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Professional Lawyers with Expertise in Finance and Taxation

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Insight: Analysis of the Regulation on Trading Prohibition for Securities Professionals

By Ivy Yang and Iris Lei

In recent years, the China Securities Regulatory Commission (CSRC) has been intensifying its crackdown on securities professionals engaging in illegal stock trading. Between 2019 and 2023, the CSRC investigated 67 cases involving securities professionals' illegal stock trading, resulting in administrative penalties for 139 individuals. On February 9, 2024, the CSRC published an administrative penalty decision on its official website, penalizing 63 securities professionals from China Merchants Securities for illegal stock trading, with one individual facing a lifetime ban from the securities market. The total amount of fines and confiscations imposed on these 63 individuals reached 81.73 million RMB. The handling of this case has sparked widespread discussion within the securities industry and fueled public discourse on the need for stricter regulatory oversight in the sector.

This article will analyze the regulations regarding the prohibition of securities professionals from trading stocks, aiming to raise awareness among industry practitioners.

I. Controversy over the Revision of the Securities Law: Should Securities Professionals Be Absolutely Prohibited from Trading Stocks?

Article 43 of the Securities Law of the People's Republic of China, as amended in 2014 (hereinafter referred to as the "old Securities Law"), stipulates that "employees of securities exchanges, securities companies, and securities registration and settlement institutions, staff of securities regulatory authorities, and other individuals prohibited by laws and administrative regulations from engaging in stock trading, shall not directly or indirectly hold or trade stocks in their own name or under an alias or someone else's name during their term or legal limit. They shall also not accept stocks as gifts from others." This absolute prohibition on securities professionals trading stocks has been a subject of ongoing debate in legal circles, particularly after the introduction of the Fund Law, which permits fund professionals to trade stocks after reporting such activities. Many have argued that securities professionals should be allowed to trade stocks after reporting.

A draft revision published on April 20, 2015, attempted to amend the original prohibitive clause, proposing that "employees of securities business institutions, securities exchanges, and securities registration and settlement institutions, staff of the State Council's securities regulatory authority, and other securities professionals, must declare their securities accounts, including those of their spouses, to their respective institutions in advance and report their securities trading activities within three days after the transaction is completed, the transaction shall not conflict with their official duties or responsibilities."

However, concerns over securities professionals using inside information to trade stocks have persisted. Particularly in cases where evidence and identification of insider trading

are difficult, allowing securities professionals to engage in stock trading could have unpredictable consequences. Therefore, in order to ensure the fairness of the market and prevent harm to investors' interests caused by information asymmetry, the revised Securities Law of the People's Republic of China (2019 amendment) (hereinafter referred to as the "new Securities Law") continues to impose an absolute prohibition on the trading of stocks by securities professionals. The scope of this prohibition was also expanded, covering "stocks or other securities with equity attributes."

II. Entities Prohibited from Participating in Stock Trading

Article 40, Paragraph 1 of the new Securities Law stipulates, "Employees of securities exchanges, securities companies, and securities registration and settlement institutions, staff of securities regulatory authorities, and other individuals prohibited by laws and administrative regulations from participating in stock trading, shall not directly or indirectly hold or trade stocks or other securities with equity attributes in their own name, under an alias, or someone else's name during their term or legal limit. They shall also not accept stocks or other securities with equity attributes as gifts from others."

Regarding the entities prohibited from participating in stock trading, the following points should be noted:

(i) Expansion of the Definition of "Securities Trading Venue"

Compared to the old Securities Law's reference to "securities exchanges," the new Securities Law broadens the scope of "securities trading venues." Securities trading venues now include not only securities exchanges but also other nationwide securities trading venues approved by the State Council, such as the National Equities Exchange and Quotations (NEEQ), regional equity markets, and the Beijing Stock Exchange.

