

In Defence of China's Public Enforcement in Equity Market

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Introduction

Professor Jackson and Professor Roe of Harvard Law School have recently published a cross-countries empirical work trying to ascertain which enforcements work to protect investors.¹ Private enforcement is examined primarily through the investigation in both disclosure and private liability rules.² On the other hand, securities regulators' resources serve as a proxy for the intensity of public enforcement.³ This article seeks to add a missing puzzle piece to Jackson and Roe's study in the sphere of public enforcement, by looking at the situation of China, which they did not cover in the study. This is to be done by especially making reference to the United States.

It is often suggested that China's regulatory system was modelled on that of the United States, in spite of many disparities between the two.⁴ As China is an emerging economic superpower, the market has been hampered by a high degree of state control and bureaucracy and will inevitably move towards a more liberal one.

Such oversight patterns are related to the nature of the market. Dispersed ownership in the Anglo-American system has been nurtured by good quality investor protection offered through various legal and market mechanisms. In contrast, the Chinese stock market is still essentially speculative and dominated by short-term investment with a high turnover ratio. In this situation, state control may be desirable to ensure the quality of issuers.

This article argues that China has been committed to public enforcement based on resource-based evidence. Yet certain path dependencies may prevent it from

functioning properly. The article first gives an overview of the regulatory framework in China and the United States. Then it moves on to compare the China Securities Regulatory Commission (CSRC) and the Securities and Exchange Commission (SEC) in light of self-regulation, the public offering system and enforcement input/output. In terms of the bases of evaluation, this article takes into account of the resource-based measures (i.e. budget and staff size) and enforcement outcomes (i.e. enforcement actions brought or financial sanctions levied). Furthermore, it highlights their potentially changing roles in response to the financial crisis. China shifts from concentrated market towards dispersed market while the United States replaces unregulated capitalism with a proactive government intervention policy. The final part concludes.

A snapshot of the securities regulatory framework in China and the United States

Generally speaking, there are three models of securities regulation: the US, the UK and the hybrid models.⁵ The US model is characterised by comprehensive securities law, which provides regulatory rule for primary and secondary markets, issuers, underwriters, brokers and investment advisors. By contrast, in the past, the UK model emphasised the listing requirements and the importance of self-regulation by securities participants rather than a substantial securities act. However, since the Financial Services and Markets Act 2000 (FSMA) in the United Kingdom authorised the Financial Services Authority (FSA) as the sole regulator for the financial markets with strong enforcement, the role of self-regulation in the UK market has been diminishing.⁶ The third model, which is popular in some emerging markets such as China, combines the first two models and fosters the regulatory role of both securities law and self-regulation. The different models of securities regulation framework share a common purpose to safeguard the designed functions of securities markets. In light of the purpose of this article, it only looks at the Chinese and US regulatory frameworks.

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¹ Howell Jackson and Mark Roe, "Public and Private Enforcement of Securities Laws: Resource-Based Evidence" (2009) 93(2) *Journal of Financial Economics* 207.

² See also Rafael La Porta et al., "What Works in Securities Laws?" (2006) 61 *Journal of Finance* 1.

³ See also Howell Jackson, "Variation in the Intensity of Financial Regulation: Preliminary Evidence and Potential Implications" (2007) 24(2) *Yale Journal on Regulation* 253.

⁴ China's Securities Law of 1999 imitated the US disclosure principle and numerous substantive provisions. To a large extent, Chinese securities law was similar to the US. In the course of its amendment in 2005, international symposia were held with foreign experts from the US as well as other countries. See Robert Art and Minkang Gu, "Securitisation of State Ownership: Chinese Securities Law" (1996) 18 *Michigan Journal of International Law* 115, 123; Xin Tang, "Protecting Minority Shareholders in China: A Task for Both Legislation and Enforcement" in Hideki Kanda et al. (eds) *Transforming Corporate Governance in East Asia* (London: Routledge, 2008); and Jian Fu and Jie Yuan, *PRC Company & Securities Laws* (Singapore: CCH Asia, 2006), p.24.

⁵ Meng Wan, "The Securities System in China", in Joseph Norton et al. (eds), *Financial Regulation in the Greater China Area: Mainland China, Taiwan and Hong Kong SAR* (London: Kluwer, 2000), p.117; and Yuwa Wei, "The Development of the Securities Market and Regulation in China" (2005) 27 *Loyola Los Angeles International and Comparative Law Review* 479, 497–498.

⁶ Chenxia Shi, "Protecting Investors in China through Multiple Regulatory Mechanisms and Effective Enforcement" (2007) 24(2) *Arizona Journal of International & Comparative Law* 451, 454. Also Sir Howard Davies identifies that the FSMA marks a formal shift in regulatory culture from the self-regulatory approach to a fully statutory basis and the end of self-regulation. See Howard Davies, "Performing Financial Regulation: Progress and Priorities" in Elis Ferran and Charles Goodhart (eds), *Regulating Financial Services and Markets in the 21st Century* (Oxford: Hart, 2001), pp.17–24. The enforcement intensity of the FSA is expected to increase further; see "Insider Dealing Probe Unit Doubled at FSA", *Financial Times*, May 6, 2008.

China's regulatory framework

The regulation of China's financial industry is subject to a model of separate regulation, placing securities, banking and insurance industries under separate supervision and administration of, respectively, the CSRC, the China Banking Regulatory Commission (CBRC) and the China Insurance Regulatory Commission (CIRC).⁷ In accordance with the law, and as duly authorised by the State Council, the CSRC performs centralised regulation of the nation's securities and futures markets. Under this system, the CSRC is responsible for drafting laws concerning the securities and futures market and organising investigation. To supplement the regulatory activities of the CSRC, the stock exchanges are in charge of the self-disciplinary and front-line supervision of members, listed companies and their related securities trading activities.

CSRC—a quasi-governmental organisation

China's stock market was established as an "experiment" in the mid-1980s.⁸ In the beginning, regulation was very fragmentary and, in the absence of laws, decisions were often ad hoc. Even after the establishment of the Shanghai Stock Exchange (SHSE) and the Shenzhen Stock Exchange (SZSE) respectively in 1990 and 1991, there was confusion over the roles of regulators as there were three regulatory agencies, the State Council Securities Commission (SCSC), the People's Bank of China and the CSRC, having overlapping duties. The two exchanges and the Ministry of Finance also regulated companies and financial intermediaries under their purview. These overlapping regulators led to uncertainties and in some cases, inaction.⁹

As an attempt to cure this somewhat chaotic situation, the Securities Law, which was enacted in 1998, provided that the CSRC was the sole regulator supervising the nationwide securities and futures markets.¹⁰ Simultaneously the SCSC ceased operations. The two stock exchanges are under the ultimate authority of the CSRC and they are delegated powers to regulate companies under their jurisdiction. The purpose of the consolidation of regulatory agencies is to remove the inconsistencies and inefficiencies once existed in the old multiple regulatory system.

