# The Rise of Non-Profit Organizations in Global Securities Class Actions: A New Hybrid Model in China†

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*Developing an appropriate legal mechanism to aggregate claims in mass securities disputes has long been a key policy issue in investor protection around the globe. The lawyer-led opt-out class action regime in the United States has generated by far the most collective securities lawsuits in the world, and yet the system remains subject to much criticism. To facilitate claims while precluding a litigious legal culture like in the United States, many jurisdictions have experimented with innovative procedural rules for collective redress. In particular, the European Union has allowed non-profit organizations (NPOs) to replace the role of entrepreneurial lawyers in representing mass tort victims. Under the NPO-led opt-out regime, the opt-out rule allows parties to resolve similar disputes all at once, while the non-profit and non-distribution attributes of NPOs suppress the filing of frivolous lawsuits.*

*The new Chinese hybrid model, adopted in the 2020 Securities Law Amendment, entrusts a government-sanctioned NPO, the China Securities Investors Service*

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*Center (the CSISC), to represent investors in opt-out class actions and only allows lawyers to lead opt-in collective litigation. This model takes a middle ground by combining both market-driven and government-controlled mechanisms. However, in China, the distinct policy of maintaining social stability and the political embeddedness of the judiciary will likely suppress the number of securities class actions. Indeed, the first opt-out class action shows traces of political influence and control over the whole litigation process, and the close ties between the CSISC and the government also raise doubts about the potential political influences that shape enforcement decisions. Nonetheless, the new Chinese hybrid model offers a comparative law reference for jurisdictions that are reluctant to accept a litigious legal culture, but at the same time, hope to enhance private enforcement of securities law.*

## INTRODUCTION

Victims of mass securities fraud are usually tens of thousands of investors who purchase shares from capital markets. As in many other mass tort accidents, the damages that individual investors suffer tend to be much smaller than the legal costs incurred by lawsuits against wrongdoers.[1] Even if individual investors are willing to bring

1. As an inherent shortcoming in securities litigation, the disproportionate litigation cost weighed against potential recovery for an individual lawsuit often hinders aggrieved investors from filing suit, despite the fact that the infringement collectively caused a huge

such "negative value" claims, a court might be overwhelmed by tens of thousands of similar claims situated in different proceedings and timeframes.[2] To facilitate the enforcement of individual rights and to enhance judicial efficiency, it is therefore essential for each jurisdiction to develop a special procedure for collective redress.[3]

An ideal collective redress procedure should solve three issues: (1) the risk of overloading the judicial system; (2) a defendant's inability to settle the case for good; and (3) a lack of incentives for victims to bring lawsuits. The U.S. class action regime solves all three problems. In 1966, the adoption of Rule 23 of the Federal Rules of Civil Procedure created an "opt-out" class action regime that included all potential victims unless they explicitly opted out of the lawsuit.[4] This opt-out rule, on the one hand, avoids the risks of overloading the judiciary by blocking all future disputes and, on the other hand, creates incentives for defendants to settle disputes permanently.

However, Rule 23—the opt-out rule—only partially contributes to the flourishing of class action litigation in the United States. Two other procedural rules resolve the disincentives of victims and support "entrepreneurial litigation"[5] in the United States: (1) the contingent fee arrangement for attorney's fees; and (2) the "American Rule" on litigation fees, which prevents shifting fees to losing parties and instead requires each party to pay for their own costs.[6] These two rules lift the financial burden of initiating a lawsuit from the shoulders

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financial loss. The U.S. Supreme Court highlighted this discrepancy in the *Shutts* case, remarking that "the plaintiff's claim may be so small, or the plaintiff so unfamiliar with the law, that he would not file suit individually." Phillips Petroleum v. Shutts, 472 U.S. 797, 813 (1985).

2. For example, in the Deutsche Telekom case, approximately 17,000 claimants brought lawsuits on the same issue, which led to the creation of the modern German litigation regime. *See* discussion *infra* Section I.C.1.

3. Otherwise, "most of the plaintiffs would have no realistic day in court if a class action were not available." *Phillips Petroleum*, 472 U.S at 809.

4. FED. R. CIV. P. 23.

5. "Entrepreneurial litigation" encompasses lawsuits brought by so-called "entrepreneurial lawyers," who zealously finance lawsuits, bear the risks, and share in the profits. As they have a financial stake in the outcome of such cases, entrepreneurial lawyers largely work for their own interests, rather than those of their clients. For a detailed discussion on the rise and fall of entrepreneurial litigation, see generally JOHN C. COFFEE, ENTREPRENEURIAL LITIGATION: ITS RISE, FALL, AND FUTURE (2015). *See also* discussion *infra* Section I.A.

6. From a comparative lens, Coffee identified three key features that support U.S. entrepreneurial class action: (1) the opt-out rule, (2) the contingent fee, and (3) the American rule. *See* John C. Coffee, *The Globalization of Entrepreneurial Litigation: Law, Culture, and Incentives*, 165 U. PA. L. REV. 1895, 1895, 1898 (2017).

of tort victims and shift it to the lawyers, who, as experienced repeat players, can finance the litigation and diversify the financial risks through a lawsuit portfolio. These procedural rules, together with Rule 23 and the Supreme Court's relaxation of the burden of proof as of 1988,[7] have spurred the growth of securities class actions in recent years.[8] The U.S. model, which is chiefly led by entrepreneurial plaintiffs' firms, has since become a key reference for jurisdictions that intend to develop collective redress procedures.[9]

Even though the class action is common in the United States, it is largely unavailable in other jurisdictions. Indeed, most jurisdictions—except for Canada, Australia, and Israel—are skeptical of U.S.-style class actions due to their fear of a litigious legal culture, where so-called "bounty-hunter lawyers"[10] actively file new cases, frivolous or not, for their own benefit.[11] The existence of collective redress procedures in the United States, however, exerts some pressure on other jurisdictions, especially after the *Morrison* case in 2010.[12] In that decision, the U.S. Supreme Court effectively barred foreign shareholders who purchased their shares outside the United States from suing in U.S. courts.[13] As a result, U.S. plaintiffs' firms serving foreign shareholders have been forced to search for alternative forums, mainly in Europe, to bring aggregated claims.[14] Furthermore, with unabating demand from local defrauded investors, many jurisdictions[15]—most crucially, China—have been experimenting

7. *See* Basic v. Levinson, 485 U.S. 224, 225 (1998). The case established the fraud-on-the-market theory, which is discussed more fully in Section I.A.1.

8. Martin Gelter, *Global Securities Litigation and Enforcement*, *in* GLOBAL SECURITIES LITIGATION AND ENFORCEMENT 70–71 (Pierre-Henri Conac & Martin Gelter eds., 2019).

9. *See* Coffee, *supra* note 6, at 1900.

10. "Bounty-hunter" is a (somewhat pejorative) term often used to describe entrepreneurial lawyers in class actions. Because U.S. class actions are largely driven by lawyers' financial incentives, this model allows lawyers to receive bounties by enforcing the provisions of law. *See* discussion *infra* Section I.A.1.

11. Gelter, *supra* note 8, at 82; *see also* Coffee, *supra* note 6, at 1897.

12. *See* Morrison v. Nat'l Austl. Bank Ltd., 561 U.S. 247, 247 (2010).

13. *See id.* (holding that "Section 10(b) does not provide a cause of action to foreign plaintiffs suing foreign and American defendants for misconduct in connection with securities traded on foreign exchanges").

14. Coffee, *supra* note 6, at 1900. Even prior to *Morrison*, a U.S. court found that it lacked jurisdiction over claims brought by foreign shareholders who bought shares on a foreign exchange. *Id.* at 1902. The class actions against *Fortis* and *Volkswagen* are examples of the spillover effect of the U.S. class action regime, largely in Europe. *Id.* at 1902–11.

15. *See infra* Part I.

with innovative collective redress procedures that are functionally similar to but deviate from U.S.-style class actions.[16]

In December 2019, China revised its Securities Law to formally introduce, as of March 1, 2020, U.S.-style opt-out class actions for mass securities-related claims.[17] This unprecedented move rendered China the second Asian jurisdiction, after South Korea,[18] to adopt an opt-out system in securities class actions. Like many other jurisdictions that have shifted to opt-out regimes, China does not follow all three key features of the U.S. system: (1) the opt-out rule; (2) the contingent fee; and (3) the "American Rule" on litigation fees.[19] Rather, China has experimented with a combination of these features and set restrictions to avoid the pitfalls that it perceives in the U.S. system.[20] Following this experimental process, on July 23, 2020, the Supreme People's Court (SPC) published the key operational rules on the new class action regime.[21] This publication importantly maps out the contours of the collective redress procedure in the second-largest economy in the world. This Article reviews this new securities class action regime in China and discusses its implications for the development of global securities litigation.

Before pivoting to this broader context, it is first essential to understand why this new hybrid model is so novel. There are two major models of the global securities class action regime: (1) the lawyer-led opt-out model in the United States; and (2) the non-profit organization (NPO)-led model found in Europe and Asia.[22] The new

16. *See infra* Part II.

17. *See generally* ZHENGQUAN FA (证券法) [SECURITIES LAW OF THE PRC] (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 28, 2019, effective Mar. 1, 2020), STANDING COMM. NAT'L PEOPLE'S CONG. GAZ. 343, Mar. 15, 2020 (China) [hereinafter ZHENGQUAN FA]; *see also* discussion *infra* Section II.B.

18. *See* Jeunggwongwanryeon jipdansosongbeob [Securities-Related Class Action Act], Act No. 7074, Jan. 20, 2004, amended by Act No. 11845, May 28, 2013, add. 1 (S. Kor.).

19. *See* discussion *infra* Sections II.C & II.D.

20. *See* discussion *infra* Sections II.C & II.D.

21. *See generally* Zuigao Renmin Fayuan Guanyu Zhengquan Jiufen Daibiao Ren Susong Ruogan Wenti de Guiding, Fashi [2020] 5 Hao (最高人民法院关于证券纠纷代表人诉讼若干问题的规定, 法释 [2020] 5号) [Provisions of the Supreme People's Court on Several Issues Concerning Securities Dispute Representative Actions, Judicial Interpretation No. 5 [2020 (promulgated by the Jud. Comm. Sup. People's Ct., July 23, 2020, effective July 31, 2020) SUP. PEOPLE'S CT. GAZ., Sept. 10, 2020, http://gongbao.court.gov.cn/PeriodicalsDic html?year=2020&number=9 [https://perma.cc/4JTB-QTAP] (China) [hereinafter *2020 SPC Opinion*]; *see also* discussion *infra* Part II.

22. Yu-Hsin Lin, *Modeling Securities Class Action Outside the United States: The Role of Nonprofits in the Case of Taiwan*, 4 N.Y.U. J.L. & BUS. 143, 148 (2007).

Chinese regime tactfully embraces both models and experiments with a mix-and-match regime that innovatively creates two possible routes for defrauded investors: (1) lawyer-led opt-in litigation; and (2) NPO-led opt-out class actions.[23] Unlike other Asian jurisdictions, China is not short of entrepreneurial lawyers practicing securities litigation, as the country permits a contingent fee that encourages lawyers to assume the litigation risk in order to share in a piece of the recovery.[24] Matching entrepreneurial lawyers with the opt-in rule curtails the scale of the claims that can be brought by lawyers and thus reduces the incentives for lawyers to bring frivolous suits. Similarly, matching approved non-profit organizations with the opt-out rule avoids the greatest pitfall of the U.S. system: a litigious culture where lawyers—not their investor clients—ultimately receive most of the compensation.[25]

Combining the best of both worlds, the hybrid model in China points to a possible future for global securities litigation: the NPO-led opt-out regime. Recent decisions in the European Union have coincided with this development. Afflicted by a general aversion to the U.S.-style opt-out regime, the European Union has struggled since 2008 to fashion a coherent scheme for collective redress.[26] This gridlock persisted until December 2020, when the European Union allowed, for the first time, an opt-out regime for mass consumer disputes.[27] This E.U. Directive mandates that NPOs or public bodies lead class actions in order to minimize the danger of lawyer-controlled

23. *See* discussion *infra* Sections II.C & II.D.

24. Robin Hui Huang, *Private Enforcement of Securities Law in China: A Ten-Year Retrospective and Empirical Assessment*, 61 AM. J. COMP. L. 757, 767–68 (2013).

25. Empirical evidence on 431 securities class action settlements in federal district courts from 2007 to 2012 demonstrates that the lawyers in such cases received an average of 23.8% of the recovery in their respective class actions. *See* Lynn A. Baker et al., *Is the Price Right? An Empirical Study of Fee-Setting in Securities Class Actions*, 115 COLUM. L. REV. 1371, 1389 (2015). This lawyerly misappropriation of client recovery funds is even more heinous in federal consumer fraud class action settlements, in which the claimants between 2010 and 2018 received on average only 23% of their designated recovery. *See* JONES DAY, AN EMPIRICAL ANALYSIS OF FEDERAL CONSUMER FRAUD CLASS ACTION SETTLEMENTS (2010–2018), at 10 (2020).

26. *See infra* note 121 and accompanying text.

27. The Member States can choose to adopt either an opt-out or opt-in scheme in consumer-related mass claim procedures. *See* Directive 2020/1828, of the European Parliament and of the Council of 25 November 2020 on Representative Actions for the Protection of the Collective Interests of Consumers and Repealing Directive 2009/22/EC, 2020 O.J. (L 409) 1, art. 9, ¶ 2 [hereinafter 2020 Directive].

litigation like that in the United States.[28] Permitting only qualified entities to represent investors in opt-out class actions can effectively minimize the risks of frivolous suits and deter a litigious legal culture. Although the proposed Directive does not apply to securities fraud cases, it is still a friendly move toward an opt-out regime in Europe which will affect the future regulation of securities class actions in European countries.

China has similarly taken a leap forward in the design of collective redress procedures for securities fraud victims. However, securities class actions in China still face various roadblocks that hinder their growth. While adopting the opt-out rule represents a convergence of global collective action procedures, such a convergence in formal rules does not necessarily lead to the same practical outcomes. Local conditions—whether political, social, or legal—usually shape a regime's enforcement. This Article finds that, in the case of China, the distinct policy of maintaining social stability and the political embeddedness of the judiciary are likely to suppress the number of securities class actions, even after the adoption of U.S.-style opt-out rules. Political concern over social stability leads to the (continuous) imposition of procedural prerequisites that hinder the growth of class actions.[29] Moreover, the "non-litigation-first" policy, which prefers alternative dispute resolution ("ADR") over confrontational litigation, channels cases to mediation and undermines the deterrence function of private enforcement.[30] When setting relevant game rules, the SPC also prioritizes its own administrative preferences, reducing judges' workloads by expanding the binding effects of opt-in lawsuits, instead of prioritizing the litigation rights of individual investors.[31] Finally, the close ties between NPOs and the government raises doubts about potential political influences on enforcement decisions.[32]

This Article begins in Part I by reviewing the U.S. class action model, and then exploring other jurisdictions' efforts to establish locally-acceptable securities class action devices, tracing their convergences with (and divergences from) the U.S. paradigm. Part II introduces the 2020 Amendment to the Securities Law of the People's

28. *See id.* art. 1, ¶ 2 ("Member States shall ensure that at least one procedural mechanism that allows qualified entities to bring representative actions for the purpose of both injunctive measures and redress measures complies with this Directive.").

29. *See infra* Sections III.A and III.B.

30. President Xi Jinping's non-litigation-first policy encourages parties to settle their dispute in a less confrontational way through ADR. *See* discussion *infra* Section III.A.

31. *See infra* Section III.C.

32. *See infra* Section III.D.

Republic of China and explicates the new Chinese hybrid model of securities class actions. Part III analyzes China's new regime against the backdrop of its existing political, social, and legal environment, preliminarily assessing its expected results. The Article then concludes that a formal convergence in procedural rules does not equate to a singular outcome across jurisdictions; rather, distinct political values and legal infrastructure shape unique outcomes in different sociopolitical contexts.

## I. GLOBAL SECURITIES CLASS ACTION REGIMES

Given the rise of large-scale securities litigation more generally,[33] countries around the world have agreed that the traditional single-party litigation model no longer sufficiently protects investors. Many countries have introduced procedures that allow representatives to file mass claims on behalf of securities fraud victims.[34] Countries that based their group-litigation mechanisms on the U.S. experience usually chose some, if not all, of the three pillars of the U.S. class action model: (1) an opt-out rule; (2) a contingent fee arrangement for attorney's fees; and (3) the "American Rule" by which each party bears its own litigation costs.[35] Though the U.S. model still stands as a benchmark for other jurisdictions, no jurisdiction has simply transplanted all three legal rules into its local legal system, possibly due to path dependence.[36] For example, the loser-pays rule, by which

33. *See* DECHERT, GLOBAL SECURITIES LITIGATION TRENDS: DECEMBER 2020 UPDATE 1, at 7 (2020) (noting the rise in securities litigation in the EU and the general global trends around securities cases).

34. For a detailed discussion on securities lawsuits in major economies, see generally GLOBAL SECURITIES LITIGATION AND ENFORCEMENT (Pierre-Henri Conac & Martin Gelter eds., 2019).

35. Coffee, *supra* note 6, at 1898.

36. Douglass North argued that economic activity and institutional changes, like the physical world, have certain kinds of inertia. Given the initial conditions in any institution—be it legal, social or cultural—it is difficult for a country's superstructure to deviate from an established path, even if an alternative equilibrium is more efficient. For a discussion of path dependence, see generally DOUGLASS C. NORTH, INSTITUTIONS, INSTITUTIONAL CHANGE, AND ECONOMIC PERFORMANCE 92–104 (1990). Of course, one cannot expect path dependence to explain all institutional changes in the world. Ronald Gilson explored path dependence in global corporate governance, noting that "initial conditions may select the path, but the institutions that emerge in response are subject to powerful environmental selection mechanisms . . . . In the end, institutions are shaped by a form of corporate governance plate tectonics, in which the demands of current circumstances grind against the influence of initial conditions." Ronald J. Gilson, *Corporate Governance and Economic Efficiency: When Do Institutions Matter?*, 74 WASH. U. L.Q. 327, 332 (1996). For additional discussion of path

the losing party is responsible for the winning party's legal costs, including court fees and attorney fees, is the predominant rule in most countries outside of the United States.[37] Legal traditions, embedded in jurisdictions' histories, also inform the institutional framework of litigation proceedings.[38] Civil law jurisdictions, for instance, tend to resist deviating from their original paths.[39] In Germany, for example, the single-party adjudication system forms the bedrock of various procedural rules. In fact, the German courts are under a constitutional obligation to hear each individual's statement, making it unconstitutional for investors with similar claims to appoint representatives to sue on their behalf.[40] Even though some jurisdictions have adopted U.S.-style opt-out rules in securities collective redress procedures, no jurisdiction—whether operating under common law or civil law—observes the same securities litigation market size as that found in the United States. After all, convergence in statutory rules may not eliminate differences in practice.[41]

Attuned to this procedural diversity, this Part explores the various collective redress procedures developed in major jurisdictions. It begins with the United States to situate similar patterns of development that are discussed later in the case of other jurisdictions. Through this comparative lens, we observe three major models: (1) the lawyer-led opt-out model in the United States, Australia, Canada, and South Korea;[42] (2) the NPO-led model in the European Union and Taiwan;[43] and (3) functionally equivalent models in Germany, the

dependence in legal transplantation, see generally Stephen Choi, *Law, Finance and Path Dependence: Developing Strong Securities Markets*, 80 TEX. L. REV. 1657 (2002).

37. *See* Coffee, *supra* note 6, at 1899.

38. Patrick H. Glenn, *The Dilemma of Class Action Reform*, 6 OXFORD J. LEGAL STUD. 262, 262 (1986).

39. *See id*. ("In civil law jurisdictions, where the Romanic tradition has been largely uninfluenced by the work of prerogative courts, an individualist concept of the party to litigation ('*pas d'intérêt, pas d'action*'; '*nul ne plaide par procureur*') has existed since the early stages of Roman law . . . ").

40. *See* Grundgesetz [GG] [Basic Law], art. 103, ¶ 1, https://www.gesetze-im-internet.de/englisch_gg/index html [https://perma.cc/F99P-K94U] (Ger.) ("In the courts every person shall be entitled to a hearing in accordance with law.").

41. Ronald J. Gilson, *Globalizing Corporate Governance: Convergence of Form or Function*, 49 AM. J. COMP. L. 329, 330–32 (2001).

42. *See* discussion *infra* Section I.A.

43. *See* discussion *infra* Section I.B.

United Kingdom, and the Netherlands.[44] We briefly introduce the key legal rules and practices in each jurisdiction below.

### *A. The Lawyer-Led Opt-Out Model*

The United States is the originator of the lawyer-led opt-out model.[45] Under this model, entrepreneurial lawyers are the key drivers of new cases, and all tort victims are automatically included in the lawsuit unless they opt out. This Section introduces the key features of the U.S. model and those of the three other jurisdictions—Australia, Canada, and South Korea—which followed suit.

#### 1. The United States

In the United States, securities fraud laws are enforced collectively by multiple entities, including the Securities and Exchange Commission (SEC), the Department of Justice (DOJ), state attorneys, and entrepreneurial lawyers.[46] Private enforcement by way of securities class action suits has traditionally been viewed as a supplement to public enforcement by the SEC.[47] In 2020, 334 securities class actions were filed by private parties, marking a 22% decrease from the previous year's 427 cases.[48] Simultaneously, the SEC enforced 715 cases.[49] During that same year, private plaintiffs recovered 4.2 billion USD in seventy-seven class action settlements,[50] while the SEC fined wrongdoers approximately 1.1 billion USD and ordered approximately 3.6 billion USD in disgorgement of ill-gotten

44. *See* discussion *infra* Section I.C.

45. *See* COFFEE, *supra* note 5, at 1–8.

46. For the interactions between each regulator, see generally Amanda M. Rose, *The Multienforcer Approach to Securities Fraud Deterrence: A Critical Analysis*, 158 U. PA. L. REV. 2173 (2010).

