Protecting Minority Shareholders in China:  
A Task for Both Legislation and Enforcement

In (forthcoming) Curtis Milhaupt (ed.) A Decade after Crisis: Transforming Corporate Governance in East Asia, London: Taylor & Francis Books

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I. INTRODUCTION

Features of China's financial system (especially strict capital controls) helped insulate the country from the Asian financial crisis (Fernald and Babson 1999: 12; Zhang 2006: 3), which was largely blamed on poor corporate governance. For China, the concept of corporate governance had in fact just appeared a few years before the crisis (Wu 1993: 189-196, 268-271; Zhang 1994: 79; Qian 1995), and the first Company Law was passed in the same period. However, from theory to practice, corporate governance has developed significantly during the past decade. At the end of 2006, for the listed companies which are the key figures of corporate governance and the subject of this essay, the Share Structure Reform (Guquan Fenzhi Gaige) - a program to convert non-tradable shares held by the state into free-floating shares tradable on the national securities exchanges—is nearly finished, which means corporate governance of those listed companies will undergo even larger transitions.

Protecting minority shareholders from opportunistic expropriation of management or controlling shareholders is always a critical principle of corporate governance, but
protection of minority shareholders was not the chief concern of the Company Law of 1994. The reason for this was not only that the Berle and Means image of the firm with separation of ownership and control, which dominated in Britain and the United States, not fit the reality of China’s prevailing principal owner type (state ownership). It was also that the enactment of the Company Law first aimed at setting down the political objective of transforming State Owned Enterprises (SOEs) into stock companies (corporatization, or Gufenzhi Gaizao), establishing a legislative authority for this transformation, and preventing possible losses of state-owned assets in the transformation.² Thus the Company Law, which is considered to be a basic statute for the common business enterprises, was (at least partially) drafted as a law for converting SOEs into stock companies.³ In this background, rights of shareholders other than the state itself were either not available, not made clear, or not clearly associated with remedies (Howson 1997: 147-9).

In the years after the birth of the Company Law, the demand for investor protection has increased significantly in Mainland China for the following reasons: The number of individual shareholders exploded due to the rapid expansion of the securities market; Scholars, some top officials of the China Securities Regulatory Commission (“CSRC”) and the public media prompted the awareness of rights of investors after corporate scandals and market turbulence; The importance of developing the stock market to lessen the oppressive pressure on banking finance was recognized by the government; A majority of SOEs have been successfully converted into stock companies, so providing guidance and privileges for such conversion was
no longer the chief concern of the legislation. All these elements have led to increased awareness of investor protection and corporate law enforcement as significant policy issues.

In October of 2005, the most important laws concerning corporate governance of listed companies in China were extensively revised to introduce measures to further the protection of minority shareholders’ interests. Devices with the function of compensation and deterrence have been established under the laws, as well as administrative regulations and stock exchanges’ rules to address those chronic illnesses of the corporate governance, especially “looting” of listed companies by their controlling shareholders. Although research has suggested that improvement of legal provisions would contribute to the performance of companies and welfare of the shareholders, as we will see, the new measures in the laws still fall short of fulfilling the demand for shareholders’ protection.

Part II of this essay introduces the protection of minority shareholders provided by the new laws and the formal enforcement measures in China. Plagued by enforcement problems, these public and private mechanisms fail to offer sufficient protection to investors. Part III discusses the possible alternative solutions to domestic enforcement regimes, including a "self-enforcing" corporate law model, cross-listings on foreign stock exchanges, and the possibility of nonprofit organizations to act as corporate law enforcement agents. Although none of the alternatives are a panacea for treatment of the governance problems, they do provide a range of partial answers to the under-production of corporate law enforcement in China. Part IV provides some
thoughts of securities-related class action remedies, which are currently absent from the law but might be another means of achieving efficient corporate governance. Part V is a brief conclusion.

II. REVISION OF LAWS AND THE FORMAL ENFORCEMENT INSTITUTIONS

Since it was believed that poor protection for minority shareholders in China has hindered the improvement of corporate governance as well as development of the capital market, drastic modifications were made to China’s twelve-year-old Company Law. Lawmakers clearly announced that one of the major objectives of the reform was to strengthen the protection of minority shareholders and to improve corporate governance in China. Further, they hoped the revised Company Law would “normalize corporate governance of the listed companies, discipline those companies and their related personnel, and promote the stable and healthy development of the capital market” (Cao, 2005). Revisions to the Securities Law were passed the same day to “improve the regulation of listed companies and raise those companies’ performance” (Zhou, 2005). At the end of 2005, a Revision Bill (Xiuzhengan) of the Criminal Law was also passed to combat “the crimes that bring severe damages to the interests of listed companies and their public investors” (An, 2005).

The new laws have been widely applauded in China (e.g. Liu 2005 a; Zhao 2005; Fan 2006: 83-85; Zhou 2006: 16-21; Liu 2005 b; Guo 2006; Tong 2006). The
revisions (although only on paper) will raise China’s scores in the “shareholder protection” index developed by La Porta and colleagues in their “Law and Finance” article (La Porta et al. 1998: 1126-34).\(^5\) They will probably also increase the welfare of minority shareholders of listed companies (Shen et al. 2004; Shen et al. 2005).

In this part, I will give a brief introduction to the protective provisions especially for the minority shareholders under the Company Law, analyze the missing concepts in the statute, then discuss the formal enforcement institutions which are being relied upon to bring the provisions on paper into reality.

**A. New protective provisions under the Company Law**

Under the new Company Law, the controlling shareholders are specifically required not to abuse their shareholders’ rights (§§ 20.1, 20.2). Unfair related-party transactions are strictly prohibited (§ 21). As responsibilities and powers of the board of statutory auditors (Jianshihui) have been expanded, the new Company Law also made it more convenient to convene a Board meeting (§§ 118.2, 119). Independent directors are required for the board of directors of listed companies (§ 123).\(^6\) In addition to a pre-existing duty of loyalty, a duty of care is now established for board members and senior officers, although “bright line rules” are only set for the former (§§ 148, 149). A company's shareholders are given the right to bring actions in court against the company's directors and officers, in which they can seek damages on behalf of the corporation for violations of the directors’ and officers’ duties to the corporation (§ 152). Cumulative voting is recommended (although not required) for
the election of members of board of directors (§§ 106). A majority of outside shareholders may even petition the court to dissolve a company if it has met such difficulty in its business operations that the continued existence of the company will cause serious losses to the interests of the shareholders, and such situation cannot be rectified by any other means (§ 183). Coupled with other protective measures already provided in the old Law, such as the “one share, one vote” principle (§ 106.1 of the old Law, § 104.1 of the new Law), a supermajority vote required for fundamental changes to a company (§ 106.2 of the old Law, § 104.2 of the new Law), the Company Law (if only on paper) will provide some protection to minority shareholders.