The Securities Law gives power to the CSRC to investigate and sanction firms and individuals over securities and corporate fraud. The CSRC is also

responsible for advising on changes to laws, formulating regulations for the securities markets, vetting listing applications, and supervising companies, securities firms, investment institutions, sponsors, stock exchanges, and professional bodies and persons (auditors, securities lawyers, stockbrokers).

On paper, the CSRC is the national regulator, charged with enforcing rules, maintaining order and generally protecting investors. Meanwhile the regulator is also a government agency, operating under party direction, and as such it has also been mandated to support the government's industrial policy.¹¹ This has primarily involved supporting former state-owned enterprises (SOEs). The operation of the quota system allowed funds to be channelled towards SOEs.¹² In addition to ensure that SOEs had access to equity market, the CSRC were under considerable pressure in the 1990s to ensure the demand for these shares was maintained.¹³ The Government allowed speculation to go on more or less unhindered since a clampdown in the secondary market would have reduced liquidity and destroyed demand for shares. This problem was one of the policy priorities and political will of the Chinese state.

Securities market: modernising and liberalising

China's legal framework for securities markets and listed companies began a path of development in the early 1990s.¹⁴ Current major laws include: the Securities Law; the Company Law¹⁵; the Securities Investment Fund Law¹⁶; the Criminal Law.¹⁷ The Securities Law and the Company Law regulate the issuance of securities and shares. Specifically, the Securities Law regulates the establishment and operation of stock exchanges and market intermediaries, information disclosure, insider trading and market manipulation.

In addition, the State Council and the CSRC regulations govern aspects of the securities market outside law in order to keep pace with new situations. In recent years, the CSRC initiated a series of reforms to boost the quality of listed companies, to protect investors' rights and interest and to promote the sustained and robust development of capital markets. These included the Code of the Corporate Governance for Listed Companies in China 2002; Opinions on Upgrading the Quality of Listed Companies 2005; and Administrative Measures on the Securities Investor Protection Fund 2005.

⁷ China's Securities Law 2005 art.6. The Securities Law was enacted on December 29, 1998, then was amended on October 27, 2005 and came into force on January 1, 2006.

⁸ Until the 1990s, Chinese leaders had continuously expressed their concerns over the compatibility of the stock market and the socialist state of China. "Are such things as securities and stock markets good or bad? Can they only exist under capitalism? Cannot they also be adapted to socialism?": Speech made by Deng Xiaoping on his Southern Excursion in 1992.

⁹ Gongmeng Chen et al., "Is China's Securities Regulatory Agency a Toothless Tiger? Evidence from Enforcement Actions" (2005) 24 *Journal of Accounting and Public Policy* 451, 457.

¹⁰ China's Securities Law 1998 art.7.

¹¹ Stephen Green, *China's Stockmarket: A Guide to its Progress, Players and Prospects* (London: Profile Books, 2003), p.168.

¹² The quota system operated in 1993 to create a governance structure that aimed to protect a pre-mature market. The fourth part of this article discusses this in detail.

¹³ Green, *China's Stockmarket*, 2003, pp.168–169.

¹⁴ See generally Daniel Anderson, "Taking Stock in China: Company Disclosure and Information in China's Stock Markets" (2000) 88 *Georgetown Law Journal* 1919.

¹⁵ It was promulgated by the Standing Committee of National People's Congress (SCNPC) on December 29, 1993, and then was amended in 1999 and 2005.

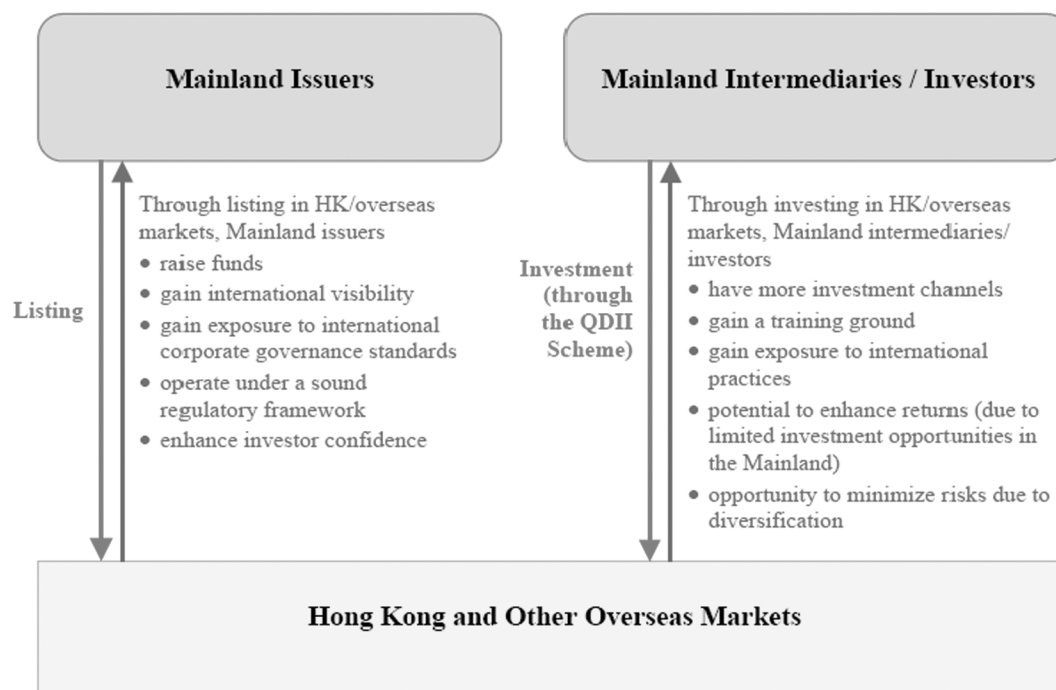
¹⁶ It was promulgated by the Standing Committee of NPC on October 28, 2003 and came into force on June 1, 2004.

¹⁷ It was promulgated by the NPC in 1979, and was amended on May 14, 1997, then came into force on October 1, 1997.

China's accession to the World Trade Organization (WTO) in December 2001 catalysed the development and regulation of its securities markets. To help to fulfil China's securities services commitments, China has launched a series of reforms to open up its market. For example, the qualified foreign institutional investor (QFII) scheme, which was introduced in December 2002 by the CSRC, opens the domestic A-shares market to selected foreign investors. Conversely, the qualified domestic institutional investor (QDII) scheme, which was launched in May 2006, allows licensed domestic institutional

investors to invest in overseas markets. These reforms make the markets more internationally competitive by encouraging further liberalisation of the securities markets and foreign investment. Meanwhile, China encourages companies to list abroad. Figure 1 shows that China is increasing participation in international markets through QDII and listing so as to hasten its convergence with international standards.

Figure 1: China Exposed to International Markets



Source: Securities and Futures Commission of Hong Kong, "Positioning of Hong Kong amid Reforms in the Mainland Financial Markets", Research Paper No.30 (2006).

