value and profitability. It made an application for listing its TDR on TWSE on November 2, 2009¹¹⁸ and has already listed TDRs on December 16, 2009.¹¹⁹ In addition, no major amendment to Taiwan's securities laws has been made in this post-relaxation period. Since the bonding effect provided by Taiwan stock markets stays constant, as Taiwanese investment banks¹²⁰, TWSE¹²¹, Investment Commission of MOEA¹²² argue, the

Certification to Taiwanese Firms Listing Shares Back in Taiwan], GONG SHANG SHI BAO [INDUSTRY & BUS. TIMES] (Taiwan), Oct. 9, 2009, available at

<http://news.chinatimes.com/CMoney/News/News-Page-content/0,4993,11050709+122009100900351,00.html>.

¹¹⁷ Jia-Qi Zhang, *Tai Shang Sheng Ma Ding Shen Qing Fan Tai Fa Xing TDR* [*Sandmartin Applies for Listing TDRs Back in Taiwan*], ZHONG GUANG XIN WEN WANG [BCC NEWS NETWORK] (Taiwan), Oct. 31, 2009, available at

<http://news.chinatimes.com/CMoney/News/News-Page-content/0,4993,130508+132009103100566,00.html>; Shu-Yi

Wang, *Kang Shi Fu Shen Qing Hui Tai Fa Xing TDR* [*Master Kang Applies for Listing TDRs Back in Taiwan*],

ZHONG SHI DIAN ZI BAO [CHINA TIMES DAILY NEWS] (Taiwan), Nov. 3, 2009, available at

<http://news.chinatimes.com/CMoney/News/News-Page-content/0,4993,130508+132009110300646,00.html>; Rui-Yi

Zhang & Jing-Wen Zhang, *Qi Jing Quang Dian Shen Qing Di Yi Shang Shi* [*Himax Technologies, Inc. Applies for*

Primary Listing], GONG SHANG SHI BAO [INDUSTRY & BUS. TIMES] (Taiwan), Nov. 13, 2009, available at

<http://news.chinatimes.com/CMoney/News/News-Page-content/0,4993,11050802+122009111300356,00.html>.

¹¹⁸ Tingyi (Cayman Islands) Holding Corp., *Filing of The Application for the Listing of Taiwan Depository Receipts* (Nov. 2009), <http://www.masterkong.com.cn/InvestorInformationen/Circulars/> (last visited Nov. 10, 2009); Jia-Qi

Zhang, *Kang Shi Fu Fan Tai Fa TDR Shi Pin Qu Jiao Hao* [*Master Kang Went Home to List TDRs, Food Stocks*

Rally], ZHONG GUANG XIN WEN WANG [BCC NEWS NETWORK] (Taiwan), Nov. 3, 2009, available at

<http://news.chinatimes.com/CMoney/News/News-Page-content/0,4993,130508+132009110300885,00.html>.

¹¹⁹ Xiu-Yun Cao, *Kang Shi Fu TDR Shi Er Yue Shi Qi Ri Gua Pai* [*Master Kang TDRs Will Be Listed on December 17*], ZHONG GUO SHI BAO [CHINA TIMES] (Taiwan), Nov. 18, 2009, available at

<http://news.chinatimes.com/CMoney/News/News-Page-content/0,4993,11050802+112009111800387,00.html>.

¹²⁰ Zong-Tong Wang & Zong-Zhi Liu, *Gui Yu Fan Xiang TDR Re Tai Gang Shi Chang Da Fan Pan* [*Listing TDRs*

Back in Taiwan like the Return of Spawning Salmon, The Game Has Been Changed between Taiwan and Hong

Kong Stock Markets], ZHONG GUO SHI BAO [CHINA TIMES] (Taiwan), Oct. 12, 2009, available at

<http://news.chinatimes.com/CMoney/News/News-Page-content/0,4993,11050802+112009101200151,00.html>;

Zong-tong Wang, *Liang An Hong Li Tai Gu Jiang Cheng Ya Tai "Na Si Da Ke"* [*The Restrictions on Cross-Strait*

Exchange Have Been Relaxed, TWSE Would Become the Asia Pacific "NASDAQ,"], ZHONG GUO SHI BAO [CHINA

TIMES] (Taiwan), Oct. 12, 2009, available at

<http://news.chinatimes.com/CMoney/News/News-Page-content/0,4993,11050802+112009101200152,00.html>.

¹²¹ Zong-Zhi Liu, *Tai Shang Hui Tai Shang Shi Ma Zheng Fu Ji Ji Tui Dong* [*The Ma Administration Aggressively*

moderation of the Capital Controls, to a great extent, contributes to the current craze of offshore Taiwanese firms listing back in Taiwan.¹²³ In other words, the remarkable rise in the listing-back rate up to now likely reflects the relaxation of the Capital Controls which previously had left listing shares in Taiwan a worse choice than in Hong Kong. This fact indirectly evidences that the quality of the mandatory disclosure law and enforcement regime of the Hong Kong stock market, is neither significantly better than those of Taiwan stock markets nor matters in the competition for cross-listing business, and that when Taiwanese firms considered listing shares in Taiwan or Hong Kong before the relaxation in 2008, the determinant affecting their decisions would likely be primarily to avoid the Capital Controls, rather than to bond their insiders. Therefore, it's difficult to jump to the conclusion that China-based Taiwanese firms spurn stock exchanges at home and choose to go public in other neighboring stock markets, especially HKSE, mainly in order to opt into the laws thereof and to bond their insiders according to the bonding hypothesis.

What's more, according to Taiwanese scholars' empirical studies explicated below, the trend that many Taiwanese firms list shares on HKSE during recent years can be primarily attributed to the fact that they cannot but avoid the Capital Controls and Constraints and then buy regulatory products of legal flexibility which HKSE and other stock markets in the Greater Chinese Economy can sell. In this case, they would rather trade the higher costs of listing incurred in the

Attracts Taiwanese Firms to List Shares Back in Taiwan, ZHONG GUO SHI BAO [CHINA TIMES] (Taiwan), Apr. 16, 2009, at A5; Jia-Qi Zhang, *Wang Wang TDR Xiao Ying Si Yue Fen You San Jia Tai Shang Shen Qing Fan Tai Gua Pai* [The Effect of Want Want China's TDR: 3 Taiwanese Firms Apply for Listing Shares Back in Taiwan this April], ZHONG GUANG XIN WEN WANG [BCC NEWS NETWORK] (Taiwan), May. 1, 2009, available at <http://news.chinatimes.com/CMoney/News/News-Page-content/0,4993,130508+132009050100851,00.html>.

¹²² *Song Bang Deng Lu Shang Xian Liu Shi Er Jia Tai Shang Ni Hui Tai Shang Shi Gui* [The Upper Limits on Investment in Mainland China Are Relaxed, 62 Taiwanese Firms Plan to List Shares Back in Taiwan], TAIWAN XIN SHENG BAO [TSSDNEWS] (Taiwan), Feb. 5, 2009, at 2.

¹²³ See also *Tai Shang Fan Xiang Gua Pai Shang Ji Wu Xian* [Taiwanese Firms' Listing Back in Taiwan Brings Much Business], DA LU TAI SHANG 1000 DA: TAI SHANG JIN HUA LUN [TOP 1000 CHINA-BASED TAIWANESE FIRMS: THE EVOLUTIONISM OF TAIWANESE FIRMS], June 12, 2009, at 153-55 (Taiwan).

short term for the legal flexibility to use funds raised in neighboring stock markets, which would offer the long-term reward of investment in Mainland China. In other words, it is more likely the Capital Controls, rather than legal bonding, that drove the choice of Hong Kong or Taiwan listing markets prior to the relaxation in 2008 as discussed below.

In a case study on Mayer Steel Pipe Corporation (“Taiwan Mayer”), the General Manager of Taiwan Mayer was interviewed for reasons why it followed a pattern similar to Hon Hai’s Restructuring to have its Mainland subsidiary, Mayer Holdings, list shares on HKSE. To begin with, Taiwan Mayer is the first specialized manufacturer of steel pipes and tubular products in Taiwan. Since its founding in 1959, Taiwan Mayer has been devoted to the production and selling of high-quality steel pipes and tubes and has also built up a powerful distribution network to ensure its market share leadership. In April 1993, Taiwan Mayer went public on TWSE. In 1997, Taiwan Mayer, through a succession of offshore transactions, established Guangzhou Mayer in Mainland China. Guangzhou Mayer has received wide recognition and support from clients, with its products already reaching Eastern and Central China markets with great success. In October 9, 2003, Taiwan Mayer incorporated Mayer Holdings in the Cayman Islands to hold a majority of shares of Guangzhou Mayer. In June 21, 2004, Mayer Holdings went public on HKSE.¹²⁴ Taiwan Mayer’s General Manager suggested that factors such as legal bonding cannot be responsible for the key underlying reason that Mayer Holdings listed shares on HKSE. He indicated that the primary cause for Mayer Holdings to list on HKSE was to find a stock market where they can use raised capital without being subject to the Restrictions.¹²⁵ He added that

¹²⁴ See Mayer Steel Pipe Corporation, <http://www.mayer.com.tw/about/about-english.htm> (last visited May 20, 2009); Cui-Huang Weng, *Tai Shang Zai Xiang Gang Shang Shi Yu Hui Tai Shang Shi Wen Ti Zhi Tan Tao* [The Discussion on Issues of Taiwanese Enterprises’ Listing Shares in Hong Kong and Back in Taiwan] 79-80 (Jan. 2006) (unpublished master thesis, National Chengchi University) (on file with author) (Taiwan).

¹²⁵ *Id.* at 86-87.

even though Mayer Holdings was listed on HKSE they were still unfamiliar with Hong Kong law and regulations, and that if Taiwan's government had not imposed the Capital Controls and Constraints, Taiwan Mayer would not have had Mayer Holdings list shares overseas.¹²⁶ This case study led to a conclusion that the principal cause for Taiwanese listed companies to have their Mainland subsidiaries or affiliates list share overseas, rather than in Taiwan, was the Capital Controls and Constraints.¹²⁷ This conclusion was also confirmed by a study conducting in-depth interviews with TWSE, a leading Taiwanese investment bank's branch in Hong Kong, the Taiwanese branch of Ernst & Young (one of the top four global accounting firms), and five Taiwan-invested firms which either listed shares in Taiwan, Hong Kong or Mainland China, or were considering where to go public.¹²⁸

¹²⁶ *Id.* at 89.

¹²⁷ *Id.* at 97.