47. William B. Rubenstein, *On What a Private Attorney General Is—And Why It Matters*, 57 VAND. L. REV. 2129, 2142–55 (2004) (describing three types of private attorney generals, one of which involves acting as a supplemental public law enforcer).

48. CORNERSTONE RSCH., SECURITIES CLASS ACTION FILING: 2020 YEAR IN REVIEW 5 (2021), https://www.cornerstone.com/wp-content/uploads/2021/12/Securities-Class-Action-Filings-2020-Year-in-Review.pdf [https://perma.cc/6PPV-PVKG].

49. U.S. SEC. & EXCH. COMM'N, DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT (2020), https://www.sec.gov/files/enforcement-annual-report-2020.pdf [https://perma.cc/Z4SU-KWXB].

50. CORNERSTONE RSCH., SECURITIES CLASS ACTION SETTLEMENTS—2020 REVIEW AND ANALYSIS 3 (2021), https://www.cornerstone.com/Publications/Reports/Securities-Class-Action-Settlements-2020-Review-and-Analysis [https://perma.cc/8AZN-2YLE].

gains.[51] While the SEC pursues significantly more cases than private attorneys do, empirical studies show that private class action attorneys target disclosure violations, a type of securities fraud, with at least as much deterrent effect as (if not more so than) the SEC.[52]

What makes U.S.-style class actions possible are the 1966 Amendments to the Federal Rules of Civil Procedure, which created the opt-out regime.[53] Under the Federal Rules of Civil Procedure Rule 23, which governs class actions at the federal level, certain prerequisites must be met before a federal court can permit a representative plaintiff to sue on behalf of a class.[54] Per Rule 23(a), the members of the class must be numerous; the class must present a common question of law or fact; the representative of the class must possess a claim or defense which is typical to all its members; and the representative must ensure that the interests of all members are protected fairly and adequately.[55] In addition to Rule 23(a), a class action must also meet one of the criteria prescribed by Rule 23(b)(1), (2), and (3).[56] Securities class actions are often brought under Rule 23(b)(3), which requires predominance and superiority—i.e., a common question of law or fact *predominates* an issue affecting only individual members, and a class action is *superior* to other methods for fairly and efficiently adjudicating the controversy.[57]

Crucially, however, an action must be certified by the court to become a class action. Once a court certifies a class action, it sends the best notice practicable under the circumstances to all qualified members.[58] Within the notice, the court must offer an "opt-out option" to individuals who do not want to join the class.[59] If these plaintiffs fail to opt-out, then the judgment will be binding on them regardless

51. .*See supra* note 49 and accompanying text.

52. *See* Stephen J. Choi & Adam C. Pritchard, *SEC Investigations and Securities Class Actions: An Empirical Comparison*, 13 J. EMPIRICAL LEGAL STUD. 27, 42–43 (2016) (counteracting the view that more precise targeting of suits by the SEC yields a stronger deterrent punch for SEC enforcement relative to class actions).

53. *See* STEPHEN C. YEAZELL, FROM MEDIEVAL GROUP LITIGATION TO THE MODERN CLASS ACTION 238 (1987); FED. R. CIV. P. 23; *see also* Steven T.O. Cottreau, *The Due Process Right to Opt Out of Class Actions*, 78 N.Y.U. L. REV. 480, 485 n.24 (1998).

54. FED. R. CIV. P. 23.

55. *Id.* subdiv. (a).

56. *Id.* subdiv. (b)(1), (2) & (3).

57. *Id.* subdiv. (b)(3).

58. *Id.* subdiv. (c)(2)(B).

59. *Id.* subdiv. (c)(2)(B)(v).

of the result.[60] The unique opt-out rule in U.S. class actions allows courts to avoid hearing multiple cases on the same issue, which maximizes the use of limited judicial resources[61] and ensures some consistency in judgment.[62] Empirical evidence suggests that defrauded investors rarely exercise their opt-out option—only 0.7% of class members excluded themselves from securities class actions from 1993 to 2003.[63]

The rise of the class action in the United States can also be attributed to two other legal rules: (1) the contingent fee arrangement for attorney's fees and (2) the "American Rule" for litigation fees by which each party bears its own legal costs.[64] Under U.S. law, the contingent fee arrangement allows a plaintiff's attorney to charge fees after receiving the final compensation or settlement amount, freeing plaintiffs from the burden of paying unaffordable attorney fees upfront—an initial obstacle that would otherwise drive many individuals away from filing suit.[65] By following the American Rule, under which parties handle their own expenses, the U.S. class action significantly reduces the financial burden of litigation, which was

60. *Id.* subdiv. (c)(3).

61. *See* Am. Pipe & Constr. Co. v. Utah, 414 U.S. 538, 553 (1974) ("[T]he efficiency and economy of litigation . . . is a principal purpose of the procedure (Rule 23 Class Action).").

62. The purpose of class actions, as implied in Rule 23, is to ensure consistent judgments. *See, e.g.*, FED. R. CIV. P. 23(b)(1)(A) ("A class action may be maintained if . . . prosecuting separate actions . . . would create risks of *inconsistent* or *varying* adjudications with respect to individual class members that would establish incompatible standards of conduct for the party opposing the class.") (emphasis added).

63. Theodore Eisenberg & Geoffrey Miller, *The Role of Opt-Outs and Objectors in Class Action Litigation: Theoretical and Empirical Issues*, 57 VAND. L. REV. 1529, 1549 (2004). However, possibly due to the bounty hunter effect and the increasing popularity of institutional ownership, the percentage of plaintiffs exiting class actions has risen in recent years. *See* John C. Coffee, *Litigation Governance: Taking Accountability Seriously*, 110 COLUM. L. REV. 288, 309–14 (2010) (finding that, because a typical securities class action settles at two to three percent of losses, institutional investors with deeper pockets often tend opt out of the class and sue on their own).

64. Coffee, *supra* note 6 at 1898.

65. The calculation of contingent fees in class actions is more complicated. The court reviews and decides the final attorney's fees using the "lodestar method," which multiplies the number of hours reasonably spent by trial counsel by a reasonable hourly rate. *See* William J. Lynk, *The Courts and the Market: An Economic Analysis of Contingent Fees in Class-Action Litigation*, 19 J. LEGAL STUD. 247, 249 (1990). Usually, the fees payable to lawyers are related to the size of recovery, but the average percentage rate decreases as the size of the recovery increases, often in response to the risks of the litigation itself. *See* Theodore Eisenberg et al., *Attorney's Fees in Class Actions 2009–2013*, 92 N.Y.U. L. REV. 937, 969 (2017).

previously not cost-effective for most, if not all, defrauded investors.[66] As a result, investors are encouraged to participate in litigation, and lawyers are incentivized to play the roles of private attorney generals in identifying potential fraud. These dynamics arguably explain the astonishingly-high number of class actions and exorbitant recovery amounts found in the U.S. market, when compared to other jurisdictions.

The provision of substantive legal requirements by the U.S. Supreme Court has further contributed to the success of the U.S. regime. In a securities class action, the court faces the unique and difficult task of evaluating a plaintiff's reliance on a defendant's allegedly false or misleading statements.[67] In 1988, the U.S. Supreme Court adopted the fraud-on-the-market theory in *Basic v. Levinson* to create a rebuttable presumption of reliance.[68] The *Basic* Rule greatly expanded the number of investors that can be admitted into the class and therefore gives lawyers more bargaining power in initiating a lawsuit.[69] Subsequently, the number of securities class actions in the United States took off.[70] In 2014, the U.S. Supreme Court reaffirmed the rebuttable presumption in *Halliburton* but gave defendants a

66. John C. Coffee, *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 COLUM. L. REV. 669, 669–70, 669 n.2 (1986).

67. The law prohibiting false or misleading statements is SEC Rule 10b-5. *See* 17 C.F.R. § 240.10b-5 (2014):

> It shall be unlawful for any person . . . (a) to employ any device, scheme, or artifice to defraud, (b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or (c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

To apply Rule 10b-5, a plaintiff investor must crucially establish its reliance upon misrepresentation by the defendant. *See generally*, N. Robert Stoll, *Reliance as an Element in 10b-5 Actions*, 53 OR. L. REV. 169 (1974).

68. In *Basic v. Levinson*, the U.S. Supreme Court held that all material information in the market is available to investors and will be reflected in the share price. As a result, the Court could create a causal link between investors who bought the shares and the misstatement, given that the misstatement is a fraud on the entire market. *See* Basic Inc. v. Levinson, 485 U.S. 224, 485 (1988).

69. The Court adopted the fraud-on-the-market theory to facilitate the enforcement of Rule 10b-5 through class actions. As class actions are driven by the incentives of investors and their attorneys, the enforcement of Rule 10b-5 would otherwise be impractical if the law were to require individualized proof of reliance. *See* Paul G. Mahoney, *Precaution Costs and the Law of Fraud in Impersonal Markets*, 78 VA. L. REV. 623, 662–64 (1992).

70. The number of filings tripled between 1988 and 1991. *See id.* at 663.

chance to rebut it by showing a lack of price impact.[71] While this Article focuses on legal innovations with respect to procedural design, substantive requirements are also crucial to the success of the regime.[72]

Since the U.S. securities class action regime confers extraordinary leverage and power on plaintiffs' attorneys, many lawyers have become entrepreneurs who invest resources to identify fraud and finance litigation in exchange for a significant, and sometimes disproportionate, share of the return.[73] Critics have maintained that this contingent fee arrangement leads to substantial conflicts of interest between lawyers and their clients.[74] Under the contingent fee system, lawyers largely work for their own interests; they would rather avoid the risk of receiving nothing than accept a low-value settlement, even though the potential awards from judgments could be higher. Although a lawyer's profits might not be maximized in a single case, being a repeat player in the litigation market diversifies a lawyer's risk portfolio, counteracting the potential loss in any one case and optimizing long-term profits in true entrepreneurial

71. Halliburton v. Erica P. John Fund, Inc., 573 U.S. 258, 278 (2014) (upholding the *Basic* presumption but allowing the defendant to rebut it by showing that the misrepresentation has had no price impact).

72. For a summary of the development of the substantive legal requirements, see Franklin A. Gevurtz, *United States: The Protection of Minority Investors and Compensation of Their Losses*, *in* GLOBAL SECURITIES LITIGATION AND ENFORCEMENT 123–32 (Pierre-Henri Conac & Martin Gelter eds., 2019).

73. Entrepreneurial litigation has influenced many jurisdictions globally. *See, e.g.*, Coffee, *supra* note 6, at 1900–16 (parsing how and to what extent entrepeurial litigation has been transplanted to the European Union and Asia).

74. For a discussion of agency problems between entrepreneurial lawyers and clients, see John C. Coffee, *The Regulation of Entrepreneurial Litigation: Balancing Fairness and Efficiency in the Large Class Action*, 54 U. CHI. L. REV. 877, 883–89 (1987). However, entrepreneurial lawyers maximizing their own gains does not necessarily harm social utility. *See* Myriam E. Gilles & Gary B. Friedman, *Exploding the Class Action Agency Costs Myth: The Social Utility of Entrepreneurial Lawyers*, 155 U. PA. L. REV. 103, 141–45 (2006). Rather, U.S.-style class actions motivate private attorneys to pursue financial benefits, voluntarily enforce securities law, and deter potential detriments. *See, e.g.*, John C. Coffee, *Rescuing the Private Attorney General: Why the Model of the Lawyer As Bounty Hunter Is Not Working*, 42 MD. L. REV. 215, 216 (1983) (noting that "as most college sophomores know, the private attorney general is someone who sues 'to vindicate the public interest' by representing collectively those who individually could not afford the costs of litigation . . . ."); *see also* Coffee, *supra* note 66, at 669 (demonstrating that "American law relies upon private litigants to enforce substantive provisions of law that in other legal systems are left largely to the discretion of public enforcement agencies"). The American Bar Association's Model Rules suggest that contingent fee arrangements be memorialized in writing to avoid disputes between lawyers and clients. MODEL RULES OF PRO. CONDUCT r. 1.5(c) (AM. BAR ASS'N 2020).

fashion.[75] Consequently, many class actions end with conclusive settlements agreed upon by so-called "bounty hunter lawyers,"[76] wrongdoers who wish to close cases permanently, and investors often receive a paltry recovery.[77] In addition, law firms usually try to bill more hours in cases with larger settlements.[78] The court's involvement in the final approval of a settlement at least requires lawyers to contribute resources toward justifying their fee requests.[79]

The bounty hunter lawyer model also raises the issue of abusive or meritless litigation. Empirical evidence demonstrates that only 3.5% of fraud cases are detected by plaintiffs' attorneys, which is far less than those spotted by other external governance mechanisms.[80] At the same time, lawyers initiated most, if not all, class actions during the same time period.[81] Pursuing high profits, these bounty hunters comb the market for possible unfavorable information about a company to then bring a meritless case and force a settlement.[82] The market therefore fears that abusing class actions may consume too

75. *See* Alexander Janet Cooper, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 STAN. L. REV. 497, 530–37 (1991).

76. "Private attorney general" and "bounty hunter" are the terms that often used to describe entrepreneurial lawyers who enforce the provisions of law for their own financial interests. *See supra* notes 10 & 74 and accompanying text. In Coffee's words, these terms—one positive and the other negative—are "[two] different sides of the same legal coin." Coffee, *Rescuing the Private Attorney General*, *supra* note 74, at 218.

77. *See* Coffee, *supra* note 66, at 677–98 (explicating incentives that drive lawyers to initiate litigation and to enter into collusive settlements with defendants); *see also* William B. Rubenstein, *Why Enable Litigation?: A Positive Externalities Theory of the Small Claims Class Action*, 74 U. MO. KAN. CITY L. REV. 709, 709 (2006) (stating that "plaintiffs in small claims class actions do nothing, they do that nothing far from the courtroom, and what they collect is likely to be about as close to nothing as was the effort they put in to collecting it").

78. Stephen J. Choi, Jessica Erickson & Adam Pritchard,*Working Hard or Making Work? Plaintiffs' Attorney Fees in Securities Fraud Class Actions*, 17 J. EMPIRICAL LEGAL STUD. 438, 438 (2020) (finding that, in anticipation of the scrutiny of fees by the court, lawyers complete additional unnecessary tasks in order to bill more hours in large settlement cases).

79. FED. R. CIV. P. 23(e).

80. Alexander Dyck et al., *Who Blows the Whistle on Corporate Fraud?*, 65 J. FIN. 2213, 2225 (2010). The study demonstrated that the SEC detected seven percent of the fraud cases, while whistleblowing employees detected 18.3% of them, marking the highest rate of detection among all external parties. *Id.*

81. On the other hand, investors are passive participants in class action initiated by lawyers. *See, e.g.*, James D. Cox & Randall S. Thomas, *Letting Billions Slip Through Your Fingers: Empirical Evidence and Legal Implications of the Failure of Financial Institutions to Participate in Securities Class Action Settlements*, 58 STAN. L. REV. 411, 425 (2005). The empirical research indicates that even large institutional investors failed to participate in securities class action settlement and instead let lawyers take control. *Id.*

82. *See* Gevurtz, *supra* note 72, at 110.

much of a firm's resources in responding to frivolous claims and thus stultify business and economic development.[83] The enactment of the 1995 Private Securities Litigation Reform Act (PSLRA), however, improved the quality of filing and settlements.[84] For example, merit factors became more important for settlements to be reached,[85] nuisance litigation reduced by PSLRA had a screening effect on cases filed,[86] and more cases with harder evidence and larger potential settlements were brought to court than before PSLRA's enactment.[87] However, when nuisance suits declined, meritorious claims also decreased, as the reform made securities class actions less profitable for plaintiffs' attorneys.[88] In addition, although PSLRA tried to implement several requirements to halt frivolous lawsuits, the total number of securities class actions has still skyrocketed in recent years.[89]

Obviously, there is a conflict that is difficult to settle: while the enforcement of securities law is a public good,[90] the United States

83. Amanda Rose, *Reforming Securities Litigation Reform: Restructuring the Relationship Between Public and Private Enforcement of Rule 10b-5*, 108 COLUM. L. REV. 1301, 1326–30 (2008). A firm's operating efficiency will be harmed while a lawsuit is pending, and defendant companies often suffer liquidation problems after settlement. Therefore, low-quality lawsuits may harm a firm's business opportunities. *See* Bai Lynn et al., *Lying and Getting Caught: An Empirical Study of the Effect of Securities Class Action Settlements on Targeted Firms*, 158 U. PA. L. REV. 1877, 1912 (2010). Empirical evidence shows that securities class actions with little merits disproportionally target high-innovation firms and lead to significant losses of shareholder value, impairing economic development. *See* Elisabeth Kempf & Oliver Spalt, *Attracting the Sharks: Corporate Innovation and Securities Class Action Lawsuits* (European Corporate Governance Institute—Finance Working Paper No. 614/2019, 2020), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3143690 [https://perma.cc/MV4T-NMRB].

84. Private Securities Litigation Reform Act of 1995, 15 U.S.C. § 78u-4.

85. *See* Marilyn F. Johnson et al., *Do the Merits Matter More? The Impact of the Private Securities Litigation Reform Act*, 23 J.L. ECON. & ORG. 627, 648–49 (2007) (concluding that restatement and abnormal insider stock sales have a correlation with litigation in the post-PSLRA era, indicating that merits matter more after the PSLRA reform).

86. *See* Stephen J. Choi et al., *The Screening Effect of the Private Securities Litigation Reform Act*, 6 J. EMPIRICAL LEGAL STUD. 35, 37 (2009).

87. Stephen J. Choi, *Do the Merits Matter Less After the Private Securities Litigation Reform Act?*, 23 J.L. ECON. & ORG. 598, 622 (2006).

88. *Id*. at 623.

89. The measures taken by the PSLRA include encouraging institutional investors who have more financial interests in the case and more resources to monitor their attorneys in order to be appointed as lead plaintiffs. *See* Private Securities Litigation Reform Act of 1995, 15 U.S.C. §§ 77z-1(a)(3)(B)(iii) & 78u-4(a)(3)(B)(iii).

90. *See* Curtis J. Milhaupt, *Nonprofit Organizations as Investor Protection: Economic Theory and Evidence from East Asia*, 29 YALE J. INT'L L. 169, 172 (2004) (stating that

relies on private hands to produce it. Consequently, this model contains certain agency costs because private attorneys are generally motivated by self-interest.[91] Perhaps lawyers' conflicts of interest and frivolous lawsuits are just the prices to be paid for the survival of the class action scheme. Although the debate on the merits of U.S.-style class actions has not been settled, securities class action as a primary method of private enforcement have now grown to be an essential *ex-post* regulatory mechanism in modern corporate governance.[92]

### 2. Australia

Australia and Canada, both commonwealth common law jurisdictions, have procedures that are most similar to U.S.-style class actions. However, these countries do not have a prosperous class action practice due to fee arrangements that depart from U.S. practice.[93]

Australia has adopted a more plaintiff-friendly opt-out mechanism and has no court-certification requirement for a class action to proceed. A class action can be brought as long as seven or more persons' claims against the same person(s) are "related" and "at least one substantial common issue of law or fact" is presented.[94] Plaintiffs do not need to provide any class member identifications to establish a class and can alter the description of the class to add new class members at any stage of the litigation.[95] Those who satisfy the description automatically become class members and are bound by the outcomes unless they opt-out.[96] Those who do not exercise the option to opt-out can be passive in all class action processes and need not take any actions.[97] Like the U.S.-style model, any settlement requires a

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"investor protection in the form of corporate and securities law enforcement is a public good: many of the benefits of the enforcement effort accrue to persons who are not required to bear their share of the enforcement costs").

91. *See* DEBORAH R. HENSLER ET AL., CLASS ACTION DILEMMAS 71 (2000).

92. *See generally* Elizabeth Chamblee Burch, *Securities Class Actions as Pragmatic Ex Post Regulation*, 43 GA. L. REV. 63 (2008).

93. Such derivation includes "less activist and entrepreneurial attorneys, and the 'loser-pays' rule." Edward F. Sherman, *Group Litigation Under Foreign Legal Systems: Variations and Alternatives to American Class Actions*, 52 DEPAUL L. REV. 401, 402 (2002).

94. *Federal Court of Australia Act 1976*, s 33C(1) [hereinafter *Fed. Ct. of Austl. Act*].

95. *See id.* ss 33H & 33K(1).

96. *See id.* ss 33ZB(b) & 33J.

97. *See P Dawson Nominees Pty Ltd v Brookfield Multiplex Ltd (No 2)* [2010] 176 FCR 16, 17.

court's approval.[98] However, contingent fee arrangements are restricted.[99] Furthermore, Australia, due to its English common law tradition, only permits a plaintiff-hostile, loser-pays rule, not the American Rule.[100] As a result, class representatives short on funds commonly rely on third-party litigation finance to bring a lawsuit.[101] Given certain restrictions on fee arrangements, Australia is rarely flooded by such litigation.[102] Yet, scholars still believe that the nation should adopt an opt-in rather than opt-out mechanism given its current overly-plaintiff-friendly regime.[103]

### 3. Canada

Like the U.S.-style model, Canadian class actions, at least in some provinces, also rely on entrepreneurial lawyers and permit a contingent fee arrangement.[104] In Québec, plaintiffs who wish to sue on behalf of a class must show sufficient interest in the case and seek a court's leave to commence litigation.[105] The court's decision binds all class members who have not excluded themselves from the class.[106] However, the scale of filed class actions in Canada does not compare to that in the United States,[107] and Canada does not fully transplant

98. *See Fed. Ct. of Austl. Act*, *supra* note 94, s 33V.

99. The contingent fee arrangement was prohibited in Australia until 2020, when Victoria became the first state to permit contingent fee arrangements in class actions. *See Supreme Court Act 1986* (Vic), s 33ZDA.

100. *Legal Profession Act 2004 (NSW)* s 325 (repealed) (Austl.); *Australian Solicitors' Conduct Rules 2011* r. 12.2.