Apart from the statutes, some mandatory rules of the CSRC and Listing Rules of the securities exchanges also contribute to the progress of corporate governance of listed companies in China. For example, the new Guide to Articles of Association of Listed Companies (Shangshi Gongsi Zhangcheng Zhiyin, “GAALC”) limits the number of inside directors to be no more than 50% of all the directors, requires the accounting firm serving as the independent auditor of the company to be only appointed at the shareholders’ meeting instead of by the board of directors alone, requires the companies to provide a means for shareholders to vote by mail or internet rather than only in person, and entitles the independent directors to propose convening an interim shareholders’ meeting. The newest Rule for Shareholders’ Meetings of Listed Companies (Shangshi Gongsi Gudongdahui Guize, “RSMLC”) requires that the company provide shareholders with all of the information they need
to make an informed decision on the issues for which they are asked to vote, orders a mechanism for providing reasonable assurance that the votes will be counted honestly, and provides for an independent tabulation team that should consist of attorneys, representatives of shareholders, and statutory auditors (Jianshi). To convene a shareholders’ meeting when the board of directors fails to provide the shareholders’ list, the board of auditors or qualified shareholder(s) may apply to the Securities Registration and Settlement Company (Zhengquan Dengji Jiesuan Jigou) for the list. The new Listing Rules of the two national securities exchanges also stipulate detailed rules of voting procedure and disclosure requirements covering all kinds of related party transactions.

B. Missing concepts

Some authors have provided insights into the fact that because transition economies have a high proportion of companies that are controlled by a single shareholder or a small group of shareholders and are also often characterized by relatively weak non-legal constraints (e.g., efficient capital and product markets) on the powers of managers and controlling shareholders to act to benefit themselves at the expense of minority shareholders, these economies should have stronger rules to protect minority shareholders than those found in developed market economies (Kiseliov, et al. 1999: 204). Although great progress has been achieved, especially from the revisions of the Company Law, the provisions in the new laws may still not be good enough to yield thorough protection for the minority shareholders in China.
1. In the statutes

The revisions to China’s laws only provide limited protections to minority shareholders. For instance, mandatory cumulative voting for members of the board of directors is not the law. Even if listed companies opt into cumulative voting, there are no rules on minimum board size or provisions on staggering of board terms. The minimum percentage of shares that entitles a shareholder to make proposals at a shareholders’ meeting, or to call for an extraordinary shareholders’ meeting (3% and 10%, respectively), is set too high, and the Company Law fails to provide a procedure for shareholders to obtain a list of other shareholders in order to solicit support for their proposals, or to provide a means for shareholders to receive all of the information they need to make an informed decision on the issues for which they are asked to vote.\(^\text{18}\) With regard to voting, there may be advantages to specifying the minimum vote required to approve fundamental changes to the company as a majority or supermajority of all voting shares, rather than a majority or supermajority of the votes of shareholders who participate in the voting, but even after the newest revisions of the Company Law, a quorum is not needed to validate a shareholders’ meeting in China.\(^\text{19}\)

The minimum percentage and period of shareholding that entitles a shareholder to bring a derivative law suit against the directors or controlling person is also set too high (the plaintiff must have individually or collectively held more than 1% of the shares of the company for more than 180 consecutive days, § 152.1 of the new Company Law). Redemption and appraisal rights of dissenting shareholders (§§ 75,
143.1(4)) are limited to very few situations --mergers or corporate divestures. In addition to the right to authorize the number of shares that may be issued, shareholders may need additional protection during the issuance of new shares to prevent such shares from being issued at an unfairly low price to selected buyers, and to prevent the use of such issuances to reduce the influence of particular shareholders. However, under current law there are no prohibitions against a company issuing or acquiring its own shares at a price lower than market value. The law does not provide for mandatory preemptive rights as protection against underpriced stock issues, "targeted" sales of new shares to other parties, or general attempts to dilute the vote of existing shareholders.

Once control of a listed company has been acquired by a shareholder, the old Securities Law provided for a system of "takeout" rights. Under this system when an investor acquires 30 percent of the outstanding shares of a listed company, the investor was required to offer to buy all remaining shares at a fair price. This gave the remaining shareholders an opportunity to decide whether to remain as shareholders in the controlled company. The system of takeout rights has been adopted by several countries in Europe and is consistent with the rules envisaged in the EU directive. However, the new Securities Law abandons the requirement that the shareholder who achieves control must extend a takeover bid to all the remaining shares (§ 88 of the new Securities Law, compared with § 81 of the old Law); the new Listed Company Takeover Rule even cancels the requirement of a fair offer price, which cripples the protection to the minority shareholders. Rules to restrict freeze-out transactions are
also absent from the statutes.

2. In the Judicial Explanations

The official explanation of the Company Law, without which courts will be impeded from hearing related cases, still must be promulgated by the Supreme People’s Court of the PRC (SPC). Whether or not the derivative suit mechanism can provide some redress to damaged listed companies and their minority shareholders may depend on rules in this forthcoming Judicial Explanation (“Si Fa Jie Shi”). The critical points to be clarified by the Judicial Explanation are as follows: (1) The litigation fee. If the fee is set as a percentage of requested damages, as in other private litigations, the amount of fees will have a chilling effect on filing suits. (2) Recovery of expenses. As plaintiffs would not be able or willing to shoulder the burden of the litigation fee, they should have a right of recovery of such expenses from the corporation. (3) Security Deposit. Whether the court will require the plaintiff shareholders in every suit to provide an “appropriate” security deposit in consideration of possible losses the defendant may incur is critical. (4) Liability of individuals. The deterrent effect of derivative litigations can be fulfilled only if the defendant directors and officers will be ordered to bear out-of-pocket liabilities (rather than being covered by insurance or company reimbursement). Some other Company Law articles which provide shareholders with a private right of action may face similar problems.
C. Control of tunneling to protect minority shareholders

Using “tunneling” as an example, let’s consider whether the revisions of company law, securities law, and even the criminal law will be helpful to reduce looting of listed firms by their controlling shareholders. In China, the principal forms of lootings are: failure by the controlling shareholders to pay for their capital contributions; direct or contingent loans to controlling shareholders; disadvantageous (to the listed company) transactions with the controlling shareholder, and even naked takings (Ho, 2003).

