

To whom it may concern,

We, as corporate and securities law professors from several leading Chinese law schools, are writing this letter in response to the request for public comments on the SEC's interim final rules with respect to the disclosure and submission requirements of the Holding Foreign Companies Accountable Act (HFCA Act) (File No. S7-03-21). From the notice released by the SEC on March 24, 2021, I note that the SEC is seeking public comments on all matters that may have an impact on the interim final rules, including "considerations that the SEC should take into account while determining how to best implement the trading prohibition requirements of the HFCA Act." Our comments will focus on this topic and suggest a pragmatic approach to solve relevant problems.

#### **A. The HFCA Act is a discriminative and unfair treatment towards U.S.-listed Chinese companies**

Although the HFCA Act is nominally applicable to all foreign issuers in U.S. capital markets, its content is obviously aimed at U.S.-listed Chinese companies. In particular, Section 3 of the HFCA Act requires foreign "covered issuers" (as defined by the HFCA Act) to disclose, among other things, the name of each official of the Chinese Communist Party who is a member of the board of directors of the issuer or the operating entity with respect to the issuer, and whether the articles of incorporation of the issuer (or equivalent organizing document) contains any charter of the Chinese Communist Party, including the text of any such charter<sup>1</sup>. It is extremely unusual that issuers are required to disclose information relating to a specific foreign political party. Such requirement clearly contradicts the market-based principles of U.S. capital markets and the professionalism of U.S. financial regulation, which reflects an inappropriate inclination to over politicize securities regulation.

#### **B. The SEC and/or PCAOB should disclose more information about enhancing U.S.-China audit supervisory cooperation**

The interim final rules released by the SEC on March 24, 2021 intend to implement the disclosure and submission requirements of the HFCA Act; however, one should keep in mind that such requirements, as well as the trading prohibition requirement, will only be triggered if the PCAOB is unable to completely inspect or investigate public accounting firms located in a foreign jurisdiction because of a position taken by an authority in that jurisdiction. In other words, whether the PCAOB could sufficiently accomplish its statutory mandate in China is a key element related to the implementation of the HFCA Act, which should not be neglected by the SEC.

As we all know, it is a common practice that cross-border inspections of audit firms could be conducted under a joint inspection arrangement, where host authorities assist the home authority to achieve the latter's objectives of inspection. Therefore, a

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<sup>1</sup> Link: <https://www.congress.gov/bill/116th-congress/senate-bill/945/text>

feasible way for the PCAOB to accomplish its statutory mandate in China is to establish a joint inspection arrangement with Chinese regulators through negotiation.

According to publicly available information, the China Securities Regulatory Commission (CSRC, the national competent authority of securities and futures markets in China) sent a new proposal for joint inspection to the PCAOB on August 4, 2020<sup>2</sup>. The CSRC has also emphasized their open attitude towards the cooperation with PCAOB on many occasions. For example, CSRC Chairman Yi Huiman and Vice-chairman Fang Xinghai took interviews with Caixin and Bloomberg respectively in June 2020 and August 2020<sup>3</sup>. Based on these facts and communications, it seems that the CSRC is willing to work with the PCAOB and has prepared proposals to assist the PCAOB to inspect China-based audit firms, rather than holding a position of refusing the PCAOB's inspections.

On the other side, no public information shows that the SEC or PCAOB has responded to the CSRC's joint inspection proposal dated August 4, 2020. To provide more transparency, the SEC and/or PCAOB could disclose more information about enhancing U.S.-China audit supervisory cooperation, including:

- What have the SEC and PCAOB done in order to implement the PCAOB's inspections on China-based audit firms? How did they communicate with Chinese national competent authorities?
- How do the SEC and PCAOB evaluate the joint inspection proposal prepared by the CSRC on August 4, 2020? Is it consistent with the access-related principles that are fundamental to accomplishing the PCAOB's statutory mandate?
- Does the PCAOB have a timetable for its negotiation with Chinese regulators on audit supervisory cooperation?

### **C. Delisting Chinese companies will harm U.S. and global investors and undermine the status of U.S. capital markets as a global financial center**

According to the PCAOB, as of December 31, 2020, there were 199 Chinese companies listed on U.S. exchanges, with a total (global) market capitalization of approximately \$2.5 trillion<sup>4</sup>. Delisting such companies, in the short run, will cause direct financial losses to investors in U.S. markets; and in the long run, will restrict

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<sup>2</sup> This message has been released by the CSRC for several times. Relevant links include:

[http://www.csrc.gov.cn/pub/csrc\\_en/newsfacts/release/202011/t20201120\\_386576.html](http://www.csrc.gov.cn/pub/csrc_en/newsfacts/release/202011/t20201120_386576.html)

<sup>3</sup> Link for Chairman Yi's interview:

<https://www.caixinglobal.com/2020-06-24/cover-story-cross-border-cooperation-is-key-to-fighting-securities-fraud-csrc-chief-says-101570538.html>

Link for Vice-chairman Fang's interview:

<https://www.bloomberg.com/news/articles/2020-08-26/china-makes-concessions-in-call-for-talks-on-u-s-audit-standoff>

<sup>4</sup> Link: <https://pcaobus.org/oversight/international/china-related-access-challenges>

U.S. investors from sharing the growth and profits of Chinese companies and influence the diversification of their investment portfolios.

Delisting these Chinese companies will also release a signal that the fundamental principles of U.S. capital markets, including market-based financing, openness and free flow of capital, are undermined by political considerations, which is detrimental to the reputation and global leading status of U.S. capital markets.

As a responsible regulator, the SEC needs to take into account such potential negative impacts and find effective ways to avoid them. U.S. regulators should actively negotiate with Chinese counterparts on audit supervisory cooperation, in order to find a mutually acceptable solution. We believe this is the right way to prevent the negative effects of delisting Chinese companies, reduce market uncertainty and mitigate the concerns of U.S. and global investors and other stakeholders.

Should you have any questions regarding my comments, please contact us by email at



Yours sincerely,

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