101. *See* Olivia Dixon & Jennifer G. Hill, *Australia: The Protection of Investors and the Compensation for Their Losses*, *in* GLOBAL SECURITIES LITIGATION AND ENFORCEMENT 1092 (Pierre-Henri Conac & Martin Gelter eds., 2019).

102. The number of securities class actions in Australia is quite small. In 2020, only thirteen securities class actions were filed in Australia, as compared to the 334 cases filed in the United States. *See* Jeff Lubitz, *Are Class Actions Under Threat in Australia?*, ISS INSIGHT (July 28, 2021), https://insights.issgovernance.com/posts/are-class-actions-under-threat-in-australia [https://perma.cc/97TL-E8ZQ]; CORNERSTONE RSCH., *supra* note 48, at 5.

103. *See*, *e.g.*, Stuart Clark & Christina Harris, *The Push to Reform Class Action Procedure in Australia: Evolution or Revolution?*, 32 MELB. U. L. REV. 775, 782 (2008).

104. H. Patrick Glenn, *The Irrelevance of Costs Rules to Litigation Rates: The Experience of Quebec and Common Law Canada*, *in* COST AND FEE ALLOCATION IN CIVIL PROCEDURE: A COMPARATIVE STUDY 99, 104 (Mathias Reimann ed., 2012).

105. *See* Code of Civil Procedure, R.S.Q., c C-25.01, §§ 85 & 574 (Can.).

106. *See id.* § 591.

107. Between 1997 and 2015, only 129 securities class actions were filed in Canada. In 2020 alone, 334 securities class actions were filed in the United States. *See* Stéphane Rousseau, *Canada: The Protection of Minority Investors and the Compensation of Their*

class action-related rules from the U.S. model. For example, Canada adopted a modified loser-pays rule under which the losing party covers the winner's litigation costs, including court fees, but not lawyers' fees.[108] As a result of this financial risk, many plaintiffs do not have enough incentives to bring a lawsuit.[109] The Canadian courts also have not yet adopted the fraud-on-the-market theory,[110] making it very difficult for investors from secondary markets to prove their reliance.[111] While Canadian law permits investors in secondary markets to sue under certain circumstances, it also imposes strict constraints, partially because the main purpose of the Canadian class action is to improve the disclosure regime, rather than compensate investors.[112] For example, the maximum compensation for investors in misrepresentation cases is either five percent of the firm's market value or 1 million CAD (0.79 million USD), whichever is lower.[113] Therefore, although Canada and Australia have adopted opt-out regimes, their class action numbers have not skyrocketed due to differences in their fee-arrangement rules.

### 4. South Korea

South Korea is a civil law jurisdiction that has also adopted the opt-out rule for securities-related collective redress cases. However, its practice further deviates from the U.S.-style model due to different traditions in its legal culture and civil procedural rules. In South Korea, one or more plaintiffs are permitted to sue on behalf of other investors following the enactment of the Securities-Related Class Action Act, which took effect in 2005.[114] Under this Act, the representative plaintiff who desires to sue must first make an

*Losses*, *in* GLOBAL SECURITIES LITIGATION AND ENFORCEMENT 143, 175 (Pierre-Henri Conac & Martin Gelter eds., 2019); CORNERSTONE RSCH., *supra* note 48, at 5.

108. *See* Rousseau, *supra* note 107, at 177–78.

109. *See* Garry D. Watson, *Class Actions: The Canadian Experience*, 11 DUKE J. COMP. & INT'L L. 269, 275–76 (2001).

110. *See supra* note 68 and accompanying text.

111. *See* Rousseau, *supra* note 107, at 164; *see also supra* note 68 and accompanying text.

112. *See* Rousseau, *supra* note 107, at 165.

113. *See* KEEPING THE PROMISE FOR A STRONG ECONOMY ACT (BUDGET MEASURES), 2002, S.O. 2002, c. 22 – Bill 198, § 138.1 (Can.).

114. *See* Securities-related Class Action Act, Act No. 7074, Jan. 20, 2004, amended in Act. No. 11845, May 28, 2013, add. 1 (S. Kor), *translated in Securities-Related Class Action Act*, KOREA L. TRANSLATION CTR., https://elaw klri.re kr/eng_mobile/viewer.do?hseq=29730 &type=part&key=8 [https://perma.cc/NB2Q-PYES].

application to the court for approval.[115] The court will then notify all plaintiffs and inform them of their rights to opt-out.[116] However, the procedural rules in South Korea are highly restrictive: no contingency fees are available; at least fifty investors possessing at minimum 0.01% of the shares must sign on before the opt-out system is triggered; and no firms can be the lead counsel more than three times in a three-year span.[117] In addition, before 2007, only large companies could be sued under the opt-out regime.[118] In South Korea, only ten class-action suits have been filed in the past thirteen years,[119] likely due to the careful calculation of plaintiffs' lawyers, creating an environment in which only cases highly likely to win and be enforced are brought to court.[120]

### *B. The NPO-Led Model*

The NPO-led model emerged as a response to address the incentives problem that plagued the model led by entrepreneurial lawyers. Given the pro-social nature of NPOs, one can expect that financial interests will not distort the litigation decisions made by NPOs when representing tort victims. The following Section considers two representative jurisdictions that have adopted this model: (1) the European Union; and (2) Taiwan.

#### 1. European Union

Twelve years after the European Union's first proposal of a collective-redress mechanism in 2008, the E.U. finally introduced a collective redress mechanism for injured consumers in 2020.[121]

115. *Id.* art. 7(1).

116. *Id*. arts. 10, 15.

117. *Id*. arts. 11(3), 12(1).

118. *Id.* add. (3).

119. Hai Jin Park, *Class Action Scarcity: An Empirical Analysis of the Securities Class Action in Korea*, 21 EUR. BUS. ORG. L. REV. 665, 665 (2020). Another study found that only thirteen securities class action cases had been filed in Korea as of August 2017. Benjamin Joon-Buhm Lee, *Saving the Korean Securities Class Action*, 39 U. PA. J. INT'L L. 247, 247, 287–90 (2017).

120. *See* Park, *supra* note 119, at 665.

121. It took the E.U. twelve years to fashion a coherent scheme for collective redress. In 2008, the E.U. published the first proposal for consumer collective redress. In the consultation paper, the E.U. was opened for public advice on whether an opt-in or opt-out regime should be adopted. *See generally European Commission Green Paper on Consumer Collective Redress*, COM (2008) 794 final (Nov. 27, 2008). Later in 2011, the E.U. published a consultation paper to set principles for E.U.-collective action. In fear of frivolous U.S.-style

Notably, however, this Directive excludes securities class actions. Yet its application is still apposite to the present discussion, as the Directive addressed similar concerns about lawyerly incentives. To avoid a litigious legal culture, the Union issued a Directive in 2020 which exhibited a clear attitude of eschewing certain elements that are essential to U.S.-style class action. Under the 2020 Directive, only "qualified entities"—that is, either consumer organizations or public bodies, not lawyers—are permitted to bring representative litigation for injunctive measures on behalf of general consumers or for compensation on behalf of a group of consumers.[122] Moreover, Member States have discretion to set qualifying eligibility criteria for entities to bring domestic collective actions.[123] To ensure legal harmonization, qualified entities across all Member States must meet certain fundamental criteria—including twelve months of actual public activities for consumer protection, a statutory purpose of consumer protection, and a non-profit nature—before initiating a cross-border class action.[124] Hence, these qualified entities must be non-profit organizations unless Member States designate public bodies to act as qualified entities.[125]

Following the E.U. tradition, a fee-shifting rule, rather than the "American Rule," requires losing parties to pay the costs of the proceedings borne by successful parties.[126] To protect consumers'

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class actions destroying E.U. legal tradition, the recommendation made it clear that "collective redress must be founded on the opt-in principle." *See European Parliament Resolution on "Towards a Coherent European Approach to Collective Redress"*, at 36 2012 O.J. (C 239 E) 32 (Feb. 2 2012). In 2013, the E.U. made another non-binding recommendation that its Member States introduce collective-action mechanisms in their domestic laws. The recommendation (issued by the European Commission) rejected most of the key features of the U.S. class action system. For example, the recommendation endorsed the "loser pays principle" and "opt-in principle." *See Commission Recommendation on Common Principles for Injunctive and Compensatory Collective Redress Mechanisms in the Member States Concerning Violations of Rights Granted Under Union Law*, at 61 ¶¶ 13, 21, 2013 O.J. (L 201) 60 (July 26, 2013) [hereinafter 2013 Commission Recommendation]. On November 25, 2020, the E.U. Parliament endorsed a Directive on collective redress that came into force on December 24, 2020. The Directive allows Member States to choose between opt-in and opt-out. *See generally* 2020 Directive, *supra* note 27.

122. *See* 2020 Directive, *supra* note 27, arts. 3, ¶ 4; 4, ¶ 1; 5, ¶ 2.

123. *See id.* pmbl. (26), art. 4, ¶ 2.

124. *See id.* art. 4, ¶ 3.

125. *See id.* art. 7.

126. Note that the loser-pays rule does not necessarily mandate that the losing party reimburse the other party's costs in full. Different jurisdictions usually have different rules for calculating reimbursable attorneys' fees. *See* OECD, PRIVATE ENFORCEMENT OF SHAREHOLDER RIGHTS: A COMPARISON OF SELECTED JURISDICTIONS AND POLICY ALTERNATIVES FOR BRAZIL 39 (2020), https://www.oecd.org/corporate/ca/Shareholder-

interests, qualified entities other than individual consumers shall bear the cost if the case is lost.[127] Regarding the choice between the opt-out and opt-in rules, for the first time since the proposal was advanced in 2008, the E.U. now accepts the opt-out regime in its Directive for collective redress, giving its Member States the discretion to adopt an opt-in and/or opt-out procedure.[128] This practice contradicts the E.U.'s former position in its 2013 Recommendation, which only permitted an opt-in regime.[129] The E.U.'s change of attitude was partially designed to accommodate the legal harmonization of Member States that formerly had diverse adoptions of the opt-in/opt-out models. For example, the Netherlands and Portugal adopted the opt-out procedure for collective redress, while thirteen other Member States exclusively applied the opt-in procedure.[130] To avoid the misuse of the collective redress mechanism, the 2020 Directive now requires courts to dismiss meritless cases at the earliest possible stages,[131] and prohibits punitive damages, which are common in the United States.[132] The Directive came into force on December 24, 2020, and the Member States will have twenty-four months to integrate its provisions into their domestic laws and an additional six months to fully implement the provisions.[133] Although the scope of the 2020 Directive only covers consumer law, not securities law, this NPO-led model may affect the future of securities class actions in the E.U. and other jurisdictions around the world.

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Rights-Brazil.pdf [https://perma.cc/ET39-WHB9]. Against this varied backdrop, the E.U. Directive only asks Member States to follow the loser-pays rule "in accordance with the conditions and exceptions provided for in national law applicable to court proceedings in general." *See* 2020 Directive, *supra* note 27, art. 12, ¶ 1.

127. *See* 2020 Directive, *supra* note 27, art. 12, ¶ 2.

128. The Directive left it open for Member States to decide how plaintiffs shall join in the lawsuit. *See id.* art. 9, ¶ 2:

> Member States shall lay down rules on how and at which stage of a representative action for redress measures the individual consumers concerned by that representative action explicitly or tacitly express their wish within an appropriate time limit after that representative action has been brought, to be represented or not by the qualified entity in that representative action and to be bound or not by the outcome of the representative action.

129. *See* 2013 Commission Recommendation, *supra* note 121, art. 21.

130. *See Report from the Commission to the European Parliament, the Council and the European Economic and Social Committee on the Implementation of the Commission Recommendation of 11 June 2013 on Common Principles for Injunctive and Compensatory Collective Redress Mechanisms in the Member States Concerning Violations of Rights Granted Under Union Law*, at 13, COM (2013) 040 final (Jan. 25, 2018).

131. 2020 Directive, *supra* note 27, art. 7, ¶ 7.

132. *See id.* recital 42.

133. *See id.* art. 22, ¶ 1.

2. Taiwan

While the NPO-led model has not been enforced in securities fraud-related disputes in the E.U., Taiwan has been experimenting with such an innovative enforcement model for almost two decades. The new Chinese hybrid model, discussed more substantively in Part II, heavily refers to the Taiwanese experience.

By way of background, Taiwan enacted the Securities Investor and Futures Trader Protection Act ("Investor Protection Law"), which took effect in 2003.[134] The Investor Protection Law's collective redress procedure is completely unlike the U.S. regime. Pursuant to the Investor Protection Law, the Securities and Futures Investors Protection Center ("SFIPC") was established to enhance investor protection and promote the sound development of the capital market.[135] The SFIPC is registered as a foundation—a private legal person for public-interest purposes—and hence is non-profit and non-distributive in nature.[136] The Investor Protection Law granted the SFIPC exclusive standing to bring opt-in collective litigation for securities-fraud victims, thereby relieving the Center of some procedural hurdles and financial burdens in pursuing related litigation for investors.[137]

The Taiwanese NPO-led model is by no means unique in Asia. Other major economies in East Asia have established NPO-led collective redress regimes as solutions to contemporary governance problems.[138] For example, in Japan, the Kabunushi Ombudsman ("KO")—consisting of activist attorneys, accountants, and individual investors—was established in January 1996 to reform the business practices of Japanese enterprises to consider the interests of individual shareholders.[139] Through litigation, shareholder proposals, and public criticism, the KO has contributed to improving Japanese corporate governance for decades.[140] In South Korea, where the capital market is dominated by chaebols (large business groups), the People's

134. The purpose of the Act is to provide protection to securities and futures investors. *See* ZHENGQUAN TOUZI REN JI QIHUO JIAOYI REN BAOHU FA (證券投資人及期貨交易人保護法) [SECURITIES INVESTOR AND FUTURES TRADER PROTECTION ACT OF THE REPUBLIC OF CHINA] (June 20, 2002), art. 1 [hereinafter TOUBAO FA].

135. *See id.* arts. 5, 7.

136. *See* CAITUAN FAREN FA (財團法人法) [FOUNDATIONS ACT OF THE REPUBLIC OF CHINA] (Aug. 1, 2018), arts. 2, 22.

137. *See infra* notes 144–155 and accompanying text.

138. *See* Milhaupt, *supra* note 90, at 175–81.

139. *Id.* at 178–79.

140. *Id.* at 180–81.

Solidarity for Participatory Democracy (PSPD) was established in 1994 to protect minority shareholders' interests against controllers.[141] As a pioneer of Korean shareholder activism, the PSPD promoted corporate watchdog activities against corporate misconduct.[142] And unlike South Korea and Japan, where NPOs are voluntarily established by market participants, the SFIPC in Taiwan was established by law to facilitate a collective redress regime.[143]

The Investor Protection Law establishes the requirements for SFIPC-initiated collective litigation in Taiwan: (1) the purpose of the litigation is to protect the public interest; (2) there are numerous securities and futures investors who suffered losses from the same misconduct; and (3) more than twenty investors have delegated their rights to bring legal action to the SFIPC.[144] Unlike the U.S.-style class action that adopted the opt-out rule, defrauded investors in Taiwan are only included in legal proceedings initiated by the SFIPC if they actively join or opt into the litigation. The SFIPC is the only institution that can file securities-related collective litigation in its own name, and it has the sole discretion to decide whether to proceed with such litigation.[145] While the SFPIC usually piggybacks on existing criminal claims to file civil lawsuits, it also independently seeks potential targets and notifies qualifying investors on its website, inviting them to join suits.[146] Those who do not join SFIPC collective actions can sue individually, and the judgment in the SFIPC case will not bind them; therefore, later judgments on similar claims may not be consistent with the relevant SFIPC cases.[147]

Taiwan's deviation from the U.S.-style model also manifests in its litigation fee-arrangement and participation mechanisms. Taiwan follows the "English Rule": that is, the loser-pays rule in civil litigation, which allows the prevailing party to recover its costs from

141. *Id.* at 175.

142. *Id.* at 176–77.

143. One of the authors discussed the economic theories underpinning the Taiwanese government-NPO partnership model in another paper. *See* Lin, *supra* note 22, at 183–89.

144. TOUBAO FA, *supra* note 134, art. 28.

145. *See id*.

146. *See* Lin, *supra* note 22, at 175. *See also* Lin Yu-Hsin, *Touzi Ren de Nuoya Fangzhou: Touzi Ren Baohu Zhongxin Yu Zhengquan Tuanti Susong Zhi Shizheng Yanjiu* (投資人的諾亞方舟： 投資人保護中心與證券團體訴訟之實證研究) [*Noah's Ark for Investors: An Empirical Study of Securities Class Action and the Investor Protection Center in Taiwan*], 229 YUEDAN FAXUE ZAZHI (月旦法學雜誌) [TAIWAN L. REV.] 75, 81–82 (2014) [hereinafter Lin, *Noah's Ark*].

147. *See* Lin, *Noah's Ark*, *supra* note 146, at 78.

the loser.[148] Even though Taiwan allows for contingent fee arrangements in most civil law cases,[149] the arrangement cannot depend on a certain percentage of the recovery amount.[150] The Taiwanese Bar Association also restricts attorneys from charging fees higher than a certain amount in an individual case.[151] As a result, the fee-arrangement rule is generally hostile to U.S.-style entrepreneurial lawyers.

Under the Investor Protection Law, the SFIPC prepays court fees and recovers only necessary costs from the compensation in a winning case without claiming any profits.[152] As a public-interest NPO, the SFIPC is prohibited from distributing profits to its members and collects no profits from investors.[153] To ensure the normal function and independence of the SFIPC, a protection fund ("SFIPC Fund") was established by key market players, such as stock exchanges and securities merchant associations.[154] The Investor Protection Law further reduced the SFIPC's financial burden by waiving some of its court fees and granting a discretionary exemption on the guaranty for a pre-trial temporary injunction.[155]

For almost two decades, the SFIPC has actively engaged in investor protection and brought securities collective actions on behalf of defrauded investors. By the end of 2020, the SFIPC had brought 268 collective lawsuits and won fifty-nine, and investors had been awarded more than 910 million USD (25.2 billion NT).[156] The cases

148. *See* MINSHI SUSONG FA (民事訴訟法) [CODE OF CIVIL PROCEDURE OF THE REPUBLIC OF CHINA] (Nov. 28, 2018), art. 78.

149. Similar to the rules in the United States, Taiwan forbids contingent fee arrangements in family disputes, criminal and juvenile cases. *See* Lüshi Lunli Guifan (律師倫理規範) [Legal Ethics] (Sept. 19, 2009), art. 35(2); *see also* MODEL RULES OF PRO. CONDUCT r. 1.5(d)(1) (AM. BAR ASS'N 2020) (the American rule on contingent fees).

150. *See* LÜSHI FA (律師法) [Attorney Regulation Act of the Republic of China] (Jan. 15, 2020), art. 45; FAWUBU (法務部) [MINISTRY OF JUSTICE], Fa Jian Zi Di 10604528660 Hao (法檢字第 10604528660 號) [Explanatory Note No. 10604528660] (Oct. 23, 2017), https://mojlaw.moj.gov.tw/LawContentExShow.aspx?id=FE304227&type=E&kw=&etype=etype3 [https://perma.cc/W7XV-55P3].

151. *See* Lin, *supra* note 22, at 171–72.

152. *See* TOUBAO FA, *supra* note 134, art. 33.

153. For a discussion of the non-distributive nature of NPOs, see Milhaupt, *supra* note 90, at 170–75.

154. *See* TOUBAO FA, *supra* note 134, art. 6.

155. *See id*. arts. 34–36.

156. SEC. & FUTURES INVESTORS PROT. INVS. PROTECTION CTR., 2020 ANNUAL REPORT 5 (2020), https://www.sfipc.org.tw/MainWeb/Article.aspx?L=2&SNO=cETUAHMWj7bwkiS59QXNww== [https://perma.cc/BU3Q-HSTG] [hereinafter SFIPC Annual Report].

initiated by the SFIPC fall into four categories: (1) financial misstatements; (2) false disclosure; (3) stock manipulation; and (4) insider trading.[157] Although the compensation amounts granted by the courts account for 93.3% of the total amount of claims, what investors actually received is far less.[158] Apparently, by the time the SFIPC decides to sue and make petitions to seize the defendants' assets, there are often few assets remaining.[159] To solve this problem, the SFIPC often enters into settlements with wrongdoers. By 2020, 201 million USD (5.6 billion NT) had been distributed to investors through settlements.[160]

Despite the total amount being much smaller than its U.S. counterpart, the number of cases brought and the scale of losses recovered by the SFIPC for investors still attest to the success of the NPO model, an innovative alternative to the attorney-driven U.S.-style model. The Taiwanese experience has become a good lesson for jurisdictions wishing to establish a securities class action regime but apprehensive about fostering a litigious legal culture.

### *C. Other Functionally Equivalent Models*

Due to distinct local conditions, some jurisdictions may be reluctant or are unable to adopt the opt-out rule and follow the U.S. model. To respond to the needs of aggrieved investors, some of these jurisdictions have developed functionally equivalent models to help resolve mass disputes collectively. In this Section, we profile three such models: (1) Model Litigation in Germany; (2) Group Litigation Order in the United Kingdom; and (3) Opt-Out Settlement in the Netherlands.

#### 1. Germany: Model Litigation

Germany strictly follows the traditional single-party adjudication system and values each individual's right to adjudication,[161] which contradicts the core meaning of an opt-out rule. However, this policy does not suggest that Germany does nothing

157. *See* Lin, *Noah's Ark*, *supra* note 146, at 76.

158. *Id*. at 83.

159. Empirical evidence indicates that investors only received eight percent of their claims from the enforcement of court judgments. *Id*.

160. SFIPC Annual Report, *supra* note 156, at 6.

161. *See supra* note 40 and accompanying text.

when a flood of defrauded investors seek compensation.[162] In 2005, the German Parliament enacted the Capital Markets Model Case Act ("KapMuG"), under which the common issues of many plaintiffs in multiple parallel lawsuits are decided in a model case that is binding on all plaintiffs.[163] This innovative procedural rule skillfully avoids choosing between the opt-in or opt-out model, creating a locally-acceptable solution that balances investors' grievances and judicial efficiency.