In contrast to the provisions in the "Measures for the Administration of Futures Companies," which explicitly prohibit the spouses of futures professionals from engaging in futures trading, the new Securities Law does not impose such strict restrictions on the individuals prohibited from participating in stock trading.

(ii) Does "Employees" Include Back-office and Middle-office Staff?

The new Securities Law does not provide a specific definition of "employees." According to the "Rules for the Administration of Directors, Supervisors, Senior Management, and Employees of Securities Companies" issued by the China Securities Association, as well as responses in press briefings, "employees" refers to individuals involved in securities business and related management work. This includes those engaged in securities brokerage, securities investment consulting, financial advisory services related to securities trading and investment activities, securities underwriting and sponsorship, margin financing, proprietary trading, market-making activities, securities asset management, and the distribution of financial products, securities investment funds, and custodial services. It also includes compliance, risk management, financial management,

auditing, information technology, settlement, and other middle-office and back-office staff involved in securities operations. Company chairpersons, directors, supervisors, and senior management personnel involved in business management are also considered employees.

However, in practice, the CSRC has expanded the scope of "employees" to include all staff working for securities companies. In the CSRC's Administrative Penalty Decision No. 116 (2019), the CSRC clarified: "The employees of a securities company, as referred to in Article 43 of the new Securities Law, not only include professional personnel engaged in securities business but also encompass staff engaged in party work, auxiliary support services, and comprehensive management within the securities company. The recognition of employees in a securities company does not depend on the possession of professional qualifications or certification."

III. The New Securities Law's Prohibition on Securities Professionals' Stock Trading Extend to Other Securities with Equity Attributes

(i) Definition of "Stocks or Other Securities with Equity Attributes"

According to Article 2 of the new Securities Law, securities include stocks, corporate bonds, depository receipts, government bonds listed for trading, securities investment fund shares listed for trading, and other securities recognized by the State Council in accordance with the law. However, the law does not provide a specific definition of what constitutes "other securities with equity attributes." It can only be interpreted literally as "securities that confer full or partial shareholder rights to the holder."

In conjunction with the China Securities Regulatory Commission's (CSRC) release of the "Several Provisions on Improving the Regulation of Specific Short-Term Trading (Consultation Draft)" in July 2023, it is clear that instruments such as depository receipts and convertible bonds (including convertible corporate bonds and exchangeable bonds), which can be converted into company stocks at a future point, are considered "other securities with equity attributes."

From the implementation of the new Securities Law, it appears that the main focus of "other securities with equity attributes" is on "convertible bonds." For example, on August 11, 2022, the Qingdao Securities Regulatory Bureau imposed a penalty on Ms. Chen, an investment advisor at a securities firm, for violating regulations on stock and convertible bond trading. It was found that during her employment, she illegally traded stocks and convertible bonds using her mother's securities account. The total transaction amount was 23,159,684.08 RMB, and the total profit was 209,394,67 RMB (after deducting commissions and taxes). The Qingdao Securities Regulatory Bureau ordered Ms. Chen to dispose of the illegally held stocks and other securities with equity attributes, confiscated the illegal gains of 209,394.67 RMB, and imposed a fine of 200,000 RMB.

Similarly, in an Administrative Penalty Decision issued by the Guizhou Securities

Regulatory Bureau on August 4, 2023, Mr. Chen, a securities broker at a securities firm, was penalized for engaging in illegal stock and convertible bond trading. The investigation revealed that Mr. Chen used another person's account to trade stocks and convertible bonds, with a total transaction amount of 5,387,657 RMB, resulting in an overall trading loss. The Guizhou Securities Regulatory Bureau ordered Mr. Chen to dispose of the illegally held stocks and imposed a fine of 50,000 RMB.

(ii) Can Securities Professionals Trade Unlisted Company Equity?

