The Agency Problem in Taiwan's Corporate Governance

Hsiang-Yi Lin, Assistant professor ,
Department of International Business Management, Ching Yun University, Taiwan

ABSTRACT

This study discusses the meaning and internal and external mechanisms of Taiwan's corporate governance, explains why this kind of mechanism cannot prevent the agency problem, and demonstrates the importance of business ethics by looking at the flaws in Taiwan's corporate governance. Other questions addressed in this study include what limitations are in the internal and external mechanisms of Taiwan's corporate governance, what makes the agency problem seem inevitable, and whether business ethics may compensate for the shortcomings in Taiwan's corporate governance.
Keywords: *Agency Problem; Corporate Governance; Business Ethics; Taiwan's corporate governance; The Sarbanes-Oxley Act of 2002*

INTRODUCTION

From the legal perspective, Taiwan's corporate governance is comprised of the Corporation Law, the Securities Exchange Act, and the regulations specified by TWSE (Taiwan Stock Exchange) and Gre-Tai Securities Market for publicly-traded corporations. Of which, the Corporation Law is the main basis for corporate governance which clearly specifies the duties of the meeting of shareholders, the board of directors, and the supervisor in the wish of achieving complete corporate governance through the balance of power between the three systems. The Securities Exchange Act focuses on the disclosure of corporate financial information and its influences on shareholders' interests. Further, the aforementioned TWSE and Gre-Tai Securities Market may help publicly-traded corporations establish and actualize corporate governance through their contracts with them (Wu, 2004: 6-7). The internal and external mechanisms of corporate governance are briefly explained below.

Meaning of Corporate Governance

As mentioned earlier, most scholars adopt the definition of corporate governance provided by OECD, which refers to the mechanism and process of instructing, managing, and actualizing corporate managers, and protecting the interests of shareholders as well as other stakeholders by improving corporate performance. A. Shleifer & R. Vishny with Harvard University (1997) believe corporate governance involves how fund suppliers' returns can be guaranteed and how they can ensure managers would not infringe their money nor invest it in ineffective plans for selfish reasons (Shleifer & Vishny, 1997). Ye, Li, and Ke (2002) proposed that a well-designed and implemented system not only helps improve the capacity of strategic management and supervise managers' behaviors but also ensures the returns deserved by external investors and protects other stakeholders' interests. The corporate governance system stresses the use of economic and legal systems in order to reach the goals proposed by Shleifer, Vishny, and Ye et al.(Ye, Li, and Ke, 2002: 33)

The focus of corporate governance thus includes the following: (1) Corporate governance should also look after the interests of stakeholders while promoting shareholders' interests (Chen, 2004: 20), (2) corporate governance is also aimed at solving the agency problem caused by the separation of ownership and managerial control that leads to the conflicts of interest between shareholders and managers, (3) corporate governance utilizes mechanisms such as rewards, supervision, disciplines, and punishment to ensure managers would reach the goal of looking after the interests of shareholders as well as stakeholders, and (4) corporate governance reinforces company performance and managers' duties. The focus of the present study is the agency problem mentioned earlier and in the above section through the

approach of business ethics. TCGA, as mentioned in Chapter 1, believes that corporate governance is an instructive and managerial mechanism that actualizes corporate managers' duties and looks after the interests of shareholders as well as other stakeholders by reinforcing company performance. In addition, it is also the belief of TCGA that the following principles should be observed when a company establishes corporate governance: (1) observing relevant regulations, (2) protecting shareholders' interests, (3) reinforcing the structure of the board of directors, (4) utilizing the supervisor's capacity, and (5) respecting the rights of stakeholders.（TCGA）In the following the internal and external mechanisms of corporate governance are explained as an attempt for us to better understand the relationships between corporate governance and the agency problem.

The Internal Mechanism of Taiwan's Corporate Governance (1)

The internal mechanism of corporate governance has the six following purposes: reinforcing the capacity of the board of directors, expressing the capacity of the supervisor, establishing and implementing the internal control system, encouraging shareholders' participation, protecting stakeholders' interests, and reinforcing information disclosure. The six purposes are explained in better details below:

(1) Capacity of the board of directors:

The board of directors must consider its scale and the number of directors before establishing different types of functional committees and must clearly specify in its charter that the functional committees are responsible to the board of directors, and their proposals are to be reviewed by the board of directors before resolutions are reached. The members of the board of directors must be honest and avoid the conflict of interest whenever possible; when making major financial decisions, the board of directors must fully consider the comments from their auditors and/or independent directors in order to prevent corruption.