The US regulatory framework

The US regulatory structure has remained largely unchanged since the 1930s even though the financial industry has undergone many fundamental changes. Regulatory oversight in the United States is complex. The SEC is responsible for the securities markets: depending on charter type, four federal agencies, as well as state agencies, overseas banking and thrift institutions. States typically maintain depository and insurance commissions that examine depositories, along with federal agencies, and supervise and regulate insurance companies. The complexity of the US regulatory apparatus has caused observers to question its efficiency, and is one of the primary reasons that the Treasury Department proposed reforms in its Blueprint.¹⁸

SEC—an independent agency

The SEC was established in 1934 by the US Congress under the Securities Exchange Act of 1934, which, like the Securities Act of 1933, which was enacted as a result of the 1929 stock market crash. It was given the duty to ensure "full and fair" disclosure of all material facts concerning securities offered for public investment. Its intention was not necessarily to prevent speculative securities from entering the market, but to insist that investors be provided with adequate information. The initiation of litigation in cases of fraud and the provision for proper registration of securities are two important supplemental objectives of the SEC. Unlike regulators in other nations, no US government entity administers or oversees the SEC. It is an independent agency, operating under the executive branch of government.

¹⁸ The Department of the Treasury's *Blueprint for a Modernised Financial Regulatory Structure* was published in March 2008. The whole text is available at <http://ustreas.gov/press/releases/reports/Blueprint.pdf> [Accessed August 18, 2010].

The SEC implements rules. The scope of the regulatory power is reflected primarily in rules and regulations adopted by the SEC in its application of several federal securities laws.

The SEC issues interpretative releases to state its position on a subject or to explain provisions of securities law which might pose problems of application. The SEC also gives individual rulings to companies upon request, in the form of either exemptive orders or no-action letters. No-action letters allow an SEC division to inform the parties making the request that it will not recommend that the SEC takes enforcement action regarding the transaction in question. No-action letters are not legal interpretations and are not binding on courts but are valuable means of asking an SEC division for a position regarding its enforcement of the rules. No-action letters play a very important role in the application of the securities law since in practice they can determine whether and in what form a proposed transaction can be carried out.

The SEC is permitted to delegate some of its regulatory powers to self-regulatory organisations, such as the stock exchanges and the National Association of Securities Dealers Inc (NASD). The rules adopted by such self-regulatory organisations must be submitted for approval by the SEC under s.19 of the 1934 Act.

Securities regulation—toughening

The United States has long had a reputation for its stringent legal system despite the wave of the Enron and Worldcom scandals and the financial crisis have cast doubt on it.

The US system of government regulation derives from the US Constitution. Under the Constitution, all powers not expressly granted to the Federal Government are reserved to the individual states. Federal regulation of the securities markets began in the 1930s following the collapse of the markets in the Great Depression. In response, the US Congress enacted a series of statutes between 1933 and 1940. These statutes were designed to protect US investors by regulating public offers and trades in the securities markets. The federal securities statutes are administered by the SEC.

To date, the federal securities laws with which the SEC is concerned are the Securities Act of 1933, the Securities Exchange Act of 1934, the Trust Indenture Act of 1939,

the Investment Company Act of 1940, the Investment Advisers Act of 1940 and the Sarbanes-Oxley Act of 2002 (SOX).

Notably, the SOX was characterised as “the most far reaching reforms of American business practices since the time of Franklin Delano Roosevelt”.¹⁹ It was a reaction to the large US corporate scandals such as Enron and Worldcom in 2001–2002. The objective of the SOX was to strengthen corporate responsibility and financial disclosures, preventing corporate and accounting frauds. It mandated a number of reforms to enhance corporate responsibility, and created Public Company Accounting Oversight Board (PCAOB) to oversee the activities of the auditing profession.

Nevertheless, the debate over the SOX never stops. Some claim that it is extremely significant to restore investor confidence.²⁰ Others argue that it is superficial and a ploy to bolster the status quo.²¹ The costs of implementation are much higher in reality, which may drive honest small and foreign companies away from public registration. According to an investigation by Karolyi and others, deregistration by foreign companies from the time the SOX was passed through 2008 increased sharply.²² Whether the SOX will create more harm than good remains to be seen.

Self-regulation: excessive or insufficient?

In some Western countries, self-regulation is generally thought to promote a liquid and efficient capital market.²³ Advocates argue that self-regulation in stock exchanges has existed since time immemorial.²⁴ In the absence of government regulation, companies were still compelled to disclose information by stock exchanges, e.g. the New York and American Stock Exchanges. Additionally, government regulations may hinder the functioning of companies.²⁵ Frequently government regulators have attempted to assert greater control on the private sector, not for reasons of good corporate governance but rather to thrust policymakers’ ideas on to the system.

Despite the official adoption of self-regulation, Chinese stock exchanges function under the mandate of the CSRC. Before the Company Law was promulgated, the CSRC released preliminary rules on the content and form required for information disclosure by listed companies in June 1993.²⁶ The rules covered share issues, the prospectus, the annual report, changes in shareholding and listing shares. The Securities Law reinforced the

¹⁹ On July 30, 2002, President George W. Bush signed the SOX into law and made this comment.

²⁰ See, e.g., “SEC Chief Set to Priorities Executive Pay Reform”, *Financial Times*, July 31, 2003.

²¹ See, e.g., Lawrence Cunningham, “The Sarbanes-Oxley Yawn: Heavy Rhetoric, Light Reform (and It Just Might Work)” (2003) 35 *Connecticut Law Review* 915, 917–923; Jeffrey Oldham, “Taking ‘Efficient Markets’ our of the Fraud-on-the-market Doctrine after the Private Securities Litigation Reform Act” (2003) 97 *Northwestern University Law Review* 995, 998.

²² They explain foreign companies list shares in the US in order to raise capital at the lowest possible cost to finance growth opportunities, when those opportunities disappear, a listing becomes less valuable to corporate insiders and they go home if then can. See Andrew Karolyi et al., “Why Do Foreign Firms Leave US Equity Markets?”, Fisher College of Business Working Paper Series (2009) available at <http://www.ssrn.com/abstract=1376450> [Accessed August 18, 2010].

²³ Self-regulation is the process of allowing industry to correct systemic problems within that industry without government intervention. Some examples of self-regulated organisations include stock exchanges and the NASD in the US. See US Securities Exchange Act 1934 s.6.

²⁴ Hemendra Aran and Alpesh Patel, *Global Financial Markets Revolution* (New York: Palgrave, 2006), p.99.

²⁵ Aran and Patel, *Global Financial Markets Revolution*, 2006, p.99.

²⁶ CSRC, “Information Disclosure and Corporate Governance in China” (1993), available at <http://www.oecd.org/dataoecd/6/60/1931117.pdf> [Accessed August 18, 2010].