To reduce litigation costs for parties, neither lawyers nor the court itself can collect any additional filing fees or attorney's fees.[164] Parties only need to pay the necessary prices for expert fees and fees arising from collecting evidence and other formalities on the *pro-rata* basis of their claims.[165] The German courts control the litigation and have the discretion to select the model case.[166] A settlement is technically allowed even when the model case is still under court review.[167] When the KapMuG was first introduced in 2005, a settlement required unanimity among all parties, making it practically impossible to reach one.[168] Later, the threshold was relaxed; settlements are now deemed effective if no more than thirty percent of plaintiffs opt-out.[169] After a judgment has been rendered for a model case, the adjudication of each plaintiff's claim can proceed to

162. The case of Deutsche Telekom's public offerings in 1999 and 2000 caused a lot of trouble for the regional court of Frankfurt—more than 17,000 claimants represented by 754 lawyers brought 2,128 lawsuits based on false statements in prospectus. This case directly led to the introduction of the Model Case Act in 2005. *See* Dirk A. Verse, *Germany: Liability for Incorrect Capital Market Information*, *in* GLOBAL SECURITIES LITIGATION AND ENFORCEMENT 363, 400 (Pierre-Henri Conac & Martin Gelter eds., 2019); Harald Baum, The German Capital Markets Model Case Act – A Functional Alternative to the US-Style Class Action for Investor Claims? 2 (Feb. 1, 2017) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2909545 [https://perma.cc/XXW4-QXBP].

163. *See* Kapitalanleger-Musterverfahrensgesetz [KapMuG] [Capital Markets Model Case Act], Aug. 16, 2005, BUNDESGESETZBLATT I [BGBL I] at 2437, revised Oct. 19, 2012, BGBL I at 2182, § 22 (Ger.) [hereinafter KAPMUG 2012].

164. *See id*. § 24(1)–(2); Rechtsanwaltsvergütungsgesetz [RVG] [Act on the Remuneration of Lawyers], May 5, 2004, BUNDESGESETZBLATT I [BGBL I] at 718, 788, last amended by Gesetz [G], Aug. 10, 2021, BGBL I at 3424, § 15(4), § 16(13), § 23b (Ger.) ("In model cases under the Capital Markets Model Case Act, the value of the claim shall be determined according to the amount of the claim asserted by or against the client in the main proceedings, insofar as this is the subject of the model proceedings.").

165. *See* KapMuG 2012, *supra* note 163, § 24(2).

166. *See id*. § 9(2).

167. *See id*. § 17(1).

168. *See* KapMuG, *supra* note 163, BGBL I at 2437, § 14(3) (Ger.).

169. *See* KapMuG 2012, *supra* note 163, § 17(1).

determine loss, causation, and damages.[170] Despite these changes, "each investor must bring an individual suit to enforce his rights" under the German model litigation regime, and the procedures have been criticized as too complex and slow.[171]

Interestingly, the German government only sees model litigation as a temporary solution, as evidenced by the structure of the KapMuG itself. When the Act came into effect, a sunset clause prescribed that it would expire on November 1, 2010; however, the KapMuG has been renewed multiple times and is now valid until December 31, 2023.[172] With the introduction of the E.U. Directive on collective redress in 2020, Germany is expected to implement the E.U. directive in the coming years.[173] Still, the German model case regime serves as an alternative to the U.S. class action model from which policymakers in other jurisdictions can learn. For example, based on the German experience, China introduced a model case-like device in 2019.[174] Unlike the German model case regime, however, the model case in China has a binding effect on parallel lawsuits, thereby facilitating future single-party litigation, mediation, and other ADRs on similar issues.[175]

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170. *See id.* § 16.

171. *See* Verse, *supra* note 162, at 406.

172. *See* Thomas Hauss & Thiemo Sch. . fer, *German Capital Investor Model Proceedings Act (KapMuG) Prolonged by Bundestag*, STEWARTS L. NEWS (Dec. 18, 2020), https://www.stewartslaw.com/news/german-capital-investor-model-proceedings-act-prolonged-by-bundestag [https://perma.cc/AQG6-T6NM].

173. *See id.*

174. The court may first try a model case on common issues of law and fact, and then mediators and judges in the later claims can directly apply the decision from the model case. *See* Zuigao Renmin Fayuan Zhongguo Zhengquan Jiandu Guanli Weiyuan Hui Guanyu Quanmian Tuijin Zhengquan Qihuo Jiufen Duoyuan Huajie Jizhi Jianshe De Yijian, Fa [2018] 305 Hao (最高人民法院中国证券监督管理委员会关于全面推进证券期货纠纷多元化解机制建设的意见, 法 [2018] 305 号) [Notice by the Sup. People's Ct. and CSRC of Issuing Opinions on Comprehensively Advancing Establishment of Diversified Resolution Mechanism of Securities and Futures Disputes, Judicial No. 305 [2018]] (promulgated by Sup. People's Ct. and China Sec. Regul. Comm'n, Nov. 13, 2018), art. 13, http://www.csrc.gov.cn/pub/newsite/zjhxwfb/xwdd/201811/t20181130_347505.html [https://perma.cc/L37D-9UEN], [hereinafter *2018 Diversified Resolution Notice*]. Before the introduction of the model-judgment mechanism in China, courts had already experimented with choosing a test case to try and to guide cases with similar claims. *See* Tang Xin (汤欣), *Lun Zhengquan Jituan Susong De Tidai Xing Jizhi Bijiao Fa Jiaodu De Chubu Kaocha* (论证券集团诉讼的替代性机制——比较法角度的初步考察) [*On the Alternative Mechanisms of Securities Class Actions—Preliminary Investigation from a Comparative Law Perspective*], 4 ZHENGQUAN FAYUAN （证券法苑） [SEC. L. REV.] 174, 178 (2011).

175. According to the Shanghai model-judgment rule, the court, when facing similar claims from more than ten claimants, can choose one case as the model case, the judgment of

2. The United Kingdom: Group Litigation Order

In the United Kingdom, specifically England and Wales, Civil Procedure Rule 19.11 established the group litigation order with opt-in provisions as the main litigation device for collective redress.[176] It is highly court-centric: with or without plaintiffs' applications, a court may issue a group litigation order to manage individual claims that give rise to common issues of fact or law,[177] but the participation mechanism is opt-in.[178] To be included in the group, every claimant must individually make claims.[179] Of course, only those who join the group are entitled to the damages awarded.[180] However, because a group litigation order is issued by a court to decide issues that are common among each individual claim, the unique issues of such claims remain individual even after the issuance of a group litigation order.[181] In other words, a management court, which makes the group litigation order, only investigates the common issues; individual claims are re-allocated to their respective courts.[182] In this way, the United Kingdom adheres to the single-party adjudication principle while maximizing judicial resources. However, the U.K. loser-pays rule and extra fees arising from the group litigation order limit the application of collective redress. As of 2020, only 109 orders had been made in England and Wales since the introduction of the group litigation order in 2000.[183]

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which will be binding on all parallel cases unless the plaintiffs object. Parties in parallel cases do not need to provide extra evidence to prove common issues of fact. *See* Shanghai Jinrong Fayuan Guanyu Zhengquan Jiufen Shifan Panjue Jizhi de Guiding Shixing (上海金融法院关于证券纠纷示范判决机制的规定 (试行)) [Provisions of the Shanghai Financial Court on the Model Judgment Mechanism of Securities and Futures Disputes (For Trial Implementation)] (promulgated by Shanghai Fin. Ct., Jan. 16, 2019), arts. 2, 37, http://www.shjrfy.gov.cn/jrfy/gweb/xx_view.jsp?pa=aaWQ9MTA2NQPdcssPdcssz [https://perma.cc/2FJL-KDHA].

176. For a general introduction to the group litigation order, see Rachael Mulheron, *Reform of Collective Redress in England and Wales: A Perspective of Need* 9–15 (2008) (Research Paper for Submission to the Civil Justice Council of England and Wales), https://www.judiciary.uk/wp-content/uploads/JCO/Documents/CJC/Publications/Other+papers/reform-of-collective-redress.pdf [https://perma.cc/ND8V-G984].

177. *See* CPR9.10, 19.11(1) (U.K.).

178. *See id*. r. 19A(1.1).

179. *Id.* r. 19B(6.1A).

180. *Id*. r. 19.12(1).

181. *Id.* r. 19.10.

182. *Id*. r. 19B(7(1)).

183. *Group Litigation Orders*, GOV.UK (June 23, 2020), https://www.gov.uk/guidance/group-litigation-orders [https://perma.cc/F8HE-WXA4].

### 3. The Netherlands: Opt-Out Settlements

In the Netherlands, class actions with opt-out provisions are also available, but the lawsuit must be brought by a set of private institutions called the "professional association of shareholders"[184] on behalf of its members.[185] Before 2020, investors were prohibited from claiming damages in collective securities actions. Instead, representative institutions could initiate collective actions on the basis of misrepresentation for a declaratory judgment from a court. In the judgment, the court would have to decide whether the defendant had committed any illegal acts, but it could not award any damages.[186] After the court had decided the case, the parties could devise settlements accordingly.[187] Even though investors cannot currently sue for damages in court under the opt-out regime, they can still settle cases under the opt-out rule. According to the Act on the Collective Settlement of Mass Claims (*Wet Collectieve Afwikkeling Massaschade*) ("WCAM"), which was enacted in 2005, once the Amsterdam Court of Appeals approves a settlement, it is binding on all qualified investors unless they opt-out.[188] The WCAM thus provides a convenient channel through which U.S. lawyers can facilitate global settlements outside the United States for suits involving foreign investors that cannot be brought within the country.[189] For example, the *Fortis* litigation was settled pursuant to the WCAM for 1.337 billion USD in March 2016 on an opt-out basis and was approved by the Amsterdam Court of Appeals in June 2017.[190]

Beginning on January 1, 2020, the Netherlands implemented a new opt-out class action regime, the Act on the Resolution of Mass Claims in Collective Action (*Wet Afwikkeling Massaschade in Collectieve Actie*) ("WAMCA").[191] Under the WAMCA, aggrieved

184. In Dutch, a typical association of shareholders is known as a Vereniging van Effectenbezitters or "VEB"; this structure is famous for providing collective redress for investors. *About the VEB*, VEB, https://www.veb.net/over-de-veb-menu/about-the-veb [https://perma.cc/PET7-ZSVC].

185. Loes Lennarts & Joti Roest, *Netherlands: Protection of Investors and the Compensation of Their Losses*, *in* GLOBAL SECURITIES LITIGATION AND ENFORCEMENT 469, 502–03, 514 (Pierre-Henri Conac & Martin Gelter eds., 2019).

186. Wet van 23 juni 2005, Stb. 2005, 340, arts. 1, 2 (Neth.).

187. *See id*.

188. *See id*. art. 1.

189. *See* Morrison v. Nat'l Austl. Bank Ltd., 561 U.S. 247, 273 (2010); *see also supra* notes 12–14 and accompanying text.

190. Lennarts & Roest, *supra* note 185, at 500 n.123.

191. *See generally* Wet van 20 maart 2019, Stb. 2019, 130 (Neth.).

investors who are Dutch residents can claim damages on an opt-out basis, while parties residing abroad can do so on an opt-in basis.[192] It bears mentioning, however, that the new law only applies to events that transpired on or after November 15, 2016.[193] Even though the collective plaintiffs can claim damages on behalf of the class members under the new law, parties must still engage in a discussion to try reaching a settlement before the court examines the case on its merits.[194] The new development is likely to augment the prevalence of class action cases in the Netherlands.

## II. CHINESE SECURITIES CLASS ACTION: A HYBRID MODEL

In this Part, we introduce China's newly reformed securities representative action regime, which combines the two key class action models: (1) the lawyer-led model and (2) the NPO-led model. Section II.A discusses the historical background and highlights the key characteristics of Chinese securities litigation. Section II.B examines the 2020 Securities Law Amendment, which introduces securities class action devices to China. Sections II.C and II.D, respectively, detail the main features of China's lawyer-led opt-in representative action and NPO-led opt-out class action.

### *A. Historical Background*

#### 1. Reliance on Public Enforcement

Historically, the Chinese domestic securities market was developed to raise funds for state-owned enterprises (SOEs) and has since been subject to the strict supervision and control of the central government.[195] While the Chinese capital market has grown to be the second-largest in the world by total market value, its legal infrastructure lags behind its market growth.[196] Not until ten years

192. *See id.* arts. 1, 2.

193. *Id.* art. 3.

194. Frank Kroes, *The Netherlands Introduces Class Action-Type Litigation*, BAKER MCKENZIE (Dec. 4, 2019), https://www.bakermckenzie.com/en/insight/publications/2019/12/netherlands-class-action-type-litigation [https://perma.cc/34AH-75FR].

195. HUI HUANG, INTERNATIONAL SECURITIES MARKETS: INSIDER TRADING LAW IN CHINA 15–16 (2006).

196. *See* Katharina Pistor & Chenggang Xu, *Governing Stock Markets in Transition Economies: Lessons from China*, 7 AM. L. & ECON. REV. 184, 184–85 (2005). This is not only the case in China. Coffee likewise examined the evolution of the global stock market and

after the establishment of the Shenzhen and Shanghai Stock Exchanges did China finally promulgate its own Securities Law in 1999.[197] At the time, however, the law could not meet market demand, so the China Securities Regulatory Commission (CSRC) had to issue notices, guidelines, and opinions to supplement it.[198] As a result, the CSRC used its administrative power to govern the market as a substitute for the weak legal system.[199]

Public enforcement in China still has its weaknesses. For instance, monetary penalties imposed by the CSRC have little deterrent effect because the old securities law only permitted the CSRC to penalize an individual no more than approximately 50,000 USD (300,000 RMB) and a company no more than 95,000 USD (600,000 RMB).[200] When the illegal gain of securities fraud outweighs the potential penalty, wrongdoers often still engage in misconduct after calculating their potential net profits.[201] In addition, the CSRC may

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noted that legal reform is a response to market development, not the other way around. *See* John C. Coffee, Jr., *The Rise of Dispersed Ownership: The Roles of Law and the State in the Separation of Ownership and Control*, 111 YALE L.J. 1, 24–59 (2001).

197. The Shenzhen Stock Exchange and Shanghai Stock Exchange were established in 1990. Yet, the first Chinese Securities Law did not come into effect until 1999. *Overview*, SHENZHEN STOCK EXCHANGE, http://www.szse.cn/English/about/overview/index html [https://perma.cc/HR2F-T22S]; *History and Development*, SHANGHAI STOCK EXCHANGE, http://english.sse.com.cn/aboutsse/overview/ [https://perma.cc/7NMV-N6W4]. *See generally* Zhonghua Renmin Gonghe Guo Zhengquan Fa 1999 (中华人民共和国证券法1999) [Securities Law of PRC 1999] (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 29, 1998, effective July 1, 1999), http://www npc.gov.cn/wxzl/wxzl/2000-12/05/content_4718.htm [https://perma.cc/VM4P-HYR5].

198. Huang Tao (黄韬), *Wei Shenme Fayuan Bu Name Zhongyao—Zhongguo Zhengquan Shichang de Yige Guancha* (为什么法院不那么重要?基于中国证券市场国家管理行为的一项分析) [*Why Courts Are Not That Important: An Observation from China's Securities Market*], 9 FALU YU SHEHUI KEXUE (法律与社会科学) [L. & SOC. SCI.], 2012, at 63, 65 (noting that unlike common law jurisdictions, where judges and regulators together compensate for the incompleteness of securities law, the residual legislative power is vested in administrative and regulatory bodies in China and in other civil law jurisdictions, which arguably explains the weakness of the court's role in securities law enforcement in China).

199. *See* Pistor & Xu, *supra* note 196, at 196.

200. *See* Zhengquan Fa (2014) (证券法 (2014年)) [Securities Law of PRC (2014)] (promulgated by the Standing Comm. Nat'l People's Cong., Aug. 31, 2014, effective June 1, 2016), ch. 11, http://www npc.gov.cn/zgrdw/npc/lfzt/rlyw/2015-04/23/content_1934291 htm [https://perma.cc/KGC2-LU7M].

201. *See* Wang Qidi (王启迪), *Neimu Jiaoyi Fakuan Shue Yingxiang Yinsu de Shizheng Yanjiu—Jiyu Zhengjian Hui 21 Fen Xingzheng Chufa Jueding Shu de Zhengli* (内幕交易罚款数额影响因素的实证研究——基于证监会21份行政处罚决定书的整理) [*Empirical Study on Influencing Factor of Forfeit Amount Imposed on Insider Trading—Based on Arrangement of 21 Copies of Administrative Penalty Decisions by China Securities*

have a selective enforcement problem against companies with powerful political connections.[202] Like other public bodies, the CSRC is also bound by its limited resources.[203] It now invests more resources in ex-post enforcement, following the implementation of the registration-based share-issuance system in 2020, which released many of its resources and workforce from the ex-ante approval process.[204] Nevertheless, private enforcement is still vital to compensate investors' losses—a need that public enforcement cannot meet.[205]

### 2. Representative Action Regime

China had no class action for securities-related mass disputes until the 2020 amendment to the Securities Law. However, the Chinese Civil Procedure Law of 1991 provided a class action-like device called "representative action," which enabled plaintiffs to initiate lawsuits even if the number of plaintiffs was uncertain at the inception of the suit.[206] In such representative actions, plaintiffs could

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*Regulatory Commission*], XING ZHENG FA XUE YAN JIU (行政法学研究) [ADMIN. L. REV.], no. 4, 2011, at 115, 125.

202. *See* Xu Nian-hang (许年行) et al., *Zhengzhi Guanlian Yingxiang Touzi Zhe Falv Baohu de Zhifa Xiaolu Ma?* (政治关联影响投资者法律保护的执法效率吗?) [*Do Political Connections Affect the Efficiency of Law Enforcement of Investors' Legal Protection?*], 12 JINGJI XUE (JIKAN) (经济学季刊) [CHINA ECON. Q.], no. 2, 2013, at 373, 402.

203. *See* Xu Wenming (徐文鸣) & Zhu Liangyu (朱良玉), *Zhongmei Zhengquan Fa Gonggong Zhixing Jizhi Bijiao Yanjiu: Jiyu Jianguan Jigou Touru Chanchu de Shizheng Fenxi* (中美证券法公共执行机制比较研究——基于监管机构投入产出的实证分析) [*A Comparison of the Public Enforcement Regime in China and the United States: An Empirical Analysis of the Inputs and Outputs of the Public Regulators*], CAIJING FAXUE (财经法学) [L. & ECON.], no. 3, 2017, at 125.

204. *See* Guowu Yuan Guanyu Jin Yibu Tigao Shangshi Gongsi Zhiliang de Yijian (国务院关于进一步提高上市公司质量的意见) [Opinions of the State Council for Further Improving the Quality of Listed Companies] (promulgated by Gen. Off. St. Council, Oct. 5, 2020) § 3 http://www.gov.cn/zhengce/content/2020-10/09/content_5549924 htm [https://perma.cc/35GW-CU8B] (China). This infers that the change from the traditional approval-based system to the registration-based share issuance system reduces the requirement to make substantial examinations of companies' financial status. *See id.*

205. Scholars have envisioned the CSRC's role shifting after the amendment to the Securities Law. *See, e.g.*, Jiang Daxing (蒋大兴), *Yintui Zhong de "Quanli Xing" Zhengjian Hui: Zhuce Zhi Gaige Yu Zhengquan Jianguan Quan Zhi Chongzheng* (隐退中的"权力型"证监会——注册制改革与证券监管权之重整) [*PowerfulCSRC in Retirement—Reform of Registration System and Reorganization of Securities Supervision Power*], 184 FAXUE PINGLUN (法学评论) [L. REV.], no. 2, 2014, at 39, 48–51.

206. Zhonghua Renmin Gonghe Guo Minshi Susong Fa 1991 (中华人民共和国民事诉讼法1991) [Civil Procedural Law of PRC 1991] (promulgated by

appoint representatives to sue on behalf of all plaintiffs who had "common rights and obligations regarding the subject matter of action."[207] When plaintiffs were numerous and their exact number was uncertain, the court could notify potential plaintiffs and ask them to register with the court if they wished to join the litigation.[208] This mechanism gave potential plaintiffs the choice to opt into the litigation, and if they joined the lawsuit, the judgment was binding on them.[209] To extend the binding effect of representative actions, the judgment was also binding on those who did not join the lawsuit, but who brought individual legal actions later.[210] However, in practice, the application of this procedure was rarely allowed by the court and never applied to securities litigation, as the court never issued any implementation rules before the 2020 Securities Law Amendment.[211]

### 3. The Judiciary's Reluctance to Accept Cases

In the past, the lack of private enforcement in Chinese corporate and securities law was partially the result of the judiciary's unwillingness to take a proactive role in deterring wrongdoers.[212] In 2003, the SPC issued a notice concerning civil securities lawsuits, mandating that such suits could only be heard by a court if a prior criminal judgment or administrative sanction were granted in the same case.[213] In addition, investors could only sue if their loss were incurred

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the Standing Comm. Nat'l People's Cong., Apr. 9, 1991, effective Apr. 9, 1991), art. 54, 55, http://210.73.66.144:4601/law?fn=chl024s123.txt&term=58 [https://perma.cc/UXL9-VYMC] [hereinafter MINSU FA 1991].

207. *See* Zhonghua Renmin Gonghe Guo Minshi Susong Fa 2017 (中华人民共和国民事诉讼法2017) [Civil Procedural Law of PRC 2017] (promulgated by the Standing Comm. Nat'l People's Cong., June 27, 2017, effective June 27, 2017), art. 53, 54, http://www.npc.gov.cn/zgrdw/npc/xinwen/2017-06/29/content_2024892 htm [https://perma.cc/BB4J-H7PN] [hereinafter MINSU FA 2017].

208. *Id.*

209. *Id.*

210. *Id.* art. 54(4).

211. *See* discussion *infra* Sections II.B, II.C & II.D.