According to Article 28 of the China Securities Regulatory Commission's (CSRC) 2022 Measures for the Supervision and Management of Directors, Supervisors, Senior Management, and Employees of Securities and Fund Management Institutions, "Directors, supervisors, senior management, and employees of securities and fund management institutions shall not engage in securities, fund, or unlisted company equity investments in violation of laws, regulations, and the provisions of the CSRC." Although this provision mentions that securities professionals are prohibited from engaging in unlisted company equity investment, the term "relevant provisions" here must be linked to specific legal texts. The applicable regulations for securities professionals are still outlined in Article 40 of the new Securities Law.

Based on the scope of securities defined by the new Securities Law, equity in unlisted companies does not fall under the category of securities and is therefore outside the regulatory scope of the new Securities Law. The authors believe that securities professionals trading unlisted company equity would not be subject to the restrictions in Article 40 of the new Securities Law. However, for investment banking professionals in securities firms and those working for securities firms with state-owned components, in addition to the constraints imposed by the new Securities Law, they are also subject to the Integrity in Professional Conduct provisions in Article 12 regarding the transfer of benefits, as well as restrictions placed on leaders of state-owned enterprises (including internal party and government regulations). Consequently, many compliance departments within securities firms require their employees to disclose internally any investments in unlisted company equity.

(iii) Can Securities Professionals Trade Stock Index Futures?

Under the new Securities Law and the Futures and Derivatives Law, stock index futures are classified as futures products, not "securities with equity attributes." As such, they do not fall under the trading restrictions imposed on securities professionals by the new Securities Law.

Moreover, according to Article 53 of the Futures and Derivatives Law, "Employees of futures trading institutions, futures exchanges, and futures clearing agencies, staff of the State Council's futures regulatory authority and futures industry associations, as well as other individuals prohibited by laws, administrative

regulations, or the State Council's futures regulatory authority from participating in futures trading, are not permitted to engage in futures trading."

The Regulations on the Administration of Futures Trading (2017 Revision), in Article 25, specifies that the following entities and individuals are prohibited from engaging in futures trading, and futures companies are not allowed to accept their orders to trade futures:

- Government agencies and public institutions;
- Employees of the State Council's futures regulatory authority, futures exchanges, futures margin custodians, and futures industry associations;
- Individuals prohibited from entering the securities and futures markets;
- Entities and individuals unable to provide account-opening documentation;
- Other entities and individuals prohibited from futures trading by the State Council's futures regulatory authority.

Therefore, if securities professionals are not prohibited from the market, they are allowed to buy and sell stock index futures.

IV. Distinguishing Between Borrowing Accounts and Managing Client Assets

Securities professionals engaged in illegal stock trading typically do so by directly or using an alias, or by borrowing others' names to hold or trade stocks or other securities with equity attributes, or by accepting stocks or securities as gifts. Based on regulatory enforcement cases, it is common for securities professionals to use others' names for trading stocks. It is important to distinguish between borrowing another person's account to trade stocks and managing client assets, as these two behaviors are treated differently under the law, with varying legal responsibilities (especially in terms of determining illegal gains).

If a securities professional borrows someone else's account to trade for personal benefit, it constitutes a violation of Article 40 of the new Securities Law. The penalty for this behavior is outlined in Article 187:

"Persons prohibited by laws and administrative regulations from participating in stock trading who violate Article 40 of this Law, by directly or using an alias, or by borrowing another person's name to hold or trade stocks or other securities with equity attributes, shall be ordered to deal with the illegal holding of such stocks or securities according to the law, have their illegal gains confiscated, and be fined an amount equal to or less than the value of the securities traded; if the violator is a government employee, further disciplinary action shall be taken according to the law."

On the other hand, if a securities professional controls a client's account for asset management purposes, they violate Article 136 of the new Securities Law, which states, "Securities company employees shall not privately accept clients' commissions to trade securities." The penalty for this is detailed in Article 210:

"Securities company employees who privately accept clients' commissions to trade securities in violation of Article 136 shall be ordered to correct the issue, be given a warning, have their illegal gains confiscated, and be fined between one and ten times the amount of their illegal gains; if no illegal gains exist, a fine of up to 500,000 RMB may be imposed."