¹²⁸ Shu-Min Li, *Tai Shang Hui Tai Shang Shi Wen Ti Ji Jie Jue Fang An Zhi Tan Tao* [The Analysis of Initial Public Offering Problems and Solutions of Returning Taiwan to Listing Security for Taiwan Overseas Companies] 78-79, 91-92 (Dec. 2004) (unpublished master thesis, National Chung Hsing University) (on file with author) (Taiwan). Not a few commentators come to similar conclusions as well. *See, e.g.*, Sen-Ying Qiu, *Da Lu Tai Shang Hui Tai Shang Shi Gui Huan Jing Zhi Yan Jiu* [The Analysis of the Environment for Listing Shares Back in Taiwan by China-Based Taiwanese Firms] 71 (May 2003) (unpublished master thesis, National Taiwan University of Science and Technology) (on file with author) (Taiwan); Yu-Chen Ling, *Wai Guo Qi Ye Lai Tai Shang Shi Gui Wen Ti Zhi Yan Xi* [A Study on the Problems of Public Listing by Foreign Enterprises in Taiwan], 4 *JING JI YAN JIU* [ECON. RES.] 135, 145, 149-50 (2003) (Taiwan); Horng-Ming Tsai, *Da Lu Zheng Quan Shi Chang Fa Zhan Dui Liang An Jing Mao Zhi Ying Xiang* [The Impact of the PRC's Stock Market Developments on Cross-Strait Economic Interactions], 5 *ZHAN WANG YU TAN SUO* [PROSPECT & EXPLORATION] (ISSUE 1) 54, 68 (2007) (Taiwan); Town-Shine Wu, *Taiwan Qi Ye Hai Wai Chou Zi Zhi Yan Jiu*—Jian Lun Hai Wai Taiwan Qi Ye [A Study on Overseas Fundraising by Taiwanese Enterprises: With Discussion on Fundraising by Overseas Taiwanese Enterprises in Taiwan] 67-68, 114, 120 (July 2008) (unpublished master thesis, National Taiwan University) (on file with author) (Taiwan); Wu, *supra* note 105, at 100-01; Yong-Kang Wang, *Da Lu Tai Shang Qi Ye Shang Shi Jue Ce Yin Su Fen Xi*—Ge An Zhe Jiang Guo Xiang Zhi Leng Gong Ye Gu Fen You Xian Gong Si [The Analysis of Factors for Decision-Making in IPOs by China-Based Taiwanese Firms—A Case Study on Zhejiang King Refrigeration Industry Co., Ltd], at 2 (of Chapter 5) (Jan. 2004) (unpublished master thesis, National Chengchi University) (on file with author) (Taiwan); YA-HUI YANG & XIAO-TIAN LONG, *ZI BEN SHI CHANG FA ZHAN YU TAIWAN QI YE CHOU ZI ZHI FEN XI* [THE ANALYSIS OF THE DEVELOPMENT OF CAPITAL MARKETS AND TAIWANESE FIRMS' FINANCING] 60 (2004) (on file with author) (Taiwan); Zai-Dong Zhao, *Tai Shang Qi Ye Zai Da Lu Shang Shi Zhi Ke Xing Xing Yan Jiu* [The Feasibility Study of Entering China Stock Markets for Taiwanese Enterprises] 49, 71 (June 2006) (unpublished master thesis, National Taiwan University of Science and Technology) (on file with author) (Taiwan); Chou, *supra* note 81, at 107-08; Hong-Yuan Chang, *Tai Shang Fu Gang Shang Shi Yu Qi Ke Neng Zhi Ying Xiang* [The Influence on Taiwan Enterprise IPO in Hongkong Stock Market], 5 *ZHAN WANG YU TAN SUO* [PROSPECT & EXPLORATION] (ISSUE 12) 11, 11 (2007) (Taiwan); Research Department, Supervision of Markets Division, The Securities and Futures Commission, *Hong Kong Consolidates its Role as a Fund-raising Platform for the Greater China Region with Increased Listing of Taiwanese Companies* 5 (May 2008),

Moreover, from July 2006 to January 2007, a research team led by I-Ru Liu, a former legislator in Taiwan and also an adjunct professor of finance in National Taiwan University, (“I-Ru Liu Team”) made research into the reasons for Taiwanese companies to list shares overseas. They held three large conferences with scholars, industries, government officials and professionals. They surveyed Taiwanese companies and investment banks by questionnaires. They also extensively interviewed a foreign investment bank and a domestic one respectively, both of which have experiences to guide and counsel listing shares overseas by Taiwanese companies. Although there are other reasons for Taiwanese companies to list overseas, the team concludes that the policy and direct reason is that the Capital Controls and Constraints compel Taiwan-invested companies to list overseas. China-based Taiwanese businesses wish to expand their markets in Mainland China. If they list shares in Taiwan stock markets, the capital raised cannot be used freely for investments in China. Encountering the Capitals Control and Constraints, they are forced to avoid the regulation and list shares overseas. For these Taiwanese firms with large investment needs in Mainland China, HKSE provides them with a capital-raising venue where they can at liberty use the capital raised to invest in China.¹²⁹ Put in

www.sfc.hk/sfc/doc/EN/research/research/RS%20Paper%2040.pdf (hereinafter *Platform*) (last visited Dec. 1, 2009) (on file with author) (H.K.); CHU-CHIA LIN, CHONG HUI JING JI GAO DIAN: LIANG AN JING MAO YU TAIWAN WEI LAI [COMING BACK TO AN ECONOMIC CLIMAX: CROSS-STRAIT ECONOMIC RELATIONS AND THE FUTURE OF TAIWAN] 148 (2008) (Taiwan) (arguing that the Capital Controls and Constraints have driven Taiwanese firms with heavy investment in China to be listed on HKSE even if listing costs are higher in Hong Kong than in Taiwan, in the sense that the capital raised in Taiwan cannot be freely used for investments in China due to the Restrictions).

¹²⁹ *Internationalization*, *supra* note 110, at 85-86. Many other commentators also arrive at the same conclusion. See, e.g., Ya-Hui Yang, *Gong Si Shang Shi Gui Ying Xiang Yin Su Yu Guo Ji Ban Yuan Jing* [Factors Affecting Firm's Listing and the Vision for International Listings], 34 QUAN QIU TAI SHANG E JIAO DIAN [THE E-FOCUS OF GLOBAL TAIWANESE FIRMS] (Sep. 6, 2005), <http://twbusiness.nat.gov.tw/>; JUNG-PAO KANG, TAI SHANG QI YE JIU DI SHANG SHI YIN YING CE LÜE ZHI YAN JIU [THE RESEARCH ON RESPONSIVE STRATEGIES OF LOCAL LISTINGS BY TAIWANESE FIRMS] 160-61(2003) (on file with author) (Taiwan); Tsai, *supra* note 113, at 237, 274; I-Ming Chang, *Da Lu Tai Shang Yu Guo Nei Shang Shi (Gui) Ke Xing Xing Yan Jiu— Yi Taiwan Zi Ben Shi Chang Wei Li* [The Study of Taiwanese Enterprises in Mainland China Launching IPO at Taiwan Securities Market] 93, 95-96 (June 2004) (unpublished master thesis, National Chiao Tung University) (on file with author) (Taiwan); Lee, *supra* note 106, at 376; Chun Min Huang, *Taiwan Yu Xiang Gang Zi Ben Shi Chang Zhi Jing Zheng Tai Shi—Jian Lun Cheng Xiao Shou Xu Fei Zhi Cha Yi* [To Evaluate the Competition between Taiwan and Hong Kong Capital Market and Follow Up the Comparison of the Management Fee] 59, 63 (June 2007) (unpublished master thesis, National Sun Yat-sen

another way, Taiwan stock markets should have been China-based Taiwanese firms' best listing option to raise funds for investments in China. But due to the Capital Controls and Constraints, HKSE turns out to be the second best choice in the sense that it provides a listing product of legal flexibility for investing raised funds in any purpose as Taiwanese firms themselves see fit.¹³⁰

Furthermore, there exists another study to interview two Taiwanese companies having been listed in TWSE. Both of them build plants in China mainly in order to lower manufacturing costs and cultivate huge local consumer markets. They both, through evasive tactics like the Restructuring of Hon Hai, have their subsidiaries list on HKSE. Their decisions are based on the ground that expansion in production in China requires more funds but parent companies in Taiwan are subject to the Capital Controls and Constraints so that they have no other choice but to list shares on such a neighboring stock exchange as HKSE to raise necessary funds.¹³¹

The last empirical study involves interviews of three other Taiwanese companies, H, Y and

University) (on file with author) (Taiwan); Fong, *supra* note 105, at 98-99; Jung-Pao Kang, *Liang An San Di Zai Na Li IPO?* [Where to do IPOs among Cross Tri-Regional Securities Markets], 362 GUAN LI ZA ZHI [MGMT. MAG.] 30, 34 (2004) (Taiwan); Lin, *supra* note 98, at 8, 89; Xiupo Wu, *Zhong Guo Wang Wang Wei He Cong Xin JiaPpo Dao Xiang Gang Shi Chang Shang Shi ?* [Why Did Want Want China Choose to Be Listed in Hong Kong Instead of Singapore?], GUO JI RONG ZI [INT'L FINANCING], June 2008, at 45 (P.R.C.); Jianhua Wang, *Xian Zhi Tai Duo Zheng Ju Bu Wen Xin Xin Bu Zu Tai Shang Bei Po Fu Gang Shang Shi* [Too Many Restrictions, Unstable Politics and Lack of Confidence Forced Taiwanese Businesses to Be Listed in Hong Kong], TAI SHENG [VOICE OF TAIWAN], Sep. 2004, at 52 (P.R.C.) (quoting General Manager of the Hong Kong subsidiary of a Taiwanese leading investment bank as saying that the greatest advantage to list shares in Hong Kong lies in the legal flexibility to use the raised funds as compared with that in Taiwan).

¹³⁰ See Kun-Yuan Xu, *Liang An San Di Tai Shang Chou Zi Ping Gu Zhi Yan Jiu* [IPO and SPO for Taiwan Enterprise in China, Hong Kong and Taiwan] 144, 162, 164, 168-69 (Jul. 2006) (unpublished master thesis, National Chengchi University) (on file with author) (Taiwan).

¹³¹ Hung-Huei Liao, *Tai Shang Xuan Ze Taiwan Huo Xiang Gang Gu Piao Shang Shi Zhi Yan Jiu* [Research of Taiwanese Enterprise's View in Deciding a Listing between Taiwan and Hong Kong Stock Markets] 55-66 (Jan. 2007) (unpublished master thesis, National Taiwan University) (on file with author) (Taiwan). See also Chen-Min Hsu, *Jian Li Taiwan Cheng Wei Ya Tai Zi Chan Guan Li Zhong Xin Yu Chou Zi Zhong Xin Zhi Fen Xi (Shang)* [The Analysis of Establishing the Center for Asia-Pacific Asset Management and Financing in Taiwan—Part I], 114 QUAN QIU TAI SHANG E JIAO DIAN [THE E-FOCUS OF GLOBAL TAIWANESE FIRMS] (Oct. 14, 2008), <http://twbusiness.nat.gov.tw/>.

S, all of which invest in Mainland China. H, a company having listed shares on TWSE, plans to have its subsidiary in China list shares on HKSE given that listing shares in Taiwan stock markets is subject to the Capital Controls and Constraints. Y, a company having been listed on the over-the-counter (“OTC”) market in Taiwan, plans to have its subsidiary list on Shanghai Stock Exchange in China given the problem associated with the Capital Controls and Constraints. S, a parent company having invested in China, intends to list its own shares in Taiwan first, because of complications in its industry and its business strategy. Nevertheless, S still worries about future obstacles created by the Capital Controls and Constraints.¹³²

In sum, the jurisdictional competition in primary listing markets in the Greater Chinese Economy is not strictly comparable to the U.S. cross-listing (secondary listing or dual listing) markets. Nonetheless, competition for primary listings among these stock markets also leads to a law market in which Taiwanese firms with mass investment in Mainland China can select a regulatory product without being subject to the Restrictions, instead of exposing themselves to regulatory burdens imposed by Taiwan’s government. These stock markets supply these China-based Taiwanese businesses with regulatory products of legal flexibility to use raised capital at liberty. Therefore, Taiwanese firms went public on HKSE, among others, like a torrent prior to the considerable lightening of the Capital Controls and Constraints in 2008. The physical exit or threats of exit regarding listing shares overseas thus activated the interest group competition in Taiwan’s political marketplace over whether to relax the Restrictions.