CSRC's position, requiring stock exchanges to timely report any abnormal trading to the CSRC and to seek CSRC approval to form rules for listing, trading and membership.²⁷

The reinforcement of the CSRC's role in the securities market is to ensure the functional operation of exchanges. Nevertheless, the tight control over the exchanges by the CSRC has limited their capacity for self-regulation and has thus constrained their independent operation.²⁸ The formulation and amendment of the constitution of a stock exchange shall be subject to the approval of the CSRC.²⁹ Also, the CSRC approves the appointment and removal of the general manager of the stock exchanges as well as the listing rules, trading rules, membership rules and other relevant rules.³⁰ The exchanges can suspend, terminate, and resume bond and share trading, as CSRC-established procedures allow.³¹ Furthermore, an application for listing shares on the stock exchange must first be submitted to the CSRC.³² The stock exchanges must also report abnormal trading to the CSRC.

In comparison, the SEC intervenes less when regulating stock exchanges and listed companies, although the US securities regulation regime is considered strict. Its authority in this area is limited to trading rules, and it does not interfere with issuer-related matters.³³

The degree of self-regulation may well reflect the nature of market. Dispersed ownership in the Anglo-American system has been nurtured by good quality investor protection offered through various legal and market mechanisms.

By contrast, Chinese stock market is still essentially speculative and dominated by short-term investment with high turnover ratio. The Chinese capital market is dominated by small retail investors. The number of investor accounts increased from 8.35 million in 1992 to nearly 138 million by the end of 2007.³⁴ However, small investors, with less than RMB 1 million in cash or shares equivalent, accounted for about 99 per cent of the total number of accounts.³⁵ The majority of them have low-to-middle income, and 55.63 per cent have an annual income below RMB 20,000.³⁶ Meanwhile, all investors tended to have relatively short investing periods with frequent trading pattern. The average turnover ratio in China's stock market is nearly seven times higher than those in more mature markets.³⁷

Moreover, Chinese institutional investors remain relatively scarce in the market and have yet to play an important role. Compared with Western countries, they tend to hold shares for shorter period of time, trade more frequently, and exhibit a stronger desire for short term investment gain.³⁸ In this situation, state control may be desirable to ensure the quality of issuers.

Public offering system

Around the world, there are two main types of systems for listing shares. One is the registration system while the other is the verification and approval system.³⁹ The former is simpler, popular in the United States, the United Kingdom, Hong Kong, Australia, Canada, Singapore, Germany and France. As long as the applicant complies with all the prescribed listing requirements, no further procedures are required. In this system, the market is the ultimate decisive factor. By contrast, under the verification and approval system, the authority will examine and verify the documents for listing, and if necessary, disallow the company's listing. Therefore, in practice, the authority has the power to decide whether a company can be floated or not. This system is adopted by China, New Zealand, Sweden and Switzerland.

Before the approval system, the quota system operated in 1993 in China with the intention of curbing the potential excessive investment demand in a premature market. The entire listing process was the component of a state plan. Provincial governments and industry supervising bodies were assigned issue quota and they would recommend enterprises for listing within the given quota. The CSRC would then review each listing applicant. The quota system allowed funds to be channelled towards important sectors such as natural resources, utilities, heavy industry and manufacturing SOEs. However, this system was damaging in at least two ways.⁴⁰ First, the Government regularly used it to manipulate market sentiment. Secondly, the whole process was inevitably vulnerable to lobbying and corruption.

The quota system was eliminated in 2000, although the CSRC has continued to operate an approval system. The Securities Law empowers the CSRC in charge of approving securities and making rules for listed companies.⁴¹ Issues such as listing companies' creditworthiness, the issuance size and time for listing

²⁷ China's Securities Law 2005 arts 115 and 118.

²⁸ Shi, "Protecting Investors in China through Multiple Regulatory Mechanisms and Effective Enforcement" (2007) 24(2) *Arizona Journal of International & Comparative Law* 451, 478.

²⁹ China's Securities Law 2005 art.103.

³⁰ Securities Law 2005 arts 107 and 118.

³¹ Securities Law 2005 arts 55, 56, 60, 61.

³² Securities Law 2005 art.50(1).

³³ See general information on the SEC website, "What We Do", available at <http://www.sec.gov/about/whatwedo.shtml> [Accessed August 18, 2010].

³⁴ CSRC, *China Capital Markets Development Report* (Beijing: China Financial Publishing, 2008), p.195.

³⁵ CSRC, *China Capital Markets Development Report*, 2008, p.269.

³⁶ Bin Chen et al., "Zhongguo Gushi GerenTouzizhe Zhuangkuang Diaocha" (An Investigative Report on the Situation of Individual Investors in China's Securities Markets) (2002) Shenzhen Zhenquan Jiaoyisuo Zonghe Yanjiusuo (Research Institute of the Shenzhen Stock Exchange) Paper No.0055, available at <http://www.sse.com.cn/cs/zhs/cxjl/jy/dtcc/jydt/news108.htm> [Accessed August 18, 2010].

³⁷ CSRC, *China Capital Markets Development Report*, 2008, pp.271-272.

³⁸ CSRC, *China Capital Markets Development Report*, 2008, p.272.

³⁹ Alex Lau, "A Study on Listing Applications in the People's Republic of China" (2007) 28 *Company Lawyer* 90, 92.

⁴⁰ Green, *China's Stockmarket*, 2003, p.161.

⁴¹ China's Securities Law 2005 art.7.

are largely controlled by the CSRC. It remains concerned not only about the veracity of company's accounts, but also about the quality of company, which industry it operates in and its ownership structure. In this sense, the approval system is prone to administrative influence and complex approval procedure.

While all listing and trading matters are largely regulated by the CSRC, the two national stock exchanges have primary control over the daily trading of domestic shares, and receive and scrutinise listing applications.⁴² Under art.50 of the Securities Law, a stock exchange may specify listing conditions which are more stringent than those specified in the legislation, as long as those conditions are first approved by the CSRC.

On the other hand, most mature markets adopt the registration system. It is largely market-driven, and there is more room for intermediaries and professional institutional investors to play a role during the process.

Under s.5 of the US Securities Act, a registered offer may be divided into three stages. The first stage is the period after a company decides to make a public offer and prior to the filing of the registration statement with the SEC (pre-filing period). The second stage is the period after the filing of the registration statement and prior to its effectiveness (waiting period). The final stage is the period after the registration statement becomes effective.

Registration statements filed with the SEC under the 1933 Act are subject to review by the SEC. However, the SEC does not judge the merits of securities offered for sale. Furthermore, its review process does not guarantee completeness or accuracy in the reports filed with the SEC. The securities laws provide for the disclosure of material financial and other information. They also impose severe penalties for presenting false and misleading information and other fraudulent acts. The SEC's role is to determine if the evidence presented in the filed reports indicates satisfactory compliance with the applicable statutes and regulations.