1. Private right of action

Many private liability provisions have been added to the Company Law, including § 20.1 (prohibition against abuse of shareholder’s rights), § 20.2 (shareholder’s liability for compensation to the company and other shareholders for abusing rights), § 21.2 (shareholder’s liability for compensation to the company for abusing “affiliation relationship”), § 152.3 (shareholder’s right to bring a derivative suit against “a third party” who infringes upon the interests of the company), and § 22.2 (shareholders’ right to challenge the resolutions of a shareholders’ meeting or a board meeting). The new Securities Law provides further remedies to the public shareholders of a listed company, such as § 69 (a controlling person who knowingly directs a false statement to be made shall bear joint and several liability with the issuer).

Protections to the minority shareholders on the books do not seem bad, but legal enforcement remains a problem. First, the court system is not active in hearing
corporate and securities cases. Listed companies and their officers still have a certain political backing, and Chinese courts are neither experienced nor politically powerful and are hence reluctant to take cases involving complicated reasoning and powerful defendants. The local courts have been reluctant and very inefficient in hearing securities-related claims, even though the SPC allowed them to take a limited category of those claims. According to a prominent securities lawyer, Yixin Song, since the first legal action filed in 1996, about 10,000 investors have initiated securities related suits, but only about 1000 have achieved some kind of compensation from settlements or judgments. In fact the number of plaintiffs is probably less than 10% of all those who have been damaged and have standing to sue, while the damages claimed may be less than 5% of the total losses arising from the illegalities (Shentu & Chang 2006). Second, class actions are not permitted in China. Although transplantation of the institution has been supported by many commentators, class actions still appear to be infeasible in foreseeable future. Third, without key institutions such as contingency fees and award of attorneys' fees, the "private attorney general" role of private litigation in the enforcement of law appears difficult to realize (cf. Coffee, 1983).

2. Administrative liabilities under the Company Law and the Securities Law

The CSRC resolved to address the tunneling problem (especially misappropriation of listed companies’ assets) in the Chinese market within 2006. That is controlling shareholders would be made accountable for assets or profits transferred illegally from listed companies. Nevertheless, the agency has been hampered in several ways
in meeting this goal. First, the Company Law does not provide the CSRC with any specific power to curb tunneling illegalities, while the new Securities Law only orders all listed companies to disclose their de facto controlling persons. Further, as the supervisor of the controlling shareholders of listed companies, the CSRC’s principal legal weapon to combat looting is to declare concealment of the underlying transaction to be a “material omission” in the statutory reports of the listed companies, subjecting the issuer and its executives to modest sanctions. The CSRC may declare the responsible persons unfit to engage in any security-related business or be elected to the board of listed companies (Shi Chang Jin Ru), but it has not used this sanction very often. Second, as a government agency with responsibility for both the enforcement of rules regarding disclosure and merit-based review of the investment quality of issuers, the CSRC has limited resources to enforce the law (Clarke 2003). Moreover, the agency still lacks sufficient administrative authority to discipline high-level state-owned shareholders behind some listed companies. The ambitious anti-misappropriation plan is not likely to be achieved by the CSRC alone.

3. Disciplinary actions of the self-regulatory bodies

China’s two national stock exchanges are joining the war against tunneling, but it is even more doubtful that they are equipped to achieve any breakthrough. The exchanges may administer private reprimands or public censures, which are not likely to be effective against those unscrupulous offenders. For more serious measures they may delist or suspend the listing of a company. However, even if the exchanges are willing to act, this sanction is more painful to the innocent shareholders than to the
guilty controllers who hold “non-tradable shares” that are not listed on the exchanges. The exchanges may declare the offender to be unfit to serve on the board of directors or board of supervisors, they may also advise the company to dismiss its secretary of the board of directors, but the exchanges seldom deploy those sanctions in the recent years.

4. Criminal liability

Revisions to China’s Criminal Law, passed in 2006, make the directors, managers and even controlling shareholder(s), or de facto controlling person(s) of a listed company, subject to criminal liability if they knowingly make the company to engage in actions causing substantial loss to the corporation. While the revision still needs to be explained by the SPC, one critical issue remains: If the profits siphoned off or assets transferred out of the listed company were used to prop up troubled firms in the same state-controlled group (e.g. to pay salaries for workers in those firms), the “criminal culpability” which is indispensable under the criminal law for an action to constitute a crime, may be very difficult to prove. Nevertheless, as the number of listed companies controlled by private capital is increasing year by year in China, and looting by controlling shareholders has also happened in these companies, well-defined criminal liabilities should have some power to deter those illegalities. Furthermore, corporate governance of Chinese listed companies is not just characterized as controlled by a dominant state-owned shareholder (yigu duda), but also as under "insider control" (neibu ren kongzhi) and "absent owner" (suoyouzhe quewei). While effective control rights are assigned to management, which generally
has a very small, or even nonexistent ownership stake (Wei, 2000), assets of state-controlled listed companies may be converted through various subterfuges into the personal property of management (Clarke 2006: 147). Thus the games played by the government, management, and outside investors become more complex than those addressed in the traditional corporate finance models (Su, 2000; Li and Zhang, 2005; Zhao, Lowe and Pi, 2005). Criminal penalties have a role to play in curbing illegal self-interested actions of management as well.

III. ALTERNATIVE SOLUTIONS TO DOMESTIC ENFORCEMENT REGIMES

If China’s formal corporate law enforcement regime remains problematic, it is useful to explore possible alternatives to improve corporate governance.

A. A self-enforcing model of corporate law

Professors Black and Kraakman (1996) argue that in emerging economies, the best legal strategy for protecting outside investors in large companies while simultaneously preserving managers' discretion to invest is a self-enforcing model of corporate law. The self-enforcing model structures corporate decision-making processes to allow large outside shareholders to protect themselves from insider opportunism with minimal resort to legal authority, including the courts. The model may be a feasible choice for emerging markets to protect minority shareholders, and
China’s legislators have been designing some of the Company Law provisions based (at least partly) on that model. For example, a rule requiring both shareholder and board-level approval for self-interested transactions is now in the law. Making loans to other enterprises or providing guarantees to individuals is permitted, when consent of the shareholders’ general meeting or the board of directors has been obtained according to the articles of association of the company. With the consent of the shareholders’ general meeting, a company may even provide a guarantee to its controlling shareholder or de facto controlling person, and directors and officers may operate for themselves or for any others any business similar to that of the company for which they work.\textsuperscript{41} Under the old Company Law, those acts were strictly forbidden.\textsuperscript{42}

As the regulator of China’s securities market, the CSRC has also been exploring ways to construct a self-enforcing corporate governance model for listed companies. In 1997, 2000 and 2001, the agency promulgated a series of important rules to strengthen the role of the shareholders’ meeting and to introduce the independent director system.\textsuperscript{43} Pursuant to another rule of CSRC,\textsuperscript{44} implementation of or application for the following matters can only be made upon the approval by the general meeting of a listed company (attended by holders of both the tradable shares and non-tradable shares), and the approval by more than half of the voting rights represented by the tradable shares’ public holders: (1) Issuing new shares publicly, issuing convertible bonds, and placing shares with existing shareholders; (2) Material asset restructurings, for which the total consideration for the assets has a premium of
at least 20% of the audited net book value of such assets; (3) Repayment of debt owed to the company by a shareholder using the shares of the company; (4) the overseas listing of a subsidiary of material importance to the company; (5) relevant matters in the development of the company which have a material impact on minority shareholders. When voting on the above matters, a company is required to provide its shareholders with a “network voting platform”, so the shareholders may vote through the internet.\(^{45}\) The rule on shareholder approval actually considers the “public shares” held by minority shareholders to be a different class of shares from those held by the controlling shareholders or de facto controllers of the company (often SOEs or even the local governments themselves).

