

# Taiwan's Development Fund opts for Israel

## Dr. James Ho explains why

*"We believe there is a natural match between Israeli and Taiwanese companies, combining state-of-the-art technology solutions offered by Israeli start-ups with the strong manufacturing and marketing capabilities of Taiwanese companies."*

Dr. James Ho

In October, 2004, the **Development Fund of Taiwan's Executive Yuan** invested for the first time in an Israeli venture capital fund (See box). **Dr. James Ho**, Deputy Executive Secretary of the Development Fund, describes the activities of the Development Fund and discusses prospects for additional investments in Israel and elsewhere in this exclusive IVCJ interview.

**IVCJ:** What is the purpose of the Development Fund?

**Dr. Ho:** The Development Fund (DF) was established in 1973 by the Executive Yuan to promote Taiwan's economic and industrial development and enhance its national competitiveness by providing equity or loan financing.

**IVCJ:** What are the direct and VC fund investment activities of the Development Fund?

**Dr. Ho:** The goal of DF direct investment is to invest in major enterprises or projects facilitating upgrading of the industrial infrastructure, which is beyond the capability or financial resources of private investors. Historically, DF investment focused on petrochemicals and semiconductors to promote Taiwanese economic development plans. More recently, investment has focused on emerging industries such as information technology, telecommunications, aerospace, digital content and biotechnology. We are emphasizing:

- goal-oriented technology projects that will develop Taiwan as a "Tech-Island"
- aggressive development of the venture capital industry in accordance with "Challenge 2008"
- promotion of high value-added sectors

As of the end of September, 2004, 35 investments totaling NT\$32 billion had been made. The current market value of these investments approximates NT\$114 billion.

VC fund investments by DF is in response to

the "Challenge 2008" campaign to improve industry infrastructure and strengthen national competitiveness via an infusion of NT\$100 billion into the venture capital sector. DF plans to participate in this program through an investment of NT\$30 billion.

**IVCJ:** What have been the principal achievements of the Development Fund to date?

**Dr. Ho:** We've had some outstanding achievements. The average annual rate of return on investments in venture capital firms is 8.5 percent. In terms of spurring economic growth and generating social benefits, these venture capital firms have reinvested NT\$13.4 billion in 524 enterprises. At this rate, we can expect the venture capital firms to reinvest in 1,500 enterprises over the full 10-year period of the plan until 2011.

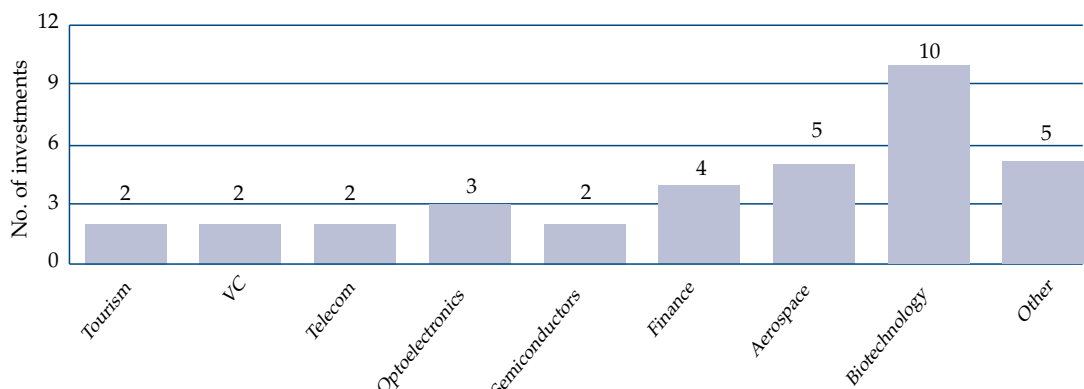
**IVCJ:** In which large companies does the Development Fund hold significant stakes?

**Dr. Ho:** Currently, the DF holds 7.4 percent of Taiwan Semiconductor Manufacturing Company (TSMC), 27.8 percent of VIS, and 6.1 percent of Mega Financial Holdings.

Taiwan Semiconductor Manufacturing Company (TSMC), founded in 1987, is the world's largest dedicated semiconductor foundry. As the founder and leader of this industry, TSMC has built its reputation by offering advanced wafer production processes and unparalleled manufacturing efficiency. From its inception, TSMC has consistently offered its customers the foundry industry's leading technologies. The company's manufacturing capacity is currently about 4.3 million wafers, while its revenues represent some 60 percent of the global foundry market.