In judicial practice, distinguishing between borrowing an account to trade stocks and managing client assets often depends on the source of the funds. Some believe that if the funds originate from the securities professional, it constitutes "using an alias or borrowing another person's name to hold or trade stocks," whereas if the funds come from others, it falls under asset management. A review of similar cases from the China Securities Regulatory Commission (CSRC) indeed suggests that fund sources are a key factor in this distinction. However, the author believe that the source of the funds is merely one aspect. The Beijing High People's Court, in an administrative lawsuit, stated that the determination of "using an alias or borrowing another person's name to hold or trade stocks" does not depend on whether the person prohibited from trading owns the stocks or funds. "Regardless of the source of the funds or whether they are owned by the person, as long as the person can actually control and use the funds to hold or trade stocks, it meets the criteria for penalty under this provision."

V. Legal Consequences of Illegal Stock Trading and Accountability Timeline

(i) Should the Fine Be Based on Illegal Gains or Securities Transaction Amount?

When securities professionals are caught illegally trading stocks, the penalties are typically based on Article 187 of the new Securities Law:

"Persons prohibited from participating in stock trading by laws or administrative regulations who violate Article 40 of this Law by directly or through an alias, or using someone else's name to hold or trade stocks or other securities with equity attributes, shall be ordered to handle the illegal possession of stocks or other securities with equity attributes in accordance with the law, and the illegal gains shall be confiscated. A fine not exceeding the equivalent of the securities traded shall also be imposed. If the violator is a state employee, disciplinary actions shall also be taken in accordance with the law."

This article uses the transaction amount as the standard for the maximum fine. However, since this provision only sets an upper limit for the fine and given that securities are highly liquid, which allows multiple transactions in a short time, the total transaction amount can quickly accumulate. Thus, calculating fines based on transaction volume may deviate from the reality of the case. As a result, in practice, the China Securities Regulatory Commission (CSRC) typically uses illegal gains as the basis for determining the fine amount.

Based on recent penalty cases handled by the CSRC and local regulatory bodies (the authors reviewed cases of securities professionals illegally trading stocks from 2021 to 2023), penalties for such violations have not been calculated based on the accumulated transaction amount. Instead, the fines are typically as follows:

- The violator is ordered to handle the illegal possession of stocks or other securities with equity attributes according to the law.
- Any illegal gains are confiscated.
- A fine is imposed roughly equivalent to the amount of illegal gains.
- If there are no illegal gains, fines ranging from 300,000 to 400,000 RMB are applied, depending on the circumstances.

Here are some summarized cases of securities professionals being penalized for illegal stock trading, for reference:

No.	Date	Authority	Violations	Amount Involved	Penalty Outcome
1	December 2023	Hebei Securities Regulatory Bureau	Stock	Cumulative transaction amount: ¥116,168,771.60, cumulative loss: ¥37,763.60	Ordered to dispose of illegally held stocks and fined ¥30,000.
2	December 2023	Chongqing Securities Regulatory Bureau	Stock	Cumulative transaction amount: ¥5.9853 million, loss: ¥143,300	Fined ¥60,000.
3	December 2023	Beijing Securities Regulatory Bureau	Stock	Cumulative transaction amount: ¥212 million, actual loss: ¥715,100	Fined ¥100,000.
4	November 2023	Shanghai Securities Regulatory Bureau	Stock	Cumulative transaction amount: ¥61.3739 million, actual loss: ¥403,500	Fined ¥100,000.
5	November 2023	Tianjin Securities Regulatory Bureau	Stock	Total transaction amount: ¥70.5445 million, loss: ¥541,100	Fined ¥30,000.
6	August 2023	Tibet Securities Regulatory Bureau	Stock	Total transaction amount: ¥3.3614 million, illegal gains: ¥100,800	Confiscated illegal gains of ¥100,800 and fined ¥100,000.
7	August 2023	Guizhou Securities	Stock and Convertible	Cumulative transaction	Fined ¥50,000.