212. *See, e.g.*, Huang, *supra* note 24, at 768–70.

213. Zuigao Renmin Fayuan Guanyu Shenli Zhengquan Shichang Yin Xujia Chenshu Yinfa de Minshi Peichang Anjian de Ruogan Guiding, Fashi [2003] 2 Hao (最高人民法院关于审理证券市场因虚假陈述引发的民事赔偿案件的若干规定, 法释 [2003] 2号)[Some Provisions of the Supreme People's Court on Trying Cases of Civil Compensation Arising from False Statements in Securities Market, Judicial Interpretation No. 2 [2003]] (promulgated by the Judicial Comm. Sup. People's Ct., Jan. 9, 2003, effective Feb. 1, 2003), art. 5, Sup. People's Ct. Gaz., Jan. 10, 2013,

by misstatement, but not on other grounds.[214] Investors could either sue individually or in a joint action; a class action device was unavailable.[215] This procedural prerequisite and other limitations imposed by the SPC attest to the judiciary's reluctance to hear civil securities lawsuits. An empirical study that collected cases filed from 2002 to 2011 that met this prerequisite (administrative or criminal liability) determined that the court only heard 25.7% (65 of 253) of the potential cases.[216]

Ideally, private enforcement in the form of securities class actions has two main functions: (1) compensating aggrieved investors and (2) deterring potential wrongdoers.[217] When civil lawsuits were subordinated to administrative and criminal decisions, private enforcement in China had a very limited deterrence effect.[218] Before the establishment of the China Securities Investors Service Center (CSISC) in 2014, securities litigation was limited, so the compensation function of private enforcement was also weak.[219] The fact that private

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http://gongbao.court.gov.cn/Details/736c8d392b7a1d755a9c1a7a1a0e7e html?sw= [https://perma.cc/7958-7TMB] [hereinafter *The 2003 Notice*].

214. *Id.* art. 1.

215. *Id.* art. 12; *see also* Zuigao Renmin Fayuan Guanyu Shouli Yin Xujia Chenshu Yinfa de Minshi Qinquan Jiufen Anjian Youguan Wenti de Tongzhi (最高人民法院关于受理证券市场因虚假陈述引发的民事侵权纠纷案件有关问题的通知) [The Notice of the Supreme People's Court on Relevant Issues of Filing of Civil Tort Dispute Cases Arising from Misrepresentation on the Securities Market] (promulgated by the Sup. People's Ct., Jan. 15, 2002), art. 4, http://www.yanyataolawyer.com/index/Article/detail/id/101 html [https://perma.cc/K8L3-LWS7].

216. *See* Huang, *supra* note 24, at 766.

217. *See* John C. Coffee, Jr., *Reforming the Securities Class Action: An Essay on Deterrence and Its Implementation*, 106 COLUM. L. REV. 1534, 1538 (2006).

218. Critics have charged that prerequisites hinder securities law enforcement. *See, e.g.*, Guiping Lu, *Private Enforcement of Securities Fraud Law in China: A Critique of the Supreme People's Court 2003 Provisions Concerning Private Securities Litigation*, 12 PAC. RIM L. & POL'Y J. 781, 795–98 (2003); *see also* Wenming Xu, *Reforming Private Securities Litigation in China: The Stock Market Has Already Cast Its Vote*, 45 INT'L REV. L. & ECON. 23, 23–24, 31 (2016) (noting that the 2002 Notice, not discussed in this Article, aggravated the collective action problem which undermined securities private enforcement). Others have demonstrated that prerequisites facilitate the litigation process. For example, after the CSRC collects evidence in issuing penalties, litigants can piggyback on the CSRC's discovery in establishing the causality between wrongdoers' tortious conduct and the damage caused. *See* Xu Wenming (徐文鸣), *Zhengquan Minshi Susong Zhidu de Shizheng Yanjiu* (证券民事诉讼制度的实证研究) [*An Empirical Study on the Civil Litigation System of Securities*], 58 ZHONGGUO ZHENGFA DAXUE XUEBAO (中国政法大学学报) [J. CHINA UNIV. POL. SCI. & L.], no. 2, 2017, at 74, 77.

219. Xin Yu (辛宇) et al., *Touzi Zhe Baohu Gongyi Zuzhi Yu Gudong Susong Zai Zhongguo de Shijian Jiyu Zhongzheng Toufu Zhengquan Zhichi Susong de Duo Anli Yanjiu*

enforcement could not compensate investors or deter wrongdoers forced China to reform its procedural rules to enable investors to initiate securities class actions.

### 4. The Emergence of NPOs as Investor Protectors

As the law provides investors with insufficient relief, defrauded investors have few means to protect themselves. For example, a 2020 survey demonstrates that only 0.52% of surveyed investors successfully enforced their rights after they suffered losses.[220] China relies on NPOs with a certain level of government connection as intermediaries to demand changes over investor-protection issues and to educate investors about defending their own interests. For example, the China Securities Investor Protection Fund Corporation Limited ("SIPF") was established by the State Council in 2006 to manage an investor protection fund, which provides compensation to investors who suffered losses due to liquidation of securities firms.[221] To further enhance the protection of securities investors, the CSISC, a registered company under the direct supervision of the CSRC, was thus established in 2014.[222] Its purpose,

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(投资者保护公益组织与股东诉讼在中国的实践—基于中证投服证券支持诉讼的多案例研究) [*Nonprofit Organization for Investor Protection and Shareholder Litigation in China: A Multi-Case Study of Securities Litigation Supported by China Securities Investor Services Center*], GUANLI SHIJIE (管理世界) [MGMT. WORLD], no. 1, 2020, at 69, 85–86.

220. Chen Jian (陈剑), *Diaocha Xianshi Geren Touzi Zhe Weiquan Zuida Nandian Shi Queshao Weiquan Qudao* (调查显示个人投资者维权最大难点是缺少渠道和维权知识) [*The Biggest Difficulty for Individual Investors to Safeguard Their Rights Is the Lack of Channels and Knowledge of Safeguarding Their Rights*], XINHUANET (Apr. 28, 2020), http://www.xinhuanet.com/fortune/2020-04/28/c_1125916132.htm [https://perma.cc/KNP5-54RP].

221. Touzi Zhe Baohu Jijin Guanli Banfa (证券投资者保护基金管理办法) [Measures for the Management of Securities Investor Protection Fund] (promulgated by the CSRC, Ministry of Fin. and People's Bank of China, Apr. 19, 2016, effective June 1, 2016), arts. 7 & 19, http://www.sipf.com.cn/tbfg/2020/03/12872.shtml [https://perma.cc/LH9N-72VE] (limiting use of the investor protection fund to solely compensating the securities companies' debtors).

222. It should be noted that, at least as a matter of law, the CSRC supervises—but does not directly control—the CSISC because the CSISC is incorporated in the form of a company and is not an administrative organ subordinated to the CSRC. *See Zhongguo Zhengjian Hui Yanjiu Bushu Xuexi Guanche Guowu Yuan Guanyu Jinyi Bu Cujin Ziben Shichang Jiankang Fazhan de Ruogan Yijian* (中国证监会研究部署学习贯彻《国务院关于进一步促进资本市场健康发展的若干意见》的相关工作) [*China Securities Regulatory Commission Study and the Several Opinions of the State Council on Further Promoting the Healthy Development of Capital Market*], CSRC (May 29, 2014), http://www.csrc.gov.cn/pub/newsite/zjhxwfb/xwdd/201405/t20140529_255106.html [https://perma.cc/J8LS-8PBC].

according to the State Council, is to provide relief for investors as an independent NPO.[223] The CSISC holds 100 shares (the minimum trading unit) in every listed company, making it a special "institutional investor" that uniquely does not trade shares or intervene in the business operations of companies.[224] Instead, the CSISC monitors companies' overall governance as a shareholder and exercises its shareholder's rights to demand changes over investor-protection issues.[225] It also amplifies the voices of other investors seeking relief. To this end, the CSISC has multiple identities: a mediator, a shareholder activist, an investor-education institution, and, as of 2020, a designated representative in securities class action.[226] Since 2016, the CSISC has supported investors in bringing securities litigation by appointing their in-house lawyers and/or outsourcing lawyers to represent these investors in court.[227] The participating investors do not need to pay lawyers' fees; they only share court fees.[228] From its creation in 2014 through September 2021, the CSISC filed forty-five cases and recovered 9.24 million USD (59.89 million RMB) for defrauded investors.[229]

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223. *See* Guowu Yuan Bangong Ting Guanyu Jinyi Bu Jiaqiang Ziben Shichang Zhongxiao Touzi Zhe Hefa Quanyi Baohu Gongzuo de Yijian (国务院办公厅关于进一步加强资本市场中小投资者合法权益保护工作的意见) [Opinions of the General Office of the State Council on Further Strengthening the Protection of the Legitimate Rights of Small Investors in the Capital Market] (promulgated by the Gen. Off. St. Council, Dec. 27, 2013), pt. 9, http://www.gov.cn/zwgk/2013-12/27/content_2555712 htm [https://perma.cc/R438-3SXQ].

224. *See* Zhongzheng Zhongxiao Touzi Zhe Fuwu Zhongxin Chigu Xingquan Gongzuo Guize (Shixing) (中证中小投资者服务中心持股行权工作规则(试行)) [Rules for Stock Holding and Exercise of Power of CSISC (For Trial Implementation)] (promulgated by the CSISC, May 15, 2019), arts. 9–10, http://www.isc.com.cn/html/xqgz/20190515/822 html [https://perma.cc/9ZXN-KYEL].

225. *Id*. art. 4.

226. A general introduction to the CSISC's duties is available on its website. *See About Us*, CSISC (2020), http://www.isc.com.cn/html/gywm [https://perma.cc/E6NK-22WV].

227. The CSISC's right to support investors in lawsuits is stipulated in Article 15 of the Civil Procedure Law and is reconfirmed by the new securities law in Article 94. MINSU FA 2017, *supra* note 207, art. 15; ZHENGQUAN FA, *supra* note 17, art. 94.

228. Zhongzheng Zhongxiao Touzi Zhe Fuwu Zhongxin Zhengquan Zhichi Susong Yewu Guize (中证中小投资者服务中心证券支持诉讼业务规则) [Rules for Support Litigation of CSISC] (promulgated by the CSISC, Aug. 7, 2020), art. 5, https://www.investor.org.cn/rights_interests_protection/rights_protection_service/methods_channels_2597/202008/P020200814500197350534.pdf [https://perma.cc/5GAT-JP2E] [hereinafter CSISC Working Rules].

229. *Weiquan Fuwu* (维权服务) [*Investor Protection Service*], CSISC (2021), http://www.isc.com.cn/html/wqfw/ [https://perma.cc/JQK7-YJH5].

### *B. The 2020 Securities Law Amendment*

To enhance investor protection and the enforcement of the securities law, the 2020 Securities Law Amendment created a new chapter specifically for investor protection.[230] The most important breakthrough was the creation of securities class actions—that is, the introduction of the opt-out class action scheme. Under Article 95 of the Securities Law, there are two types of securities representative actions: (1) "general representative actions," an *opt-in* collective-litigation scheme initiated by general investors, and (2) "special representative actions," an *opt-out*, U.S.-style class action represented only by the CSISC.[231] The prerequisite for the CSISC to represent investors in an opt-out class action is authorization by more than fifty investors in matters that significantly involve the public interest.[232]

The 2020 Securities Law Amendment sketches out the general principles of the new securities class action regime, which are too bare-bones to implement in practice. In China, it is largely the SPC's responsibility to decide whether a specific law actually takes effect by issuing judicial interpretations or litigation rules.[233] Importantly, the SPC has spoken on this subject. On July 31, 2020, the SPC issued the "Provisions of the Supreme People's Court on Several Issues Concerning Securities Dispute Representative Actions" ("2020 SPC Opinion"), which detailed the operative rules and cleared the path for the Chinese version of securities class actions.[234] On the same day, the CSRC and CSISC issued their own rules governing the principles and procedure of opt-out class action.[235] On January 21, 2022, the SPC

230. ZHENGQUAN FA, *supra* note 17, ch. 6.

231. *Id.* art. 95.

232. *Id*.

233. According to the organic law of the court, the SPC may interpret specific issues on the application of law in adjudication. *See* Zhonghua Renmin Gonghe Guo Renmin Fayuan Zuzhi Fa (中华人民共和国人民法院组织法) [Organic Law of the People's Courts of the PRC] (promulgated by the Standing Comm. Nat'l People's Cong., Oct. 26, 2018, effective Jan. 1, 2019), art. 18, http://www npc.gov.cn/zgrdw/npc/xinwen/2018-10/26/content_2064483 htm [https://perma.cc/CYV9-LYZS] [hereinafter *Organic Law*]. In practice, the SPC exercises residual legislative power by making rules that have the same effect as legislation. *See* Qi Ding (齐玎), *Zuigao Renmin Fayuan Sifa Jieshi Quan: Shifa Yihuo Zaofa* (最高人民法院司法解释权: 释法抑或造法) [*The Legal Interpretation Right of the Superme People's Court: Interpreting the Law or Making the Law*], 27 XIAMEN DAXUE FAXUE PINGLUN [XIAMEN UNI. L. REV.] 66, 66 (2016).

234. *2020 SPC Opinion*, *supra* note 21.

235. *Guanyu Zuohao Touzizhe Baohu Jigou Canjia Zhengquan Jiufen Tebie Daibiaoren Susong Xiangguan Gongzuo de Tongzhi* (关于做好投资者保护机构参加证券纠纷特别代表人诉讼相关工作的通知) [*Notice for*

issued another judicial interpretation which repealed the 2003 Notice and removed the criminal or administrative procedural prerequisite for individual lawsuits.[236] These actions laid out a comprehensive view of China's securities class actions.

One distinct feature of China's securities class actions is that the court serves as a gatekeeper in initiating litigation. For general representative actions, if the number of plaintiffs is uncertain when the representatives file the suit (which is typical for securities law cases), only the court can make a public notice and solicit potential investors to register as plaintiffs.[237] The filing of representative actions is not complete until after the registration process.[238] In other words, the court has the power to decide whether a potential case can be filed. This court's discretion also applies to special representative actions—that is, NPO-led opt-out class actions.[239] The only way for the CSISC to initiate a special representative action is to transform an existing general representative action; it cannot "initiate" class actions, but rather takes over existing opt-in representative actions.[240] Hence, the court also indirectly controls the initiation of special representative actions, so its attitude is decisive on the effectiveness of class action in promoting the private enforcement of securities law in China.[241]

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*Investor Protection Institution to Effectively Participate in Special Representative Actions over Securities Disputes*] (promulgated by CSRC, July 31, 2020), http://www.csrc.gov.cn/pub/newsite/zjhxwfb/xwdd/202007/t20200731_380952.html [https://perma.cc/4T57-FL9S] [hereinafter *CSRC Opinion*]; CSISC Working Rules, *supra* note 228.

236. Zuigao Renmin Fayuan Guanyu Shenli Zhengquan Shichang Xujia Chenshu Qinquan Minshi Peichang Anjian de Ruogan Guiding, Fashi [2022] 2 Hao (最高人民法院关于审理证券市场虚假陈述侵权民事赔偿案件的若干规定, 法释 [2022] 2号)[Provisions of the Supreme People's Court on Trying Cases of Civil Compensation Arising from False Statements in Securities Market, Judicial Interpretation No. 2 [2022]] (promulgated by the Judicial Comm. Sup. People's Ct., Dec. 30, 2021, effective Jan. 22, 2022), arts. 2, 35, https://www.court.gov.cn/zixun-xiangqing-343221 html [https://perma.cc/D9GV-BY23] [hereinafter The 2022 Notice].

237. *See* ZHENGQUAN FA, *supra* note 17, art. 95; *see also 2020 SPC Opinion*, *supra* note 21, art. 7.

238. *See 2020 SPC Opinion*, *supra* note 21, art. 5.

239. *See id.* art. 33.

240. *See id.* art. 32.

241. This is not only the case in China; empirical evidence from Italy also demonstrates that judges' roles are crucial in corporate and securities law enforcement, which has shaped the image of investor protection. *See* Luca Enriques, *Off the Books, But on the Record: Evidence from Italy on the Relevance of Judges to the Quality of Corporate Law*, *in* GLOBAL MARKETS, DOMESTIC INSTITUTIONS: CORPORATE LAW AND GOVERNANCE IN A NEW ERA OF CROSS-BORDER DEALS 257, 281–82 (Curtis Milhaupt ed., 2003).

### *C. Lawyer-Led Opt-In Representative Action*

As mentioned above, under the hybrid model, there are two types of securities collective litigation: (1) lawyer-led opt-in representative actions; and (2) NPO-led opt-out class actions. The former, also known as "*general* representative actions" in the 2020 SPC Opinion, refer to cases initiated by investors represented by self-appointed representatives.[242] Conversely, the latter, also known as "*special* representative actions," refer to cases chosen and represented by the CSISC.[243] The next two Sections dissect the key features of these two actions by comparing their major procedural rules alongside other models.

#### 1. Procedural Prerequisites

The newly-issued 2022 Notice throws off the shackles that used to bind investors under the 2003 Notice.[244] According to the 2022 Notice, defrauded investors are allowed to bring an individual lawsuit against misstatement if "relevant evidence" that proves investors' losses is presented.[245] This officially removes the administrative/criminal procedural prerequisites for civil securities lawsuits against misstatement.[246]

However, the SPC still set additional thresholds for aggrieved investors if they wish to sue in a class. Under the new regime, investors are permitted to sue on a wider range of grounds, including misstatement, insider dealing, and market manipulation.[247] In addition to the prerequisite of a prior administrative sanction or criminal judgment, the court will also accept a case if the plaintiff can provide other preliminary evidence, including the defendant's confession and self-disciplinary regulatory measures or disciplinary actions imposed by a stock exchange.[248] Although the new regime relaxes the

242. *2020 SPC Opinion*, *supra* note 21, art. 1.

243. *Id.*

244. *The 2003 Notice*, *supra* note 213, art. 6; *The 2022 Notice*, *supra* note 236, arts. 2, 35.

245. *The 2022 Notice*, *supra* note 236, art. 2.

246. *Id.* art. 35.

247. *2020 SPC Opinion*, *supra* note 21, art. 1.

248. If these prerequisites are not met, article 5 of the SPC Opinion mandates that courts not try the case in a representative litigation but instead break the case into parallel individual lawsuits. *Id.* art. 5.

procedural prerequisites, the new requirements still piggyback on public or quasi-public enforcement.[249]

### 2. Opt-In Rule

Under the current regime, the court must hear a case in the form of a general representative action with the opt-in rule if: (1) the prerequisites are satisfied; (2) more than ten investors present the court with common questions; and (3) two to five representatives are proposed.[250] Like U.S.-style class actions, the court decides whether certain investors are in a class.[251] Once the identification of the class has been determined, the court publishes a notice for thirty days, inviting qualifying investors to register with the court to become plaintiffs.[252] In principle, investors falling within the description of the class must register with the court within this time period, but they can also choose to opt-in before the trial at the court of the first instance.[253] To consolidate parallel lawsuits, investors in parallel proceedings are allowed to drop their cases and join the representative action.[254] In that case, the court fees in the parallel lawsuits are refunded.[255]

Unlike other jurisdictions, opt-in representative actions in China have an expanded binding effect.[256] The 2020 SPC Opinion stipulated that later courts must apply the judgment of an opt-in representative action, without holding a court hearing, if the future case has the same set of facts and applicable laws and is brought by investors who also fall within the description of the class.[257] The result is that, unless the opt-out investors never bring a lawsuit, the judgment of the opt-in representative action will apply to all investors within the class in one way or another.

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249. *See* discussion *infra* Section III.B.

250. *Id.*

251. *Id.* art. 6.

252. The notice states the case facts, the claims of the plaintiffs, basic information about the defendant, a description of the class, the period in which investors can register with the court, representatives' basic information, documents provided by representatives to the courts, and a statement notifying investors that representatives shall have special authority in the course of litigation. *See id.* art. 7.

253. *Id.* art. 8.

254. *Id.* art. 10.

255. *Id.*

256. MINSU FA 2017, *supra* note 207, art. 54.

257. ZHENGQUAN FA, *supra* note 17, art. 95; *2020 SPC Opinion*, *supra* note 21, art. 29.

### 3. Fee-Arrangement Rule

Litigation costs have always been the main concern for investors interested in bringing a collective action.[258] Like the United States, China has an attorney-friendly fee-arrangement rule. Under Chinese law, contingent fees, also known as "risk agency fees" (风险代理收费), are available to litigants with an upper limit of no more than thirty percent of the recovery.[259] Of course, China has no shortage of entrepreneurial lawyers.[260] Even before introducing the opt-out regime, entrepreneurial lawyers in China actively sought clients after misrepresentations became known. What drives investors out of court, then, seems to be court fees.[261]

Court fees mainly refer to filing fees and fees for injunctive relief. Since there is a mandatory cap on fees for injunctive relief at 732 USD (5,000 RMB), the fees associated with requesting an injunction are not the major concern.[262] What might be at stake is the requirement to advance filing fees. Before a court hears a case, filing fees, calculated on a staggered basis, must be paid in advance by the plaintiff.[263] For example, for a claim of 1.5 million USD (around 10 million RMB), the plaintiff must pay 119,700 USD (809,000 RMB) in filing fees.[264] Even though this amount is reasonable, its scale may dissuade plaintiffs from making large claims.[265]

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258. *See, e.g.*, Wallace Wen-Yeu Wang & Jian-Lin Chen, *Reforming China's Securities Civil Actions: Lessons from PSLRA Reform in the U.S. and Government-Sanctioned Non-Profit Enforcement in Taiwan*, 21 COLUM. J. ASIAN L. 115, 130–31 (2008).