(2) The supervisor's functions:

The supervisor's duty is to monitor a corporation's daily operations, check the directors and manages for dereliction of duty, or even to authorize professional auditors or lawyers to review relevant matters that are beyond his/her power. As a result, a person who works as the supervisor must be honest and just, experienced and well-trained in his/her domain, and spend much time and energy in order to fulfill his/her duty as an independent supervisor and prevent corruptions in the company.

(3) Establishing and implementing the internal control system:

The most fundamental basis is for a company to have and faithfully implement a complete internal control system. In a publicly-traded corporation, the board of directors and managerial level should fully supervise the implementation of the company's self-evaluation as well as analyze the results of self-audits conducted by each department and prepare an internal control report. The report is not only accessed by the supervisor through relevant regulations but should also be submitted to the authority.

(4) Shareholders' participation:

The company should also encourage its shareholders to be more active and participate in the meetings held by the board of directors. Minor shareholders should also be given the right to acquire company-related information and to ask questions in a meeting held by the meeting of shareholders in order to facilitate supervision.

(5) Stakeholders' interests:

The company should value and protect the interests and rights of all of its stakeholders, including its employees, creditors, suppliers, and nearby residents. To the outside world, channels of communication between the company and external stakeholders should be kept clear; to the inside of the company, the employees should have the right to make themselves heard by their managerial levels, directors, or supervisors regarding major policies that involve their rights. A win-win situation can be achieved when collaborations between a company's internal and external stakeholders are established.

(6) Reinforcing information disclosure:

Publicly-traded corporations are supposed to obey the Corporation Law, the Securities Exchange Act, and regulations announced by TWSE and Gre-Tai Securities Market. Fully disclosed financial and business information not only allows investors, the government, and the public to clearly understand a company's internal information, but perpetrators of dishonest acts or corruptions may also be brought to justice in a timely manner. In addition, a company should have dedicated personnel who constantly gathers and discloses relevant information in order to ensure all stakeholders and shareholders may gather needed information.

The External Mechanism of Taiwan's Corporate Governance (2)

The formulation and implementation of all sorts of legal regulations and organizational systems are extremely important in order to ensure rational returns for corporate managers and stakeholders' interests. These regulations are briefly explained below:

(1) Revising the law:

The government's legislation and enforcement of law often lag behind the market's dynamics, yet the government's role becomes more important when the market does not have the needed mechanisms. Therefore, the government needs to appropriately revise the existing law in order to address illegal behaviors and fix loop holes in the market system before the corporate governance system can be improved. In addition, Corporation Law and the Securities Exchange Act that are clearly written, effectively protect shareholders' interests, and define the duties of directors and supervisors are needed in order to ensure that an auditing standard over company transactions and essential information can be formulated for the company and its auditors to follow（Ye, Li, and Ke, 2002: 64）.

(2) Functions of external professionals:

The authority is often overburdened due to the complexity of business activities and transactions; therefore, the most important external professionals for corporate governance – auditors, play an important role in this regard. For example, auditors' duties such as auditing publicly-traded corporations, working as consultants, or designing corporate governance regulations have become the fundamental elements that ensure smooth market operations. Financial reports and forecast audited by auditors as well as the credibility of other relevant financial information have constantly proven themselves to be the critical foundation relied upon by all stakeholders in corporate governance. Auditors who fail to fulfill their duty as the external professional, compromise the quality of their audition, and lose the sense of independence are accomplices in market turbulence.

In addition, effective corporate governance not only requires a company's internal and external system and an efficient market system but also the active participation by private professionals and groups, including lawyers, auditors, credit evaluation organizations, investment banks, the media, research institutes, analyzers, corporate investors, and private groups who provide services and information needed in the financial and capital market. These external professionals should also participate in a company and beware of the behaviors demonstrated by its owner and the management level, and ask the company to disclose needed information. By doing so, the external professionals form another force that supervises the market.