		Regulatory Bureau	Bond	amount: ¥5.3876 million, overall trading loss	
8	July 2023	China Securities Regulatory Commission (CSRC)	Stock	Cumulative profit: ¥7.2405 million	Confiscated illegal gains of ¥7.2405 million and fined ¥7.2405 million.
9	June 2023	Anhui Securities Regulatory Bureau	Stock	Cumulative transaction amount: ¥908 million, trading loss after deduction of relevant taxes	Fined ¥250,000.
10	June 2023	Tianjin Securities Regulatory Bureau	Stock	Total transaction amount: approximately ¥217 million, profit: ¥221,300	Confiscated the party's illegal gains of ¥221,300 and fined ¥200,000.
11	June 2023	Xinjiang Securities Regulatory Bureau	Stock	Cumulative transaction amount: ¥18.6293 million, profit: ¥25,900	Confiscated illegal gains of ¥25,900 and fined ¥30,000.
12	April 2023	Heilongjiang Securities Regulatory Bureau	Stock	Cumulative transaction amount: ¥16.3821 million, overall trading loss	Fined ¥50,000.
13	March 2023	Hubei Securities Regulatory Bureau	Stock	Cumulative transaction amount: ¥13.7844 million, overall trading loss	Fined ¥30,000.
14	February 2023	Guangxi Securities Regulatory Bureau	Stock	No available data	Issued a warning letter.

15	January 2023	Beijing Securities Regulatory Bureau	Stock	Cumulative transaction amount: ¥724 million, loss: ¥1.8274 million (excluding transactions and gains during the unemployment period)	Fined ¥250,000.
16	January 2023	Shenzhen Securities Regulatory Bureau	Stock	Cumulative transaction amount: ¥36.3107 million, loss: ¥52,900	Fined ¥60,000.
17	January 2023	China Securities Regulatory Commission (CSRC)	Stock	Purchased stocks: ¥5.6042 million, sold stocks: ¥6.2635 million, profit: ¥667,500	Confiscated illegal gains of ¥667,500 and fined ¥667,500.

(ii) Statute of Limitations for Accountability

According to the Administrative Penalty Law of the People's Republic of China and the Administrative Penalty Measures for Securities and Futures Violations, the general statute of limitations for penalties imposed by the securities regulatory authorities is two years. If no violation is discovered within this period, no administrative penalty shall be imposed. However, if the violation involves financial security and has harmful consequences, the statute of limitations extends to five years.

The time limit for penalties is calculated from the date the violation occurred. If the violation is ongoing or continuous, the time limit is calculated from the end of the wrongful act. For example, in Shanghai Regulatory Bureau's Administrative Penalty Decision No. Hu [2022] 3, Liu's actions from September 24, 2013, to June 3, 2020—involving the use of five different securities accounts, including Qin's account, for trading stocks—constituted a continuous violation. The Shanghai Regulatory Bureau initiated an investigation into the case in August 2020, which was within the statute of limitations.

Finally, we remind securities professionals to strictly adhere to the red lines of the Securities Law. It is especially important to strengthen the management of personal identification documents, registered phone numbers, internet-enabled devices, and other related assets. Securities professionals should not lend their accounts to others for login purposes, nor should they use the securities accounts of family members, friends, or

clients to trade stocks or manage securities business.

Case Analysis: Can a creditor file a lawsuit against non-contributing shareholders for the company’s debts in the location of the plaintiff’s domicile?