259. Lüshi Shiwusuo Shoufei Chengxu Guize (律师事务所收费程序规则) [Procedure Rules on the Charging of Law Firms] (promulgated by Ministry of Justice on Mar. 16, 2004, effective May 1, 2004), art. 4, http://www.gov.cn/gongbao/content/2005/content_63288 htm [https://perma.cc/576U-D8UF] (China). Lüshi Fuwu Shoufei Guanli Banfa (律师服务收费管理办法) [Measures on Lawyers Service Fee Management], art. 11, http://www.gov.cn/zwgk/2006-04/19/content_257940.htm [https://perma.cc/VAN8-LRMR] (China).

260. *See* Huang, *supra* note 24, at 768.

261. *See* Wang & Chen, *supra* note 258, at 130–31.

262. *See Susong Feiyong Jiaona Banfa* (诉讼费用交纳办法) [*Measures of Charging Litigation Fees*] (promulgated by the St. Council on Dec. 29, 2006, effective Apr. 1, 2007), art. 14(2) http://www.gov.cn/zwgk/2006-12/29/content_483407 htm [https://perma.cc/7XAA-3QJ8] (China) [hereinafter *Measures on Charging*].

263. *See id*. art. 13.

264. *See id*. The authors manually calculated this number based on the *Measures on Charging*, *supra* note 262.

265. *See* Lu, *supra* note 218, at 800–01. However, some commentators have argued that the filing fee is not a serious obstacle because it is not unreasonably high, and entrepreneurial lawyers are sometimes willing to advance the fees for plaintiffs. *See, e.g.*, Robin Hui Huang,

These filing fees might continue to be a concern for investors under the new regime because no specific rule has been made in this regard. However, since China adopted the loser-pays rule, some courts have exempted plaintiffs from the advancement obligation and allowed the filing fees to be paid by the losing party after the lawsuit.[266] With such strict prerequisites, the success rate of securities claims is likely to be high in China, and the adoption of the loser-pays rule implies that the filing fees, even if they must be prepaid, will most likely be returned to the plaintiffs.[267] Furthermore, the SPC adopted a more plaintiff-friendly loser-pays rule more recently—the 2020 SPC Opinion stipulates that, in addition to filing fees, investors can claim attorney fees and other administrative fees from the defendant at a rate determined by the court if they win.[268] Such a loser-pays rule does not work the other way around, meaning that defendants cannot claim attorney fees from the plaintiffs and are only limited to requesting filing fees.

### 4. Who Is in Control: Entrepreneurial Lawyers or Investors?

A central issue in the U.S. system is that class actions and settlements are essentially under the control of entrepreneurial lawyers, not defrauded investors, so there is often a misalignment of interests between lawyers and investors.[269] The Chinese legislators and SPC are well aware of this issue and have designed their rules to give investors a greater voice in important decisions regarding litigation and settlement. Even though the entire opt-in regime in

*China: Private Securities Litigation: Law and Practice*, *in* GLOBAL SECURITIES LITIGATION AND ENFORCEMENT 879, 902 (Pierre-Henri Conac & Martin Gelter eds., 2019).

266. *See Shenzhenshi Zhongji Renmin Fayuan Guanyu Yifa Huajie Qunti Xing Zhengquan Minshi Jiufen de Chengxu Zhiyin (Shixing)* (深圳市中级人民法院关于依法化解群体性证券侵权民事纠纷的程序指引(试行)) [*Shenzhen Intermediate People's Court's Procedural Guidance on Resolving Civil Disputes of Group Securities Infringement (For Trial Implementation)*] (promulgated by Shenzhen Intermediate Ct., Apr. 20, 2020, effective Apr. 20, 2020), art. 74, https://www.lawyerwh.com/7967 html [https://perma.cc/66LW-GK5W] (China); *Shanghai Jinrong Fayuan Guanyu Zhengquan Jiufen Daibiao Ren Susong de Guiding (Shixing)* (上海金融法院关于证券纠纷代表人诉讼机制的规定(试行)) [*Provisions of Shanghai Financial Court on the Litigation Mechanism of Representative Actions in Securities Disputes (For Trial Implementation*] (promulgated by Shanghai Financial Ct., Mar. 24, 2020, effective Mar. 24, 2020), art. 19, http://www hshfy.sh.cn/shfy/gweb2017/xxnr.jsp?pa=aaWQ9MjAxNjI1NTEmeGg9MSZsbWRtPWxtMTcxz [https://perma.cc/P4ZD-4RPP] (China).

267. *See* Huang, *supra* note 265, at 902.

268. *2020 SPC Opinion*, *supra* note 21, art. 25.

269. *See* discussion *supra* Section I.A.

China still relies on the profit motives of entrepreneurial lawyers to trigger the judicial process, the enhanced participation of investors greatly constrains lawyers' power over litigation in the new Chinese regime.

Under the new system, a plaintiff can only be appointed as a representative if they have a substantial financial stake in the claim, and their attorney has professional experience and the ability to execute litigation.[270] The court can also appoint the CSISC as a representative in a general representative action, where the CSISC acts as the plaintiff or is authorized by the investors to carry out litigation on their behalf.[271] In cases where the CSISC is not involved, the plaintiffs with the largest stakes are highly likely to be appointed as the representatives. In the United States, institutional investors are normally appointed as lead plaintiffs and are expected to counterbalance the plaintiffs' lawyers in litigation and settlement.[272] In China, institutional investors with deeper pockets and professional skills seldom engage in litigation.[273] To fulfill the professional experience and litigation capability requirements, most retail investors have no choice but to rely on professional lawyers.

China has a potentially large market for entrepreneurial lawyers. As contingent fees are available, entrepreneurial lawyers, who call themselves "securities rights-defense lawyers" (证券维权律师), actively screen market information related to securities fraud to seek potential cases and proactively solicit potential investors to be plaintiffs.[274] Under the current regime, those who obtain the most attorney contracts from investors, or who represent the investors with the largest stakes, enjoy the right to appoint

270. Representatives should meet the following requirements: (1) they are willing to take on responsibility; (2) their claims constitute a considerable proportion of the total claims; (3) they (or their attorney) have sufficient litigation capability and professional skill; and (4) they can protect all plaintiffs' interests with reasonable care and skill. *2020 SPC Opinion*, *supra* note 21, art. 12. The procedure for appointing representatives is as follows: representatives whose names are on the original complaint will be elected as representatives of the case if investors raise no objections; if any obligation is raised, two to five representatives shall be elected on a one person, one vote basis, and one must receive more than fifty-percent of the total votes to be elected as the representative. *Id.* arts. 13 & 14. If there is a deadlock among plaintiffs, the court shall have the discretion to appoint representatives from among the litigants. *Id.* art. 15. Investors who vote against elected representatives to represent them will have an option to opt out from the case and bring an individual lawsuit. *Id.* art. 16.

271. *Id.* art. 12.

272. *See* discussion *supra* Section I.A (examining the PSLRA reform).

273. One study found that of around 12,000 plaintiffs in private enforcement from 2002–2011, only eight were institutional investors. *See* Huang, *supra* note 24, at 787.

274. *See id.* at 768.

representatives and thus control the litigation.[275] For-profit lawyers are thus expected to actively monitor the market and organize investors to bring actions against wrongdoers in China. Investors also have considerable economic incentives to join cases organized by lawyers, as the lawyers will likely pay upfront filing fees and other expenses.[276] Even if investors must pay fees at the outset, the new fee-shifting rule allows them to demand lawyers' fees from the losing party after the litigation has concluded. In fact, just a few days after the enactment of the new law, multiple law firms collectively initiated the first opt-in representative action in the *Hangzhou Wuyang* case on the basis of misrepresentation in the prospectus against multiple parties, including the Wuyang Group, its controller, auditors, law firms, and securities firms.[277] In that case, four representatives sued on behalf of 496 investors who collectively claimed 123 million USD (810 million RMB) in losses.[278]

Since the 2003 SPC Notice, the Chinese civil securities litigation market has enjoyed a short history of two decades.[279] Only a few law firms have entered this market. For instance, between 2014 and 2017, only thirty-eight law firms represented investors in court, and the three biggest law firms in Shanghai collectively represented two-thirds of them.[280] When the market is small and concentrated in the hands of a few law firms, concerns about abusive practices arise due to the lack of competition between private attorneys. This market concentration was partially the result of limited demand due to strict procedural prerequisites, an inefficient judicial system, and a lack of collective redress procedures.[281] Although lawyers can file opt-in collective litigation under the new regime, and the SPC has relaxed the prerequisite to include self-disciplinary sanctions from stock

275. *See supra* note 270 and accompanying text.

276. *See supra* note 259 and accompanying text.

277. *See* Zhu Linna (朱琳娜), *Quanguo Shouli Zhengquan Jiufen Daibiaoren Susong An Kaiting* (全国首例证券纠纷代表人诉讼案开庭) [*China's First Securities Representative Litigation Was Heard by the Court*], CNSTOCK (Sept. 5, 2020), https://news.cnstock.com/news,qy-202009-4588796 htm [https://perma.cc/9MHE-T7BH].

278. *Id.*

279. *See* discussion *supra* Section II.A.

280. Xu, *supra* note 218, at 80.

281. *See* Xu Wenming (徐文鸣), *Zhengquan Minshi Susong Zhidu Shishi Xiaoguo de Shizheng Yanjiu Yi Xujia Chenshu Anjian Weili* (证券民事诉讼制度实施效果的实证研究——以虚假陈述案件为例) [*An Empirical Research on the Implementation of Securities Civil Lawsuits: Taking Misrepresentation as an Example*], 2017 ZHENQUAN SHICHANG DAOBAO (证券市场导报) [SEC. MKT. HERALD], 29, 31 (2017).

exchanges, prerequisites may still hinder the efficiency of entrepreneurial lawyers.[282]

In addition to potentially enhancing competition among private attorneys, the new law also tries to constrain lawyers' power by augmenting plaintiffs' participation and control over important decisions. Under the current regime, investors must give representatives special authority that allows them to revise claims, enter into settlements, apply for appeals, apply for enforcement, and hire attorneys.[283] However, any settlement entered into with defendants by their representatives needs the court's examination and plaintiffs' approval.[284] Plaintiffs who object to a settlement have the right to demand a hearing and request amendments to the settlement.[285] After the hearing, the court must decide whether to prepare a conciliation statement based on the settlement agreement, considering the plaintiffs' opinions and the settlement's legitimacy, feasibility, and appropriateness.[286] Those who still disagree with the settlement after the hearing and court's examination can opt-out of the settlement and continue with the trial.[287]

Likewise, any material decisions made by the representatives, such as revising claims and dropping the case, need the court's approval based on all plaintiffs' opinions.[288] Investor plaintiffs can also appeal individually if they are dissatisfied with a judgment.[289] In the past, lawyers preferred to overestimate investors' damages to attract more investors to join their cases, since filing fees could be recouped from the losing party after the trial.[290] With a court's close supervision and plaintiff's participation, the Chinese opt-in representative action regime is expected to constrain this potential

282. *See* discussion *infra* Section III.B.

283. *2020 SPC Opinion*, *supra* note 21, art. 7.

284. The court will first examine the legitimacy, morality, and fairness of the settlement. If the plaintiff's case passes the court's examination, then the court will issue a notice for investors to approve the settlement. *Id.* art. 19.

285. *Id.* art. 20.

286. *Id.* art. 21.

287. *Id.*

288. *Id.* art. 22.

289. *2020 SPC Opinion*, *supra* note 21, arts. 27–28.

290. The information asymmetry between investors and professional securities lawyers leaves investors no choice but to rely on lawyers' judgment. Lawyers will receive extra benefits if claims are accepted by the court, but investors will be burdened with the high court's fee if the lawsuit loses. *See* Xu, *supra* note 218, at 82.

expropriation by lawyers. Investors can still control their own destiny in opt-in representative action with the help of the court.

### *D. NPO-Led Opt-Out Class Action*

The introduction of NPO-led opt-out class actions—also known as special representative actions[291]—is a breakthrough in the development of global securities class action regimes.[292] It is a mixed model of the U.S.-style opt-out regime[293] and the European-style NPO-led regime,[294] an innovative hybrid model that attests to the regulatory innovation of the Chinese regime. This Section introduces its key features by comparing it with the general representative actions introduced in the previous Section and referring to the practices of other jurisdictions.

#### 1. Taking Over Existing Opt-In Representative Actions

The opt-out rule under the new Chinese securities class action regime is different from the U.S. rule because it only applies if the CSISC joins the general representative action.[295] Once it joins, the litigation transforms into an opt-out special representative action, which means the result will be binding on all class members, unless they opt-out.[296] In other words, the law grants the CSISC the right to pick and choose from existing general representative actions, meaning that the application of the opt-out rule resides in the hands of the CSISC.

The CSISC has the discretion to join an existing general representative action if more than fifty investors authorize it to sue on their behalf before the close of the thirty-day registration period.[297] According to the CSRC Notice and the CSISC's internal rules, the CSISC may choose to join a representative action if the following prerequisites are satisfied: (1) wrongdoers have received an

291. *2020 SPC Opinion*, *supra* note 21, art. 1.

292. It also bears mentioning that the rules discussed above governing general representative actions also apply to special representative actions unless otherwise specified by law. *See id.* art. 41.

293. *See* discussion *supra* Section I.A.

294. *See* discussion *supra* Section I.B.

295. *2020 SPC Opinion*, *supra* note 21, art. 32.

296. *Id.* art. 34.

297. *Id.* art. 32.

administrative penalty or criminal liability; (2) the case is typical and important, with severe negative social impact, and it serves as a model for other cases; (3) the defendant is solvent; and (4) other conditions apply that the CSISC deems fit.[298] The prerequisites set by the CSRC and CSISC are narrower than those in the Securities Law and the SPC Notice. The CSISC follows the old prerequisites of requiring a prior administrative sanction or criminal judgment and adds the two additional requirements of cases being typical and defendants being solvent.[299] Apparently, it was not the court that did not want to take the cases, as was conventionally believed, but the administrative agency itself that did not want the CSISC to broaden the realm of enforcement.[300]

As the CSISC is taking over the cream-of-the-crop from entrepreneurial lawyers, lawyers have no incentive to bring big cases because of the risk that the CSISC will take them away, eliminating any profit. Imagine a lawyer expelling time and effort to find a case, organize investors, and bring the case to court, only to have the CSISC whisk it away. In that situation, entrepreneurial lawyers may only initiate smaller cases that do not meet the CSISC prerequisites. In the event that no entrepreneurial lawyer brings a case that is also targeted by the CSISC, the organization will probably independently seek cases that meet its prerequisites and ask ten investors to initiate the opt-in class action to meet the procedural requirement.

### 2. Opt-Out Rule

Once the CSISC decides to join a case, it becomes the sole representative of all the plaintiffs.[301] Plaintiffs in the already-initiated opt-in representative action are given the option to stay with their case (opt-out) or to join the CSISC case.[302] The court again issues a notice and provides the CSISC's information, special authority, and most importantly, an option to opt-out of the litigation.[303] Those unwilling to join must notify the court within fifteen days and are not restricted from bringing an individual lawsuit; otherwise, those who fall within

298. CSISC Working Rules, *supra* note 228, art. 16; *CSRC Opinion*, *supra* note 235, art. 4.

299. *Id.*

300. *CSRC Opinion*, *supra* note 235, art. 4.

301. *2020 SPC Opinion*, *supra* note 21, art. 32.

302. *Id.*

303. *Id.* art. 33.

the description of the class become plaintiffs in the CSISC case.[304] Once the CSISC class action has been certified, the litigation continues, even if the number of registered plaintiffs falls below fifty individuals during the course of litigation.[305] As in the opt-in representative action, investors can opt out of the settlement or appeal in the special representative action.[306] However, few investors are likely to opt-out, as the judgment or settlement will be binding on them anyway, as discussed in the previous Section. In addition, retail investors in China have a reputation for being passive over corporate matters.[307] If they are passive in demanding governance changes, they will likely also be passive in exercising their rights to opt-out.

### 3. Preferential Fee Arrangement

In an NPO-led model, granting preferential fee arrangements to organizations is important because NPOs are not driven by financial gains and thus require special legal treatment to alleviate the financial burden of bringing a securities class action. Like the fee-arrangement rule in the Taiwanese model,[308] the 2020 SPC Opinion granted preferential fee treatment to the CSISC in opt-out class actions.[309] For example, investors need not prepay filing fees and can apply for deductions or exemptions, even if they lose the case.[310] If they win, according to the modified loser-pays rule, they can also recoup attorney fees, filing fees, and other necessary fees from the defendants, as in the general representative action.[311] The court may also exempt the CSISC from providing a guaranty to the court when applying for property-preservation measures.[312] To alleviate the financial burden on investors, the CSISC does not charge attorney fees to investors—

304. *Id.* arts. 34–35.

305. *Id.* art. 36.

306. CSISC Working Rules, *supra* note 235, arts. 25, 27.

307. *See generally, e.g.*, Kong Dongmin (孔东民) et al., *Lengmo Shi Lixing de Ma? Zhongxiao Gudong Canyu Gongsi Zhili Yu Touzi Zhe Bao Hu* (冷漠是理性的吗? 中小股东参与公司治理与投资者保护) [*Is Silence Rational? Minority Shareholder Participation, Governance, and Investor Protection*], 11 JINGJI XUE (JIKAN) (经济学季刊) [CHINA ECON. Q.] 1 (2012).

308. *See* discussion *supra* Section I.B.2.

309. Lin, *supra* note 22, at 170–75.

310. *2020 SPC Opinion*, *supra* note 21, art. 39.

311. *Id.* art. 25.

312. *Id.* art. 40.

just necessary fees, such as filing fees.[313] In this case, investors are normally inclined to opt-in.

### 4. Centralized Jurisdiction

To ensure consistent court judgments, opt-out class actions are governed by the courts where stock exchanges have their domiciles.[314] That is to say, once the CSISC joins a case, the court shall hand it over to one of three designated courts: (1) the Shanghai Financial Court for companies listed on the Shanghai Stock Exchange; (2) the Shenzhen Intermediate People's Court's Financial Tribunal for companies listed on the Shenzhen Stock Exchange; or (3) the Beijing Financial Court for companies listed on the National Equities Exchange and Quotations (the so-called "new three boards": a stock market for smaller companies) and the newly established Beijing Stock Exchange. All three courts are established to handle financial-related cases and have a team of expert judges that are well-experienced in securities lawsuits.[315]

Previously, all cases were governed by courts where the defendant company had its domicile, which encouraged local protectionism.[316] In China, courts are often under local governmental pressure to consider economic indicators in cases involving listed companies.[317] Despite opt-in cases still following the old rules, centralizing the jurisdiction of opt-out class actions in the hands of courts with more specialized expertise and less political influence from

313. CSISC Working Rules, *supra* note 228, art. 5, 12.

314. *2020 SPC Opinion*, *supra* note 21, art. 2.

315. Quanguo Renmin Daibiao Dahui Changwu Weiyuan Hui Guanyu Sheli Shanghai Jinrong Fayuan de Jueding (全国人民代表大会常务委员会关于设立上海金融法院的决定), [Decision of the Standing Committee of the National People's Congress on Forming the Shanghai Financial Court] (promulgated by Standing Comm. Nat'l People's Cong., Apr. 27, 2021) (China), http://www npc.gov.cn/npc/c30834/201804/f2365478a9944d588b49a35ead41e207.shtml [https://perma.cc/2LTD-A3YW]; Quanguo Renmin Daibiao Dahui Changwu Weiyuan Hui Guanyu Sheli Beijing Jinrong Fayuan de Jueding (全国人民代表大会常务委员会关于设立北京金融法院的决定) [Decision of the Standing Committee of the National People's Congress to Form the Beijing Financial Court] (promulgated by the Standing Comm. Nat'l People's Cong., Jan. 22, 2021) STANDING COMM. NAT'L PEOPLE'S CONG. GAZ. 349, Feb. 18, 2021 (China), http://www.npc.gov.cn/npc/c30834/202101/51ce8706d4cd435783f4eb8b62ed6702.shtml [https://perma.cc/2UPQ-SZ4X].

316. *The 2003 Notice*, *supra* note 213, art. 9; *2020 SPC Opinion*, *supra* note 21, art. 2.

317. Huang, *supra* note 24, at 795.

domiciliary governments can eliminate the concern over local protectionism, an issue that has long plagued the Chinese judiciary.[318]

## III. ASSESSING THE NEW HYBRID MODEL

The hybrid model in China marks a new milestone in the global development of securities class action regimes. It is an innovative regulatory attempt to converge extant but dispersed developments in various jurisdictions. However, legal reforms are usually built upon existing legal infrastructures and shaped by local political and social conditions, introducing a path dependency that determines the outcome of legal reforms.[319] This Part analyzes China's new regime against the backdrop of the existing political, social, and legal environments in China and discusses how these local conditions influence its expected results, which eventually bring China to a different direction in global collective redress regimes.

### *A. Social Stability or Investor Protection?*

In the past few decades, China has transplanted various legal rules and governance mechanisms from the United States to modernize its legal environment for investor protection.[320] However,

318. Meanwhile, the requirement on centralized jurisdiction may also aim to maintain social stability. *See* discussion *infra* Section III.A.

319. *See supra* note 36 and accompanying text.