The CSRC does not limit its corporate governance rules to the internal decision-making processes of listed companies. It also attempts to enlist assistance from the financial intermediaries who are deemed to be the “watchdogs” of the market. To cure false representations in the annual report and financial statements of listed companies, the CSRC requires issuers applying to make public share offerings or convertible corporate bonds issuance to appoint a qualified securities company as a “sponsor” (Baojianren). As the chief underwriter of the public offering, the sponsor must comply with the principles of honesty, trustworthiness and due diligence in conducting its review of the issuer’s application. The sponsor must also supervise the operation and reports of the issuer even after its shares have been listed for one or two years (depending on various conditions).\(^{46}\) The sponsor bears joint and several liability, with the issuer or the listed company for losses suffered by the investors for
false representations or material omissions in those documents or reports, unless they can prove that they are not at fault. Misrepresentations or omissions in the sponsoring documents themselves subject the sponsor and responsible staff to fines and other administrative penalties.

In the newest Takeover Rule, the CSRC establishes the key role of the financial consultants (Caiwu Guwen) in maintaining order in takeover activities. Except for a few particular circumstances, the rule obligates the acquirer of a target company to retain a financial consultant who will issue an expert opinion on whether the acquirer has fulfilled its obligations under the rule. The board of directors of a target company facing a tender offer, or the independent directors of a company facing a management buy-out offer, must also retain financial consultants to help them confirm whether the offer is fair. Moreover, the rule contains a special chapter defining the financial consultant's duties and responsibilities in the takeover of listed companies. Some of these duties include due diligence and follow-up tracking during the takeover transaction, as well as continuous supervision after the takeover transaction. As with the aforementioned sponsors, financial consultants are qualified, supervised, and disciplined principally by the CSRC. As “watchdogs” in takeover transactions, they are responsible to the market regulator, not to the courts.

It remains to be seen if the self-enforcing corporate law provisions or the market watchdogs will play a major role in overcoming China’s enforcement problem. But as Black and Kraakman pointed out, even the self-enforcing model cannot respond completely to the need for legal provisions addressing liabilities and their formal
enforcement. The key point is, since company laws and securities regulations are inherently “incomplete”, ambiguous provision, or gaps in the self-enforcing law, will have to be explained or filled in by a regulator or court. Moreover, plagued by collective action problems, the general meeting of shareholders may be too weak to provide real protection to its members. Finally, the supporters of a self-enforcing model may overrate the effectiveness of “self-enforcing” laws in an emerging market with very weak judicial enforcement, imperfect market constraints, and faint reputation bonding.

B. The role of cross-listings

Professor Coffee predicts that when the large firms around the world opt into higher regulatory and disclosure standards, “bonding” themselves to governance standards more exacting than those of their home countries, the U.S. securities laws will accommodate functional convergence - both through migration and harmonization - raising governance and disclosure standards. According to Coffee, good enforcement can be attained when firms in weak enforcement regimes bond themselves to "good" corporate law in a regime imposing high disclosure requirements and subjecting listed firms to a stringent regulatory and private enforcement mechanism (Coffee 2002: 1757).

China’s Securities Law of 1999 imitates the US disclosure principle and numerous substantive provisions (evidence of formal convergence). As its US counterpart
(Coffee 1999: 690-1), China’s securities law presently seems capable of regulating controlling shareholders to some extent through the following junctures: (1) Articles 86 and 87 of the new Securities Law require any investor who has attained a 5% shareholding in a listed company to disclose the fact within three days. The report must include the name and address of the investor, description and quantity of the shares held by it, and the date on which the shareholding or change in shareholding reaches the threshold. The takeover rule of CSRC requires much fuller disclosure, including (among others) the identity of the investor and the persons who agree to act in concert with respect to attaining more than five percent of shares, purpose of the acquisition, and disclosure of transactions of the listed companies’ shares within 6 months before the acquisition. \(^{53}\) As a result, the provisions, just like section 13(d) of the Securities Exchange Act of the US, deny the possible new controllers of the company the veil of anonymity by requiring a transparent ownership structure. (2) Insider trading rules restrict (with criminal penalties) the controlling shareholders’ ability to purchase or sell based on material, nonpublic information. \(^{54}\) (3) The takeover rule assures, through both disclosure and substantive rules (particularly regarding timing, withdrawal, and proration rights), all shareholders of a listed company an equal opportunity to participate in any tender offer for their shares. \(^{55}\) (4) The continuous disclosure system generally requires issuer’s timely disclosure of the controlling shareholders’ material developments relating to its shareholding. \(^{56}\) (5) A controlling shareholder with fault is subject to civil and administrative liabilities for disclosure by its controlled company containing fraudulent information, misleading
representations or material omissions which cause investors to suffer losses in securities transactions;\textsuperscript{57} (6) The rules provide the remaining shareholders a “sell-out right”, that is, the right to sell their shares to the acquirer of a listed companies at a fair price when the company is delisted following the completion of an acquisition. This rule allows those shareholders a chance to escape possible oppression by the new controller.\textsuperscript{58} Nevertheless, plagued by the enforcement problem, those provisions may remain on paper, instead of being applied in fact. Therefore, some of the best local firms seeking any variety of goals - to show a credible and binding commitment by the issuer and its controller not to exploit minority investors, to raise more equity capital, to increase share value, or to achieve worldwide recognition - may decide to list on a developed stock exchange and thereby opt into foreign governance standards. This kind of immigration to the foreign market may help ease the enforcement problem in China.