2. Interest Group Competition to Seek Deregulation

¹³² Yi-Qing Ye, *Tai Shang Gua Pai Zhi Dong Ji Yu Hui Tai Shang Shi Mo Shi Tan Tao* [The Research on Taiwanese Firms’ Motivations to List Shares and Models of Listing Back in Taiwan] 93-116 (Jul. 20, 2006) (unpublished master thesis, Soochow University) (on file with author) (Taiwan).

Accordingly, the demand side of the law market, in the first place, sparks competition for the supply by neighboring stock markets like HKSE of a primary-listing legal environment without being subject to the Capital Controls and Constraints. The exit of Taiwanese companies seeking to avoid the Restrictions creates overwhelming costs but little benefit for anti-regulatory and exit-affected interest groups in Taiwan. Therefore, the demand side in turn drives those directly or indirectly affected by the Restrictions to voice their petition for relaxation of the Restrictions not only for themselves but also on behalf of exiting firms to an extent. The anti-regulatory interest groups include China-based Taiwanese firms represented by local chambers of commerce¹³³ as well as even foreign investors mostly represented by the European Chamber of Commerce Taipei (“ECCT”)¹³⁴ and American Chamber of Commerce in Taipei (“AmCHam”).¹³⁵ These anti-regulatory interest groups are all directly burdened by the Restrictions and thus promote ease of the regulation.¹³⁶ The anti-regulatory interest groups’

¹³³ For example, two major players in Taiwan are the Chinese National Federation of Industries (“CNFI”) and the General Chamber of Commerce of the R.O.C. (“ROCCOC”). The former is “a non-profit organization consisting of 152 member associations in their respective fields of manufacturing industry in the Republic of China. With each member association representing its specific line of manufacturing, all the associations together stand for more than 100,000 industrial companies in this country.” CNFI, <http://www.cnfi.org.tw/kmportal/front/bin/ptdetail.phtml?Reg=100020&Part=ENGLISH-homepage> (last visited Dec. 1, 2009). The latter is also “a non-profit organization of leading commercial chambers, trade associations in the Republic of China (Taiwan). It was founded on Nov. 1, 1946 mainly to represent the interests of Taiwanese business community” ROCCOC, <http://www.roccoc.org.tw/english/> (last visited Dec. 1, 2009).

¹³⁴ Tsai, *supra* note 128, at 68-69 (citing a report issued by ECCT in October 2007 that the Capital Controls also drove European firms to exit from Taiwan’s markets since Taiwanese firms with whom they cooperated were so restrained that they had no other option but to dissolve their strategic alliances).

¹³⁵ See, e.g., *Dao Nei Gong Shang Jie Ji Wai Shang Hu Yu Tai Dang Ju Ying Song Bang Liang An Jing Mao Zheng Ce [Local Industries and Foreign Businesses Appeal to Taiwan’s Government for Loosening Limits on Investment in the Mainland]*, ZHONG XIN SHE [CHINA NEWS SERVICE] (P.R.C.), Dec. 4, 2005, <http://big.china.com.cn/chinese/TCC/1050949.htm> (last visited Nov. 2, 2007); Yen-Po Tang, *Liang An Jing Mao Fa Zhan Qu Shi Yu Zhan Wang [The Developmental Trend and Outlook of Cross-Strait Trade]*, 5 ZHAN WANG YU TAN SUO [PROSPECT & EXPLORATION] 20, 34 (2007) (Taiwan) (describing that both ECCT and AmCHam keenly called on Taiwan’s government to promote stronger economic ties with China—otherwise Taiwan would lose its competitiveness).

¹³⁶ See *Rian He Wan Bao: Ri Yue Guang Shi Jian Xuan Gao Bian Zheng Fu Zhi Zheng Shi Bai [United Evening News: The ASE Case Demonstrates the Failure of the Chen Administration’s Policy on Mainland-Investment Restrictions]*, REN MIN WANG [PEOPLE’S DAILY ONLINE] (P.R.C.), Nov. 28, 2006, available at <http://tw.people.com.cn/BIG5/14811/14872/5100043.html> (last visited Nov. 2, 2007); *Guan Zhi Tai Yan Taiwan*

voice appears to be so strong that some legislators¹³⁷ and even government officials of the former ruling party DPP came out in support of them as well.¹³⁸

Since Taiwan's economy highly relies on foreign trade and investment, foreign investors are interesting examples of anti-regulatory interest groups which merit highlighting here. In general, foreign firms trust Taiwanese companies' business reputation and the better-governed legal environment (e.g. intellectual property protection) in Taiwan than China.¹³⁹ They want to use Taiwan as their base or fortress and team up with Taiwanese businesses to enter markets in China.¹⁴⁰ Therefore, once Taiwanese companies are fettered with the Restrictions and prohibited

Fang Di Chan Ye Cu Dang Ju Fang Kuan Deng Lu Men Kan [Taiwan's Real Estate Industry Appeals for Loosening Limits on Investment in the Mainland], ZHONG XIN SHE [CHINA NEWS SERVICE] (P.R.C.), Nov. 2, 2006, http://www.china.com.cn/overseas/txt/2006-11/03/content_7311026.htm (last visited Nov. 2, 2007); *Tai Shang Tou Zi Da Lu Chuang Xin Gao Bu Man Tai Lian Dang Zu Nao Liang An Kai Fang [The Investment in the Mainland by Taiwanese Companies Hit a New High While Pro-Regulatory Legislators are Criticized for Impeding the Deregulation]*, REN MIN WANG [PEOPLE'S DAILY ONLINE] (P.R.C.), <http://tw.people.com.cn/BIG5/14810/4618949.html> (last visited Nov. 2, 2007).

¹³⁷ *Lü Wei Pi Bai Fen Zhi Si Shi Shang Xian Tai Yan Ke Wang Liang An Jing Mao Da Dan Kai Fang [A DPP Legislator Criticizes the Harshness of Limits on Investment in the Mainland and Expects a Brave Deregulation]*, REN MIN WANG [PEOPLE'S DAILY ONLINE] (P.R.C.), July 26, 2006, <http://tw.people.com.cn/BIG5/14812/14875/4627533.html> (last visited May 21, 2009). In 2003, Tai-san Ciou, a DPP legislator, has already argued that if a Taiwan-invested firm has established its headquarter in Taiwan, legal barriers restraining Taiwanese enterprises' global management and planning, such as the Capital Controls and Constraints, should also be removed. This argument is similar to one of the relaxation measures later taken since KMT took power in 2008. Ciou & Kang, *supra* note 115, at 58.

¹³⁸ *Tai Qi Ri Yue Guang Xiao Ying Kuo Da Tai Dang Ju Mo Xu Deng Lu Shang Xian Song Bang [Impacted by the ASE Case, Taiwan's Government Acquiesced in the Direction of Loosening Limits on Investment in the Mainland]*, REN MIN WANG [PEOPLE'S DAILY ONLINE] (P.R.C.), Nov. 26, 2006, <http://tw.people.com.cn/BIG5/14812/14875/5101410.html> (last visited Nov. 2, 2007).

¹³⁹ Chen-Yuan Tung, *Taiwan Dui Wai Jing Ji Zhan Lue Zhi Jian Tao Yu Jian Yi [The Review and Suggestion of Taiwan's International Economic Strategies]*, 98 YAN XI LUN TAN YUE KAN [FORUM ON TRAINING AND DEVELOPMENT] 15, 20-21 (2009) (Taiwan).

¹⁴⁰ See Koong-Lian Kao, *Taiwan Jing Ji Xu Yao Hong Guan De Liang An Jing Mao Zheng Ce [A Macroscopic Cross-Strait Economic Policy Is Required for Taiwan's Economy]*, 1 ZHAN WANG YU TAN SUO [PROSPECT & EXPLORATION] (ISSUE 5) 38, 46 (2003) (Taiwan). For example take Japanese companies:

There are quite a few cases where strategic alliances have been formed between Taiwanese and Japanese companies in order to invest in Mainland China. There are a number of different alliances including joint ventures, Japanese companies licensing Taiwan brands and granting the use of Japanese technology to manufacture in China, Japanese companies purchasing products from Taiwanese companies in China and transferring technology to them. There is a clear picture that shows Japanese and Taiwanese companies cooperating with each other to develop the Mainland market. The primary reason for collaboration is so [sic] companies can take advantage of management systems and market development. Japanese and Taiwanese firms get along together because they have complementary qualities. Through strategic alliances, companies

from investing in China mainly in accordance with their business demands, foreign investors will also directly assume the cost of this excessive regulation and begin to consider exiting from Taiwan.¹⁴¹ We may obtain the very answer from a quote of I-Ru Liu Team's interview with a domestic investment bank and a foreign one, both of which possess much experience as underwriters for Taiwanese companies listing shares overseas:

Many foreign investors interested in investing in China expressed that they did not trust Chinese companies and were willing to make deals with Taiwanese companies directly. Yet, Taiwan's regulation on investing in China drove away the foreign capital. Besides, many foreign firms wished to cooperate with Taiwanese management and R & D teams to do business in China. For instance, a Swedish firm intended to buy out a leading Taiwanese company in traditional industries and wished to employ the same management in this Taiwanese company to help them invest in China. Taiwan's government, however, intervened in this deal pursuant to the Capital Controls. It was incredible for this Swedish firm to find that it was also subject to the Capital Controls that they forwarded money from abroad to Taiwan and subsequently to China for investment. This Swedish firm cannot understand that even though they were willing to make local investment and pay the tax on behalf of their Taiwanese subsidiary after the buy-out, Taiwan's government would keep preventing them from investing in China through their Taiwanese subsidiary, which meant that Taiwan's government required them to exit from markets in Taiwan. In consequence, this Sweden firm, after buying out the Taiwanese company in question, did exit from Taiwan towards China. Nothing was left in Taiwan. Taiwan lost everything.¹⁴²

Moreover, O'Hara and Ribstein note:

obtain mutual benefits and increase their competitive strengths. Taiwanese companies obtain technology and scalability from the manufacturer, which increases Taiwan's industrialization. On the other hand, Japanese companies are able to break into the Chinese market and acquire cheaper products and parts. Furthermore, collaboration has accelerated the globalization of companies, which will lead to stronger competitiveness in the world market.

Yan Zhu, *Tai Shang Da Lu Tou Zi De Ri Ben Yin Su Yu Jing Ji Quan Qiu Hua Yi Han* [Japan's Influence on Taiwan's Globalization and Investment in Mainland China], in JING JI QUAN QIU HUA YU TAI SHANG DA LU TOU ZI: CE LÜE BU JU YU BI JIAO [ECONOMIC GLOBALIZATION AND TAIWAN'S INVESTMENT STRATEGIES IN CHINA] 319, 320 (Te-Sheng Chen ed., 2008) (Taiwan).

¹⁴¹ Li, *supra* note 128, at 81. See also Chou, *supra* note 81, at 118.

¹⁴² *Internationalization*, *supra* note 110, at 69.