(3) Supervision by the authority or stock exchange:

Complementing the trend of "unified financial supervision," the Financial Supervisory Commission of the Executive Yuan (referred to as the FSC hereinafter) was established on July 1st, 2004, which is in charge of supervising the development of the financial market and financial services. In corporate governance, each supervisory authority's responsibility is to develop a set of effective corporate regulations and an enforcement system; in other words, the protection of shareholders' interests and responsibilities of directors and supervisors must be clearly stated in the Corporation Law and the Securities Exchange Act. In addition, the formulation of audit standards must consider the reliability in auditing, and the formulation of accounting standards should focus on company transactions and disclosure of essential information. On the other hand, the law should also appropriately punish the perpetrators of transactions that violate the rules and information disclosure and/or are untruthful and unlawful in order to complete the corporate governance system（Ye, Li, and Ke, 2002: 64-65; Securities & Futures Institute, 2005）.

(4) Expressing the legal system:

Common economic crimes due to failed corporate governance in Taiwan are usually indicted in accordance with the law on treachery or work-related embezzlement. According to the statistics of crimes in cases discussed in our study, common crimes include the offense of counterfeiting valuable securities, the violation of Business Account Act, the violation of the Securities Exchange Act, forgery, and the violation of the Money Laundering Prevention Act. Despite the legal process, major stock-exchange related crimes are still common in the recent years (see Appendix 2), and it seems the existing law cannot effectively deter and prevent the transmission of interest. As a result, there is still room for improvement regarding how the legal system and enforcement agencies can hold the last defense line against criminals in order to uphold justice, ensure market stability, and fully protect the interests of stakeholders in corporate governance.

(5) Operations of self-discipline institutes:

The purpose of self-discipline institutes is to help the government actualize its policies. Of the self-discipline institutes for Taiwan's corporate governance, TCGA plays an important role in the evaluation of corporate governance, and another important player of self-discipline is the Association of Directors. These institutes often participate in all sorts of official and unofficial evaluations and can thus provide the authority with valuable comments on future legal revisions.

As mentioned earlier, OECD and World Bank have formulated a complete corporate governance system in the original corporate governance system and the design of its internal and external mechanisms. The experiences of corporate governance in Taiwan and other countries, however, reveal repeated offenses of false financial reports and financial crises, suggesting that although the current corporate governance system is constantly being refined, there is still room for improvement in terms of protecting the interests of all stakeholders.

Regarding how the capacity of Taiwan's corporate governance can be improved, Chen (2004) proposed four strategies for reaching effective corporate governance: (1) an enforcement system involving administrative guidance, supervision, and disciplining from the administrative authority, and prosecution and compensation for investors from the legal authority, (2) market response, information evaluation, and corporate governance evaluation in information disclosure, (3) the quality-control capacity expressed by organizational investors and bank creditors, and (4) promoting transparency of a company's internal information, especially in terms of accounting and financial information, in order to establish an instant information disclosure and evaluation system while the market trends are constantly being watched. The Securities Exchange Act and the Corporation Law should be revised appropriately, and organizational investors should be encouraged to participate in the supervision and evaluation of corporate governance. On the other hand, committees dedicated to the board of directors should be established – especially those on auditing corporate financial reports, in order to complete the corporate governance system (Chen, 2004: 8-13). Ye (2005) believes an independent audit committee formed by recruited, independent directors may increase the transparency of financial reports by evaluating the performance and independence of accountants and internal auditors and reviewing the transactions between major stakeholders, which also reduces ambiguous inter-stakeholder transactions (Y. Ye, 2005: 256). A detailed framework of corporate governance is shown in Fig.1-1

