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Civil Liability for Misrepresentation in the Securities Market: A Comparative Study of China, Taiwan and U.S.
証券市場虛假陳述行爲的民事責任：中國大陸、臺灣和美國之比較研究

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Abstract

Securities market has been established in modern China for about 20 years and thousands of retail investors have been involved directly in the market. However, severe misrepresentations contained in the prospectus and continuous financial reports, which caused economic loss and severely harmed the integrity of the market, can be frequently found in the emerging market. The thesis aims to examine the current civil liability system for misrepresentation in the securities market, which was initiated just ten years ago, and check whether it is efficient in protecting the investors in the securities market. Comparative law approach has been followed and reference has been made to the civil liability systems for misrepresentation in the securities market in the U.S. and Taiwan respectively. The U.S. has a sophisticated investor protection system and hence its experience in this area is valuable while the EU and Japan hold a conservative attitude towards this issue. Besides, China and Taiwan, as civil law jurisdictions, both have transplanted some of the U.S. experience, though the results are to a certain extent different.
The issuer company has the legal obligation to make correct disclosure not only in the process of public offering but also in the secondary market. In both processes, multiple parties participate in the preparation of the disclosure documents. In the public offering, the issuer company makes information disclosure, decides the offering price and receives the payment, and the investors are delivered the disclosure, accept the offering price and pay for the securities. While in the secondary market, though the company makes continuous disclosures, the trading is made between investors, without the participation of the listed company. Therefore the misrepresentation in the offering is severer in harming the investors than that in the secondary market. It is reasonable to distinguish the civil liability rules for the misrepresentation in the offering and that in the secondary market. The Chinese rules mix the two scenarios and cause confusion in applying the rules to protect the investors. The current prerequisite of an effective court judgment or an administrative sanction decision which is required to bring a private lawsuit against the wrongdoer also limits the investors’ civil right to sue for damages and should be removed.
For misrepresentation in the primary market, more parties are involved in the preparation of the prospectus than those in the continuous disclosure and the injured investors can benefit from the broad scope of defendants. The existing rule in China does not have a clear definition on the misconduct of misrepresentation so that the court may be confronted with difficulties in characterizing the material misrepresentation. The test of a prudent investor may make up the deficiency. It would be better to disregard the role of causation in this action. With respect to the measurement of the pecuniary loss, the current approach in China tries to get the true value of the security that fully reflects the impact of the misrepresentation, but the single formula cannot reflect the complex situations in the market and a fair price cannot be easily achieved.

In the secondary market, four essential elements are required to establish the civil liability for misrepresentation: material misrepresentation, economic loss, the causation between material misrepresentation and economic loss, and fault of the wrongdoers.
The issue of materiality should be determined by the test of a prudent investor. The 2003 Judicial Interpretation of China currently presumes the element of causation, just as the U.S. approach is based on the fraud on the market theory. However, it is an issue whether this theory can be applied in China. This thesis tries to prove that the securities market of China is in the level of efficiency between the weak form of efficiency and the semi-strong form of efficiency and could be deemed as an efficient market and hence the presumption of causation can to a certain extent be established in China. Only favorable misrepresentation currently leads to civil liability in China, which is unfair for the injured investors who suffer pecuniary loss from adverse or gloomy misrepresentation. The scope of misrepresentation that leads to civil liability should be extended to adverse or gloomy misrepresentation for the purpose of the integrity of the securities market. Besides, the doctrine of joint and several liability should be applied to the joint misrepresentation in the securities market for the protection of the investors. The perspective of balancing the liability of the defendants with the share of fault is reasonable and the proportionate liability should be applied to make up the deficiency of
the joint and several liability doctrine. Exceptions may be allowed to provide better compensation for the victims.
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