[V]oice and exit intersect. When a jurisdiction loses or fails to attract people and firms because of its laws, those who forgo or lose business have an incentive to lobby to improve the law. Put differently . . . [e]xit by some can add voice to others who benefit by the presence of those who have exited. These “exit-affected groups” are then added to the mix of proregulatory and antiregulatory groups competing to enact their preferred laws. In a world of enhanced mobility, outside interests are often powerful despite their lack of physical proximity to local lawmakers.¹⁴³

Good examples of these exit-affected interest groups in the Taiwan case are local securities industries, securities professionals, TWSE, and not least Taiwanese retail investors. The problem that the Restrictions adversely impact Taiwan stock markets can be observed from the fact that Taiwan’s total capital-raising dollar amount of IPO deals in 2006 is the lowest during the last decade because many Taiwanese firms, following patterns similar to Hon Hai’s Restructuring, do their IPOs on HKSE instead.¹⁴⁴ This problem can also be noted from the fact that the total number of companies listed in Taiwan has been declining according to the statistics in 2006, and even backslides to the last among East Asian Tigers—including Hong Kong, South Korea, Singapore and Taiwan. An FSC official in private admitted that one of the significant causes of this distress is the political obstacle, namely, the Restrictions which discourage China-based Taiwanese firms from listing shares in Taiwan.¹⁴⁵ Therefore, it is reasonably presumed that the

¹⁴³ Erin A. O'Hara & Larry E. Ribstein, *Rules and Institutions in Developing a Law Market: Views from the U.S. and Europe*, 82 TUL. L. REV. 2147, 2155 (2008).

¹⁴⁴ *Tai Shang Shi Gong Si Chou Zi Chuang Shi Nian Xin Di* [Capital-Raising Dollar Amount of IPOs in Taiwan at the Lowest in 10 Years], PEOPLE'S DAILY (P.R.C.), Nov. 21, 2006, available at <http://tw.people.com.cn/BIG5/14812/14875/5066386.html>. See also Taying Liaow et al., *Qi Ye Jin Rong Fa Zong Lun* [The Overview of Law on Business Association and Finance], in QI YE CHOU ZI FA WU YU GE AN FEN XI [CASE STUDIES AND LEGAL AFFAIRS ANALYSIS OF CORPORATE FINANCING] 1, 10 (Taying Liaow et al. eds., 2008) (Taiwan) (discussing that according to TWSE's statistics from 1998 to January 2008, the number of IPOs has been decreasing since 2002 year by year).

¹⁴⁵ *Tai Gu Chen Lun Shang Shi Gong Si Zong Shu Wei Suo Diao Ya Zhou Si Xiao Long Zhi Wei* [Taiwan's Stock Market is Backsliding with the Smallest Number of Listing Companies among East Asian Tigers], REN MIN WANG [PEOPLE'S DAILY ONLINE] (P.R.C.), Nov. 27, 2006, <http://tw.people.com.cn/BIG5/14812/14875/5092097.html> (last visited Dec. 1, 2009). It is said that most Taiwanese firms that exit from Taiwan's stock markets and list shares overseas intend to get rid of impediments created by the Capital Controls and Constraints, and to seek out legal flexibility for investments in China somewhere else. According to the business community's statistics, of the capital

financial services industry in Taiwan is one of the exit-affected interest groups that indirectly feel negative impact of the Restrictions. In particular, listing-related benefits do not come to the local financial services industries, such as investment banks, law firms, and accounting firms, (and indirectly, to their local economies in terms of tax revenue, employment rates, real estate prices and the like), as more and more China-based Taiwanese corporations do their IPOs in other capital markets, HKSE among others, to avoid Taiwan's jurisdiction. Furthermore, Gordon Shu Chen, then board chairman of TWSE (another exit-affected interest group), in May 2007 also stressed that more and more international private equity funds were coming to Taiwan to acquire Taiwanese listed companies owing to lower stock prices in Taiwan¹⁴⁶ and to the Capital Controls. Therefore, he advocated the Restrictions should be further relaxed in the near future.¹⁴⁷

More importantly, Taiwanese retail investors are also exit-affected interest groups that indirectly assume regulatory costs of the Restrictions. Specifically, the majority traders in Taiwan stock markets are domestic retail investors. For example, in 2007 they have accounted for around 70% of local stock market turnover.¹⁴⁸ Taiwan had a population of 23 million in 2008, among

raised by Taiwanese firms in 2004, 13% of IPOs and 60% of Secondary Public Offerings ("SPO") were done overseas; this trend accelerated. For instance, Taiwanese firms filed 40 IPO applications with HKSE in 2005 whereas there were only 17 IPO applications in Taiwan. According to Fong, this problem of listing overseas was pinpointed by a survey by McKinsey & Company that more than 200 of China-based Taiwanese firms were inclined to raise capital in Hong Kong in two or three years so as to meet their financial demand for investments in China. Fong, *supra* note 105, at 98.

¹⁴⁶ In the whole year of 2007, the benchmark of Taiwanese stocks, Taipei's Weighted Price Index, rose 8.7%, and "ranked as the second-worst performing regional market behind Japan's Nikkei Stock Average, which fell 11.1%." Chris Oliver, *Taiwan Stocks Rally after Pro-China KMT Landslide*, MARKETWATCH, Jan. 14, 2008, <http://www.marketwatch.com/story/taiwan-stocks-rally-after-pro-china-partys-election-win> (last visited Dec. 1, 2009).

¹⁴⁷ *Tai Zheng Jiao Suo Dong Shi Zhang Hu Yu Song Bang Taiwan Qi Ye Fu Da Lu Tou Zi* [Chairman of Taiwan Stock Exchange Advocates Easing Mainland-Investment Restrictions], ZHONG GUO TAIWAN WANG [CHINA TAIWAN ONLINE] (P.R.C.), May 10, 2007, http://big5.chinataiwan.org/xwzx/bwzx/200705/t20070510_371567.htm (last visited Nov. 19, 2007).

¹⁴⁸ *Platform*, *supra* note 128, at 6; James J. Kung & Wing-Keung Wong, *Efficiency of the Taiwan Stock Market*, 60 JAPANESE ECON. REV. 389, 390 (2008) (Taiwan's annual trading "drops from 89.30% in 1996 to 68.80% in 2005 for local individual investors . . .").

which as many as 8.5 million had opened securities accounts.¹⁴⁹ Since these ordinary Taiwanese citizens, as domestic retail investors, dominated Taiwan stock markets, they are an exit-affected interest group impacted severely when Taiwan-invested firms list shares overseas to avoid the Capital Controls and Constraints. In addition, before the relaxation of the Restrictions in the second half of 2008, in order to fully enforce the Capital Controls, the Taiwanese government restrained ordinary Taiwanese citizens from buying stocks listed in Mainland China, Hong Kong and Macau through stock brokers located in Taiwan. Both offshore and domestic mutual funds offered and sold in Taiwan could not invest more than 0.4% of their net asset values in stocks listed in Mainland China and 10% in stocks listed in Hong Kong and Macau.¹⁵⁰ Therefore, due to the Restrictions, Taiwanese retail investors are deprived of opportunities to directly and indirectly share the returns from these prosperous China-based Taiwanese firms as these companies do not list shares in Taiwan.¹⁵¹ Perceiving the former DPP government maintaining and even re-tightening the Capital Controls in 2006, Taiwanese retail investors could arguably join anti-regulatory groups in the March presidential election in 2008 as a strong exit-affected interest group given that they were a large percentage of voters.¹⁵² The influence of these retail

¹⁴⁹ Editorial, *Bu Jian Lu Shan Zhen Mian Mu, Zhi Yuan Shen Zai Ci Shan Zhong—Zong Ti Jing Ji Zhi Biao VS. “Shu Min Jing Ji” Zhi Biao* [A Layperson Could Hardly Understand Macro-Indexes—On the Indexes of Macroeconomics VS. the Reference of the “Grassroots Economy”], GONG SHANG SHI BAO [INDUSTRY & BUS. TIMES] (Taiwan), Sep. 21, 2009, at A2.

¹⁵⁰ Chang Kao & Cheng-Hsu Wang, *Liang An Guan Xi De Hui Gu Xin Qing Shi Yu Qian Zhan* [The Review, New Circumstances and Foresight of Cross-Strait Relationship], 9 YUAN JING JI JIN HUI JI KAN [PROSPECT Q.] (ISSUE 3) 167, 188 (2008) (Taiwan); Jing Wai Ji Jin Tou Zi Gang Gu Xian Zhi Wan Quan Qu Xiao Zheng Yuan Tong Guo [The Executive Yuan Lifted the Bans on Offshore Mutual Funds’ Investing in Stocks Listed in Hong Kong], FA YUAN FA LU XIN WEN [LAWBANK’S L. NEWS] (Taiwan), July 4, 2008, http://www.lawbank.com.tw/fnews/news.php?keyword=%B9%D2%A5%7E%B0%F2%AA%F7%A7%EB%B8%EA%B4%E4%AA%D1%AD%AD%A8%EE%A7%B9%A5%FE%A8%FA%AE%F8&sdate=&edate=&type_id=1,10,19,20,21,22&total=1&nid=61411.00&seq=1 (last visited Dec. 1, 2009).

¹⁵¹ Chou, *supra* note 81, at 118; Editorial, *He Jian An Zui Da Shu Jia Shi Zheng Fu* [The Biggest Loser in the UMC Case is Taiwan’s Government], ZHONG GUO SHI BAO [CHINA TIMES] (Taiwan), Oct. 28, 2007, at A2 (reporting that the Restrictions compelled Taiwanese firms to delist from Taiwan and list shares in Hong Kong, that the Capital Controls led offshore mutual funds to retreat from Taiwan, and that for the last three years 23 offshore mutual funds have left Taiwan such that products of investment Taiwanese investors can choose turned fewer).

¹⁵² After the legislature election on the weekend in January 2008 in which the then-opposition party KMT won a landslide victory, Taiwanese stocks climbed sharply by 1.8%, or 144.1 points to 8,173.41 immediately on Monday.

investors¹⁵³, who should have benefited from Taiwan-invested corporations' local listings, might help explain the interest group competition on the supply side within Taiwan's political marketplace.

In consequence, the Restrictions not only forced Taiwanese companies with substantial investment in China to list their shares abroad, mostly on HKSE, to raise capital for investments in Mainland China, but also discouraged many China-based Taiwanese businesses not yet doing their IPOs from listing stocks back at home. Wave upon wave of leading large conglomerates in Taiwan like Hon Hai decided to have their business substantially based in China exit from Taiwan. This physical exit substantially undermined Taiwan's reputation as an investment

The news report from MarketWatch said:

"The election signals *a reordering of national priorities toward growth and commercial prospects, and away from idealistic issues such as national identity*," said Bear Stearns strategist Michael Kurtz in a research note Monday.

Saturday's result saw the Kuomintang take 81 seats with 51.3% of the popular vote while the Democratic Progressive Party held on to 27 seats, with a 36.9% share of the vote.

Taiwanese President Chen Shui-bian stepped down as chairman of the DPP hours after the results were announced. A key pillar of Chen's administration had been Taiwan's independence from China.

....
"With the KMT in power *investors in general* feel that the policies will be more turning towards collaboration with China," [Pauline Dan, a fund manager with MFC Global Investment Management,] said, adding *the KMT was likely poised to win the upcoming presidential elections*.