By Iris Lei

Case Summary:

In 2017, Zhang signed a lease agreement with Beijing Zhongtian Ren Construction Engineering Co., Ltd. (hereinafter referred to as "Zhongtian Ren"). According to the agreement, Zhongtian Ren leased steel pipes and other construction materials from Zhang. Later, due to Zhongtian Ren’s failure to pay rent, Zhang filed a lawsuit with the People's Court of Tancheng County, Shandong Province. The court issued Civil Judgment No. (2018) Lu 1322 Min Chu 4567, ordering Zhongtian Ren to pay Zhang over 380,000 yuan in rent. Zhang then applied for compulsory enforcement, but the People's Court of Tancheng County, Shandong Province terminated the enforcement on the grounds that no enforceable assets were found at that time.

Afterwards, Zhang discovered that Zhongtian Ren had a registered capital of 8 billion yuan, but the company had paid in zero capital as of 2020. As a result, Zhang filed a lawsuit requesting the court to order nine shareholders, including Lan, to bear supplementary compensation liability for the portion of Zhongtian Ren’s debts that could not be repaid, up to the extent of their unpaid capital contributions.

Upon accepting the case, the People's Court of Tancheng County, Shandong Province, received an objection to jurisdiction from five of the shareholders, who argued that the nine defendants did not reside in Tancheng County, Shandong Province, and that Zhongtian Ren’s domicile was in Miyun District, Beijing. Therefore, the case should be under the jurisdiction of the People's Court of Miyun District, Beijing. The People's Court of Tancheng County, Shandong Province, found the objection valid and transferred the case to the People's Court of Miyun District, Beijing for trial.

Views of the Courts:

The People's Court of Tancheng County, Shandong Province, considered the defendants' objection to jurisdiction valid and issued Civil Ruling No. (2022) Lu 1322 Min Chu 3341 on July 21, 2022, transferring the case to the People's Court of Miyun District, Beijing. The People's Court of Miyun District, Beijing, believed that the transfer ruling made by the People's Court of Tancheng County, Shandong Province, was inappropriate and therefore reported the matter to the Beijing High People's Court.

The Beijing High People's Court held that this case was not related to corporate organization litigation and should not fall under the jurisdiction of the court at the company’s domicile. Instead, it is a dispute concerning shareholders' liability for harming the interests of the company's creditors, which should be under the jurisdiction of the court at the place where the tort occurred or the defendant’s domicile. Since the plaintiff’s

domicile is in Tancheng County, Shandong Province, and the result of the alleged infringement occurred there, it can be used as a connecting factor to determine the court with jurisdiction. The People's Court of Tancheng County, Shandong Province, thus has jurisdiction over this case.

After failing to reach an agreement with the Shandong High People's Court, the matter was submitted to the Supreme People's Court for determination of jurisdiction.

View of the Supreme Court:

Disputes involving corporate organizational actions are subject to the provisions of Article 27 of the Civil Procedure Law of the People's Republic of China, which states: “Lawsuits arising from disputes concerning the establishment of a company, confirmation of shareholder qualifications, profit distribution, and dissolution shall be under the jurisdiction of the court at the company’s domicile.”

However, Zhang argues that Lan and the other eight shareholders failed to make their capital contributions, thereby harming the interests of Zhang, a creditor of Zhongtian Ren. This is not a dispute involving corporate organizational actions, but rather a dispute concerning shareholders' liability for harming the interests of the company’s creditors. According to Article 29 of the Civil Procedure Law of the People's Republic of China, “Lawsuits arising from torts shall be under the jurisdiction of the court at the place where the tort occurred or where the defendant is domiciled,” and Article 24 of the Interpretation of the Supreme People's Court on the Application of the Civil Procedure Law of the People's Republic of China states, “The place where the tort occurred, as stipulated in Article 29 of the Civil Procedure Law, includes both the place where the tort was committed and the place where the result of the tort occurred.” Zhang's domicile can be considered the place where the result of the tort occurred. Zhang resides in Tancheng County, Linyi City, Shandong Province. Therefore, the People's Court of Tancheng County, Shandong Province, has jurisdiction over the case, its decision to transfer the case to the People's Court of Miyun District, Beijing, was inappropriate, and this Court hereby corrects it.