Chen (2004) also has high expectations for organizational investors and bank creditors because the former could utilize retirement funds and funds managed by investment companies to reduce investments in companies with poor corporate governance or nations and regions that lack corporate governance through active "shareholderism," or through published manuals for corporate governance evaluation and investment references. Bank creditors should be more active in their supervision over the corporate governance in a borrower's company in order to ensure re-payments. In addition, banks could adopt short-term share ownership intervention for companies with financial difficulties, get involved in the board of directors through debenture stocks or reply memo and help them establish the complete corporate governance in order to ensure re-payments in the future (Chen, 2004: 8-13). Two characteristics of Taiwan's stock market are that most shareholders are individual investors and the market turn-over rate is quite high. Therefore, in the development of corporate governance, FSC often plays the role of the leader and actively implements the following: encouraging publicly-traded corporations to have independent directors and supervisors, reinforce information disclosure, reinforce the business accounting system, establish the external supervision system, internal

control system, and financial auditing system, value and implement corporate governance, and formulate the "Securities Investors Protection Act" in order to further complete the internal and external mechanisms in Taiwan's corporate governance (Securities & Futures Institute, 2005: 26-33).

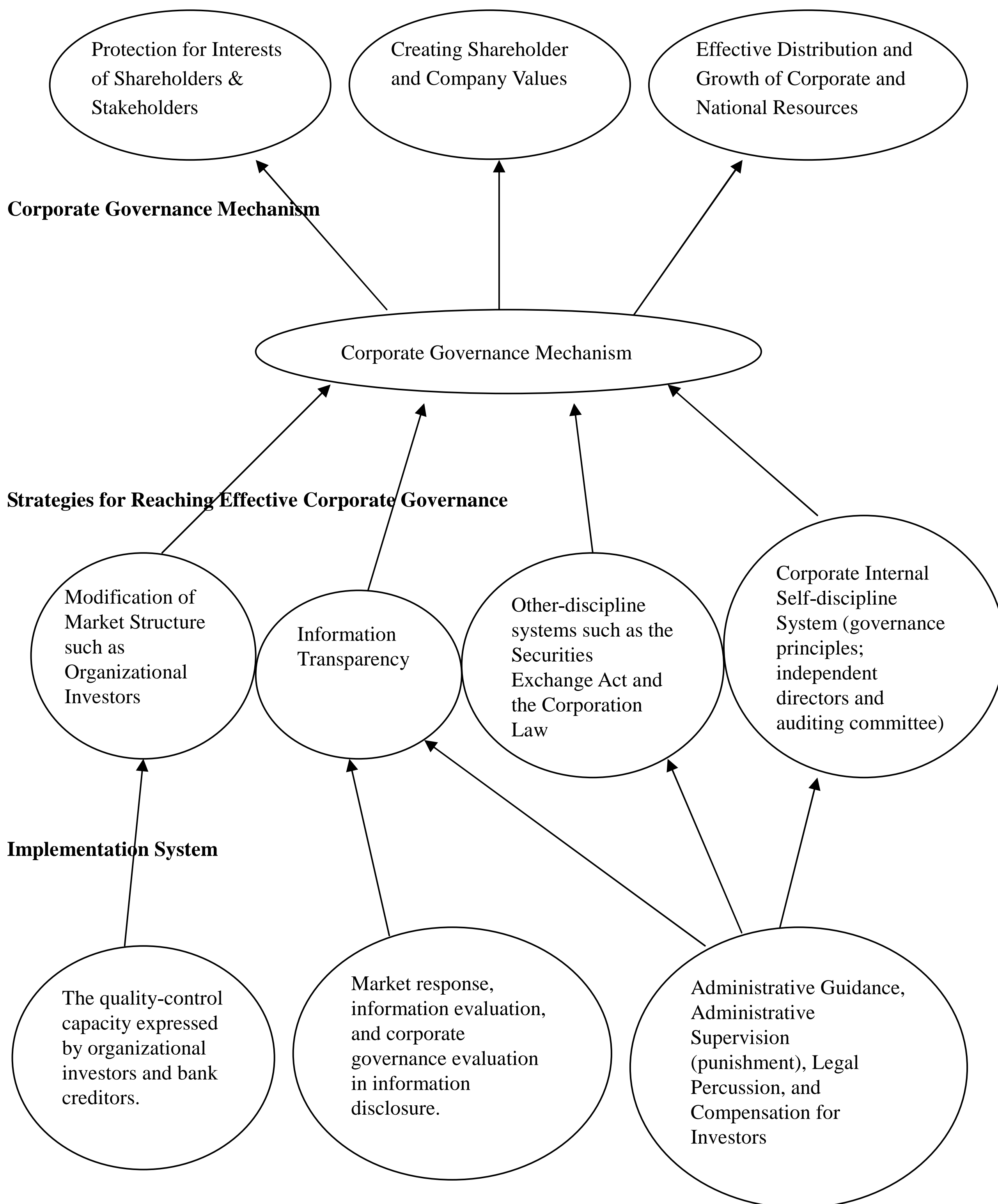

Figure 1-1: Framework of Strategy of Taiwan's Corporate Governance .Source: Chen (2004: 13)