320. One of the most important reasons that jurisdictions converge with U.S. rules is that the United States has long been one of the most powerful economies with a highly-developed capital market. Jurisdictions have transplanted U.S. rules with the hope that, by adhering to U.S. standards, they can also develop a strong capital market. As Edward Rock noted: "The intuition that one can fruitfully transplant legal rules or institutions from one system to another is as old as the law itself. The temptation is to try to get something for nothing, or at least at a discount." Edward B. Rock, *America's Shifting Fascination with Comparative Corporate Governance*, 74 WASH. U. L.Q. 367, 368 (1996). Legal rules that have been transplanted from the United States to China include independent directors, audit committees, dual-class shares, and takeover defenses. *See generally, e.g.*, Wang Qian (王倩), *Lun Gudong Yizhi Hua Beijing Xia Gudong Quanli Chayi Hua Peizhi Jiqi Liyi Pingheng—Jianping Kechuang Ban "Biaojue Quan Chayi Anpai" Zhangjie* (论股东异质化背景下股东权利差异化配置及其利益平衡—兼评科创板"表决权差异安排"章节) [*The Differentiation of Shareholders' Rights and the Balance of Their Interests under the Background of Shareholder Heterogeneity: Comments on the "Differential Voting Rights" Rule in the SSE Star Market*], 2019 ZHENGQUAN FAYUAN (证券法苑) [SEC. L. REV.] 143 (2019), https://xueshu.baidu.com/usercenter/paper/show?paperid=19180ry0ye3e0a707d030g80bf245075 [https://perma.cc/6HQD-E5PU]; JUAN CHEN, REGULATING THE TAKEOVER OF CHINESE LISTED COMPANIES: DIVERGENCE FROM THE WEST 137–73 (2014); Ling Zhou, *The Independent Director System and Its Legal Transplant*

convergence in formal rules does not necessarily lead to the same outcome due to divergence in local political, social, and legal conditions.[321] Unlike the United States, where the market is the driving force behind corporate law and governance, the formation of corporate legal rules in China is often embedded in and directed by the Party-State's policy and social goals.[322] Ultimately, the distinct policy of maintaining social stability and the political embeddedness of the judiciary in China are likely to suppress the number of securities class actions in China, even after the adoption of U.S.-style opt-out rules.

Indeed, China's judiciary has long been considered a subordinate constituent of the political institution.[323] The existing literature has demonstrated that laws are not the only rules that Chinese judges follow; they also consider political, social, administrative, and economic factors when making decisions.[324] The courts are deeply embedded in the overall political agenda set by the Party-State. In fact, the Chinese Communist Party (CCP) has long treated law as a tool to maintain (social) stability (维稳) and to exercise social control.[325] By extension, judges must follow the political goal of maintaining social

*into China*, 6 J. COMP. L. 262 (2011); Zhijun Lin et al., *The Roles, Responsibilities and Characteristics of Audit Committee in China*, 21 ACCOUNTING, AUDITING & ACCOUNTABILITY J. 721, 721 (2008).

321. *See* Rock, *supra* note 320, at 390–91 (noting that various local conditions "push[] comparative law in a fundamentally different direction" and therefore "one cannot take advantage of its benefits without the appropriate institutional infrastructure"). Empirical studies on legal transplantation in transitional economies suggest that "history is an important determinant for the effectiveness of legal institutions." Katharina Pistor et al., *Law and Finance in Transition Economies*, 8 ECON. TRANSITION 325, 356 (2000); *see also* Jeffrey N. Gordon, *Convergence and Persistence in Corporate Law and Governance*, *in* OXFORD HANDBOOK OF CORPORATE LAW AND GOVERNANCE 28 (Jeffrey N. Gordon & Wolf-Georg Ringe eds., 2018); Gilson, *supra* note 41, at 330.

322. For example, the state may use its control over SOEs not for wealth-maximization but for other purposes, such as enhancing employment rates. *See* Donald C. Clarke, *Corporate Governance in China: An Overview*, 14 CHINA ECON. REV. 494, 495 (2003).

323. Under Article 129 of the Chinese Constitution and Article 42 the Organic Law of the People's Courts, the SPC is responsible to the National People's Congress and its Standing Committee, and the President of the SPC is selected by the National People's Congress. *See* XIANFA art. 129, § 1 (1982) (China); Organic Law, *supra* note 233, art. 42. Before 2015, the budgets of the courts were under the control of local governments. *See* Peter C. H. Chan, *An Uphill Battle: How China's Obsession with Social Stability Is Blocking Judicial Reform*, 100 JUDICATURE 14, 15–16 (2016); Feng Chen & Xin Xu, *Active Judiciary: Judicial Dismantling of Workers' Collective Action in China*, 67 CHINA J. 87, 88 (2012).

324. KWAI HANG NG & XIN HE, EMBEDDED COURTS: JUDICIAL DECISION-MAKING IN CHINA 20–28 (2017).

325. *Id*. at 20.

stability while adjudicating cases.[326] In mass tort cases, such political considerations have led to the suppression of mass dispute events and the avoidance of using litigation as a major dispute-resolution avenue. For example, empirical studies have confirmed that Chinese courts split collective labor dispute cases into individual ones to maintain social stability.[327]

In addition to adjudication, courts in China often act as quasi-legislators and, by issuing judicial interpretations, effectively "make the law" to meet the practical needs of adjudication.[328] The 2020 SPC Opinion is an example of judicial lawmaking in relation to securities class actions.[329] Determined to maintain social stability, Chinese courts were once reluctant to hear securities fraud cases, especially those with numerous plaintiffs.[330] The 2020 SPC Opinion reflects the same political influence and belief. While the new Securities Law did not establish any pre-conditions to bringing securities class actions, the 2020 SPC Opinion limited the scope of litigation by requiring additional procedural prerequisites of prior administrative sanction, criminal penalty, stock-exchange disciplinary actions, or a plaintiff's confession.[331] Such procedural prerequisites substantially limit the litigation rights of investors for the purposes of social control and stability. Likewise, putting opt-out securities class actions in the hands of a government-sanctioned NPO and centralizing the jurisdiction of opt-out cases in certain designated courts may stem from the same social stability consideration.

Furthermore, the SPC weighs another important policy when designing rules.[332] President Xi Jinping's "non-litigation-first" policy

326. *Id*.

327. Chen & Xu, *supra* note 323, at 90–92.

328. *See generally* Chao Xi, *Local Courts as Legislators? Judicial Lawmaking by Subnational Courts in China*, 34 STATUTE L. REV., 39 (2013).

329. *See generally 2020 SPC Opinion*, *supra* note 21.

330. As indirect proof, lawyers are encouraged to carefully handle cases with more than ten plaintiffs and to solve them peacefully, such as by resorting to mediation. *See Zhonghua Quanguo Lüshi Xiehui Guanyu Lüshi Banli Qunti Xing Anjian Zhidao Yijian* (中华全国律师协会关于律师办理群体性案件指导意见) [*Guiding Opinions of the All China Lawyers Association on Lawyers Handling Mass Cases*], ZHONGHUA QUANGUO LÜSHI XIEHUI WANGZHAN (中华全国律师协会网站) [ALL CHINA LAWYER ASSOCIATION SITE], (Mar. 20, 2006), http://www.acla.org.cn/article/page/detailById/18922 [https://perma.cc/V3GV-4N65].

331. *2020 SPC Opinion*, *supra* note 21, art. 5.

332. Recent scholarship has revealed a trend in Asian countries to adopt globally-recognized legal rules for local purposes. *See* Gen Goto et al., *Diversity of Shareholder Stewardship in Asia: Faux Convergence*, 53 VAND. J. TRANSNAT'L L. 829, 836 (2020) (noting that "[t]his trend suggests that corporate governance convergence at a superficial (i.e. formal)

encourages parties to settle their disputes through mediation rather than lawsuits.[333] Thus, within what is called a "diversified securities dispute resolution mechanism," litigation, mediation, and arbitration collectively provide relief for aggrieved investors.[334] While the SPC sets various prerequisites and conditions for investors to initiate representative litigation, the terms for investors to engage in mediation can be very favorable.[335] Parties can settle their disputes with a publicly-funded mediator in a timely, efficient manner and then submit the mediation agreement to a court for judicial confirmation.[336] For securities-fraud cases with large-scale claims, a model case-like device was also introduced under which the court may first decide a model case on common issues of law and fact before mediators apply the model decision to help parties find a solution.[337] While the SPC allows a securities class action to proceed, it also obliges the court to encourage the parties to undergo mediation in all court proceedings.[338] As a result, if applied successfully, ADR will do away with cases that used to be settled through litigation. Thus, it is possible that the number of securities fraud cases will fall, even with the new class action regime.[339]

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level is occurring, but that corporate governance remains considerably local, path dependent, and, ultimately, divergent in practice").

333. Liu Yuxiang (柳玉祥), *Jianchi Ba Feisu Jiufen Jiejue Jizhi Tingzai Qianmian* (坚持把非诉讼纠纷解决机制挺在前面) [*Insists on Putting Non-Litigation Dispute Resolution Mechanism in the First Place*], RENMING FAYUAN BAO (人民法院报) [CHINALAW] (Jan. 9, 2020), http://legal.people.com.cn/n1/2020/0109/c42510-31540968 html [https://perma.cc/4M66-4935]; *see also supra* note 30 and accompanying text.

334. Under the dispute-resolution mechanism, not only investors who suffered losses from securities fraud can engage in mediation, but those who have contract or tort disputes relating to capital markets can also apply for mediation. *See 2018 Diversified Resolution Notice*, *supra* note 174, art. 10.

335. For example, mediation will be free for investors. *See id.* art. 8.

336. *Id.* arts. 5, 11.

337. *Id.* art. 13. The SPC did not set prerequisites for public enforcement of the model judgment case, meaning that it also allows the case to fall within the scope of representative litigation. The purpose of adopting a model judgment, as suggested by scholars, is to reduce the court's workload by avoiding confrontational litigation. *See* Ye Lin (叶林) & Wang Xiangchun (王湘淳), *Woguo Zhengquan Shifan Panjue Jizhi de Shengcheng Lujing* (我国证券示范判决机制的生成路径) [*The Generating Path of China's Securities Model Judgment Mechanism*], 24 YANGZHOU DAXUE XUEBAO (SHEHUI KEXUE BAN) (扬州大学学报(人文科学版)) [J. YANGZHOU U. (HUMAN. & SOC. SCI)] 62, 67 (2020) [https://perma.cc/MCB7-H6BG]; *see also* discussion *supra* Section I.C.1 (analyzing similar features in the German example).

338. *2020 SPC Opinion*, *supra* note 21, art. 3.

339. Interestingly, the U.S. Supreme Court has also held that companies could waive class action liability with a valid arbitration clause. Am. Express Co. v. Italian Colors Rest., 133 S.

### *B. Procedural Prerequisites Hinder Growth*

One criticism of the 2003 SPC Notice is that it narrowed the scope of application by setting prerequisites of prior administrative or criminal sanctions and limiting the legal grounds for misrepresentation. The new regime seems to open the field on both ends.[340] The 2020 SPC Opinion expanded, rather than removed, the prerequisites to include defendants' confessions and disciplinary sanctions or self-regulatory management measures issued by stock exchanges, likewise extending the legal grounds to include insider dealing and stock manipulation.[341] However, the apparent expansion of application might not raise the amount of meritorious securities-related claims.

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Ct. 2304, 2304–05 (2013). Such a decision has not yet applied to securities class action, but commentators have predicted that the use of arbitration clauses may bring an end to U.S. class action. Brian T. Fitzpatrick, *The End of Class Actions?*, 57 ARIZ. L. REV. 161, 161 (2015).

340. The prerequisites for securities litigation have been controversial since the 2003 Notice came into force. And over the years, the judiciary was hesitant to remove them. In 2015, the SPC expressed its opinion on exempting the precondition for whether the court will hear a securities fraud case. *See Zuigao Renmin Fayuan Guanyu Dangqian Shangshi Caipan Zhong De Ruogan Juti Wenti* (最高人民法院关于当前商事审判工作中的若干具体问题) [*Some Specific Issues of the Supreme People's Court on Current Commercial Trial Work*] (promulgated by Sup. People's Ct., Dec. 24, 2015), https://pkulaw.com/chl/194dc8ae331d6b52bdfb html?keyword=最高人民法院关于当前商事审判工作中的若干具体问题 **[**https://perma.cc/3HL3-CT3R**].** However, in practice, local courts exhibit conflicting attitudes. For example, in 2017, the Zhejiang High Court signaled that the court cannot dismiss a case for the reason that prerequisites were not satisfied. *See* Jingsong Yu Tianjin Kuaijishi Shiwusuo, Zhejiang Shuijing Guangdian Keji Gufen Youxian Gongsi (松与天健会计师事务所、浙江水晶光电科技股份有限公司) [Song Jing v. Pan-China Certified Public Accts. & Zhejiang Crystal-Optech, Co., Ltd.], China Judgments Online, 2017 Zhe Minzhong 72 Hao (2017 浙民中 72 号) [2017 Zhejiang Second Instance Civil Ruling No. 72], (Zhejiang High People's Ct.).) While the Shanghai High Court agreed to hear a securities misrepresentation case, it later dismissed the case on the grounds that the prerequisite was not satisfied. *See* Dai Guoping Yu Ruiqi Konggu Gufen Youxian Gongsi, Wu Mingting Zhengquan Xujia Chenshu Zeren Jiufen Ershen Minshi Caiding Shu (酈国平与锐奇控股股份有限公司、吴明厅证券虚假陈述责任纠纷二审民事裁定书) [Dai Guoping v. Ruiqi Holdings Co., Ltd. and Wu Mingting Securities False Statement Liability Dispute, Second Instance Judgment], China Judgments Online, 2017 Hu Minzhong 390 Hao (2017 沪民终390号) [2017 Shanghai Second Instance Civil Ruling No. 390], (Shanghai High People's Ct., Jan. 31, 2018) . At the time when the SPC Opinion expanded the prerequisites for a group of investors to sue, it left investors who brought individual lawsuits in an uncertain position. It was only in 2022 that the SPC removed the procedural prerequisites for individual securities lawsuits. *See supra* note 236, art. 2.

341. 2020 SPC Opinion, *supra* note 21, art. 5.

### 1. Prerequisites for Entrepreneurial Lawyers

Under the new regime, lawyers' power to initiate a securities representative litigation is still, in a way, subordinate to public or quasi-public enforcement because stock exchanges in China are state-owned and under the direct administration of the CSRC.[342] Also, lawyers might be unable to act on disciplinary actions by stock exchanges due to the nature of such actions. From July 2017 to August 2020, the Shanghai Stock Exchange issued 1,056 disciplinary sanctions, while the Shenzhen Stock Exchange issued 2,000.[343] Most of these disciplinary actions involved minor violations in disclosure obligations, which might not result in damages to investors.[344] In these cases, the new regime does not substantially expand the grounds for securities class actions. With the loser-pays rule in effect, lawyers inevitably pursue cases with higher probabilities of winning, such as

342. *See supra* notes 195 and 197 and accompanying text.

343. This Article's authors manually gathered sanction recordings from two stock exchange websites. *See Shanghai Stock Exchange Sanction Records*, SHANGHAI STOCK EXCH., http://www.sse.com.cn/disclosure/credibility/supervision/measures/ [https://perma.cc/2NR4-BT98]; *Shenzhen Stock Exchange Records*, SHENZHEN STOCK EXCH., httphttp://www.szse.cn/disclosure/supervision/measure/measure/index html [https://perma.cc/T2Y2-RZQ9].

344. For example, on August 24, 2020, the Shenzhen Stock Exchange issued a regulatory letter to Zhejiang Hailide New Material Co., Ltd., on the ground that the company wrongfully disclosed material information on the Shenzhen Stock Exchange's online platform, rather than a designated disclosure platform. *See Guanyu Dui Zhejiang Haili de Xin Cailiao Gufen Youxian Gongsi de Jianguan Han* (关于对浙江海利得新材料股份有限公司的监管函) [*Regulatory Letter of Shenzhen Stock Exchange to Zhejiang Hailide New Material Co., Ltd.*], SHENZHEN STOCK EXCH., (Aug. 24, 2020) http://reportdocs.static.szse.cn/UpFiles/jgsy/gkxx_jgsy_00220657048.pdf [https://perma.cc/9B9U-EQN5]. In another example, on August 28, 2020, the Shenzhen Stock Exchange issued a regulatory letter to Beijing Etrol Technologies Co., Ltd., on the ground that the company failed to disclose a lawsuit against the company. *See Guanyu Dui Beijing Ankong Keji Gufen Youxian Gongsi de Jianguan Han* (关于对北京安控科技股份有限公司的监管函) [*Regulatory Letter of Shenzhen Stock Exchange to Beijing Etrol Technologies Co., Ltd.*], SHENZHEN STOCK EXCH., (Aug. 28, 2020), http://reportdocs.static.szse.cn/UpFiles/jgsy/gkxx_jgsy_30037034564.pdf [https://perma.cc/CRH3-YNFH]. Even in other cases of severe violations for which the Stock Exchange issues a public condemnation, the wrongdoing may not amount to misrepresentation. For example, Zhengzhou Sino-Crystal Diamond Co. and its management received a public condemnation from Shenzhen Stock Exchange on April 29, 2020, because the company did not disclose a loan to a non-connected company. *See Guanyu Dui Zhengzhou Huajing Jingang Shi Gufen Youxian Gongsi Ji Xiangguan Dangshi Ren Jiyu Jilu Chufen de Jueding* (关于对郑州华晶金刚石股份有限公司及相关当事人给予纪律处分的决定) [*Decision of Shenzhen Stock Exchange on Imposing Disciplinary Sanction to Zhengzhou Sino-Crystal Diamond Co. and Relevant Persons*], SHENZHEN STOCK EXCH. (Apr. 99, 2020),https://reportdocs.szse.cn/UpFiles/cfwj/2020-05-06_300064710.pdf?random=0.8566063614191086 [https://perma.cc/A6NC-EGT7].

those where criminal or administrative liabilities have already been imposed on defendants. Even if the filing fees are not usually a serious financial burden on plaintiffs, as suggested by some commentators, entrepreneurial lawyers will still naturally only pursue cases with higher probabilities of success.[345] However, according to the 2020 SPC Opinion, the large, high-profile cases are subject to the pick-and-choose discretion of the CSISC. Because the CSISC deprives entrepreneurial lawyers of the cream-of-the-crop under the new regime, entrepreneurial lawyers are likely to pursue only small and medium-sized cases that meet the previous prerequisite of administrative or criminal actions after careful cost-benefit analyses. Therefore, if insufficient new cases emerge from stock exchanges' disciplinary actions, the number of actionable cases for entrepreneurial lawyers under the new regime may decrease. Coupled with the application of the opt-in rule, the bargaining power of lawyers in China will not be as strong as that of U.S. lawyers. Taken together, the deterrence effect of general representative litigation is questionable due to the prerequisites. Hence, it remains to be seen whether the entrepreneurial lawyer model will thrive under the new regime.

### 2. Prerequisites for the CSISC

As for the NPO-led opt-out regime, the CSISC enjoys a monopoly position to pick and choose cases from general representative actions. Before the reform, the CSISC engaged in similar litigation, but on an opt-in basis.[346] The new law granted it greater bargaining power because it can represent more investors in a case due to the opt-out rule. As a result, defendants might have a greater incentive to settle cases with the CSISC. However, the cases that the CSISC can pursue seem rather limited—more limited than those that can be brought by entrepreneurial lawyers in opt-in representative actions. The notice published by the CSRC on July 31, 2020 further requires the CSISC to restrict their cases to those that satisfy the prerequisites of prior administrative or criminal actions, which are the same prerequisites as the old regime.[347] Whether the CSRC will follow suit to relax the procedural prerequisites after the

345. Huang, *supra* note 265, at 902.

346. The CSISC has initiated supporting litigation, in which the CSISC sued on behalf of investors by appointing their officials and outsourcing lawyers to represent them in court. Such rights to support investors in lawsuits are stipulated in Article 15 of the Civil Procedure Law and reconfirmed by the new Securities Law in Article 94. *See* MINSU FA 2017, *supra* note 207, art. 15; ZHENGQUAN FA, *supra* note 17, art. 94.

347. *CSRC Opinion*, *supra* note 235, art. 4.

2022 Notice remains to be seen. At least for now, the CSISC cannot pursue cases based on defendants' confessions or stock exchanges' disciplinary actions. Furthermore, the CSRC requires that cases be typical and important and the defendant to be solvent, which substantially narrows the ambit of NPO-led class actions.[348]

One justification for the prerequisites is that, as a publicly-funded entity, the CSISC has limited resources to fulfill its responsibilities. Bringing securities class actions is only part of the CSISC's business; it has other missions to fulfill, such as investor consultation and education, support litigation, shareholder engagement, and mediation.[349] Considering its excessive workload, it is unsurprising that the CSISC does not bring class actions unless the public interest is involved, especially when another opt-in channel is available to investors. The burden of establishing a defendant's liability is also daunting. Because discovery procedures in U.S. class action are not available in China[350], the costs of collecting the information necessary to establish a case with merit might be too high for a non-profit entity. No reasonable bystander can expect the CSISC to proactively screen all relevant market information to find wrongdoers. Therefore, piggybacking on administrative and criminal proceedings can help allocate the CSISC's resources more effectively.

With these strict prerequisites in place, the deterrent effect of opt-out securities class action is greatly compromised. The main function of this new regime, then, seems to be symbolic and compensatory. It is symbolic because the CSISC only pursues high-profile, high-impact cases. The non-profit and publicly-funded nature of the CSISC justifies its narrow focus on public interest-related litigation. The many investors involved also justify the imposition of

348. CSISC Working Rules, *supra* note 228, art. 16; *CSRC Opinion*, *supra* note 228, art. 4.

349. *See About Us*, CSISC (2020), http://www.isc.com.cn/html/gywm [https://perma.cc/7RGE-4EKS]; *see also supra* note 226 and accompanying text.

350. Public bodies, on the contrary, can conduct investigations and inspections to gather evidence, and companies are under legal obligations to cooperate. This ability leaves the CSRC in a better position to discover evidence. *See* ZHONGHUA RENMIN GONGHE GUO XINGZHENG CHUFA FA (中华人民共和国行政处罚法) [LAW OF THE PEOPLE'S REPUBLIC OF CHINA ON ADMINISTRATIVE PENALTY] (promulgated by the Standing Comm. Nat'l People's Cong., Jan. 22, 2021, effective July 15, 2020), arts. 54–56, http://www.npc.gov.cn/npc/c30834/202101/49b50d96743946bda545ef0c333830b4.shtml [https://perma.cc/4HUS-2R3C]. For a discussion of CSRC procedures in discovering evidence, see generally *Zhongguo Zhengjian Hui Guanyu Jinyi Bu Jiaqiang Jicha Zhifa Gongzuo de Yijian* (中国证监会关于进一步加强稽查执法工作的意见) [*Opinions of CSRC on Further Strengthen the Inspection and Law Enforcement*] (promulgated by CSRC, Aug. 19, 2013), http://www.csrc.gov.cn/ [https://perma.cc/N6JS-MRRD].

the opt-out rule to solve mass disputes. It is also compensatory because the CSISC considers the financial conditions of defendants when deciding whether to initiate a representative action. The current regulation obligates CSISC to only pursue cases when the defendants are solvent.[351] As a promise to deter true wrongdoers, the CSISC has clarified that it will follow the "going-after-the-leading-wrongdoer" principle when initiating a lawsuit and list the controlling shareholders or the actual controller of the company as the leading defendant(s) to avoid the pocket-shifting circularity problem.[352] It is still unclear whether and how this principle can effectively deter wrongdoers given the availability of directors' and officers' ("D&O") insurance. In the end, the CSISC will likely repeatedly face a dilemma between accepting compensation from D&O insurance to enhance the compensatory power of securities class actions, and limiting its reach by pursuing only cases in which defendants are personally solvent.