Law enforcement

The intensity of enforcement efforts by securities regulators differs widely among jurisdictions, but common law countries are assumed to be much more active enforcers than civil law countries. Scholars attempt to test this assumption from different perspectives. La Porta et al. developed a public enforcement index based on formal characteristics of the regulators such as their investigative powers and capacity to impose civil sanctions to measure public enforcement strength.⁴³ Jackson and Roe adopted a resource-based approach

including their staffing levels and budgets, and again reached a similar conclusion.⁴⁴ Coffee has sought to explain the motivation of common law countries to invest more because their stock markets are larger, more valuable national assets.⁴⁵ Another explanation is the social contract theory that social democracies in Continental Europe press managers to stabilise employment and to forego some profit maximising opportunities.⁴⁶

Enforcement efforts can be sensibly measured in terms of inputs (i.e. budget and staff size) and/or outputs (i.e. enforcement actions brought or financial sanctions levied). Hence, this section will compare the public enforcement in China and the United States in accordance with these indicators

The baseline

In China, the law vests the CSRC with the primary power to implement regulations and supervise markets. It uses three tools to punish listed companies. First, for lesser infractions, the CSRC may issue reprimands called "correction orders", in which a company or individuals is told to correct certain behaviour. However, correction orders are not formal administrative sanctions and thus do not make target companies eligible for civil lawsuits. Secondly, it issues more serious administrative sanctions which may be in the form of formal warnings or fines.⁴⁷ Fines for companies range from RMB 300,000 to 600,000; individuals are subject to fines ranging from RMB 30,000 to 300,000.⁴⁸ Thirdly, individuals who commit serious violations may also be barred from participation in the securities markets and from serving as a senior manager or director of a listed company.⁴⁹

Meanwhile, two national stock exchanges play their self-regulatory role.⁵⁰ They have four regulatory tools at their disposal including oral warnings (*koutou jinggao*), letters of oversight and supervision, notice of criticisms (*tongbao piping*) and public censure (*gongkai quanze*). Generally, public censure is made public, the less severe sanctions are considered to be non-public "internal oversight measures".

By contrast, US securities enforcement efforts are notable in the number of governmental agencies and quasi-governmental agencies. The SEC is responsible for investigating suspected violations of the federal securities law. Apart from the SEC, the Department of Justice, the state securities commissions, plus the NASD and NYSE also play major roles and impose substantial sanctions on wrongdoers in securities markets.

⁴² Securities Law 2005 arts 48, 52–54.

⁴³ La Porta et al. "What Works in Securities Laws?" (2006) 61 *Journal of Finance* 1. However, their argument attracted lots of criticisms. For a summary, see John Coffee, "Law and the Market: The Impact of Enforcement" (2007) 156(2) *University of Pennsylvania Law Review* 229, 258.

⁴⁴ Jackson and Roe, "Public and Private Enforcement of Securities Laws" (2009) 93(2) *Journal of Financial Economics* 207.

⁴⁵ Coffee, "Law and the Market" (2007) 156(2) *University of Pennsylvania Law Review* 229, 297.

⁴⁶ For general discussion, see Mark Roe, *Political Determinations of Corporate Governance: Political Context, Corporate Impact* (Oxford: OUP, 2006); and Mark Roe, "Legal Origins, Politics, and Modern Stock Markets" (2006) 120 *Harvard Law Review* 460.

⁴⁷ In most cases companies or individuals are both fined and warned while in a small number of cases the CSRC has imposed either only a warning or only a fine.

⁴⁸ China's Securities Law 2005 art.193.

⁴⁹ Securities Law 2005 art.233.

⁵⁰ Securities Law 2005 art.102.

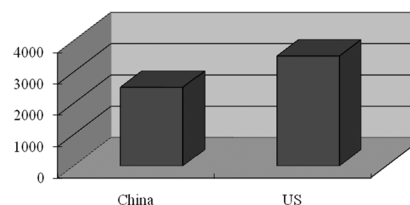
Enforcement inputs

The value of public enforcement of securities law can be evaluated based on the regulator's budgetary resources and staffing levels. This methodological approach is used by some scholars such as Jackson, Roe and Coffee.⁵¹ Higher budgets and greater staffing allow the regulator to examine allegations of wrongdoing, to write its rule, to conduct market surveillance and review filings, and to act more often to remedy, prevent and punish wrongdoing. Regulatory independence and high levels of agency authority are of little value to effective enforcement if the agency's budget is minuscule and its staffing thin.

Two measures of public enforcement inputs are feasible: the first is the size of regulatory staff scaled by stock market capitalisation; the second is the securities regulatory budget scaled by stock market capitalisation. Unfortunately, the budget of the CSRC in China is not available. All revenue and expenditures of the CSRC are included into the fiscal budget of the Central Government. The supervision fees levied by the CSRC on securities and futures market participants are paid directly into the National Treasury. Expenditures of the CSRC are covered by budgetary appropriation. But this data is not publicised. Hence this section only compares staffing in China and the United States owing to data limitations.

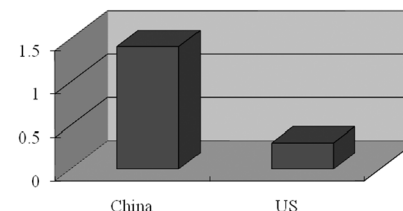
High staffing would make it easier for the public authorities to conduct market surveillance. In 2008 total number of staff in the SEC was 3,511 while China had 2,512 staffs.⁵² In the same year, the market capitalisation in the United States reached about US\$11,737 billion while China had US\$1778 billion worth of shares in equity market.⁵³ These variables are described in Figure 2 and reported in Figure 3 regarding the value of the staffing per billion stock market capitalisation. Surprisingly, the ratio of staff to market capitalisation in China was more than four times than that in the United States. As regards, China is apparently committed to enforcement and has devoted significant resources for the purpose. This is reflected from the fact that, although the central organisational structures of both regulators are essentially similar, the CSRC has triple the number of regional offices than the SEC.⁵⁴

Figure 2: Staff in CSRC and SEC in 2008



Source: SEC Performance and Accountability Report 2008 and CSRC Annual Report 2008.

Figure 3: Staff per Billion of Stock Market Capitalisation in 2008



Source: SEC Performance and Accountability Report 2008; CSRC Annual Report 2008 and World Federation of Exchanges.

Enforcement outputs

Input data has its limitations.⁵⁵ Alternatively, enforcement can be gauged either in terms of the number of actions brought or the aggregate financial sanctions levied. For the former, Figure 4 shows the annual average number of actions brought by the SEC and the CSRC over the 2002 to 2004 period. The total number of actions by the SEC was high, averaging 639 actions per year.⁵⁶ In contrast, the CSRC was extremely inactive with only 33.6 actions per year in the same period⁵⁷ (see Figure 4). However, the observation is different when enforcement actions were scaled by each billion of stock market capitalisation (see Figure 5). The enforcement in China was surprisingly more intense. This is inconsistent with the perception that the United States has one of the toughest public securities regulators, while the law enforcement in China is suboptimal. One of the possible explanations is that a public regulator is not the only law enforcer in the market. The role of stock exchanges and other quasi-government agencies cannot be underestimated. By taking them into account, the number of actions in the United States per annum in that period would rise to around 3,600 and dwarf that of China immediately.⁵⁸

⁵¹ Jackson and Roe, Public and Private Enforcement of Securities Laws" (2009) 93(2) *Journal of Financial Economics* 207; Coffee, "Law and the Market" (2007) 156(2) *University of Pennsylvania Law Review* 229, 297.

