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Structured Notes Dispute Resolution in Taiwan – Update

By Dr. George Lin, Eric Hsu & Ross Darrell Feingold

As in other jurisdictions, disputes between structured notes investors in Taiwan and distributor banks increased dramatically from September 2008's financial crisis when such products lost significant value or ceased to trade. Under Taiwan's regulatory structure, investors purchased the notes via non-discretionary trust account at a distributor bank, which in turn purchased the note from an offshore product note issuer. Tens of thousands of investors complained to government agencies such as the Financial Supervisory Commission's ("FSC") and the Consumer Protection Committee, as well as non-government organisations such as the Securities and Futures Investors Protection Center and the Consumers' Foundation. The Consumer Protection Committee refused to take jurisdiction on the basis that such disputes are not within its scope of authority.

Development of Taiwan's Financial Ombudsman System

In order to efficiently resolve tens of thousands of investor claims, the FSC worked with relevant stakeholders to establish a sufficiently resourced and knowledgeable Ombudsman Committee for Financial Disputes under the auspices of Taiwan's Bankers Association (the "Ombudsman Committee"). The Ombudsman Committee heard investor claims without fees charged to the claimants. The FSC also encouraged financial institutions to settle with claimants, especially those claimants meeting vulnerability criteria similar to that in other jurisdictions such as Hong Kong and Singapore.

According to statistics issued by the Banker's Association, of 68,435 disputes, 43,221 were settled (including those settlements reached directly between the investors and financial institution), with 8,285 cases resulting in compensation paid to investors. The amount of compensation and the reasons therefor

in specific cases where compensation was awarded are not publicly available. However, the Bankers Association has published data that in those cases where compensation was awarded, the average payment was 24.04% of the claim amount.

To better protect financial institution clients, on 30 December 2011 a Financial Consumer Protection Act came into effect. Drafted by Lin & Partners, the law includes the first financial ombudsman scheme in a civil law country, the Financial Ombudsman Institution (the "FOI"). The FOI is modelled on the United Kingdom scheme and covers disputes over a range of financial products whether banking (thus superseding the earlier Ombudsman Committee), insurance or securities. When a dispute is heard by the FOI over an investment product, any ruling requiring payment up to a maximum of one million New Taiwan Dollars (approximately USD33,000) is binding on the financial institution. For disputes over non-investment products, any ruling requiring payment up to a maximum of one hundred

thousand New Taiwan Dollars (approximately USD3,300) is binding on the financial institution. However, the investor has the right to accept or reject the FOI decision.

Litigation

For investors dissatisfied with the Ombudsman Committee or FOI decision, compensation may be pursued via litigation in Taiwan's courts. Following the financial crisis, the financial institution or the investor both had a chance of success when litigating such disputes. However, starting from 2011 the trend of Taiwan Supreme Court decisions is to rule against the investors and in favour of the financial institution. In fact, in almost all cases after 2013 the financial institution succeed in its defences. The key items in recent Taiwan Supreme Court rulings include:

- (1) Investors failed to prove that the structured note product or the distributor bank did not comply with applicable laws and regulations at the time the product was offered;



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(2) The investors failed to prove their argument that the bank defrauded the investor by failing to clearly explain what the underlying is, and thus the contract should be invalidated.

(3) The 2008 financial crisis, an unforeseeable event, caused investors losses;

(4) There is no causation between the structured notes marketing and the investor's losses.

Conclusion

As in other jurisdictions, disputes over structured note products attracted much attention in Taiwan and following the financial crisis and outcry from investors, media and politicians, the FSC has substantially revised the regulatory

framework for offering to investors in Taiwan offshore issued structured notes. Financial institutions must comply with more robust know your customer requirements among other regulations, in order to avoid such disputes from erupting again on such a large scale. However, from case law, we also see that investors must bear the burden of their losses, and where the underlying of a structure note product is complex, the courts have ruled that investors must make an effort to carefully evaluate the product. Post financial crisis, in light of the higher settlements that financial institutions paid to investors in Hong Kong and Singapore, a favourable litigation environment, and with investor interest in structured products increasing again, issuers are once again evaluating Taiwan's market potential.

Lin & Partners is an independent law firm in Taiwan established by Dr. George Lin who has nearly 30 years legal experience. The firm is known for its work in financial products, litigation and gaming. George Lin is recognised by Chambers Global as a leading attorney for gaming in Asia, and by Legal 500 and AsiaLaw Profile in areas including Banking & Finance. George is a chief arbitrator for Taiwan's Arbitration Association, hearing cases across a range of sectors. Eric Hsu is a litigation partner specialising in financial product litigation. Ross Darrell Feingold is of counsel.