Re-thinking the Agency Problem in Taiwan's Corporate Governance

From the above discussions we can see that Taiwan's corporate governance is consisted of the Corporation Law, the Securities Exchange Act, the FSC, TWSE, and Gre-Tai Securities Market, along with the internal and external mechanisms of corporate governance. Though this may seem enough, corporate financial crises due to poor corporate governance still frequently occur; therefore, the agency problem in corporate governance deserves a closer look. Corporate governance has been practiced in advanced nations for years, and related experiences and suggestions are thus available; however, as mentioned earlier, violations of the U.S. Securities Exchange Act as well as false financial reports among American corporations have been frequently exposed since 2001; of which, the well-known accounting firm "Arthur Anderson" was involved in the Enron scandal. While the U.S. Capitol was scrutinizing these incidents, the White House passed The Sarbanes-Oxley Act of 2002 (referred to hereinafter as The Sarbanes-Oxley Act) in order to address these issues. The feature of this Act is that it addresses the failure of corporate governance in the U.S. and reinforces governmental supervision in order to fix the loop holes in the market system, and the key points include: establishing an independent committee that reports directly to the U.S. government and supervises accountants' conducts, specifying additional financial duties for CEOs and chief financial officers, announcing that CEOs are civilly responsible for investment losses due to their corruptions, and giving the government the power to relieve chief financial officers of their duties in case of violations (Chen, 2004: 51-55). As indicated by the eleven titles in Table 5-1, The Sarbanes-Oxley Act is consisted of eleven chapters; in which, the authority of accounting firms is the Public Corporation Accounting Oversight Board (POCAB), which has announced many new regulations over corporate internal control and auditing. The regulations are discussed in Table 1-1 (Moeller, 2006: 4-5).

In addition, Chapter 4 of The Sarbanes-Oxley Act stresses the effective moral codes can be an important tool for corporate governance, which are managed by the chief ethics officer that plays an important role in this effort. The Ethics Officer Association founded in 2003 is a professional organization consisted of members who are corporate morality managers or chief ethics officers (Moeller, 2006: 86-87, 120). Table 1-2 lists all the duties of the chief ethics officer and clearly indicates that the primary duty of the chief ethics officer is to manage and promote corporate moral norms. Though the mandatory moral norms specified in The Sarbanes-Oxley Act applies to a company's entire stakeholders and thus better promotes the development of corporate governance, a company's internal auditing helps it establish and fulfill a code of conduct that meets honest business behaviors (Moeller, 2006: 97-98). Another important duty of the chief ethics officer is to design a mechanism that allows employees or stakeholders to report illegal corporate dealings anonymously and protects them from recriminations. The chief ethics officer may establish an informant hotline or a hotline that deals with morality-related issues, and should provide employees with training on how they could use the informant mechanism to report illegal corporate conducts so the hotline would not just be a mere formality. The Sarbanes-Oxley Act also stresses that if an informant receives unfair treatments and retaliations in the future, he or she will become a protected informant and protected by the law (Moeller, 2006: 106-108, 116, 120).

Another purpose of Chapter Four of The Sarbanes-Oxley Act is to help a company allow its chief financial officer to insist on proper values and "do the right thing." Therefore, the Act requires a company's board of directors to have the chief financial officer sign a public announcement of morality that includes the elements of business ethics specified in The Sarbanes-Oxley Act (Moeller, 2006: 87). This kind of practice is consistent with the proposal by Mondy & Noe (2005) in which the bills on the actualization of business ethics and corporate social obligations will be passed under public anticipation, and the legalization of business ethics and morality norms will become the trend (Mondy & Noe, 2005: 27).