⁵² SEC, "Performance and Accountability Report 2008", p.9, available at <http://www.sec.gov/about/secpar/secpar2008.pdf> [Accessed August 18, 2010], and CSRC, "Annual Report 2008", p.7, available at http://www.csrc.gov.cn/pub/csrc_en/about/annual/200907/P020090701496625000834.pdf [Accessed August 18, 2010].

⁵³ World Federation of Exchange, Domestic Market Capitalisation 2008, available at <http://www.world-exchanges.org/statistics/annual/2008/equity-markets-0> [Accessed January 15, 2010].

⁵⁴ For the organisation charts of the CSRC and the SEC, see "CSRC Annual Report 2008", p.5, at http://www.csrc.gov.cn/pub/csrc_en/about/annual/200907/P020090701496625000834.pdf [Accessed August 18, 2010], and SEC, "Performance and Accountability Report 2008", p.9, at <http://www.sec.gov/about/secpar/secpar2008.pdf> [Accessed August 18, 2010].

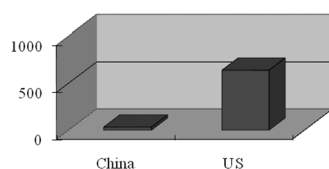
⁵⁵ Simply because a securities regulator has ample resources does not guarantee it utilises them to bring enforcement actions, to write good rules and to hire good people. For arguments, see Jackson and Roe, Public and Private Enforcement of Securities Laws" (2009) 93(2) *Journal of Financial Economics* 207, 210-211.

⁵⁶ Jackson, "Variation in the Intensity of Financial Regulation" (2007) 24(2) *Yale Journal on Regulation* 253, 280.

⁵⁷ Benjamin Liebman and Curtis Milhaupt, "Reputational Sanctions in China's Securities Market" (2008) *Columbia Law Review* 929, 942.

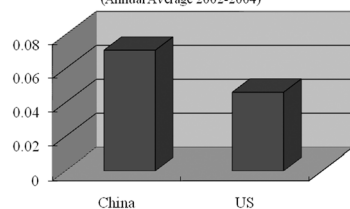
⁵⁸ Liebman and Milhaupt, "Reputational Sanctions in China's Securities Market" [2008] *Columbia Law Review* 929, 942.

Figure 4: CSRC and SEC Enforcement Actions
(Annual Average 2002-2004)



Source: Jackson, “Variation in the Intensity of Financial Regulation” (2007) 24(2) *Yale Journal on Regulation* 253; Liebman and Milhaupt, “Reputational Sanctions in China’s Securities Market” [2008] *Columbia Law Review* 929.

Figure 5: Actions per Billion Stock Market Capitalisation
(Annual Average 2002-2004)



Source: Jackson, “Variation in the Intensity of Financial Regulation” (2007) 24(2) *Yale Journal on Regulation* 253; Liebman and Milhaupt, “Reputational Sanctions in China’s Securities Market” [2008] *Columbia Law Review* 929; and World Federation of Exchanges.

Turning from the number of actions brought to the aggregate monetary sanctions imposed, the data of 2008 for the SEC and the CSRC was revealing. In 2008, the number of actions brought by the SEC was 671, six times more than the CSRC, which took 107 actions in the same year.⁵⁹ Accordingly, the SEC required the violators to disgorge illegal profits and to pay penalties total of approximately US\$1030 million,⁶⁰ while US\$46.83 million was confiscated by the CSRC.⁶¹ Monetary penalties in the United States exceeded that in China, by a ratio of 22 to 1. It is worth noting that the size of the US market was just around six times larger than that of China.

Regulatory response to the financial crisis

The financial crisis has revealed the vulnerabilities of the international financial system. A broader consensus has emerged around the view that an inadequate regulatory framework and passive government intervention have been at the root of the problem. Government is often blamed for market failure with significant losses in output and employment.⁶² Another cause of blame is bad regulation or supervision.⁶³ The third is the failure of some institutions to manage the freedom that comes with deregulation and financial liberalisation.⁶⁴ The policy question for government is “how far to allow the unfettered private sector to manage risks in the financial sector?”. Few governments are willing to turn a blind eye to the inherent political and economic issues involved. This section will explore how the Chinese and US governments step into markets and their regulatory reforms in response to the financial crisis.

China: from concentrated market towards dispersed market

Ongoing non-tradable shares reform

Admittedly, the non-tradable share reform is not a direct action in response to the financial crisis. It is a part of China’s strategic plan to modernise the Chinese capital market. Non-tradable shares can be traced back to the establishment the SHSE and the SZSE, when large SOEs were increasingly transformed into joint-stock companies. The State Council of China invented three different shares categories in order to prevent the mass privatisation of SOEs. They were state shares, legal person shares and employee shares. This market segmentation had considerable impacts on market liquidity, as two-thirds of all shares (state and legal person shares) cannot be traded on stock exchanges. Such division serves two main purposes: to keep control of SOEs that are floated on the market firmly in the state’s hands, and to maximise IPO proceeds.⁶⁵

With the expansion of the market, the hangover of the non-tradable share on the growth of the capital market has become increasingly imminent. This raised the concerns over China’s commitment to market-oriented principles, market stability and protection of minority shareholder rights. In 2004 the State Council issued

⁵⁹ SEC, “Select SEC and market Data Fiscal 2008”, p.3, available at <http://www.sec.gov/about/secstats2008.pdf> [Accessed August 18, 2010]. CSRC, “CSRC Annual Report 2008”, p.34, available at http://www.csrc.gov.cn/pub/csrc_en/about/annual/200907/P020090701496625000834.pdf [Accessed August 18, 2010].

⁶⁰ SEC, “Select SEC and Market Data Fiscal 2008”, p.2, available at <http://www.sec.gov/about/secstats2008.pdf> [Accessed August 18, 2010].

⁶¹ CSRC, “CSRC Annual Report 2008”, p.35, available at http://www.csrc.gov.cn/pub/csrc_en/about/annual/200907/P020090701496625000834.pdf [Accessed August 18, 2010]. The CSRC reported monetary sanctions in RMB. The figure here is based on exchange rates on August 20, 2009.

⁶² See, e.g., Carlos Pelaez, *Government Intervention in Globalisation: Regulation, Trade and Devaluation Wars* (Basingstoke: Palgrave MacMillan, 2008), pp.80–81; and Martin Wolf, *Why Globalisation Works* (New Haven: Yale University Press, 2005), p.14.

⁶³ See, e.g., Financial Services Authority (FSA), “The Turner Review: A Regulatory Response to the Global Banking Crisis” (2009), p.36.

⁶⁴ John Pattison, *Financial Services Regulation: A Global Approach* (Toronto: University of Toronto Press, 2007), pp.38–39.