Vanguard International Semiconductor Corporation (VIS) is a leading specialty IC foundry. Since its founding in 1994, VIS has been achieving continuous success in its technology development and production efficiency. VIS

**Equity Investments by Industry**



Source: Executive Yuan Development Fund

consistently offers customers cost-effective solutions and high value-added services. VIS currently has one 8-inch fab with monthly output of 55,000 wafers.

Mega Financial Holding (formerly CTB Financial Holding), the second largest financial holding company in Taiwan, was founded in 2002. Currently, paid-up capital is NT\$113,657 million and total consolidated assets stands at NT\$2 trillion. Its seven subsidiaries include Chiao Tung Bank, The International Commercial Bank of China, Chung Hsing Bills Finance Corp., Baits International Securities Co., Ltd., Chung Kuo Insurance Co., Ltd., Mega Investment Trust Corp, and Mega Asset Management Corp.

**IVCJ:** What industry sectors does Taiwan want to develop?

**Dr. Ho:** Taiwan's industrial development is currently facing external and internal challenges. China, with its cheap labor force, low land costs and opening of its huge market after joining the World Trade Organization, is highly attractive for investors, speeding up the exodus of Taiwan's labor-intensive and low added-value industries. In order to tackle the challenges of a knowledge-based economy, Taiwan has begun focusing its industrial development on those industries in which it has already achieved a leading position, such as semiconductors and displays through the Two Trillion Plan, and is seizing the opportunity presented by the globally emerging digital content and biotechnology industries through its Twin Stars Plan. In addition, we would like to see the wireless network industry be the Third Trillion Industry as part of the government's effort to build "Tech-Island" in Taiwan.

**IVCJ:** What steps has Taiwan taken to create a more favorable investment environment?

**Dr. Ho:** Taiwan has received high marks from several important surveys on national competitiveness this year. Taiwan ranked fifth among all nations and first among Asian countries in the World Economic Forum's survey of global growth competitiveness. In the 2004 *World Competitiveness Yearbook* published by the Institute for Management Development in Switzerland, Taiwan placed twelfth, the highest ranking Taiwan has earned from that survey. All the achievements should be credited to the reforms we have implemented in the past few years to improve the investment environment. These include constitutional revisions of the Legislative Yuan, government reengineering through simplification of government structure, completion of first-stage financial reforms and the launching of second-stage financial reforms. Currently, the government has finalized the draft of the "Limited Partnership Act" and is speeding up the privatization of government-owned financial institutions.

**IVCJ:** Are government financial incentives or supporting programs available for non-Taiwanese companies that set up operations in Taiwan?

**Dr. Ho:** Yes. For instance, The Action Plan for Encouraging Foreign Companies to establish their

In October, The Development Fund, Executive Yuan of Taiwan agreed to invest NT\$450 million (US\$13 million) in Giza IV, the latest fund being raised by Giza Venture Capital. The investment was part of a strategic alliance between Giza and the Development Fund aimed at combining state-of-the-art technology solutions of Israeli start-ups with the manufacturing and marketing capabilities of Taiwanese companies. Said Yi-Fu Lin, the chairman of the Development Fund, Executive Yuan, "This is a perfect match-up of Israel's experience in science and technology innovation and R&D with Taiwan's manufacturing prowess. In the long term, it will certainly be helpful to tapping the mutual complementarities of our two countries' competitive strengths and creating more opportunities for industrial cooperation."

regional headquarters in Taiwan was approved in February 2002. By providing business income tax exemption and incentives for land acquisition and supplying talent, the Government is actively encouraging enterprises to establish their operational headquarters in Taiwan where Taiwan serves as a center for business management as well a hub for corporate operations, such as R&D, production, trade, marketing, finance and logistical support.

**IVCJ:** How does Israel play a role in your efforts to build the competitiveness of the technology sector in Taiwan?

**Dr. Ho:** We believe there is a natural match between Israeli and Taiwanese companies, combining state-of-the-art technology solutions offered by Israeli start-ups with the strong manufacturing and marketing capabilities of Taiwanese companies. The new partnership between Giza and the Development Fund is aimed at developing this synergy. Exchanging technologies will increase innovation and create a dynamic duality of compatibility and competitiveness in Taiwan and create further opportunities for industrial cooperation. It creates an association that will be sure to give a marked boost to Taiwan's international clout in venture capital and science and technology.

**IVCJ:** Can Israeli companies that partner with Taiwanese firms benefit from Taiwan's relationships with other regional countries? How?