Reviewing Title 1, 2, and 6 in Table 1-1, it seems that besides additional funding for stock management committees, the main focus is still to provide a legal basis for an independent and fair accountant-supervision committee, along with the "revolving-door" article that prevents the relationship between accountants and a company's internal auditing committee from hindering the completeness of corporate governance. Title 3 and 4 are new regulations focusing on the internal mechanism of corporate governance – especially its scope. For example, a company's CEO and chief financial officer are completely responsible for the financial reports, and compensations and bonuses received from the company are to be returned when a filed financial report turns out to be untruthful. Other new rules announced include that loans without avoiding the conflict of interest must be prohibited, high-level financial

personnel are asked to strictly follow moral obligations, and a company's internal information should be disclosed regularly and in a timely fashion (Chen, 2004: 51-55). Title 5 mentions that new regulations are needed to improve stock analyzers' independence, and they should be separated from investment banks' operations in order to avoid the conflict of interest. Title 8, 9, and 11 state that an act of infringement caused by false financial reports is subject to the charge of fraud, informants are to protected, punishments for financial crimes will become more severe, CEOs and chief financial officers are subject to severe punishments for uncertified corporate financial reports, and punishments for violations of the Securities Exchange Act will also be increased (Chen, 2004: 51-55).

Table 1-1: Summary of The Sarbanes-Oxley Act of 2002

Title	Summary
Title 1: POCAB (public corporation accounting oversight board)	The establishment, tasks, and funding for POCAB. Investigations of accounting firms.
Title 2: Auditor Independence	Auditors' duties and limitations, rotations, interactions with the audit committee, and the revolving-door article.
Title 3: Corporate Responsibility	Audit committees, financial report responsibilities, compensations and bonuses received by the CEO or chief financial officer from the company are to be returned when a filed financial report is untruthful, prohibited behaviors and punishments regarding managers and directors, an insider is prohibited from buying the company's shares during the blackout period of his/her retirement fund, lawyers' duties, and fair funds for investors.
Title 4: Enhanced Financial Disclosures	Regular financial reports, off-balance sheet transaction, Pro Forma reports, and the scope of special purpose entities (SPE), additional regulations regarding the conflict of interest (such as denying loans to managers and directors), disclosure of transactions between managers and major shareholders, disclosure of internal control evaluations, the code of ethics for high-level financial staff, disclosure of audit committees' financial experts, SEC's reinforced reviews of corporations' regularly disclosed information, and instant disclosure of major information.
Title 5: Analysts' Conflicts of Interest	Adds the rule of having analysts' reports on stock exchanges outside of investment banks' operations in order to disclose the conflict of interest.
Title 6: SEC's Resources and Authority	Improves SEC's budget and authority.
Title 7: Studies and Reports	Studies and reports that should be underway, including the mergers of accounting firms, credit assessment institutes, violators and nature of violations, enforcement effectiveness, and investment banks.
Title 8: Corporate and Criminal Fraud Accountability	Punishments for file alterations, debt non-dischargeable for violators, fraud statutes of limitations – including the term of validity of litigation, re-examining the Federal Sentencing Guidelines, protecting insider informants who provide evidence of fraud, and punishments for frauds against shareholders.
Title 9: White-collar Crime Penalty Enhancements	Increased punishments for white-collar crimes, punishments for those with intent and accomplices, CEOs and chief financial officers required to certify financial reports, and severe punishments for deliberate failure to provide certified and truthful financial reports.
Title 10: Corporate Tax Returns	Federal income tax return of a corporation must be signed by its CEO.
Title 11: Corporate Fraud and Accountability	Punishments for those tampering with records or official procedures include SEC's temporary freeze authority over extraordinary payments regarding employees in a company who may have committed violations, revised Federal Sentencing Guidelines, and SEC's authority to prohibit certain individuals from taking on positions or working as directors. Increased

	punishments for violations of the Securities Exchange Act; punishments for those who retaliate against informants who provide law enforcement with evidence of crime.