Ruling:

On September 7, 2023, the Supreme People's Court issued Civil Ruling No. (2023) Supreme Court Min Xia 96, which stated:

1. The Civil Ruling No. (2022) Lu 1322 Min Chu 3341 issued by the People's Court of Tancheng County, Shandong Province is hereby revoked;

2. This case shall be tried by the People's Court of Tancheng County, Shandong Province.

Regulatory Updates

The Financial Regulatory Administration Revises and Releases the "Measures for the Administration of Consumer Finance Companies (Draft for Public Comments)"

In order to thoroughly implement the spirit of the Central Financial Work Conference, further strengthen the supervision of consumer finance companies, prevent financial risks, optimize financial services, and promote high-quality industry development, the Financial Regulatory Administration has revised and formed the "Measures for the Administration of Consumer Finance Companies (Draft for Public Comments)" (hereinafter referred to as the "Draft for Comments"). The heads of competent departments within the Financial Regulatory Administration addressed questions from the press regarding the revised draft.

1. What is the background of the revision of the "Draft for Comments"?

Since the revision and release of the "Measures for the Pilot Administration of Consumer Finance Companies" (China Banking Regulatory Commission Order No. 2 of 2013), it has played a crucial role in guiding consumer finance companies to focus on their core function of consumer credit, and in promoting the fundamental role of consumption in the economy. After years of development, both the business model and risk characteristics of the consumer finance industry have undergone significant changes, making the current regulations inadequate for meeting the needs of high-quality development and effective supervision of consumer finance companies. Additionally, in recent years, the Financial Regulatory Administration has introduced a series of regulatory policies on corporate governance, equity management, consumer protection, and other aspects. The "Draft for Comments" further supplements and improves relevant content, aligning with the current regulatory framework.

2. What are the main revisions in the "Draft for Comments"?

The "Draft for Comments" consists of 10 chapters and 79 articles, with revisions mainly focusing on optimizing entry policies, emphasizing tiered business supervision, strengthening corporate governance, enhancing risk management, focusing on consumer protection, regulating the management of cooperative institutions, and improving the market exit mechanisms.

- Higher entry standards: The revised measures increase the assets, revenue, and minimum shareholding requirements for major investors, ensuring shareholders actively contribute to the company and bear their responsibilities. It also enhances the required shareholding proportion for investors with management experience in consumer finance and risk control, thereby improving compliance and risk management. The minimum registered capital requirement for consumer finance companies is also increased to strengthen their risk resilience.
- Strengthened tiered business supervision: The new measures distinguish between core and specialized business areas, eliminating non-core and non-essential activities, and implementing strict tiered supervision. Financing channels will be appropriately expanded to support liquidity.
- Strengthened corporate governance supervision: The regulations require full implementation of recent supervisory rules on corporate governance, equity, related-party transactions, and disclosure, and address the specific features of consumer

finance companies, such as their organizational structure and shareholder system. Specific rules for party-building, shareholder duties, compensation management, related-party transactions, and information disclosure are clearly defined.

- Strengthened risk management: The revised draft specifies supervision requirements for managing credit, liquidity, operational, technology, and reputational risks. It optimizes and adds new regulatory indicators and improves the market exit mechanism.
- Enhanced consumer protection: The revised measures place greater emphasis on consumer protection, requiring consumer finance companies to take primary responsibility for consumer rights. The draft also stresses the importance of establishing comprehensive consumer protection systems and enhancing the management of cooperative institutions to safeguard consumer interests.

3. Why does the "Draft for Comments" raise the minimum shareholding ratio for major investors in consumer finance companies?

The "Draft for Comments" increases the required shareholding ratio for major investors from no less than 30% to no less than 50%. The key reasons are as follows:

- Recent regulatory practices have shown that raising the shareholding ratio of major investors helps to ensure shareholder responsibility, encourages greater participation in company operations, leverages shareholder resources more effectively, and facilitates shareholders in supporting the company.
- A higher shareholding ratio helps improve decision-making efficiency and avoids governance issues caused by too dispersed shareholding.