....
Analyst said the DPP's thrashing at the polls and subsequent resignation of Chen will likely inspire *a shift in the party's strategy towards economic and environmental issues to win back voters. A softer approach by the DPP would like mean fewer political flare-ups between Beijing and Taipei regardless of who's in power*.

"The DPP will attempt to rebrand itself in the future as a more moderate party, which . . . could shift Taiwan's entire political center of gravity rightward," Bear Stearns' Kurtz.

Oliver, *supra* note 146 (emphasis added) (alteration in original). This quote could to some extent imply that investors in general, a large percentage of which are the retail investors, show their confidence in KMT's potential victory in the March presidential election with the rise of the stock market index, and that retail investors as an exit-affect interest group may probably join anti-regulatory interest groups to push for the moderation of the Capital Controls in the arena of the presidential election.

¹⁵³ To illustrate their influence in another context, in early August 2007 when the U.S. financial crisis had just started, as Taipei's Weighted Price Index was also negatively impacted and thus plunged by around 10%, it is argued that the pressure from retail investors was so great that Taiwan's government was pushed to intervene in the stock market by buying stocks with money from public pension and retirement funds, insurance funds and deposit funds of post offices, in order to stop the drop. Editorial, *Cong Liang Jian Shi Kan Zheng Fu Shi Zheng Pin Zhi* [Observing the Quality of the Government Administration in Light of Two Incidents], GONG SHANG SHI BAO [INDUSTRY & BUS. TIMES] (Taiwan), Aug. 6, 2007, at A2.

environment. Afterwards many foreign investors, direct or indirect, gradually lost their confidence in Taiwan's markets and exited as well. The physical exit and threats of exit bolstered the voice rights of anti-regulatory and exit-affected interest groups, thus helping them dominate the arena especially in the March presidential election in 2008. This can be evidenced by the fact that prior to the presidential election, candidates from both major parties similarly suggested in the second half of 2007 that the Capital Controls should be relaxed.¹⁵⁴ As Coates explains why SOX was then enacted, “[i]n a democracy in which most voters own stock either directly or indirectly through their pension and retirement funds, government was certain to react. The only question was the shape the reaction would take.”¹⁵⁵ Similarly in Taiwan, since the Restrictions substantially adversely impacted Taiwan stock markets, the pressure on politicians of both parties to lighten the Restrictions—especially from a huge number of retail investors as an exit-affected interest group—was so great that maintaining the Restrictions was not an option. In other words, it is likely that anti-regulatory and exit-affected interest groups' voice rights strengthened by exit were successfully exercised to push presidential candidates from both camps to advocate the easing of the Capital Controls. Therefore, because of these firms' continuous exit from local markets, Taiwan, under the decisive interest group competition over whether to deregulate, experienced a radical change of political power in the first half of 2008 as Chang-Ting Xie (Frank Hsieh), from the former President Chen's own DPP, was defeated while President Ying-Jeou Ma of KMT, advocating anti-regulatory and pro-China policies, won the presidential election. An editorial in the *China Times*, a major Taiwanese newspaper, argued that when in power in Taiwan, the more proactively the former DPP government intended to contain Taiwan's outward investment in Mainland China, the more sophisticated tactics these firms would take to

¹⁵⁴ Chou, *supra* note 81, at 3-4.

¹⁵⁵ John C. Coates, *The Goals and Promise of the Sarbanes–Oxley Act*, 21 J. ECON. PERSP. 91, 91 (2007).

evade the Capital Controls while investing more in Mainland China, and that since the DPP government overlooked the voice for relaxation of the Capital Controls from KMT and the business community, Taiwanese citizens just voted out DPP to say no to the re-tightened regulation in 2006.¹⁵⁶ Apparently, pro-regulatory interest groups in Taiwan failed. Immediate relaxation of the Restrictions was under way.¹⁵⁷

3. Ensuing Liberalization

President Ma in his interview on June 18, 2008 by New York Times and The International Herald Tribune said:

There are so many Taiwanese businesspeople around the area [who] now keep their money out of Taiwan. You know, in the last five, four years, many Taiwanese companies went

¹⁵⁶ Editorial, *Min Jin Dang Hai Yao Bu Yao Chong Fan Zhi Zheng?* [Does DPP Want to Come Back into Power?], ZHONG GUO SHI BAO [CHINA TIMES] (Taiwan), Apr. 13, 2009, available at <http://news.chinatimes.com/2007Cti/2007Cti-News/2007Cti-News-Content/0,4521,11051402+112009041300109,00.html>.

¹⁵⁷ Lin Lin, *Mei Bao: Shi Xian Xuan Zhan Cheng Nuo Ma Ying-Jeou Jiang Mian Lin Zhong Da Tiao Zhan* [Wall Street Journal: To Implement His Promise during the Campaign President Ma Will Face Major Challenges], ZHONG YANG SHE JI SHI XIN WEN [CENTRAL NEWS AGENCY NEWS], Mar. 23, 2008, <http://tw.news.yahoo.com/article/url/d/a/080324/5/vxu.html> (last visited Mar. 23, 2008). As Bradsher reports,

President Ma Ying-jeou of Taiwan called on Wednesday for a rapid expansion of economic relations between Taiwan and mainland China over the next year or two. . . . Mr. Ma said he wanted broad access to the mainland market for Taiwanese financial services businesses, an end to double taxation by government agencies in Taipei and Beijing and *the removal of investment restrictions*. . . . Mr. Ma led his Nationalist Party to a decisive victory in the March elections, prevailing over a candidate warier of closer ties with mainland China. Mr. Ma had promised to strengthen the Taiwanese economy through reconciliation

Keith Bradsher & Edward Wong, *Taiwan's Leader Outlines His Policy toward China*, N.Y. TIMES, June 19, 2008, available at http://www.nytimes.com/2008/06/19/world/asia/19taiwan.html?_r=1&sq=China%20Taiwan&st=cse&oref=slogin&cp=4&pagewanted=print (emphasis added). Hui-Ru Zhou, *Ma Xiao Xin Zheng—Fan Suo Guo Jing Ji Wei Wang* [President Ma's New Deal: Stop Closing Taiwan to Cross-Strait Exchanges and the Economy Is the King], DA LU TAI SHANG 1000 DA: LIANG AN HE PING SHENG SHI TAI SHANG DA FU HUO [TOP 1000 OF CHINA-BASED TAIWANESE FIRMS: CROSS-STRAIT PEACE RISES AND TAIWANESE BUSINESSES WILL THRIVE AGAIN], June 6, 2008, at 42 (Taiwan) (arguing that in the 2008 presidential election Ying-Jeou Ma of KMT won more than half of the votes, which showed that relaxation of regulation on cross-Strait trade and investment was expected by most people in Taiwan).

public on Hong Kong's stock exchange. More than 60 of them. Large companies. Without even thinking about coming back to Taiwan. Some even left Taiwan's stock market to invest in the mainland. So that was really, you know, very bad for Taiwan. Now, we certainly want to change that. We want to attract more foreign capital, and capital of [locally-based] companies that have made billions of dollars on the Chinese mainland.¹⁵⁸

Therefore, the KMT government started a series of relaxations of the Capital Controls and Constraints. First, MOEA revamped the Capital Controls, mainly Point 3 of the Principles, to loosen the upper limit of investment in China from 40 % to 60% of a corporation's net worth. Furthermore, if a corporation is qualified by MOEA to be a subsidiary of a Multi-National Enterprise or to establish its headquarter in Taiwan, there will be no upper limit for this corporation. Responding to the large-scale relaxation of the Capital Controls, the FSC revised the Constraints as follows:

- (1) Article 7 of Regulations Governing the Offering and Issuance of Securities by Securities Issuers is revised so that Taiwanese issuers are allowed to directly or indirectly invest up to 60 % of capital raised in Taiwan stock markets in Mainland China.
- (2) According to the revised Capital Controls the FSC declared that public Taiwanese companies can use up to 60% capital raised through each private placement, no matter whether located in Taiwan or overseas, for investments in Mainland China.¹⁵⁹
- (3) Subsequent to the revision of Article 9 of Regulations Governing the Offering and Issuance of Overseas Securities, funds raised from the issuance of securities in overseas stock markets in each offering are all allowed to be used for direct or indirect investments in Mainland China despite the upper limit, 60% of net worth.
- (4) After Regulations Governing the Offering and Issuance of Securities by Foreign Securities Issuers are revised, funds raised in Taiwan stock markets by foreign issuers can all be used for investments in Mainland China. Hence, a parent company in Taiwan such as Hon Hai can, as they see fit themselves, invest in Mainland China through its foreign subsidiary like FIH which is incorporated in the Caymans Islands. In another word, a Taiwanese parent company

¹⁵⁸ *An Interview With President Ma Ying-jeou*, N.Y. TIMES, June 19, 2008, available at <http://www.nytimes.com/2008/06/19/world/asia/19taiwan-interview.html?ref=asia>.

¹⁵⁹ *Placements*, *supra* note 48.

can first establish a holding company in an OFC and have this offshore company list shares in Taiwan stock markets. Since this offshore subsidiary or affiliate is a foreign issuer, the capital raised by this offshore company is not subject to the Capital Controls and can all be used for investments in China.¹⁶⁰

These measures seemed to have broadcast messages of liberalization successfully. Hon Hai thus started to take into account founding its Asian logistics hub in southern Taiwan, and having its subsidiary FIH (already listing shares on HKSE) list its TDRs back in Taiwan.¹⁶¹ The FSC added that, by October 2008, 54 China-based Taiwanese businesses expressed their intense willingness to list their shares or TDRs in Taiwan. 30 of these firms planned to cross-list on TWSE by issuing TDRs while the rest 24 of them intended to do primary-listings by directly listing shares in Taiwan's OTC market.¹⁶² Accordingly, more and more Taiwanese firms already incorporated overseas and listing shares in China or Hong Kong began to contemplate listing shares back in Taiwan or even moving back their headquarters towards their motherland. For example, Want Want China Holdings Limited ("Want Want China"), a Taiwan-invested firm and the largest maker of rice cakes and flavored milk in China, was incorporated in the Cayman Islands, headquartered in Shanghai, and listed on HKSE in 2007. In light of the large-scale

¹⁶⁰ See Rui-Yi Zhang & Shu-Fang Zheng, *Fa Ling Song Bang Tai Gu Yue Ju Tai Shang Shang Shi Shou Xuan [With the Laws Relaxed Taiwan Stock Markets Are Turning into the First Choice for Taiwanese Firms' Listing Shares]*, GONG SHANG SHI BAO [INDUSTRY & BUS. TIMES] (Taiwan), Mar. 9, 2009, available at <http://news.chinatimes.com/CMoney/News/News-Page-content/0,4993,11050802+122009030900284,00.html>; also An-Ni Lin, *Tai Shang Ke Yi Kong Gu Ming Yi Hui Tai Shang Shi Bu Shou Deng Lu Bai Fen Zhi Liu Shi Shang Xian Xian Zhi Mian Jiao Bai Fen Zhi Er Shi Wu Ying Suo Shui [Taiwanese Firms Can List Back in Taiwan in the Name of Holding Companies, Which Is Not Subject to the 60% Upper Limit on Investment in the Mainland and the 25% Profit-seeking Enterprise Income Taxation]*, JING JI RI BAO [ECONOMICS DAILY] (Taiwan), Aug. 2, 2008, at A6.