**Dr. Ho:** Many Israeli start-up technology companies are looking towards the Asian market for customers, distributors, and manufacturing partners in areas in which Taiwan has proven to be very strong. Importantly, Taiwan has the same culture and language as Mainland China and has established relationships that can be accessed by Israeli companies through Taiwan. One of the key points of the relationship between DF and Giza is the identification and promotion of opportunities for cooperation between Taiwanese and Israeli technology companies to enable both to capitalize

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## Tax exemptions encourage VC investment

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the fund. As in the past, such a pre-ruling is issued to foreign partnerships whose investors are foreign residents, which fulfills the condition of “focus of the investment in Israel”.

Israeli partners may invest together with the foreign investors in a co-existing Israeli partnership. Because of the above-mentioned legal amendment, income realized by Israel resident investors is deemed capital gains and is subject to tax, in whole or in part (in accordance with the date of acquisition of the asset), at a rate of 25 percent.

The principal conditions for receipt of a pre-ruling in this regard are as follows:

- *Amount of investment* – commitments for investment of \$10 million from Israeli and foreign investors, of which at least \$5 million is from foreign investors. As for annex funds, provided the original fund fulfills this requirement, the annex fund will be deemed to be in compliance.
- *Number of investors and rate of investment* – no less than 10 investors (Israeli and foreign), and no individual investor with more than 20 percent of the fund (unless specific approval is given for an exception); investors in a fund of the fund will be deemed investors in the venture capital fund itself.
- *Kind of investments* – At least 50 percent of the fund is to be invested in entitled investments, i.e. in Israeli companies primarily involved in the establishment or enlargement of facilities in the industrial, agricultural, tourism, transport, construction, water, energy, communications, computer, medical or biotechnology sectors, or research and development in any of these sectors. In addition, 30 percent of the fund is to be invested in Israel-resident companies that hold the IP and/or in foreign resident

companies with Israeli subsidiaries with such IP. Fund investments are required to be distributed so that not more than 15 percent is invested in any one company.

- *Prohibited investments* – The fund may not invest in real estate rights or in real estate associations; in addition, the fund may not hold short-term marketable securities or monetary deposits except as interim investments.
- *Method of investment* – At least 75 percent of the investment is to be implemented through allocation of shares or options by the investee companies.
- *Location of investment* – The fund is required to establish an office in Israel that will serve as a fixed place of business and from which all investments in Israel resident companies and in companies “connected with Israel” will be implemented.

### Summary

Foreign VC investor entitlement to tax exemptions in venture capital funds is subject to receipt of a pre-ruling from the Israeli Income Tax Commissioner for the fund.

Since a full exemption is now available to foreign investors in venture capital funds that invest in “entitled investments” in Israel, clear preference exists for investment in Israeli companies via venture capital funds whose investment composition enables receipt of such an exemption.

Clearly, extension of the exemption policy will encourage investment by foreign residents in venture capital funds operating in Israel and will, in turn, encourage growth in the high-tech sector. ■

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on the rapidly growing technology market opportunities in the Asia-Pacific region.

**IVCJ:** How can Israeli companies leverage the Development Fund's relationships with Taiwanese companies such as TSMC?

**Dr. Ho:** The DF/Giza agreement provides a good example of how cooperation between Israeli technology companies and Taiwanese companies can be enhanced. DF will introduce relevant Giza portfolio companies to Taiwanese technology firms that can be prospective R&D or marketing partners, manufacturing partners or customers; introduce Giza portfolio companies to prospective Taiwanese investors; and introduce Giza and its portfolio companies to relevant government agencies to facilitate business opportunities in Taiwan.

**IVCJ:** How does the domestic industry perceive the investment in Giza Venture Capital - the first pure foreign VC investment made by the Development Fund?

**Dr. Ho:** The domestic industry is happy to see

our investment in Giza, hoping that, through this international cooperation initiative, many benefits will result in terms of technology, trade and investment opportunities. Moreover, the domestic industry sees this pact as a forerunner of Development Fund investments in other international funds.

**IVCJ:** Is this a prospect then? Can we anticipate Development Fund investments in other international or Israel-based VCs?

**Dr. Ho:** Yes. Our door is open for all domestic and foreign funds. In fact, when it was revealed that the Development Fund was preparing to cooperate with Giza, many recognized Israeli and international capital firms have approached us to inquire about how they might apply for investment from the Development Fund.

The Development Fund is moving towards internationalization through overseas investment. The investment in Giza IV is a forerunner of future moves that will enable us to step up our international investment cooperation. ■