Until now, some locally well-known companies have been listed in US, UK, Hong Kong, or Singapore markets. Some companies and their officers and directors have been hit with class action lawsuits filed in the United States (e.g., Chinalife, Chinadotcom, NetEase). The chairman of a company listed in Hong Kong exchange (Skyworth Digital Holdings Ltd.) was even sentenced to jail for misappropriating funds and conspiring to defraud in connection with the granting of share options. But it remains to be seen whether the corporate governance in Mainland China can achieve convergence to global standards mainly by encouraging the local companies to list in the US or other developed markets. To the present, not that many companies
have been permitted to list their shares on developed markets. At the end of June 2007, there were only 60 Chinese companies listed on the London Stock Exchange, and even less listed on NYSE and NASDAQ (Zhu 2007). The influence of those companies’ governance on their locally listed counterparts may be limited. Also, as there have been very limited channels for domestic citizens to invest in foreign markets and the national exchanges in China have not been fully opened to foreign capital, real competition among local and foreign stock exchanges has not yet begun. Thus, exchange harmonization will be slow. Finally, cross-border supervision of cross-listed companies requires more efficient cooperation among regulators and even courts of different jurisdictions, without which there will be a failure of enforcement.

Cross-listing may help to improve corporate governance in some local companies, but as Bernard Black pointed out, even if those firms have "escaped" their weak home country institutions through foreign listings, such escape is only partial without the help of local enforcement and other institutions.

C. The Role of the nonprofit organizations

Professor Milhaupt maintains that nonprofit organizations (NPOs) have emerged as perhaps the most important corporate law enforcement agents in Korea, Japan, and, Taiwan area, and their action may be another partial solution to the problem of weak investor protection and corporate law enforcement (Milhaupt, 2004).

As widely known, China does not have a tradition of active NPOs, but a similar
“organization” of securities lawyers has recently emerged.

After the CSRC published its administrative penalties against Kelong (a locally listed company which submitted false accounting reports) and Deloitte (an international accounting firm which gave an unreserved opinion on the financial report of Kelong), 60 lawyers from 45 law firms around the country formed a “Justice Claiming Team for the compensation from Kelon and Deloitte’s false statement” (Kelon, Deqing Xujiachenshu Minshi Peichang An Quanguo Lushi Weiquantuan). The “Justice Claiming Team” consists of lawyers who have been participating in securities-related civil compensation lawsuits in the country. Boasting rich practical experience, the team released its Movement Statement through high-profile media, claiming that the lawyers’ group was a loose and open-ended organization that would accept any qualified Kelon shareholders’ actionable claims. Most importantly, the group announced that if there were any similar misrepresentation cases in the future, all the members of the team would automatically form a new “Justice Claiming Team” automatically (Shentu & Chang 2006). According to Yixin Song, one of the conveners of the “Justice Claiming Team”, the Team is the biggest lawyers group aiming at one single case in China’s history, with three tasks from now on: (1) Organizing the member lawyers to discuss the difficult law issues in the Kelon and Deloitte cases, coordinating the lawyers and law firms involved in the case, and exploring ways to improve securities-related civil suits and the private compensation law system; (2) Coordinating with the CSRC, the SPC, and related lower courts, accepting their guidance, and providing professional comments and advice; (3)
Providing practical legal education to investors and persuading them “to believe in the strength of the law, and believe in the strength of themselves.” (Yue & He 2006)

The “Justice Claiming Team” is not likely to be registered with the local government as a NPO, rather, it is now a forum for the securities lawyers to exchange experience and information gathered from the cases they have represented. But that difference does not seem so important. Unlike in Japan or Korea, there appears to be less public antipathy in China toward allowing lawyers to play a larger role (even if basically for profits) in the resolution of economic problems, at least before the emergence of real corporate and securities law-related NPOs in the country. In such an environment, the high-profile group of activist lawyers could still be a partial (if transitory) response to the public goods problem of corporate law enforcement. In the future, the role of the NPOs may also be played by a government sponsored “Securities Investor Protection Fund Limited Liability Company” (SIPFLLC) in charge of the financing, management, and using of the “Securities Investor Protection Fund”. The attitude of the court system will be the most important determinant of the role of the NPOs in the corporate governance of China’s companies (See Yu 2006).

IV. CLASS ACTIONS

China’s Civil Procedure Law and Securities Law does not provide for a US-style class action suit. The Judicial Explanations relating to civil liability for misrepresentation in the securities market made it clear that plaintiffs in securities
litigations can adopt “representative suits with a fixed number of litigants” (*Renshu Queding De Daibiaoren Susong*, § 54, the Civil Procedural Law), but not “class actions”. For multi-party litigations (*Quntixing Susong*), government agencies and the Lawyers’ Association have just announced strict control over plaintiffs’ lawyers.

At the same time, since fraud has been so common in the securities market, and the supply of investor protection is far from sufficient, the regulators, stock exchanges, business lawyers, and public media have increasingly voiced their support for the establishment of a securities-related class action system (Cheng & Wu 2005, Xia 2005, Wang 2005).

Whether a securities-related class action system should be established in China may be examined by balancing the pros and cons. The answer to the question also depends on how the system, the securities regulation framework, and the overall legal infrastructure are setting.

**A. Overview of conflicting arguments**

Since the adoption of the Civil Procedure Law in early 1990s, scholars have noted the differences between “representative suits without a fixed number of litigants” (*Renshu Buqueding De Daibianren Susong*) under China’s Civil Procedure Law and US-style class actions. Many scholars argued the “representative suits without a fixed number of litigants” had better support in the theories of civil procedure law and might be better suited to meet the demands of local reality. In the intervening years, however, more scholars have inclined to endorsed a class action system.
B. Advantages of a class action system

The primary benefit of allowing securities-related class action lawsuits is the expansion of the effect of the judgment, meaning the ruling of the court will bind those who have not actually opted into the lawsuit, thereby providing an efficient means of giving relief to a much larger class. Thus, a class action helps to overcome the collective action problem among dispersed individual plaintiffs. Without the system, the damages claimed by a single plaintiff may be minimal and the cost of litigation prohibitive, thus precluding any incentive for plaintiffs to litigate individually. Finally, a class action system will effectively deter fraud and irregularities when limited administrative penalties can not achieve the same result.

C. Problems of a class action system

There are, on the other hand, many problems entailed in a class action system. First, class actions permit some plaintiffs to appoint themselves as the representative of the entire plaintiff class, which conflicts with the prevailing legal theory. Second, if China does not have the political, social, and judicial infrastructure to accommodate a class action system, the courts may decline to hear class actions even if they are introduced into the law. Third, class action litigation is not the only means of providing relief to a group of individuals. Government regulators, local governments, and local or industrial self-regulatory organizations, may be in a better position to solve social problems. Fourth, it is almost impossible for the class members to supervise the actions of their representatives and lawyers. Fifth, instead of realizing social justice,
class actions may be abused by corporate attorneys who only focus on their potential profitability. Sixth, the influx of numerous class actions could create a huge burden on the potential defendants (especially securities issuers and financial intermediaries) and the courts. Finally, it cannot be overlooked that the US has experienced problems with class actions, to date no other major jurisdiction has widely utilized the institution.