¹⁶¹ Zong-Zhi Liu & Qiong-Yu Yan, *Hong Hai Za Qian Yi Jian Shu Wei Huan Bao Ke Ji Cheng [Hon Hai Will Spend More than 100 Billion NT Dollars on Establishing A Digital Eco-Tech City]*, ZHONG SHI DIAN ZI BAO [CHINA TIMES DAILY NEWS] (Taiwan), Aug. 7, 2008, available at <http://tw.news.yahoo.com/article/url/d/a/080807/4/noh.html>; *Hong Hai Zi Gong Si Fu Shi Kang Chou Hua Hui Tai Shang Shi [FIH Is Planning for Listing Back in Taiwan]*, ZHONG GUANG XIN WEN WANG [BCC NEWS NETWORK] (Taiwan), Aug. 6, 2008, <http://tw.news.yahoo.com/article/url/d/a/080806/1/mdl.html> (last visited Aug. 7, 2008).

¹⁶² Xiang-Zhi Xue & Zhen-Ling Peng, *Jin Guan Hui: Wu Shi Si Jia Tai Shang Fan Xiang Shang Shi [FSC: 54 Taiwan Companies Will List Back at Home]*, GONG SHANG SHI BAO [INDUSTRY & BUS. TIMES] (Taiwan), Nov. 5, 2008, available at <http://news.chinatimes.com/CMoney/News/News-Page/0,4442,content+120601+122008110500317,00.html>.

liberalization of the Restrictions, Want Want China became the first runner for listing TDRs on April 28, 2009 to back up the Ma administration's regulatory transition to more legal flexibility.¹⁶³ In addition, Natural Beauty, a franchise chain of cosmetics originating in Taiwan, headed towards China to develop the Chinese market more than a decade ago and listed its shares in Hong Kong in 2002. Nevertheless, Natural Beauty returned to Taiwan to set up its global headquarters in Taipei on November 25, 2008.¹⁶⁴ Under the cluster effect of industries, foreign firms attempting to carve out their business in Mainland China may follow Taiwan-invested firms' steps, and the inflows of FDI into Taiwan may be in an upsurge again.¹⁶⁵ Consequently, accounting, legal services and other industries or markets supporting capital markets and local corporate headquarters would be thriving again.

Finally, according to a study by Jia-Ke Hung and Chen-Yuan Tung, before the large-scale lightening of the Capital Controls in 2008, the Capital Controls drove TDI in China to change into underground economic activity by circuitously transferring Taiwanese funds to corporations registered in OFCs such as the Cayman Islands and BVI and later investing these funds in China.

¹⁶³ Zong-Tong Wang, *Hui Tai Gua Pai Shang Shi Zhong Guo Wang Wang Qiang Tou Xiang* [Want Want China Is the First Runner to Be Listed Back in Taiwan], ZHONG GUO SHI BAO [CHINA TIMES] (Taiwan), Apr. 1, 2009, available at <http://news.chinatimes.com/2007Cti/2007Cti-News/2007Cti-News-Content/0,4521,5010502+112009040100345,00.html>; Hong-Hui Guo, *Zhong Guo Wang Wang TDR Jin Zheng Shi Shang Shi!* [Want Want China Is Listing Its TDRs Today!], ZHONG SHI DIAN ZI BAO [CHINA TIMES DAILY NEWS] (Taiwan), Apr. 28, 2009, available at <http://news.chinatimes.com/2007Cti/2007Cti-News/2007Cti-News-Content/0,4521,5010860+132009042800566,00.html>.

¹⁶⁴ Li-Man Li, *Cai Yan Ping Hui Tai She Quan Qiu Zong Bu* [The Founder of Natural Beauty Is Going Home to Set Up the Global Headquarter], GONG SHANG SHI BAO [INDUSTRY & BUS. TIMES] (Taiwan), Nov. 19, 2008, available at <http://news.chinatimes.com/CMoney/News/News-Page/0,4442,content+120601+122008111900387,00.html>.

¹⁶⁵ See, e.g., Mo-Yun Wang, *Hu Di Wen: Liang An Reng Xu Jia Kuai Kai Fang Jiao Bu* [Bayer's Head in Taiwan Branch: Deregulation of Taiwan's Cross-Strait Policy Should Be Accelerated], ZHONG GUO SHI BAO [CHINA TIMES] (Taiwan), Oct. 9, 2008, available at <http://news.chinatimes.com/2007Cti/2007Cti-News/2007Cti-News-Content/0,4521,110507+112008100900035,00.html> (last visited Oct. 13, 2008) (reporting that the board chairman of the Taiwanese subsidiary of Bayer, a German chemical and pharmaceutical company, expressed that even though there is a global economic downturn, Bayer promises to establish two major R & D centers in Taiwan, given that teaming up with Taiwanese firms Bayer can process orders in Taiwan while final products can be manufactured in Mainland China and Vietnam and shipped from there).

These funds were not indentified by both Taiwanese and Chinese officials as TDI.¹⁶⁶ From 1979 to 2008, if these funds transited via the Cayman Islands and BVI were recognized as TDI in China, Taiwanese capital would be estimated to be approximately \$122.285 billion, which is 14.34% of total FDI in China as well as the second largest FDI inflow to China (FDI from Hong Kong and Macau still ranked as the top one), even though TDI at face value in the same period is indentified as the fifth largest FDI (the top four in order: Hong Kong and Macau, BVI, Japan, and the U.S.) according to Chinese statistics.¹⁶⁷ This number of TDI in China (\$122.285 billion) has so far been recognized by many Chinese and Taiwanese scholars as the closest to the reality.¹⁶⁸

On the other hand, according to FDI statistics made public on Sep. 15, 2009 by PRC's Ministry of Commerce, as the Capital Controls are largely relaxed in the second half of 2008, TDI at face value climbed from the ninth largest FDI inflow to China in 2008 to the second largest (only second to Hong Kong) in the period of January-August 2009, without the inclusion of Taiwanese funds circuitously through those OFCs. Also, in the same period, FDI from OFCs including BVI, the Cayman Islands, Samoa, Mauritius and so forth turned out to be out of top 10 FDI inflows to China. Although OFCs' lower ranking was possibly owing to the fact that PRC's tax authorities recently strengthened their investigation of tax evasion via OFCs, it was more

¹⁶⁶ Jia-Ke Hung & Chen-Yuan Tung, *Tai Shang Dui Zhong Guo Jing Ji Fa Zhan De Gong Xian: 1999-2008 Nian* [Contributions of Taiwan Businesspeople towards the Economic Development of China: 1988-2008], Address at Symposium of the Center for China Studies, National Chengchi University, Taipei, Taiwan: *Tai Shang Da Lu Tou Zi Er Shi Nian: Jing Yan Fa Zhan Yu Qian Zhan* [Taiwan Businesspeople Invested in China for Two Decades: Experience, Development & Foresight] 5-6 (Oct. 3-4, 2009) (on file with author).

¹⁶⁷ *Id.* at 7-8.

¹⁶⁸ Wen-Hui Li, *Zi Xun Bu Ming Zao Cheng Yan Jiu Kun Nan* [The Insufficiency of Information Creates Difficulties over Research], *ZHONG GUO SHI BAO* [CHINA TIMES] (Taiwan), Oct. 23, 2009, available at <http://news.chinatimes.com/2007Cti/2007Cti-News/2007Cti-News-Content/0,4521,50501637+112009102300154,00.html>; Wen-Hui Li, *Xue Zhe Yan Jiu Tai Shang Dui Lu Gong Xian Du Pai Di Er* [According to the Scholar's Study Taiwan Is Ranked as the Second Largest FDI in China], *ZHONG GUO SHI BAO* [CHINA TIMES] (Taiwan), Oct. 23, 2009, available at <http://news.chinatimes.com/2007Cti/2007Cti-News/2007Cti-News-Content/0,4521,50501637+112009102300150,0.html>.

likely that the liberalization of the Capital Controls started in the second half of 2008 substantially removed Taiwanese firms' incentives to indirectly invest in China via OFCs such as BVI and the Cayman Islands, which thus galvanized the considerable increase of TDI in China at face value.¹⁶⁹ The above evidence explicates that the Capital Controls enforced from 1997 to 2008 cannot overcome the market reality that Taiwanese firms' vigorous business demands rendered themselves the second largest FDI inflow to China from a perspective of substance, and that Taiwanese capital emerging from underground thanks to the relaxation in question largely narrowed the gap between official estimation and Taiwanese firms' real investment value to China.

C. Summary

The economic and political entanglement between Taiwan and China provides rich materials for examining the interaction between the state and business in the era of globalization. Leng argues: "Cross-Taiwan Straits economic interaction is a political as well as an economic issue. General trends of economic interdependence and globalization that are weakening the role of the nation state should promote a focus of shared 'civilian governance' between Taiwan and mainland China."¹⁷⁰ As Leng adds,

[f]rom the political perspective, however, rivalry across the Taiwan Straits in the past decades forces the Taiwanese state to intervene in economic transactions. Attempts to guarantee "economic security" and a web of national security have been in great debate since Taiwan opened trade links with mainland China in 1987. However, experiences in the past decade show that economic globalization has made traditional methods of economic regulation and constraint policies invalid. . . . National security considerations

¹⁶⁹ Zhang-Rong Kang, *Taiwan Jin Nian Yue Sheng Ya Jun* [*Taiwan Rises to the Runner-up this Year*], GONG SHANG SHI BAO [INDUSTRY & BUS. TIMES] (Taiwan), Sep. 16, 2009, available at <http://news.chinatimes.com/CMoney/News/News-Page-content/0,4993,11050706+122009091600245,00.html>.

¹⁷⁰ Leng, *supra* note 50, at 261

have always been of serious concern for Taiwan in managing cross-Straits economic relations. As Taiwan's economic development becomes more dependent on the mainland market, the Taiwanese state perceives rising pressures to accommodate *business interest* and political quests of autonomy. On the other hand, recent trends of economic globalization further weaken the regulatory capacities of national states and introduce external factors such as World Trade Organization (WTO) to institutionalize normal economic relations with Mainland China.¹⁷¹

To tentatively summarize, the removal of trade barriers for Taiwan's and China's joining the WTO in 2002 ("the institutionalized force of globalization")¹⁷² combined with the capital mobility enhanced by the "denationalization of financial capital"¹⁷³ could exert transformative pressures on Taiwan's government to seek progressive deregulation of the Capital Controls to meet business demands created under the power of economic globalization.

Let's return to the conundrum confronted by MOEA. Why does MOEA run into such high difficulties in enforcing the Capital Controls? We might find the answer from international jurisdictional competition prompted by globalization. In theory, as regards underlying factors spurring jurisdictional competition in a global setting, as Macey argues,

increased competition, specifically increased global competition among private sector actors, makes it difficult or impossible for administrative agencies [in regulatory jurisdictions] unilaterally to regulate national firms. . . . This increased competition is caused by a number of factors. Technological change and greater efficiencies in transportation networks have increased global competition by making it easier for distant companies to compete with local businesses. Similar market advances have made it easier for local manufacturers and service providers to engage in regulatory arbitrage [especially via OFCs] by moving their operations overseas. These developments [regarding the evolvement for firms to become

¹⁷¹ *Id.* at 261-62 (footnote omitted) (emphasis added).