Source: Chen (2004: 53-55)

Table 1-2: DutiesoftheChiefEthicsOfficer:

- Manage and implement the code of ethics, compliance, and business conducts such as complying to The Sarbanes-Oxley Act.
- Lead, supervise, and provide professional consultations in order to ensure the company follows and complies to the code of ethics, and formulates relevant policies for development, interpretation, and implementation
- Be responsible for tasks regarding any code of conduct the company is involved with, including the ethical relationships among employees, clients, contractors, suppliers, shareholders, and other stakeholders.
- Formulate plans for compliance and risk management in order to come up with effective evaluation, sequencing, and management of regulations specified by the law and the authority.
- Be in charge of the company's informant task, allowing employees, clients, suppliers, and other stakeholders to reveal a behavior in a company that violates the code of conduct, law, or corporate policies without having to worry about retaliations.
- Formulate strategies in order to manage the company's annual code of ethics and compliance training, and facilitate communications for daily code of ethics, compliance, and business code of conduct.
- Hold investigations on violations of ethics, compliance, and business code of conduct, and provide suggestions regarding how an offender should be punished.
- Evaluate a company's performance in terms of compliance and the code of ethics.
- Provide high-level managers and each committee under the board of directors with detailed reports.

Source: Moeller (translated by T. Shih and C. Kuo) (2006:88)

The above content of The Sarbanes-Oxley Act is not about promoting the good but about deterrence, and the focus is on the external mechanism of corporate governance and increased punishments. In addition, this Act also announces new regulations over accountants' independence and duties, prohibits an accounting firm from investing in their client's company, and clearly defines and prohibits debt relations between the accountant and the client. However, more time is required before we can see whether the Americans' after-the-fact amendments would truly be successful. As mentioned earlier, today's corporations have separated ownership and managerial control, and not all the members at the high-level management are corporate owners. Under this separation, it is inevitable to see issues such as the agency problem, agency risks, moral hazards, and all sorts of agency cost. As a result, a corporate manager's duties and goals regarding the interests of the company's entire stakeholders have become the unavoidable challenges for corporate governance.

In fact, the operations of corporate governance reveal there are significant and opposing conflicts of interest between a company's shareholders, managers, and stakeholders. For example, a creditor may want to the company to adopt low-risk plans in order to ensure the debtor can make repayments with interests; a manager who wants to maximize his/her interests would prefer a policy that yields a higher salary; the company's resources can be turned into personal gains, or job security despite the company's poor earnings. Major shareholders of a company might increase their returns at the cost of minor shareholders' interests, and this would involve the interests of the employees, suppliers, clients, or even the entire society. Therefore, what the corporate governance mechanism pursues is to minimize the costs caused by the conflict of interest between these stakeholders and rationally arrange their rights, obligations, and duties in order to maximize the interests of shareholders and prevent the management level sacrificing other stakeholders' rights for personal gains. This task, however, is certainly an extremely difficult feat.

CONCLUSION

On the issue of corporate governance and a company's social obligations, Liu (1995) believes that most resources in the modern society are owned by corporations whose policies that are against the social expectations or well-being may cause the public to question corporate legitimacy, yet a complete design of corporate governance may supervise and guide corporations to fulfill their social obligations (Liu, 1995: 226). The function of the board of directors, however, is the core of corporate governance. The board of directors takes the role of the principal in the agency problem and entrusts the company's CEO or general manager with the company's daily operations. In other words, the agent takes on the agency cost and moral hazards, which include the costs of implementation and supervision in the transaction cost and the cost of information-acquisition – another category of the agency problem in corporate governance. On the other hand, if a company's major shareholders are also the actual managers, the above design of corporate governance will not be able to supervise agents in the management level due to the fact that if the board of directors and the management level are working as the president and CEO at the same time, the supervisory capacity will not only be lost but the duties given at the meeting of shareholders (minor shareholders) will also be abandoned – a common cause of many current issues with corporate governance around the world and demonstrates why minor shareholders need to be represented by independent directors（Ye, Li, and Ke, 2002: 23）. The phenomenon of the agency problem becoming one with corporate governance is a very common category of agency problems in corporate governance.