In sum, the expectation that the new securities class action regime will open a new path alongside public enforcement to deter wrongdoers may be much ado about nothing if prerequisites remain in effect. This Article suggests the removal of procedural prerequisites so that entrepreneurial lawyers can play the role of "private attorney generals" to deter wrongdoers, especially when the loser-pays rule largely rules out the possibility of meritless litigation.[353] The Chinese

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351. *CSISC Working Rules*, *supra* note 228, art. 16.

352. Qi Doudou (祁豆豆), *Toufu Zhongxin Jiang Tuijin Zhengquan Qunti Xing Susong Jizhi* (投服中心将推动证券群体性诉讼机制落地) [*CSISC Promotes the Implementation of Securities Group Litigation Mechanism*], CNSTOCK (Dec. 30, 2019), http://news.cnstock.com/news,yw-201912-4470838 htm [https://perma.cc/5BAQ-TPUE]. The pocket-shifting problem hinders the efficiency of private enforcement. *See* Coffee, *supra* note 217, at 1534:

> Securities class actions impose enormous penalties, but they achieve little compensation and only limited deterrence. This is because of a basic circularity underlying the securities class action: When damages are imposed on the corporation, they essentially fall on diversified shareholders, thereby producing mainly pocket-shifting wealth transfers among shareholders. The current equilibrium benefits corporate insiders, insurers, and plaintiffs' attorneys, but not investors.

For more discussion on the circularity problem of settlements paid through D&O insurance, see Jill E. Fisch, *Confronting the Circularity Problem in Private Securities Litigation*, 2009 WIS. L. REV. 333, 337 (2009).

353. Because lawyers are driven by profits, they may be willing to allocate more resources in collecting evidence, even if there is no discovery procedure. Until the market for entrepreneurial lawyers becomes more efficient, the lack of discovery procedure is not cause for concern. In fact, the first opt-in case under the new regime compensated investors well. The judgment of the opt-in case was delivered on December 31, 2020. In it, 487 investors received 114.31 million USD (740 million RMB), and a 579,000 USD (3.75 million RMB) filing fee was paid by the defendants in full. The judgment suggested that lawyers shall not receive a significant amount from the compensation, as the court only rendered plaintiffs

government seems to agree with such a reform direction. In July 2021, the Party and the State Council expressed in an opinion that the procedural prerequisites be removed.[354] Following the Opinion, the 2022 SPC Notice removed prerequisites for individual lawsuits.[355] It is possible that the procedural prerequisites for representative litigation will be removed in the foreseeable future. From the judiciary's perspective, requiring procedural prerequisites can help alleviate the burden on the court to investigate evidence in complex securities cases. Complementary measures are therefore needed to address the concern over inadequate evidence in filing and during the litigation due to the lack of discovery procedures in China.[356] Based on Taiwan's experience, we suggest allowing the CSISC to independently bring special representative litigation and granting the CSISC the power to demand documents from listed companies and relevant parties for the purpose of bringing representative litigation.[357]

### *C. Expansion of Binding Effect in Opt-In Cases*

The 2020 SPC Opinion specifies that if investors do not join an opt-in representative action and later file separate lawsuits, the court

16,900 USD (110,000 RMB) in attorney's fees. Thus, the amount of the attorney's fee payable to the plaintiff is not plaintiff-preferential and may even disincentivize plaintiffs from bringing suit because they must later pay a significant portion of the lawyers' fees. *See Kaofang Yu Wuyang Jianshe Jituan Gufen Youxian Gongsi* (翱放与五洋建设集团股份有限公司) [Bondholders v. Wuyang Constr. Grp., Co., Ltd.], China Judgments Online, 2020 Zhe 01 Minchu No. 1691 (2020 浙01民初1691号) [2020 Zhejiang First Instance Civil Ruling No. 1691], (Hangzhou Intermediate People's Ct., Dec. 31, 2020). However, the deterrence effect is still in question if further reform is not conducted.

354. *See Zhonggong Zhongyang Bangong Ting Guowu Yuan Bangong Ting Yinfa Guanyu Yifa Congyan Daji Zhengquan Weifa Huodong de Yijian* (中共中央办公厅国务院办公厅印发《关于依法从严打击证券违法活动的意见》) [*Opinions of the General Office of the CCP Central Committee and the General Office of the State Council on Strictly Crack Down upon Violation of Securities Law and Regulations in Accordance with the Law*] (promulgated by Gen. Off. CCP Central Comm. and Gen. Off. St. Council, July 6, 2021), art. 7.

355. The CSRC in a press release expressly declared the 2022 Notice was issued according to the State Council's Opinion. *See Zuigao Renmin Fayuan Fabu Guanyu Shenli Zhengquan Shichang Xujia Chenshu Qinquan Minshi Peichang Anjian de Ruogan Guiding* (最高人民法院发布《关于审理证券市场虚假陈述侵权民事赔偿案件的若干规定》) [*Supreme People's Court Issued Some Provisions of the Supreme People's Court on Trying Cases of Civil Compensation Arising from False Statements in Securities Market,*, CSRC (Jan. 21, 2022), http://www.csrc.gov.cn/csrc/c100028/c1780919/content.shtml [https://perma.cc/2QPE-8A3L].

356. *See supra* note 350 and accompanying text.

357. TOUBAO FA, *supra* note 134, art. 17.

will apply the decision on the same matter of law and facts in the latter case without holding a hearing.[358] It is therefore questionable whether the lawyer-led general representative action is genuinely opt-in. In effect, the lawyer-led and NPO-led models seem to be opt-out lawsuits because the binding effect of an opt-in lawsuit also extends to all investors who fall within the class and later bring lawsuits. The difference is that, to the defendants, the opt-in action does not resolve the dispute once and for all, and thus reduces the defendants' incentives to settle the case in the first place. In the U.S.-style class action, the defendant usually has an incentive to settle the case with plaintiffs because the settlement will resolve the case for good by including all potential plaintiffs within the class.[359]

The unique design of the expanded binding effect of opt-in cases is grounded in the representative action in Civil Procedural Law.[360] Scholars have criticized that the expanded binding effect on unregistered rightsholders finds no ground in legal theory because the expansion deprives these individuals of their litigation and appeal rights.[361] The adoption in the 2020 SPC Opinion apparently does not aim to increase defendants' incentives to settle because such an expansion does not solve the case for good. Rather, the 2020 SPC Opinion demonstrates that the consideration of judicial efficiency outweighs the need to resolve disputes at once or to protect individuals' litigation rights.[362] In lawyer-led and NPO-led models alike, the SPC, as the head of the judiciary, considers its own interest

358. *2020 SPC Opinion*, *supra* note 21, art. 29.

359. Gelter, *supra* note 8, at 82 (noting that "opt[ing] out can be advantageous for defendants as well because a settlement or verdict, even if it is costly, preempts the possibility of further lawsuits in the matter in question and thus reduces uncertainty").

360. *See* MINSU FA 2017, *supra* note 207, art. 54(4) (noting that "such a judgment or ruling shall also apply to actions instituted during the time limitation by rights holders which have not registered with the people's court").

361. *See*, *e.g.*, TANG WEI-JIAN (汤维建) & XIANG TAI, (向泰), MINSHI SUSONG FA (民事诉讼法) [CIVIL PROCEDURE LAW] 121 (2014); Liu Xuezai (刘学在), *Daibiao Ren Susong Zhi Caipan Xiaoli Kuozhang de Jige Chengxu Wenti* (代表人诉讼之裁判效力扩张的几个程序问题) [*Several Procedural Issues on the Extension Effect of the Representative Litigation's Judgment*], 2 FAXUE (法学) [L. SCI.] 55, 56 (1999); Xiao Jianhua (肖建华), *Qunti Susong Yu Woguo Daibiao Ren Susong de Bijiao Yanjiu* (群体诉讼与我国代表人诉讼的比较研究) [*A Comparative Study on Group Litigation in Other Juridictions and China's Representative Litigation*], 1999 BIJIAO FA YANJIU (比较法研究) [J. COMP. L.] 227, 239 (1999) (arguing that one possible justification is that an expanded binding effect may better protect public interests and stabilize the legal system).

362. *See* Shi Wei (施玮), *Woguo Susong Daibiao Ren Zhidu Pingxi* (我国诉讼代表人制度评析) [*On Chinese Representative Litigation*], 2 FAZHI YANJIU (法治研究) [RES. RULE L.] 31, 32–33 (2009).

and aims more to reduce the workloads of judges in the design of securities collective-redress procedures. The judiciary thus becomes the largest interest group, setting the game rules that embed not only political priorities, but also its own administrative preferences.[363]

### *D. Investor Protection Institution: NPO or Public Agent?*

The non-distribution constraint inherent in NPOs makes them more trustworthy producers of public goods than for-profit lawyers and addresses the abusive practices evident in the entrepreneurial lawyer model in the United States.[364] However, China's hybrid model also fails to avoid the agency problem. While the agency problem between lawyers and clients that plagues the U.S. system has been eased under the NPO-led model, the relationship between the CSISC and investors creates another layer of agency costs because the principal-agent relationship persists: NPOs serve as the agents of investors in securities class action.[365] Agents are self-interested entities with their own preferences and motivations.[366] Although not motivated by legal fees, NPOs may place the interests of a regulatory body, stock exchange, or even the whole market over the interests of investors because the NPO and its private-enforcement authority are created by the government through legislation. Drawing on Taiwan's experience, this conflict is probably inevitable for any jurisdiction that embraces a government–NPO partnership model.[367]

In Taiwan, scholars have attributed governmental influence on private securities litigation to the SFIPC's close relationship with the

363. One possible justification, as discussed above, is that the court shall contribute to social stability. Thus, the judge's job is more than simply to try the case, but also to engage in mediation and promote settlement. Judges are often subject to excessive workloads and sometimes have no choice but to prioritize efficiency over justice. For a discussion on social stability and overworked judges, see HANG NG & HE, *supra* note 324, at 53–54.

364. *See* Milhaupt, *supra* note 90, at 171; Lin, *supra* note 22, at 177–80.

365. Because NPOs have no substantial economic interests in litigation, they may face a more severe agency problem than lawyers. *See* Tang Xin (汤欣), *Siren Susong Yu Zhengquan Zhifa* (私人诉讼与证券执法) [*Private Litigation and Securities Law Enforcement*], 1 QINGHUA FAXUE (清华法律) [TSINGHUA L. REV.] 92, 115 (2007).

366. The basic assumption of this theory is that everyone is an economic person who is committed to maximizing their own utility. *See* DENNIS C. MUELLER, PUBLIC CHOICE III, at 473 (2003).

367. *See* discussion *supra* Section I.B.

Financial Supervisory Commission ("FSC").[368] Various parties fund the SFIPC, including stock exchanges and the association of securities and futures firms.[369] The FSC directly supervises it, enjoying the right to appoint its directors and supervisors.[370] For NPOs in China, the CSISC is under the direct supervision of the CSRC, and its shareholders consist of four stock and futures exchanges, the China Securities Depository, and Clearing Corporation Limited.[371] All these shareholders are state-owned. The CSRC has clarified that it will supervise every decision the CSISC makes in the course of class action.[372] The CSISC must also regularly communicate with the CSRC, stock exchanges, and even courts during litigation, as well as prepare a report for the CSRC after each case is closed.[373]

Today, the CSISC heavily relies on ties with regulators to exercise its power, and the market still treats it as an agency under the CSRC.[374] Considering that many listed companies are SOEs, including some in even higher administrative strata than the CSRC, it is unlikely that the CSISC will aggressively enforce the law against such companies. Despite the CSRC's emphasis that, as an investor-protection institution, it independently decides whether to bring class actions, it remains to be seen whether the CSISC is more willing to enforce against privately-owned companies than SOEs.

368. *See* Wallace Wen-Yeu Wang & Jhe-Yu Su, *The Best of Both Worlds? On Taiwan's Quasi-Public Enforcer of Corporate and Securities Law*, 3 CHINESE J. COMP. L. 1, 13 (2015) (noting that the decision-making of SFIPC is greatly influenced by the FSC).

369. TOUBAO FA, *supra* note 134, art. 18.

370. *Id*. arts. 3, 11, 15.

371. *See Zhong Zheng Zhongxiao Touzi Zhe Fuwu Zhongxin Zuzhi Jiagou* (中证中小投资者服务中心组织架构) [*Ownership Structure of CSISC*], Zhong Zheng Zhongxiao Touzi Zhe Fuwu Zhongxin (中证中小投资者服务中心) [CSISC], http://www.isc.com.cn/html/zzjg/ [https://perma.cc/PYZ6-H35Y].

372. *CSRC Opinion*, *supra* note 235, art. 12; *CSISC Working Rules*, *supra* note 228, art. 5.

373. *CSRC Opinion*, *supra* note 235, arts. 12–15; *CSISC Working Rules*, *supra* note 228, art. 5.

374. In China, most NPOs, including the CSISC, play the roles of government-affiliated institutions and function under the supervision of the government. *See* Yan Ruosen (严若森), *Zhongguo Fei Yingli Zuzhi de Zhengfu Xing Yihua Jiqi Shiying Xing Zhili* (中国非营利组织的政府性异化及其适应性治理) [*The Government Dissimilation and Adaptive Governance of Chinese Non-Profit Organizations*], 7 GUANLI SHIJIE (管理世界) [MGMT. WORLD], 167, 167 (2010).

### *E. Towards a State-led Model? A Case Study on China's First Opt-out Representative Litigation*

As China's securities representative litigation is closely monitored by public authorities, entrepreneurial lawyers can hardly play the role of "private attorney general". It is therefore questionable whether this regime is a hybrid model or in effect a state-led one. The first opt-out representative litigation may shed light on the state's involvement in securities collective redress procedures in China.

On March 26, 2021, the CSISC issued a notice expressing that it would take over an existing general representative litigation against Kangmei Pharmaceutical Co., Ltd and other responsible persons.[375] This securities fraud case caused widespread public concerns in that the company fabricated a significant number of sales (4.63 billion USD) from 2016 to 2019. At that time, it was the biggest securities fraud in the A-share market's history.[376] The CSRC, on May 13, 2020, issued an administrative penalty to the company and persons involved in the fraud.[377] As the company has been penalized by the public enforcer, little debatable issues are left on the case's merits. The class action is only subordinate to the CSRC's action and compensates the defrauded investors. However, the prerequisite of the company being solvent was not enforced in this case. Kangmei was ordered by Jieyang Intermediate Court to enter into the reorganization procedure

375. Toufu Zhongxin Jieshou Kangmei Yaoye Xujia Chenshu Minshi Peichang An Touzi Zhe Weituo de Shuoming (投服中心接受康美药业虚假陈述民事赔偿案投资者委托的说明) [*Notice of the CSISC Accepting the Authorities of Investors in the Civil Compensation Case Against Kangmei Pharmaceutical Co. Ltd.'s False Statement*], Zhong Zheng Zhongxiao Touzi Zhe Fuwu Zhongxin (中证中小投资者服务中心) [CSISC], http://www.isc.com.cn/html/kmyya/20210326/3701 html [https://perma.cc/4B72-QRZR].

376. Kangmei Yaoye 3 Nian Zaojia Yue 300 Yi Woguo Shou Dan Zhengquan Jiufen Tebie Daibiao Ren Susong Zhengshi Qidong (康美药业3年造假约300亿 我国首单证券纠纷特别代表人诉讼正式启动) [*Kangmei Pharmaceutical Co., Ltd. Conducted 30 Billion RMB Financial Fraud in Three Years, and China's First Special Securities Representative Litigation Is Launched* ], CCTV.COM (Apr. 19, 2021), https://m.news.cctv.com/2021/04/19/ARTIVvdlpSh75DwlnLPf1FEE210419.shtml [https://perma.cc/L884-HT9Q].

377. *Zhongguo Zhengjian Hui Xingzheng Chufa Jueding Shu (Kangmei Yaoye Youxian Gongsi Ma Xingtian Xu Dongqin Deng 22 Ming Zeren Renyuan* (中国证监会行政处罚决定书 (康美药业股份有限公司、马兴田、许冬瑾等22名责任人员) [*China Securities Regulatory Commission Administrative Penalty Decisions (22 Responsible Persons Including Kangmei Pharmaceutical Co., Ltd., Xingtian Ma, Dongqin Xu, etc.)*], CCTV.COM (Apr. 19, 2021), http://www.csrc.gov.cn/pub/zjhpublic/G00306212/202005/t20200515_376440 htm [https://perma.cc/WLF7-MKKP].

on June 4, 2021 because the company was unable to pay its debt.[378] It is clear that when the CSISC took over the case, the company's solvency was questionable.

The judgement of the Kangmei case was rendered by the court on November 12, 2021, in which 55,326 investors received approximately 390 million USD (2.46 billion RMB), 50.5% of their claims.[379] Compared with German's Deutsche Telekom case,[380] the Chinese regime is highly efficient in terms of the time span between the filing of the case and court's judgment, and the amount of recovery granted by the court. On November 26, 2021, the Jieyang court approved Kangmei's reorganization plan.[381] According to the plan, several local SOEs will inject capital into Kangmei to bail the company out and thus allow investors to recover their losses timely.[382]

It is clear that the first opt-out class action is one that the state and the subordinated judiciary and agencies carefully orchestrated. The CSISC carefully selected a case that widely concerned the public; the judiciary rendered the judgment within a short timeframe; and the SOEs bailed out the defendant company to compensate defrauded investors. The first Chinese opt-out securities class action appears to be a perfect case for the global securities class action regime considering its efficiency and compensatory function. However, it remains to be seen whether China is moving towards a state-led model

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378. *See Announcement of Kangmei Pharmaceutical Co., Ltd. on the Court's Decision to Accept the Company's Reorganization and the Company Is Traded on Risk Alert Board*: SOHU (June 5, 2021), https://q.stock.sohu.com/newpdf/202144896171.pdf [https://perma.cc/6HAD-MH7Z].

379. Gu Huajun, Huang Meixiang, Xiang Deng 55326 Ming Touzi Zhe Yu Kangmei Yao Ye Gufen Youxian Gongsi (顾华骏，黄梅香等55326名投资者于顾华骏，黄梅香等55326名投资者) [Investors and Kangmei Pharmaceutical Co., Ltd., First Instance Civil Judgment] (2020) Yue 01 Minchu 2171 Hao (粤01民初2171号)[2020 Guangdong Civil Judgment No. 2171] (Guangzhou Intermediate People's Ct., Nov. 11, 2021).

380. It took a Frankfurt court eleven years to hand down the first model case judgement. *See* Axel Halfmeier, *Class Actions in Context*, *in* LITIGATION WITHOUT END? THE DEUTSCHE TELEKOM CASE AND THE GERMAN APPROACH TO PRIVATE ENFORCEMENT OF SECURITIES LAW 290 (Deborah R. Hensleret al. eds., 2016).

381. *See Announcement of Kangmei Pharmaceutical Co., Ltd. Regarding the Court Ruling Approving the Company's Restructuring Plan*, KANGMEI (2021), https://qxb-pdf-osscache.qixin.com/AnBaseinfo/edc6646d026ff59fcd0cd80dfe502cf7.pdf [https://perma.cc/7HY3-6YFM].

382. *See* KANGMEI, CHONGZHENG JIHUA (重整计划) [REORGANIZATION PLAN] 12–13, 27 (2021), https://pdf.dfcfw.com/pdf/H2_AN202111261531237416_1.pdf [https://perma.cc/QC9A-K35E]. According to the court judgment, the company shall first compensate investors and then is allowed to reimburse from other persons who are jointly liable. *See supra* note 379 and accompanying text.

or a truly hybrid model where entrepreneurial lawyers can still play the role of private attorney general as those in the United States.

## CONCLUSION

This Article critically assesses the latest developments in global securities class action regimes and introduces the key features of the new Chinese hybrid model. This hybrid model exemplifies an innovative regulatory breakthrough that endeavors to integrate different legal practices from other jurisdictions into the local Chinese legal environment. The U.S. lawyer-led model is subject to much criticism, and the Chinese experience importantly points in a new direction: the NPO-led opt-out regime. Non-profit and non-distribution attributes render NPOs suitable candidates to lead class actions because they avoid conflicts of interest between lawyers and investors and the litigious legal culture resulting from the U.S. lawyer-led model. Recent reforms in the European Union's collective redress mechanism further attest to the practicability and feasibility of the NPO-led model.

Another novelty of the Chinese hybrid model is that it embraces certain aspects of the U.S. experience by allowing entrepreneurial lawyers to participate in the opt-in scheme. This model takes a middle ground by combining both market-driven and government-controlled mechanisms. However, a close examination of the judicial interpretation published by the SPC and the first opt-out class action shows traces of political influence and control over the whole securities collective redress mechanism. Indeed, the policies of maintaining social stability and avoiding confrontational litigation greatly shape the contours of the new investor-protection regime in China. While there appears to be a formal convergence in procedural rules between the United States and China, the differences in political values and legal infrastructure are determinative of the reform's outcomes. Ultimately, the new Chinese hybrid model offers an innovative comparative law reference for jurisdictions that are reluctant to accept a litigious legal culture, but at the same time, hope to enhance private enforcement of securities law.