¹⁷² *Id.* at 262.

¹⁷³ See Dignam & Galanis, *supra* note 41, at 217 (discussing that "with the denationalization of financial capital, significant constraints have been imposed on national authorities' discretion to formulate macroeconomic policies," and that "global financial integration has led to a loss of national autonomy, at least in the sphere of macroeconomic policy making").

MNCs] have had a direct effect on regulators, because they have made it easier for firms [with the capability of international planning and management] to mitigate the effects of unwanted regulation or to avoid such regulation altogether by moving their activities beyond the jurisdiction of the regulator that has promulgated the unwanted regulation.¹⁷⁴

In short, under globalization, the increase of international production factor mobility and technological improvement lowers firms' exit cost, arms firms with the ability of international operation, and then intensifies the international jurisdictional competition for mobile factors. Out-flowing capital and firms as well as emigrating labor would thus compel regulatory jurisdictions to improve on the quality of their regulations.

In the Taiwan case, the change in the Capital Controls reveals the dynamics of international jurisdictional competition among global legal centers, or the demand and supply forces underlying the international law market at work. The Capital Controls promulgated by the executive branch of the government, specifically MOEA, are evidently excessive and against business demands, so that China-based Taiwanese firms turn to other regulatory jurisdictions to satisfy their demands for legal flexibility. The international jurisdictional competition for corporate charters, listings and other local economic activity among global legal centers emerges under the influence of globalization and firm or capital mobility bettered by technologic and transportation advances. Since there are a variety of suppliers, e.g. the Cayman Islands (for corporate charters and relevant financial services) or Hong Kong (for listings), of alternative regulatory products without being subject to the Capital Controls, these Taiwanese MNCs could attempt regulatory arbitrage. At this time although Taiwan's government agencies, knowing futility of acting unilaterally, intend to look for regulatory cooperation, or "regulatory

¹⁷⁴ Jonathan R. Macey, *Regulatory Globalization as a Response to Regulatory Competition*, 52 EMORY L. J. 1353, 1355 (2003) (alteration in original).

globalization,”¹⁷⁵ to enforce the Capital Controls, those competing jurisdictions have no reasons to help Taiwan’s agencies to enforce the Capital Controls, given their own markets for those prosperous China-based Taiwanese firms and that Taiwan has no bargaining chips for coordination. In consequence, economic globalization resulting from technological change, market processes, and other exogenous variables deprives Taiwan’s government of the power to act alone. Discovering these firms’ continuous “exits” from local markets, Taiwan, under the interest group competition to “voice” the petition for liberalization, experiences a radical change of political power in 2008 particularly as President Ma of KMT, advocating anti-regulatory and pro-China policies, wins the presidential election. Large-scale relaxation of the Capital Controls is subsequently launched in a timely manner.

IV. COMPARISONS BETWEEN THE PHENOMENA OF THE U.S. AND TAIWAN

A. Differences

What implications can we derive from the cross-listing competition in the SOX case discussed in Section II.C and the primary-listing competition in the Taiwan case? Before comparing the actual scope of loosening the regulation in both cases, some might suppose that there should be certain differences to the extent that cross-listing markets in SOX’s case should

¹⁷⁵ As Macey argues,

regulatory globalization is a competitive response employed by administrative agencies when they perceive a threat to their power. Where exogenous technological forces threaten to make an agency acting alone obsolete or irrelevant, a natural response is regulatory globalization. In short, when regulated firms attempt a “divide and conquer” strategy of isolating regulators and engaging in regulatory arbitrage, regulators have little choice but to band together and offer a coordinated response.

Id. at 1377. See also Leng, *supra* note 49, at 35, 38; John Whalley, *Globalisation and Values*, 31 *WORLD ECON.* 1503, 1513 (2008), available at <http://ssrn.com/abstract=1288887> (arguing that “[t]o political scientists, globalisation suggests global political processes in which there are challenges to national authority structures as mobility across nations accelerates and transfer of nation state functions to supra-national authorities occurs. It leads to evaluation of transnational political processes, assessments of constraints on the autonomy of national authorities . . .”).

impose more discipline upon U.S. government than primary-listing markets in the Greater Chinese Economy upon Taiwan's government. They might advance the hypothesis that it would be easier for cross-listing firms to exit from U.S. markets than Taiwanese firms to exit from their home country. Accordingly, global cross-listing markets would, in theory, exercise more discipline on US government than primary listing markets in Taiwan's case upon Taiwan's government, in that costs of foreign issuers' exiting from US markets are lower than those of Taiwanese firms' exiting from Taiwan's stock markets, and that the mobility of foreign firms in SOX's case is thus higher than Taiwanese firms'. Nevertheless, the truth is that the SEC merely makes partial exemptions for foreign firms and even fewer substantive changes for domestic issuers whereas Taiwan's government makes such a large-scale substantive change on the Capital Controls and Constraints. Therefore it seems that the above hypothesis is wrong. Why?

We might come forward with the following explanations. First, as Hart argues, the best explanation to enact SOX is "that the pressure on politicians to act—from the public, interest groups, and the politicians themselves—was so great that nonintervention was not an option."¹⁷⁶ The U.S. thus has a stronger need to regulate domestic firms than foreign firms to react to corporate catastrophes like Enron's. With respect to the regulatory necessity, cross-listing firms are not as important as domestic firms. Therefore, in order to retain or attract back foreign issuers, the U.S. government is willing to supply foreign issuers with some exemptions while maintaining the intensity of the regulation on domestic issuers.

Second, even if many Taiwan-invested firms are incorporated overseas, their direct or indirect equity owners are mostly still Taiwanese who generally have stronger voice in Taiwan's

¹⁷⁶ Oliver Hart, *Regulation and Sarbanes-Oxley*, 47 J. ACCT. RES. 437, 444 (2009).

political marketplace than foreign issuers in the U.S. politics. Therefore, foreign issuers could pressure the SEC to exempt them from some SOX mandates merely via their exit and weaker voice in the U.S., whereas Taiwanese firms can exert greater pressure on Taiwan's government in the legislature and especially in the presidential election in 2008 to liberalize the Restrictions on a large scale. This is largely because Taiwanese firms' mobility via listing shares overseas might motivate a strong exit-affected interest group, local retail investors, to join anti-regulatory interest groups, especially in the March presidential election in 2008.¹⁷⁷ This probably drove the presidential election candidates from both major parties to countenance the petition that the Capital Controls should be further relaxed. Put simply, the Restrictions deterring Taiwanese firms from making significant local investments and listing shares at home trigger a larger local

¹⁷⁷ Immediately subsequent to KMT's landslide victory of the legislature election in January 2008, stock analysts indicated that "[w]ith the KMT in power investors in general feel that the policies will be more turning towards collaboration with China," and that "the KMT was likely poised to win the upcoming presidential elections." Oliver, *supra* note 146. This might, as discussed above, suggest that the Capital Controls were so against general investors' interests as to tilt to KMT their potential support for the triumph of the prospective presidential election in March 2008. Also, after President Ma was sworn in May 2008, Horng-Ming Tsai, the Vice Secretary General of CNFI (one of the two major Taiwanese chambers of commerce), was invited to accept the honorary position of Advisor of National Security Council and then became an adviser to President Ma. See Fong-Ying Chen, *Gao Charng Tsai Horng-Ming Ru Lie Deng Lu Song Bang You Wang [With Charng Gao and Horng-Ming Tsai Joining the Ma Administration Bans on Investment in China Are Expected to Be Lifted]*, ZHONG GUO SHI BAO [CHINA TIMES] (Taiwan), May. 12, 2008, available at <http://news.chinatimes.com/2007Cti/2007Cti-News/2007Cti-News-Content/0,4521,110501+112008051200058,00.html>; Ci-Ti Cui, *Guo An Hui Zi Wei Tsai Horng-Ming Ci Zhi Tsai Wei Chan Ye Jie Zai Guo An Hui De Wei Yi Dai Biao Shi Fou Yin Fa Gu Pai Xiao Ying Bei Shou Guan Zhu [Horng-Ming Tsai Resigns His Commission as Advisor of National Security Council; Given Tsai Is the Only Representative from the Business Community in that Council Whether His Resignation Will Bring About A Domino Effect Deserves to Be Watched]*, GONG SHANG SHI BAO [INDUSTRY & BUS. TIMES] (Taiwan), Aug. 24, 2009, at A2. Before KMT won the presidential election, Mr. Tsai had written many articles to advocate the relaxation of the Capital Controls, which resonated with CNFI's consistent petition. Given that Tsai engaged the service of the close advisor to President Ma after the election, it might, at least partially, be argued that before the election the Capital Controls would prompt businesses to shift to KMT in terms of support such as campaign contributions or endorsements. More importantly, the endorsement from the business community for Ma's bid for presidency might be confirmed by the fact that when Mr. Ma attended the Conference of Chairpersons of Taiwanese Chambers of Commerce in China, most attendant China-based Taiwanese businessmen publicly expressed their support to KMT and Mr. Ma in the presidential election. See *Min Jin Dang Guang Shuo Bu Zuo Tai Shang Qun Qi Ting Lan [DPP Only Pays Lip Service without Any Actual Action; Taiwanese Businessmen Altogether Support KMT]*, ZHONG GUO PING LUN XIN WEN [CHINA REVIEW NEWS] (P.R.C.), June 4, 2007 <http://www.chinareviewnews.com/doc/1003/8/1/4/100381470.html?coluid=7&kindid=0&docid=100381470> (last visited Dec. 3, 2009) (reporting that even if both Mr. Ma and Mr. Hsieh advanced the similar policy to open up cross-strait exchange, most Taiwanese businessmen said they did not trust the latter and DPP, but believed that the victory of the former and KMT would really help them out).

political backlash against the regulation than in SOX's case.

Third, as compared with Taiwan, the U.S. is a much larger and richer country and has a more captive market that local interest groups can exploit, in part, by lobbying to assure the maintenance of regulatory intensity on domestic issuers.¹⁷⁸ Meanwhile, domestic firms more tied to the U.S. market are more stuck in their home country and thus less mobile than foreign firms, because the former rely more on listing shares in the U.S. stock markets to develop or keep their reputation for local business¹⁷⁹ whereas the latter can just exit and go public in other markets such as LSE. The U.S. political jurisdiction can thus enforce her laws against domestic firms that have higher costs of exit. Put somewhat differently, domestic firms would be less willing than foreign issuers to incur the costs of listing shares outside the United States. Conversely, cross-listing firms are less locally based and more likely to be listed somewhere except the U.S. stock markets. Since foreign issuers are less tied in the U.S. captive market and have greater ability to expatriate than domestic firms, they are relatively less burdened by the costs of shopping for laws in the global cross-listing markets.

By contrast, Taiwan has been an economy heavily relying on foreign trade and investment, without a comparably captive market as the U.S. does to keep domestic firms home and even lure foreign issuers from elsewhere. Because, to Taiwanese and foreign firms with the intent and

¹⁷⁸ There is an analogous discussion under the U.S. Federalism by O'Hara and Ribstein:

The discipline that mobility exerts on state politicians depends on the benefits states can offer firms to offset bad laws. The more desirable a location is because of its non-law attributes such as its labor pool, its extensive consumer market, or its plentiful natural resources, the more it can get away with harsh regulations promoted by local interest groups. We would therefore expect large and rich states like California to be less responsive to the law market than small states like Delaware. In short, physical mobility works to enhance, but not to guarantee, the enforcement of choice-of-law clauses.