On the other hand, according to Taiwan's current Corporation Law, the power to select accountants is at the hands of the board of directors being supervised. Given the fierce competition in the accounting and auditing industry, accountants are under certain influences from the board of directors. Moreover, the income of an accountant who also works as a company consultant that provides services regarding taxes, finance, and human resources may be far higher than that of an accountant who provides traditional certification services. As a result, the account may lose the sense of independence and fails to fulfill the role of the external supervisor for corporate governance. A way to solve this is to take back the right to appoint accountants from the board of directors or to prohibit an accountant from providing certification and consultation services at the same company (Huang, 2006: 25-26). However, if an accountant stands firmly on his/her ethics and does not lose his/her independence, the board of directors is unlikely to deliberately influence his/her certification efforts or cause him/her to disobey the duties as a good manager due to the compliance with business ethics. Major Taiwanese regulations over directors' obligations are shown in Table 1-3.

Table 1-3 indicates that in order to prevent collusions between directors and managers or minor shareholders' interests being affected by directors who want to compromise accountants' independence, Taiwan's civil and business laws have regulations regarding directors' obligations which focus on warning directors not to forget the duties given by the shareholders, not to infringe their interests or betray their trust, and to exercise due care (Article 22 of the Trust Act, Article 23 of the Corporation Law, and Article 5 of the Merger and Acquisition Law). Though it is difficult to define the legal concept of "exercising due care," its definition can still be made clear when problems of failed corporate governance such as illegal transfer of company funds, manipulating stock prices, forgery, and frauds are clarified (Liu, 2002: 154-156).

Table 1-3: Taiwan's Legal Regulations over Directors' Duties

Name	Content
The Corporation Law (Article 23, 192) Civil Law (Article 535)	Duties of a Good Manager
The Corporation Law (Article 209)	Prohibition of Unfair Competitions
The Corporation Law (Article 206, 178)	Avoiding Conflict of Interest and Voting
The Corporation Law (Article 224)	Prohibition of Double Agency
Civil Law (Article 342)	Crime of Treachery
Civil Law (Article 335)	Embezzlement
The Trust Act (Article 22), the Corporation Law (Article 23), the Merger and Acquisition Law (Article 5)	Exercise Due Care
The Securities Exchange Act (Article 171)	Prohibition of Non-arm's Length Transaction
The Securities Exchange Act (Article 157-1)	Prohibition of Insider Trading

The Securities Exchange Act (Article 157)	Prohibition of Short-term Trading
The Corporation Law (Article 369-4)	Preventing a parent company from using its subsidiary company for non-arm's length transaction or non-profit transactions.

Source: Liu (2002:155)

Article 23 of the Corporation Law that explains the director's compensation responsibilities towards the company or a third-party does not make the distinction based on the scale of a company. A larger company has more complex transactions and involves more stakeholders, which poses not only a major challenge in terms of corporate governance but a director's compensation may exceed his/her capacity. This hinders the recruitment of exceptional directors, causes problems for the implementation of the external director system, and does not help improve corporate governance. If a director is only responsible for compensations due to intentional or major errors, or relieving or reducing a director's responsibilities through the company's charter or special resolutions reaching in the meeting of shareholders before or after an incident, the recruitment of exceptional directors and the establishment of the external director system are facilitated; however, the above systems could be adopted by shareholders with the ill intent to keep a director at fault from compensating other stakeholders (Huang, 2006: 22-23). These two scenarios lead to a dilemma in the issue of directors' compensations. For the second scenario, however, as long as the president or shareholders can uphold business ethics when relieving a director of his/her compensation obligations, the dilemma will not occur, and the recruitment of directors and establishment of the external director system can still be facilitated.

The agency problem is still an inevitable challenge to corporate governance. After corporate governance and relevant regulations were introduced to Taiwan after the financial depression in 1997, cases of failed corporate governance are still pervasive a decade later. Scandals involving Re-bar (embezzlement of company funds) and YHi (false financial reports) in 2007 force us to re-think the values of business ethics and its roles in Taiwan's current corporate governance.

NOTES

(1) The following information on the internal and external mechanisms of corporate governance is compiled from the works by D. Wu. (Wu, 2004: 6-10.) and L. Wu, H. Chou, M. Shih, Y. Chen, and S. Jian (2003). "Corporate governance -- how directors and supervisors carry out their duties." Taipei: Securities & Futures Institute. pp. 9-21.

(2) Compiled from the works by D. Wu. (Wu, 2004: 11-13) .

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