4. What adjustments have been made to the business scope of consumer finance companies in the "Draft for Comments"?

The "Draft for Comments" refines the scope of business activities to focus more on core functions. On the one hand, the draft distinguishes between basic and specialized business activities, incorporating seven activities, including "personal consumer loans" and "issuance of non-capital bonds," into the basic business category, while placing four activities, including "asset securitization" and “fixed-income securities investment business”, and "consulting services related to consumer finance," under specialized business. On the other hand, non-core and non-essential activities are eliminated. For instance, due to the high level of specialization and frequent complaints, the business of "selling insurance products related to consumer loans" has been removed.

5. What new regulatory indicators have been added in the "Draft for Comments"?

To address risk prevention and control, some consumer finance companies have long been overly reliant on partnerships with guarantee companies and insurers, using these arrangements to mitigate loan risks. However, this practice sometimes leads to a lack of adequate credit checks on borrowers, insufficient independent risk management, and a potential risk where guarantee companies may fail to fulfill their obligations. In addition to

paying loan interest, borrowers are also required to pay guarantee fees, which indirectly increases the overall loan interest rate. The "Draft for Comments" stipulates that the balance of guarantee-enhanced business cannot exceed 50% of a company's total loan balance, with a transition period provided for adjustments. Additionally, consumer finance companies are required to maintain a leverage ratio of no less than 4%, limiting excessive expansion.

6. What considerations does the "Draft for Comments" include for protecting financial consumers?

Consumer finance companies mainly serve low- and moderate-income groups. The "Draft for Comments" introduces two new chapters specifically on "consumer rights protection" and "cooperative institution management," which further enhance the protection of consumer interests. On the one hand, it reinforces the primary responsibility of consumer finance companies for consumer protection by requiring the integration of consumer rights protection into corporate governance, the establishment of a sound consumer protection mechanism, the creation of a Consumer Rights Protection Committee, and the improvement of consumer protection information disclosure mechanisms and personal data protection systems. On the other hand, it strengthens the regulatory oversight of cooperative institutions, requiring consumer finance companies to improve the entry standards management, concentration management, and ongoing monitoring and evaluation of cooperative institutions. It sets out prohibitive provisions for cooperative institutions to prevent violations of consumer rights, especially by non-compliant collection agencies. Furthermore, consumer finance companies are required to take responsibility for managing collection practices, establish performance evaluation and reward/punishment mechanisms for collection agencies, and ensure that outsourcing of collection activities complies with the law, thereby effectively safeguarding the legitimate rights and interests of financial consumers.

Fortran News

1. In March 2024, Attorney Clara Yang was appointed as an Industry Mentor for the Taxation Program at Fudan University. The appointment term is from January 2024 to December 2028.
2. On March 9, 2024, Attorney Summer Qu was invited by East China Normal University to lecture on the course "Drafting Tender Documents and Bid Documents" for postgraduate students at the School of Law.
3. On March 16, 2024, Attorney Xiaofen Deng was invited by East China Normal University to deliver a lecture on the course "Writing a Complaint" for postgraduate students at the School of Law.
4. On March 23, 2024, Attorney Susan Yang was invited by East China Normal University to lecture on the course "Practical Aspects of Writing Lawyers' Letters" for postgraduate students at the School of Law.
5. On March 28, 2024, Attorney Susan Yang delivered a lecture titled "Analysis of

Bankruptcy Reorganization, Settlement Models, and Asset Disposal Cases" at the Henan Provincial Institute of Certified Public Accountants.

6. On March 30, 2024, Attorney Jane Chen was invited by East China Normal University to lecture on the course "Writing International Legal Documents" for postgraduate students at the School of Law.