⁶⁵ Bernardo Bortolotti and Andrea Beltratti, “The Nontradable Share Reform in the Chinese Stock Market”, FEEM Working Paper No.131.06 (2006), p.2, available at <http://ssrn.com/abstract=944412> [Accessed August 19, 2010].

Several Opinions on Promoting the Reform and Opening-up and the Stable Development of the Capital Market as the basis of the reform.⁶⁶ This document states that stable steps should be taken to solve the circulation problem of the non-tradable shares.⁶⁷ Subsequently in 2005, the CSRC issued *Circular on Relevant Issues Regarding Pilot Programmes of Non-tradable Share Reform of Listed Companies* and launched the non-tradable share reform. The reform was intended to lift such restrictions and make these shares publicly tradable. By the end of 2007, 1,298 companies listed on the SHSE and SZSE had either initiated or completed the process of non-tradable share reform, accounting for 98 per cent of the total listed companies that were subject to the reform.⁶⁸

The reform was remarkable not only for solving legacy structure problems in the market, but also for paving the way for further innovation and dispersed ownership. The Chinese state as the largest shareholders in many listed companies was meant to be eliminated through the non-tradable share reform. As Table 1 shows, among the 916 listed companies in the sample, there were a total of 356 companies controlled by a shareholder who held over 50 per cent shares of a company before the reform.⁶⁹ By contrast, the number of such companies decreased to 74 after the reform.

However, it remains to be seen whether the reform will be successful. For the largest 30 companies in China, the overall percentage of tradable A-shares was only 28 per cent as of August 2008.⁷⁰ For some of them, the percentage was under 10 per cent.⁷¹ This illustrates that the state remains particularly cautious in unwinding the non-tradable shares of the largest and generally most important SOEs. The crucial stage should be in 2009 and 2010 when US\$1,300 billion of shares, accounting for more than 60 per cent of all non-tradable shares, have been scheduled to unlock.⁷²

Stability is the utmost concern

China is said to be a less affected economy in the financial crisis. Therefore the main tasks of the CSRC are to maintain the stability of domestic capital markets rather than to tackle frauds arising from the crisis. For example, the CSRC had suspended all IPOs since September 2008 in order to stabilise the market and prevent investors from losing in the downturn.⁷³ The downside of this measure

is that Chinese companies have been forced to raise funds through alternative channels, for example, overseas listing. During this period, 10 Chinese companies went public in Hong Kong.

Meanwhile, one new and unique requirement for an IPO in China, is that 10 per cent shares of a state-owned company must be transferred to the National Council for Social Security Fund (NCSSF) when the company launches an IPO.⁷⁴ The NCSSF is an institutional investor, which was set up by the central government in August 2000, for managing and operating social security assets. This requirement has two policy motivations. First, it aims at decreasing state shares in a public company, without actually selling the shares on to the market. Secondly it aims to inject more assets into the fund for better social security coverage.

Furthermore, concerns have been raised that the global financial crisis threatens China's rapid economic development and leads to financial difficulties encountered by small and medium-size enterprises (SMEs). There is an urgent need for an effective allocation of resources. In the past, Chinese SMEs mostly sought funds by cross-listing on the Hong Kong GEM or the United Kingdom's Alternative Investment Market (AIM). To build a multi-tier domestic securities market and provide financing opportunities for SMEs, China launched the Growth Enterprises Board (GEB).⁷⁵ On March 31, 2009, the CSRC promulgated the Tentative Administrative Measures of the IPO and Listing on the Growth Enterprises Board, which came into force on May 1, 2009.

US: from laissez faire to a public approach to tightened financial regulation and supervision

The changing role of the government

The financial crisis proved the idea that unregulated capitalism would always produce the best outcomes was wrong. According to the standard classical theory, which goes back to Adam Smith with his *Wealth of Nations* in 1776, an economy can be corrected by an "invisible hand". If people rationally pursue their own economic interests in free markets they will exhaust all mutually beneficial opportunities to produce goods and exchange with one another. The theory also applies to financial

⁶⁶ This document was issued by the State Council on January 31, 2004. Apart from the non-tradable share problem, it also addresses eight other issues such as perfecting the existing regulatory framework, improving the quality of listed companies, co-operation of various departments, etc.

⁶⁷ For more details regarding the process of the non-tradable share reform, see Wai Ho Yeung, "Non-tradable Share Reform in China: A Review of Progress" (2009) 30(11) *Company Lawyer* 340.

⁶⁸ CSRC, *China Capital Markets Development Report*, 2008, p.208.

⁶⁹ Gaosheng Zhang and Shanna Chu, "Guquan Fenzhi Gaige Hou Shangshi Gongsi Guquan Jiegou de Bianhua jiqi dui Gongsi Zhili Jizhi de Yingxiang" (The Influence of Split Share Structure Reform on Ownership Structure and Corporate Governance) (2007) 62 *Xiandai Jingji (Modern Economics)* 17.

⁷⁰ "30 Jia Dashizhi Gongsi jin Sancheng Xianshou Gu yi Liutong" (30 Percent of Shares in the Largest 30 Companies are Tradable), *Zhengquan Ribao* (China Securities Daily), August 28, 2008, available at http://big5.xinhuanet.com/gate/big5/www.cs.com.cn/ssgs/02/200808/t20080828_1568727.htm [Accessed May 20, 2009].

⁷¹ "30 Jia Dashizhi Gongsi jin Sancheng Xianshou Gu yi Liutong" (30 Percent of Shares in the Largest 30 Companies are Tradable), *Zhengquan Ribao* (China Securities Daily), August 28, 2008, available at http://big5.xinhuanet.com/gate/big5/www.cs.com.cn/ssgs/02/200808/t20080828_1568727.htm [Accessed May 20, 2009].

⁷² "Insight: Chinese Bubble Won't Burst yet", *Financial Times*, April 7, 2008 and "Better Stock Performances Expected in Q2", *China Daily*, July 14, 2008.

⁷³ "Investors Prepare for Fresh Flood of Chinese Offerings", *Financial Times*, June 17, 2009.

⁷⁴ Measures on the Transfer of Certain State Shares from the Domestic Securities Markets to the NCSSF 2009 was enacted on June 19, 2009 and came into force on the same day. It was issued by Ministry of Finance, State-owned Assets Supervision and Administration Commission of the State Council, CSRC and NCSSF.

⁷⁵ For more details, see Wai Ho Yeung, "Just another Casino? The Case of Launching the Growth Enterprise Board in China" [2010] *I.C.C.L.R.* 68.

markets. It assumes that people will do due diligence in seeing that what they are buying is worth what they are paying. This theory has been widely accepted by economists and policymakers and is developed into *laissez faire*, characterised by free markets, little or no state intervention and private ownership of property.⁷⁶

However, the financial crisis gives human being an opportunity to rethink and challenge the traditional theory. The financial turmoil started from a subprime crisis in the US in 2006 and has caused ruptures across many other countries in the form of financial failure and as global credit crunch, The collapse of Lehman Brothers, the bailout plans of various financial institutions and a few large automobile manufacturers have cast doubt on the sustainability of the Anglo-American style of market economy. Some scholars realise the economic theory fails to take account of how the animal spirits affect economic behaviour.⁷⁷ Free market without government intervention may lead to economic disasters. The role of governments is to create macroeconomic conditions to ensure a wise *laissez faire* approach rather than free-for-all capitalism.

