Chinese business & finance

China plans audit concession in face of US delisting threat

Impasse on financial disclosure rules threatened more than $2tn of shares in US-listed Chinese companies

The central business district in Beijing. If realised, the latest move would represent the first significant movement by China on the disclosure of financial information outside its borders. © Qilai Shen/Bloomberg

Tabby Kinder in Bangkok and **Eleanor Olcott** in London YESTERDAY

Beijing is preparing to make a concession on the disclosure of Chinese audit information in an effort to resolve an impasse threatening more than $2tn of shares in US-listed Chinese companies.

The plans could result in some Chinese companies that are listed in the US being able to provide some audit information to US accounting regulators, according to three people familiar with the matter. They would also clarify what information can and cannot be disclosed abroad, the people said.

The move towards a resolution of the long-simmering tension over foreign access to Chinese company audit papers comes a week after the Securities and Exchange Commission threatened to delist some Chinese companies from US exchanges. The threat prompted a sharp fall in Chinese tech stocks.

Experts say Beijing has been wary of permitting foreign regulators to dive into company accounts and documents due to the risk they could access sensitive intellectual property or data that carries national security implications.

As part of the potential shift, financial regulators in Beijing are finalising plans which people close to the decision say will clarify a law currently prohibiting overseas regulators from conducting investigations within China.

The statute — Article 177 of China's revised securities law — also prevents Chinese entities from providing information to foreign regulators without first receiving approval from the China Securities Regulatory Commission. The CSRC did not respond to a request for comment.

Laws in China can be ambiguously written, and in this case the government did not provide guidance on the scope of Article 177 or formally define key terms that explain what materials or activities it encompasses.

Beijing intends to put in place a "red light, green light" system for companies and auditors regarding what financial audit information can be disclosed abroad, according to two of the people.

If realised, it would represent the first significant movement by China on the disclosure of financial information outside of its borders.

One person familiar with the matter said that a number of companies had been told that regulators in China are preparing the more "nuanced approach" to defining what is sensitive information accessible to foreign auditors.

Beijing has long prohibited foreign access to the files of Chinese companies. That clashes with the US Holding Foreign Companies Accountable Act, passed in 2020, which forces Chinese and Hong Kong companies to allow the US Public Company Accounting Oversight Board to examine their audits.

The stalemate reached a climax last week when the SEC said five Chinese companies had three years to comply with audit requests or they would be delisted from New York exchanges. Hundreds more Chinese companies are expected to be handed the same deadline.

"No matter how optimistic or pessimistic you were two years ago or two months ago, this has gone totally beyond anyone's expectations in the last two weeks," said the chief executive of a large international asset manager that owns shares in large Chinese companies. "Global and Chinese investors are in this together. Everyone is hurt."

The same person said he expected “the majority” of companies to qualify for the more “nuanced approach” but noted that the concessions had been agreed in Beijing before the Ukraine war increased geopolitical tensions between the US and China. There is also no certainty, he said, that the SEC would accept Beijing’s concessions on what information companies can provide and halt the delistings.

The SEC did not respond to a request for comment.

China’s potential compromise comes as the country’s top economic official Liu He on Wednesday reassured investors that Beijing would take measures to support the economy and financial markets after a sharp sell-off in Chinese equities that was exacerbated by Russia’s invasion of Ukraine.

John Zolidis, president of the New York-based equity research firm Quo Vadis Capital said greater transparency for US auditors would “improve investor confidence in US-listed Chinese companies” after a bruising year when the valuations of large internet giants including Alibaba and Tencent have slashed over 40 per cent following Beijing’s regulatory moves to break up their monopoly power.

The Hang Seng index that tracks Chinese tech stocks fell to a six-year low after the SEC’s threats last week. However, it has recovered most of its losses since then and was up over 20 per cent on Wednesday.

“Chinese regulators always felt the [US-listed Chinese equities] market was mostly US investors, but now they are noticing how much Hong Kong is bleeding as a result and they need to rethink the strategy,” said a portfolio manager at a large asset manager in the territory.

This article has been amended since first publication to correct the name of John Zolidis