D. The need for a class action system

In view of a variety of factors, introducing a class action mechanism for securities suits is both necessary and possible. China’s securities market is nascent, cultural, legal, and market constraints are too weak to provide practical protection to inexperienced individual shareholders, who constitute the main body of investors. A robust enforcement mechanism such as the class action institution is needed to address gaps in the supply of investor protection and corporate law enforcement, which cannot be filled by other means. Moreover, government officials and commentators agree that some brazen misconducts in the securities market should be punished to achieve deterrence. Securities-related class actions are highly technical and professional, which makes it possible for them to be insulated from politically-sensitive public policy issues. After more than 10 years’ construction, a set of comparatively detailed securities statutes and rules have been established, making it much easier to discover and confirm illegalities than before. The adoption and revision of the Securities Law and related Judicial Explanations have provided private rights of actions to sue the wrongdoers. Through the handling of these cases, some
intermediate and superior courts have gained first-hand experience in hearing misrepresentation cases. More and more research on the US class action system has been introduced into China, making it easier to draw lessons from the US experience. A team of institutional investors has been born to provide potential candidates for lead plaintiffs. The rapidly expanding group of business lawyers and law firms has been able to provide qualified legal services to litigants. After the revision of the Securities Law, the CSRC is even better equipped to detect and punish illegalities, signaling to the plaintiff's bar that attractive cases are available. The agency will also be very helpful in providing expert opinions as Amicus curiae.

According to the experiences in US and Korea’s markets, to devise an efficient class action regime for China lies in balancing three separate problems: (1) the problem of blocking frivolous suits while allowing meritorious suits, (2) the agency problem between plaintiffs' attorneys and the plaintiff class, and (3) the lack of incentive of plaintiffs' attorneys to focus on smaller companies (Choi 2004: 1510). While the implementation is of concern, the reform should first focus on misrepresentation cases with which some courts have become familiar. The SPC ought to permit experimental practices of “representative suits without a fixed number of litigants” (§ 55, the Civil Procedural Law), and then establish a class action system.

E. Infrastructures for a class action system

1. Plaintiff lawyers

In large Chinese cities, an active, professional corporate and securities bar is
forming, although most the business lawyers still focus on work other than litigations, however, familiarity with corporate and securities laws grants them particular advantages in becoming trial lawyers and developing expertise in pursuit of a securities class action. Today, China has only a few large law firms with over one hundred attorneys. Thus diversifying the risk that any given class action may not result in a positive return for the firm may be problematic. Nevertheless, diversification may still occur across firms, as several plaintiffs’ firms may jointly share in the co-representation of different classes in several different lawsuits.

2. Institutional investors

The presence of institutional investors who are able to take an active role in class actions is one of the keys to success of the system. A group of institutional investors (including securities investment funds, insurance companies, the Social Insurance Funds, securities companies, Qualified Foreign Institutional Investors (QFIIs), and Foreign Strategic Investors) have appeared in China. However some of the institutional investors - especially the Securities Investment Funds - are widely criticized as being inclined to make speculative and risky investments instead of maintaining stable shareholdings (e.g., Li 2002:72-3). They appear unconcerned with listed companies’ governance and share few interests in common with individual investors. They have even been involved in market manipulations and other scandals (Ping & Li 2000; Xu 2005: 79). Another main type of institutional investor, the local Social Insurance Funds, have been reported to have severe governance problems for themselves (Hu et al. 2006). It is thus doubtful if these institutional investors can
actually be counted on to act as lead plaintiffs. In the future, responsible institutional investors have to be raised.

3. Judges and courts

Specialized judges and courts have better ability to handle class actions. They may develop expertise in distinguishing between frivolous and meritorious claims, and may be able to sanction frivolous suits. Specialized judges may also apply doctrines (such as reliance and causation, or measures of damages) more consistently, contributing to the predictability of judicial outcomes, and increasing the probability of settlement. To some extent, China should employ a number of specialized sub-courts (Shenpanting) in the Peoples’ courts. For example, the intellectual property sub-courts with specialized judges in major cities have successfully earned a reputation as comparatively efficient and professional. Employing similarly specialized courts with expert judges for corporate and securities cases may provide significant benefits to a shareholder class action system.

V. CONCLUDING REMARKS

China’s corporate governance has undergone more than ten years’ development. As awareness of investor protection created a significant policy issue, the most important statutes related to corporate governance have been revised to meet the increasing demand for the protection. Research has suggest that improvement of formal legal provisions would contribute to the performance of companies and the welfare of shareholders. However, when plagued by enforcement problems, some
good law provisions on paper would fall short of fulfilling the demand for better governance. The alternative solutions to public and private enforcement regimes include a "self-enforcing" corporate law model, cross-listings on foreign stock exchanges, and the possibility of nonprofit organizations to act as corporate law enforcement agents. They will help to partially ease the chronic illnesses of the securities market, but there is no complete substitute for institutions at the heart of a good national investor protection system and corporate governance, especially formal enforcement mechanisms. Among other mechanisms, a securities-related class action system may be a good institution choice for China going forward.
Notes:


2 See §§ 81, 80.1, 24.1, the Company Law of 1994.

3 For example, as stated in the Company Law of 1994: The Law was promulgated “with the aim to establish a modern enterprise system…” (§ 1); The state assets held by a company belong to the state (instead of by the company itself)(§ 4.3); When a SOE is to be converted into a company, the conversion of management style shall be conducted in accordance with the laws and administrative regulations (§ 7); Where a SOE is converted into a stock company, the state assets is strictly prohibited to be under-valued in exchange for shares, be sold at prices below the prevailing market price, or be allocated to any person without consideration (§ 81); The establishment of a stock company (the only type of company which has access to equity financing market) shall have the approval of the ministries authorized by the State Council or the relevant provincial government (§ 77).


5 Just like Allen, Qian and Qian (Allen et al. 2005: 57–116), we give China score on
shareholder rights law following the LLSV law and Finance methodology. For old company law provisions applying to listed companies China was assigned an antidirector rights score of 3 (out of 6) (the “old score”). After the revision, the score is now up to 4 (the “new score”). When the old score put China’s shareholder rights score below the English-origin average (4) but above both the German-origin average (2.33) and French-origin average (2.33), which would make China to rank right at the average of all LLSV countries (developed and developing) for shareholder rights if China had been in the LLSV list of countries, with the new score, China is now doing as good as the average of English-origin jurisdictions, and will be in the fore part of all LLSV country list.