O'HARA & RIBSTEIN, *supra* note 13, at 68

¹⁷⁹ See BUTLER & RIBSTEIN, *supra* note 7, at 74.

need to invest in China, Taiwan's local markets are not as attractive as broader markets in China, Taiwan-invested firms that are mobile enough are more incentivized to exit from Taiwan so as to evade the Capital Controls and Constraints. In order to react to these firms' continuous exodus, Taiwan's government is pressured to lighten the Restrictions significantly. Therefore, this demonstrates that primary-listing markets in Taiwan's case impose more discipline than cross-listing markets in SOX's case.

Nonetheless, globalization promotes mobility of capital and talent, or of firms, and then reduces their costs of exit from a country. This in turn helps materialize the rise of international jurisdictional competition, or international law market. What implications can we gather from this phenomenon? We can observe a lesson from a perspective of business strategy. Mihir Desai argued:¹⁸⁰

Following the uproar over Stanley Works proposed move to Bermuda, for example, the United States enacted legislation that limits the ability of U.S. firms to change their legal domicile. . . . Such efforts may work in the short run for very large countries. They will likely fail for smaller countries that cannot censure companies by withholding government contracts. And they will surely fail in the long run as the global market for corporate control can circumvent local efforts to retain ownership. In other words, saying an American corporation can't leave for Bermuda is a recipe for a foreign acquirer to buy the American firm and achieve the same result in other ways.

Therefore, in the long run, whether jurisdictions are large countries and possess local captive markets or not, they are treated equally by law market forces underlying international jurisdictional competition. That is, if their regulation on firms is over-burdensome, they would all be disciplined the by international law market and then pressured to moderate the excessive

¹⁸⁰ Mihir A. Desai, *The Decentering of the Global Firm*, 32 WORLD ECON. 1271, 1282 (2009).

regulation to some degree.

B. Similarities

As for how the law market operates, O’Hara and Ribstein argue:

Our analysis of the market for law begins with the role of party mobility in producing a kind of market for public goods, or government services. We then extend that market concept to consider markets for law, in which people select among given packages of legal rules, and, in turn, these selections also help shape the laws that states offer.¹⁸¹

International jurisdictional competition of securities regulation in both cases of the U.S. and Taiwan similarly illustrates the above market for law in action.

In the case of SOX, jurisdictional competition in securities regulation is through cross-listing markets—that is, listing ADRs on American stock exchanges outside their home country. As Ribstein & O’Hara discuss,

The demand side of this market consists of [FPIs] that seek to “bond” their disclosures by willingly subjecting themselves to tight U.S. disclosure standards and fraud rules [or the regulation provided by other advanced markets such as LSE]. On the supply side, interest groups in cross-listing countries, including lawyers, accountants, and investment bankers, get significant benefits from cross-listing and therefore incur costs if cross-listings dry up. This law market is quite competitive, since cross-listing firms can fairly easily avoid the United States and stay home or go to other capital markets like London if the cross-listing country raises the cost or lowers the benefit of its regulation. All of this was brought home with a thud when foreign companies started avoiding the United States after the adoption of stringent new regulation in the Sarbanes-Oxley Act.¹⁸²

In other words, FPIs take the “exit” option to respond to decline in benefit of the cross-listing

¹⁸¹ O’HARA & RIBSTEIN, *supra* note 13, at 27.

¹⁸² Ribstein & O’Hara, *supra* note 1, at 711 (alteration in original) (footnote omitted).

regulatory product created by SOX. The demand force in turn sparks the supply force within the United State. That is to say, both the anti-regulatory interest groups on behalf of FPIs and exit-affected interest groups like the U.S. law firms who are affected by the exodus of cross-listers take the “voice” option to pressure the U.S. government to partially exempt foreign issuers from U.S. law.

In the case of the Capital Controls and Constraints in Taiwan, jurisdictional competition among global legal centers occurring in the Greater Chinese Economy is through primary-listing markets—that is, listing shares for the first time on securities exchanges outside Taiwan. Due to the excessiveness of the regulation on outward investment in China, Taiwanese firms with major investment in China cannot but exit from Taiwan’s stock markets and through evasive tactics seek out a regulatory product without being subject to the Constraints, in order to raise necessary funds to meet financial demand of investments on the Mainland. On the supply side, most of these Taiwanese firms go public on HKSE primarily to “avoid” the Restrictions, rather than to “bond” their insiders by willingly subjecting themselves to seemingly a little stricter Hong Kong laws. The torrential “exit” of these Taiwanese firms could therefore activate interest group competition in Taiwan to seek the relaxation of the Restrictions. Finally, anti-regulatory interest groups arguably joined by exit-affected interest groups, mainly represented by local retail investors, successfully voice their petition for liberalization. A series of large-scale relaxation measures are thus followed subsequently.

The fact that Taiwan’s government enforces the regulation on investment in China equals wielding its local regulation against foreign companies as domestic firms turn into pseudo-foreign corporations to a degree. This scenario resembles the U.S.’s attempt to enforce its

securities regulations against foreign issuers listing in the U.S. stock markets. The similarity rests on that both Taiwan and the U.S. intend to expand their local regulation extra-territorially against corporations incorporated in a foreign jurisdiction. Nevertheless, the U.S., a global superpower with a relatively captive market that local interest groups can exploit, still confronts “difficulties in enforcing disclosure regulations against foreign firms because of problems of gathering evidence, particularly given U.S. pleading and discovery burdens. Accordingly, it must rely on foreign cooperation.”¹⁸³ On the other hand, compared with the U.S., Taiwan is a Lilliputian state and barren locale with fewer chips to bargain over the type of regulatory cooperation with Hong Kong and other OFCs such as the Cayman Islands, all of which also compete for benefits derived from corporate charters, listings and other related local economic transactions of China-based Taiwanese companies. Therefore, Taiwan certainly faces a higher difficulty of enforcement, which meanwhile highlights one of the problems created by the Capital Controls. The other problem is that, as discussed above, there is little benefit and tremendous cost to deviating from the market realities of comparative advantages generated by economic complementation between China and Taiwan under economic globalization, as well as ignoring business demands for investment in Mainland China accordingly.

V. CONCLUSION

Some might suppose that since Hong Kong is also located in the Greater Chinese Economy¹⁸⁴, why did Taiwan and Hong Kong (as a competitor against Taiwan in the

¹⁸³ Ribstein, *supra* note 6, at 108.

¹⁸⁴ Macau is also located in the Greater Chinese Economy; it is labelled as “Las Vegas in Asia” with its economy mainly based on the gambling industry. *Bo Yi Fa Zhan Ao Men Zheng Fu Cai Sha Che [Macau Government Brakes the Development of the Gambling Industry]*, JIN RI XIN WEN [NOWNEWS] (Taiwan), Oct. 13, 2009, <http://tw.news.yahoo.com/article/url/d/a/091013/17/1sw15.html> (last visited Oct. 13, 2009). As Macau is not a comparable competitor to Hong Kong and other OFCs with the institutional and regulatory architecture which is

jurisdictional competition) take different paths when faced with Mainland China? What relevant differences could account for why Hong Kong did not impose restrictions on outward investment in Mainland China similar to the Capital Controls?

First of all, as Clough puts it in terms of the cross-Strait political antagonism, “[a] trip made by President Lee Teng-hui to the United States [in June 1995], in an effort to enhance [Taiwan]’s international image, triggered the PRC’s [1995-1996] military reaction—a serious warning to the United States and Taiwan that it would not tolerate an independent state of Taiwan.”¹⁸⁵ The 1995-1996 Taiwan Strait tensions illustrate that China did not recognize Taiwan as an independent sovereign political entity and has been intimidating it with political and military forces. This political antagonism accentuated between 1995 and 1996 contributed to the imposition of the Capital Controls especially as a response to Chinese military intimidation. On the contrary, Hong Kong is subordinate to Chinese authority after re-integrated back to China in 1997. Therefore Hong Kong and China have been one country since then. It is impossible that Hong Kong would impose some restrictions similar to the Capital Controls (which is surely not allowed by China). In addition, China elected to preserve the Hong Kong law by promoting “one country, two systems” policy, and then opened its door wide open to Hong Kong corporations through the Closer Economic Partnership Agreement (CEPA, which can be seen as a Free Trade Agreement) signed in 2003.¹⁸⁶ The signing of CEPA is proved a catalyst for the recent economic upspring in Hong Kong. Through CEPA, Hong Kong wholly embraced Mainland China’s market surely without any national security concern, not to mention the imposition of the investment

indispensible in the international jurisdictional competition, the discussion here is focused on Hong Kong.

¹⁸⁵ RALPH N. CLOUGH, *COOPERATION OR CONFLICT IN THE TAIWAN STRAIT?*, at ix-x (1999) (alteration in original).

¹⁸⁶ Chien-Huei Wu, *One Country, Two Systems, and Three Memberships: Legal and Economic Integration between China and its Two SARs*, *GLOBAL JURIST* Vol. 7, Issue 3 (Advances), Art. 7., 1 (2007), available at <http://www.bepress.com/gj/vol7/iss3/art7>.

restrictions like the Capital Controls on national security grounds.

To return to the theme, as in the SOX context, the elements of the law market dynamics also apply in the international context of the Taiwan case. Specifically, Taiwanese firms' physical exit and threats of exit from Taiwan demonstrate the demand side of the law market in seeking legal flexibility, which first provokes the supply side in the international context. Further, where multiple suppliers such as Hong Kong and the Cayman Islands, by providing regulatory products of legal flexibility, participate in the international jurisdictional competition for these fleeing corporations' corporate charters, listings and other local economic transactions, the international supply force subsequently sparks the supply side in the domestic environment. That is, torrential economic exits in turn send signals to the political marketplace within Taiwan. Fugitive Taiwanese firms and those negatively affected by their exits voiced the petition for legal flexibility in the ensuing interest group competitions, which finally pressured Taiwan's government to meet business demands, or to loosen the excessive regulation. From the case study showing that Taiwanese companies' exit to elude the Restrictions brings about large-scale ease of investment limits, we can learn that the jurisdictional competition among listing markets in the Greater Chinese Economy dominated by Hong Kong responds by exit and voice to the same demand and supply consideration once again. We can thus find that just as expansion of the U.S. federal law may be constrained by an international jurisdictional competition fuelled by cross-listing,¹⁸⁷ the Taiwanese government's excessive regulation may be constrained by the jurisdictional competition fuelled by Taiwanese companies to list shares overseas.

Finally, both of the U.S. and Taiwan stories regarding international listing markets imply

¹⁸⁷ Ribstein, *supra* note 6, at 122-39.

that although somewhat disparate from the corporate law market under federalism in the U.S., there are also general law market forces at work in the international context:¹⁸⁸ The mobility of capital and talent enhanced by globalization serves as fuel to ignite and maintain the operation of international jurisdictional competition, which eventually leads to local legal changes. To conclude, both phenomena of the U.S. and Taiwan regarding listing markets tell with one accord that law market forces underlying international jurisdictional competition could provoke a change in parochial excessive regulation to a more flexible regime.

¹⁸⁸ Ribstein & O'Hara, *supra* note 1, at 710.