In the face of the crisis, the actors are forced to reconsider the architectures of financial supervision. A larger role of government's involvement has been called for in market regulation.⁷⁸ For example, in March 2008, US Secretary Henry Paulson announced that his team would undertake a comprehensive examination of the regulatory overlaps in the US financial supervision architecture and launched the *Blueprint for a Modernised Financial Regulatory Structure*.⁷⁹ The Blueprint indicates that government oversight should become broader and deeper. State authorities are empowered to respond to local conditions through two options: first, they could be given a formalised role in rulemaking process; second, state could play an active role in monitoring compliance and enforcement.⁸⁰

SEC moves to rebuild its reputation

The SEC has in the past year been criticised for being slow, inept and captive to industry. Hence the SEC has taken a number of actions to address significant issues that have arisen in the credit crisis. Assertive law enforcement and disclosure are two main focuses. In 2008, the SEC brought 671 enforcement actions—the second highest number of enforcement actions in history. 1,355 investigations had been closed, 260 per cent more than in 2007 (see Table 2). While financial disclosure

cases continued to be the largest category of cases filed, securities offering cases were a significantly higher proportion of the caseload.

The trend of active enforcement has continued. Since 2009 the SEC has opened 10 per cent more cases than the same period last year. And it issued 224 formal orders of investigation, compared with 93 over the same period last year, and filed 147 per cent more temporary restraining orders.⁸¹ In a novel move with a case filed in July 2009, the SEC also attempted to use, for the first time, a “clawback” law against an executive who is not accused of personal wrongdoing. Until then, the commission had only used the clawback provision in the 2002 SOX to pursue individuals accused of involving in a fraud.

Recently, the SEC has taken even more active approach to rebuild its reputation, e.g. a suit against Bernard Madoff and the settlements with Bank of America, General Electric and Hand Greenberg, the former chief executive of AIG. However, there are questions about the SEC's existing resources and its ability to beef up its enforcement programme while simultaneously tackling a broad range of controversial issues, including proxy access allowing shareholders to nominate corporate board members.⁸²

Apart from toughening enforcement, other significant actions in connection with the crisis include improving disclosure. A new database system called IDEA (interactive data electronic applications) was introduced, which would give investors faster and easier access to key financial information about public companies and mutual funds.

Conclusion

Recently, we have witnessed a worldwide wave of reforms and reactions in securities supervisory oversight. Among these regulatory changes, the United States and China as paradigms of developed and developing nations deserve much attention. Undoubtedly, different historical, social and economic environments account for the development of regulatory framework from country to country. Comparing the CSRC and the SEC with respect to self-regulation, public offering system and enforcement capacity, some conclusions can be drawn.

⁷⁶ See generally Chicago school of economics such as Ronald Coase and Milton Friedman, believed that *laissez-faire* government policy was more desirable than government intervention in the economy. Also Alan Greenspan, the former Federal Reserve Chairman, opposed regulation during his 18-year reign in the position. But he concedes to a “flaw” in his market ideology after the credit crunch.

⁷⁷ When confidence is high, and since financial assets are hard to evaluate, people will buy snake oil. And when that is discovered, as it invariably must be, the confidence disappears and the economy goes sour. See “A Failure to Control Animal Spirits”, *Financial Times*, March 8, 2009.

⁷⁸ John Coffee, “Redesigning the SEC: Does the Treasury Have a Better Idea?” (2009) 95 *Virginia Law Review* 707.

⁷⁹ In this report, the Treasury presents a series of short-, intermediate and long-term recommendations for reform of the US regulatory structure. The short-term recommendations present actionable changes to improve regulatory coordination and oversight immediately, including modernise the President's Working Group (PWG) and create a new federal commission for mortgage origination. The intermediate ones focus on eliminating some of the duplication of a functional regulatory system. Treasury also includes a long-term model for discussion. This model holistically addresses the inadequacies of the current functional regulatory system.

⁸⁰ *Blueprint*, 2008, pp.20–21, at <http://ustreas.gov/press/releases/reports/Blueprint.pdf> [Accessed August 18, 2010].

⁸¹ “Enforcement Push Gives SEC Image Boost”, *Financial Times*, August 7, 2009.

⁸² “SEC Moves to Rebuild its Reputation”, *Financial Times*, August 5, 2009.

First, unlike the United States, the CSRC has the dominant regulatory role in the operation of China's stock exchanges, and trading and listing matters. The excessive power by the CSRC restricts self-regulation of the stock exchanges and limits the autonomy of listed companies.

Secondly, since both jurisdictions use different offering systems, the roles of market authorities differ. In the United States, as long as the applicant satisfies all the prescribed listing requirements by exchanges, no further procedures are required. By contrast, the CSRC has the utmost power to decide offering and listing, leaving the stock exchanges little control over them. This may create policy-driven markets. When domestic fund raising channels are restricted, companies would find a way out to list abroad.

Thirdly, probably the most striking contrast is the difference between their enforcement inputs and outputs. Even though the SEC is superior to China in absolute terms regarding the staffing level, the number of enforcement actions brought and the magnitude of the sanctions imposed, China is not inferior to the United States after taking the size of markets into account.

However, the experience of the financial crisis and the inadequacy of the present systems give the two countries impetus to go further. To the United States, it reinforces government intervention, and relies less on spontaneous market discipline and more on holistic supervision.

Meanwhile, the SEC has taken a visibly aggressive stance and brings a raft of high-profile actions to restore market confidence.

To China, the Government continues to carry out the non-tradable share reform, reduces state ownership in public companies and paves the way for dispersed market and the internationalisation. Nonetheless, the problem of state control remains acute. The willingness of the Government to relinquish control in SOEs is doubtful. Three years after the implementation of reform, merely 10 per cent of the unlocked non-tradable shares had actually been sold to the market.⁸³ Conflicts of interests between the state as the owner of many listed companies and as the regulator persist. Encountered by daunting difficulties and pressures, the CSRC insists upon a prudent regulatory approach and has launched a series of policies and initiatives to maintain market stability. China may be committed to enforcement. For example, the CSRC has far more regional offices than the SEC. However, this is not necessarily an advantage. Enforcement teams have been scattered around the country with insufficient manpower.⁸⁴ Also, political influence, owing to interventions or pressure from various interest groups, often rendered the investigations ineffective.⁸⁵ Unless some fundamental problems are to be resolved, throwing in more resources alone may not sufficiently enhance the enforcement efficiency and effectiveness.

⁸³ "Insight: Chinese Bubble won't Burst yet", *Financial Times*, April 7, 2008.

⁸⁴ CSRC, *China Capital Markets Development Report*, 2008, p.279.

⁸⁵ CSRC, *China Capital Markets Development Report*, 2008, p.279.