6 When Principles of Corporate Governance for Chinese Listed Companies (Zhongguo Shangshi Gongsi Zhili Zhunze) issued by the CSRC in 2002 required companies to “establish an independent director system in accordance with relevant rules.” And according to an even earlier Guidance Opinion on the Establishment of an Independent Director System in Listed Companies (Guanyu Zai Shangshi Gongsi Jianli Duli Dongshi Zhidu De Zhidao Yijian), listed companies were required to have at least two independent directors by June 30, 2002, and such directors were to constitute at least one third of the board by June 30, 2003. “Independent directors” does not find its place in the law until the revisions of the Company Law in 2005.

7 Such fundamental changes include, e.g., amendments of the article of association, increasing or decreasing the charter capital, merger, division (or separation) or liquidation of the company.

8 Revised and entered into effect since 16 March 2006.

9 GAALC § 96.3, “insider directors” means those directors who also serve as executive officers or the representatives of employees of the company.

10 GAALC § 159, while the Company Law (§ 170.1) entitles the company’s articles of association to determine if the board should also have the power to hire or/and dismiss
the auditor of the company.

11 GAALC § 44.2.

12 GAALC § 46.1, if the board declines the independent directors’ proposal to convene such a shareholders’ meeting, it has to have the reasons to be publicized, see GAALC § 46.2.

13 Revised and entered into effect on 16 March 2006.

14 RSMLC § 16.

15 RSMLC § 37.

16 RSMLC § 11.

17 Shanghai Securities Exchange Listing Rule and Shenzhen Securities Exchange Listing Rule (revised and entered into effect on May 19, 2006), Chapter 10 “Related-party Transactions”.

18 Similar requirements are provided for in the CSRC rules, as mentioned before. But the requirements in the rules are set too narrowly, and sometimes the provisions are so important (e.g., the rights to the information) that they should be included in the law itself.

19 “The lack of any mention of a quorum requirement (with respect to shareholders’ meetings)…does not evidence any consciousness on the part of the Company Law drafters of the rights of minority shareholders.” See, Howson 1997: 146-7.

20 There should have been a number of other instances where appraisal and redemption rights can be made available: (1) for a charter amendment that limits shareholder rights; (2) for a reorganization; and (3) for a major transaction. A judge or an independent appraiser is also needed to determine the value of the redeemed shares.

21 Securities Law of the People's Republic of China (adopted by the 6th Session of the
Standing Committee of the 9th National People's Congress on Dec. 29, 1998, and effective July 1, 1999) [hereinafter “Securities Law of 1999” or the “old Securities Law”].


23 § 35, Measures for Administration of Takeover of Listed Companies (Shangshigongsi Shougou Guanli Banfa, revised and published on July 31, 2006).

24 The first Judicial Explanation of the new Company Law has been published on April 48, 2006, which only address the coordination of the new and old Company Laws.

25 High shareholding thresholds for the exercise of important shareholder rights and the significant economic risks of filing suit have historically been major obstacles to shareholder activism in other East Asia jurisdictions. See, Milhaupt 2004: 169.

26 E.g., § 22.2 (Shareholders’ right to challenge the resolution of a shareholders’ meeting or a board meeting); § 183 (In very limited situations, shareholders may petition the court to dissolve the company).

27 The term “tunneling” is used in the meaning of Johnson et al. (2000) to refer to the transfer of assets or profits out of a company to its controlling shareholders.

28 “affiliation relationship” refers to the relationship between the controlling shareholder, de facto controlling person, director, supervisor, or senior officer of a company and the enterprise under their direct or indirect control and any other relationship that may lead to the transfer of any interest of the enterprise. However, the enterprises in which the state holds a controlling interest do not have an affiliation relationship.
relationship between them simply because the state holds a controlling interest in them. See § 217(4) of the Company Law.

29 Although not stated clearly, “a third party” can be understood to refer especially to the controlling shareholder and/or de facto controlling person of the disputed company.

30 In our statistics to the middle of 2006, since SPC permitted the shareholders to sue the listed companies and their executives for the misrepresentations in the prospectus and other statements (SPC, 2003), when about 120 companies (and related executives, controllers, and accountants) may have met the strictly formulated criteria to fall into the small group of possible defendants, among them only 17 companies have really been sued to the courts, and even fewer have been held to be responsible for or have agreed through settlements to pay the losses of the plaintiff investors. Source: News reports on the financial newspapers, such as China Securities (Zhongguo Zhengquan Bao), Shanghai Securities (Shanghai Zhengquan Bao), Securities Times(Zhengquan Shibao).

31 Supporters of securities related class action include Chairman of CSRC, CEO of Shenzhen Securities Exchange and many commentators. See Part IV of this essay.

32 E.g., under the Lawyer Service Fee Regulatory Rule (Lushi Fuwu Shoufei Guanli Banfa, April, 2006) promulgate by the State Development and Reform Commission and the Justice Ministry, contingent fee is not permitted in multi-party litigations.

33 §§ 54, 66, 67.2(8), the Securities Law of 2006. Under the Company Law, the term “de facto controlling person” means any person who is not a shareholder of a company but has de facto control of the acts of the company by means of investment relationship, agreements or any other arrangements.
§ 71.1, the new Securities Law. Under the new Company Law, the term “controlling shareholder” means a shareholder whose capital contribution accounts for more than 50% of the total capital of a limited liability company, or a shareholder whose shareholdings accounts for more than 50% of the total equity of a company limited by shares, or a shareholder whose capital contribution or shareholdings account for less than 50% but who holds the voting rights on the strength of its capital contribution or shareholdings that are enough to have an important influence on resolutions of the shareholders’ meeting or the shareholders’ general meeting. See, § 217(2), the Company Law of 2006.

§ 193, the new Securities Law.

Since 1997 when the CSRC provided itself with the power of Shi Chang Jin Ru, it has employed the power in about 30 securities law cases. See CSRC (2006).


The harmful actions include: (1) provide funds, commodities, service or other assets to other units or persons while receiving no considerations; (2) provide or accept funds, commodities, services or other assets under manifestly unfair conditions; (3) provide funds, commodities, services or other assets to manifestly insolvent units or persons; (4) provide collateral for the debts of manifestly insolvent units or persons, or provide collateral for the debts of any units or persons without justified reasons; (5) disclaim a property right or bear a debt for others without justified reasons; (6) damage the listed company in other ways. See, § 169-1, the Criminal Law of PRC (revised on June 29, 2006).

As the end of 2004, the listed companies with its first large shareholder to be collectively-owned enterprise, privately-owned enterprise, foreign enterprise or
Limited Liability Company amount to 390, about 28.32% of all listed companies. The other 987 companies (71.68% of all listed companies) were still controlled by the government or by SOEs. As the end of 2003, the corresponding figures are 347 (26.96%) for non-state-controlled companies and 940 (73.04%) for state-controlled companies respectively. See: CSRC (2004 & 2005).

There are reports that only in March 2006, at least three controlling persons of several listed companies are facing criminal charges for looting those companies. They are Qiu Baozhong, chairman of the board of directors of ST Long Chang (600772, SH), de facto controlling person of both Fujian Sannong (000732, SZ) and Zhejiang Haina (000925, SZ); Zhang Liangbin, chairman of the board of directors of Zhaohua Jituan (000688, SZ); Zhong Xiaojian, chairman of the board of directors of Shuma Wangluo (000578, SZ). In August, the chairman of board of ST Sanlong (000732.SZ) was also arrested. As reported, since the “tunneling” problems were revealed in the listed companies controlled by the private-owned enterprises, about 15 companies’ chairman or CEOs have been under investigation, detained or arrested. See, He (2006).

§§ 16, 149, Company Law (2006) of PRC.

See, §§ 60.1, 60.3, 61.1 and 123.2, Company Law (1994) of PRC.

See especially the Guidelines for the Articles of Association of Listed Companies (Shangshi Gongsi Zhangcheng Zhiyin), issued on Dec. 16, 1997, revised on Mar. 16, 2006; Regulatory Opinions for General Meetings of Listed Companies (Shangshi Gongsi Gudongdahui Guifan Yijian), issued on May 18, 2000, revised on Mar. 16, 2006; and Guidance Opinion on the Establishment of an Independent Director System


45 § 1.1, Certain Rules Regarding Strengthening the Protection of Interests of Public Shareholders.


47 § 69, the new Securities Law.

48 § 192, the new Securities Law; §§ 60, 65, Provisional Measures of Sponsorship System for Issuing and Listing of Securities.

49 Such as in the administrative allocation of state-owned stocks, in the transfer of stocks that does not result in the change of the de facto controller, and the obtaining of stocks by inheritance.

50 §§ 9, 17, 28, 32, 51, Measures for Administration of Takeover of Listed Companies.

51 §§ 65-71, Measures for Administration of Takeover of Listed Companies.

52 “We can only reduce, not wholly avoid, the need for official enforcement.” (Black & Kraakman 1996: 1918). Also see Black 2001: 790-1 (Effective regulators, prosecutors, and courts are the most important institutions that control information asymmetry, which is critical for developing strong public stock markets).

53 § 16, Measures for Administration of Takeover of Listed Companies.

54 Shareholders who hold 5% or more of the shares of the company, the de facto
controlling person of the company and its directors, supervisors and officers are
deeled to be “insiders”, it is illegal for them to buy or sell securities of the company
or divulge such information or procure others to buy or sell such securities before
related insider information is made public. See §§ 73-76, 202 of the new Securities
Law, § 180 of the Criminal Law.

55 Especially §§ 37, 42, 43.1, Measures for Administration of Takeover of Listed
Companies.

56 § 67 of the new Securities Law.

57 §§ 69, 193.3 of the new Securities Law.

58 § 97.1 of the new Securities Law, § 44, Measures for Administration of Takeover
of Listed Companies.

59 As a comparison, to the end of 1996, there were 416 foreign listings on NASDAQ,
305 on the New York Stock Exchange, and 63 on the American Stock Exchange, for a
total of 784, and this number continued to grow rapidly. See, Licht 1998: 566.

60 E.g., presently there are more and more finance scandals revealed in the Mainland
China’s companies listed in Hong Kong, but the local regulators and courts of HK
have felt impotent in the inquiries and legal enforcement against those companies’
illegalities since the companies’ assets, business and even the illegal facts are all in
Mainland instead of HK, the key personnel may choose to stay in Mainland or have
been detained there and then will not be reached by HK’s law enforcers. See Wang
2006.

61 "A company's reputation is strongly affected by the reputations of other firms in the
same country. And reputation unsupported by local enforcement and other institutions
isn't nearly as valuable as the same reputation buttressed by those institutions." See
Black 2001:784.
As to § 134 of the new Securities Law, a securities investors protection fund (“SIPF”) has been established by the state government. The Fund comprises funds contributed by the securities companies and other funds raised. According to § 7 of the Measures for the Management of Securities Investor Protection Funds (Zhengquan Touzizhe Baohu Jijin Guanli Banfa)(issued by the CSRC, Ministry of Finance and Peoples’ Bank of China on June 30, 2006), the funds of the SIPF are only used to compensate the securities investors as customers of a securities company when it goes into bankruptcy, be closed or took over by the government. The SIPF LLC was registered on Aug. 30, 2006.

§ 14, Supreme People's Court “Several provisions on the adjudication of civil suits for damages arising out of false representations in securities markets” (Zuigao Renmin Fayuan Guanyu Shenli Zhengquan Shichang Yin Xujia Chenshu Yinfa De Minshi Peichang Anjian De Ruogan Guiding), issued on 9 January 2003, hereinafter “2003 SPC False Representation Provisions”.

“Class action is not applicable to securities related actions”, see § 4, Circular of the Supreme People's Court Concerning Issues Relating to Acceptance of Civil Tort Suits Filed Due to False Representation on the Securities Market (Zuigao Renmin Fayuan Guanyu Shouli Zhengquan Shichang Yin Xujia Chenshu Yinfa De Minshi Qinquan Jiufen Anjian Youguan Wenti De Tongzhi), issued on Jan. 15, 2002, hereinafter “2002 SPC False Representation Circular”.

Under the Lawyer Service Fee Regulatory Measures (Lushi Fuwu Shoufei Guanli Banfa, issued in April, 2006) promulgate by the State Development and Reform

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62 “We don’t need, either plan to register the Justice Claiming Team as a corporation or association”, by Yixin Song, Song 2006.

63 As to § 134 of the new Securities Law, a securities investors protection fund

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Commission and the Justice Ministry, contingent fee is not permitted in multi-party litigations. Under the Guideline to Multi-party Litigations (*Zhonghua Quanguo Lushi Xiehui Guanyu Lushi Banli Quntixing Anjian Zhidao Yijian*, issued in March 2006) promulgate by the National Lawyer Association, those litigations are subject to “supervision” of the Association.

67 Several theoretical issues (especially frivolous litigation and the relationship between the professional plaintiffs' attorneys and the plaintiff class of investors) exist in contemplating the value of private securities class actions in the United States. In the mid-1990s, the U.S. enacted the Private Securities Litigation Reform Act of 1995 that sought to address these issues. Model after the U.S. securities regime, Korea has adopted a securities-related class action law that took effect in January 2005. See, Chung 2004: 165.
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