Chapter 17

Heading towards Good Governance

A Case Study of the Chinese Commercial Banks

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17.1 Introduction

The developments of the Chinese banking industry have attracted a lot of attention in recent years. These developments not only reflect on the industrial structure as a whole, but also on the level of performance of individual banks. Furthermore, the developing strategy of the Chinese banking industry is not limited to the domestic level, but is also aimed at the international expansion. On July 6, 2012, Industrial and Commercial Bank of China (ICBC) and The Bank of East Asia (BEA) concluded ICBC's acquisition of an 80% interest in BEA (U.S.A.), and became the controlling shareholder of latter.[1] The acquisition indicated that the overseas expansion of Chinese banks has stepped into a new stage. Looking back at the development of the Chinese banking industry; corporate governance, as a central issue, has improved significantly over the last few years. However, in spite of the rapid development of financial system and the lack of relevant laws and regulations, corporate governance of the Chinese banking industry still needs to be further enhanced; in particular, further improvements of corporate governance have been hindered by various existing problems in this area; for instance, the inefficient legal framework, weak enforcement structure and an inaccurate corporate disclosure regime.

The development of corporate governance in the Chinese banking sector is tightly associated with the economic reform. This chapter examines the approaches adopted by the Chinese commercial banks, targeted at improving corporate governance in banking sector. The first part of the paper illustrates the structure of the Chinese banking industry. Secondly, the paper examines the development of the legal regime with regards to corporate governance and

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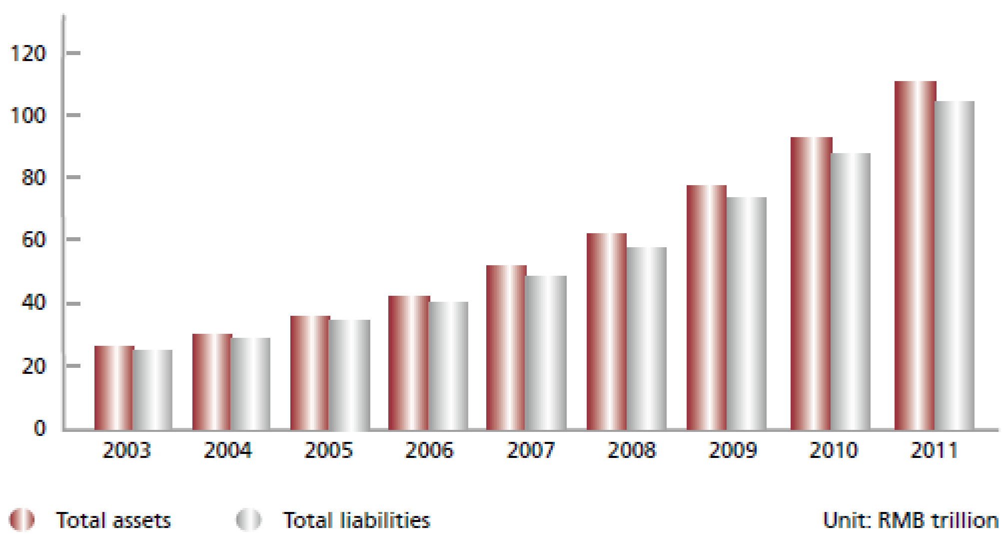
[1] "ICBC and BEA Conclude the Sale and Purchase of the Bank of East Asia (U.S.A.)", http://www.icbc.com.cn/icbc/newsupdates/icbc%20news/ICBC%20and%20BEA%20Conclude%20the%20Sale%20and%20Purchase%20of%20The%20Bank%20of%20East%20Asia%20(U.S.A.).htm, last accessed: 16 December 2012.

financial regulators in China. Thirdly, taking the concept of corporate governance, corporate social responsibility (CSR) and information disclosure regime as examples, this paper analyzes different approaches adopted in order to enhance corporate governance in the banking industry. Last but not least, conclusions are made based on this study.

17.2 The Chinese Banking Industry

The Chinese banking institutions perform a unique role in the socialist market economy. Today, the function of Chinese banks has already evolved from the simple deposit taking and loan issuing to providing diversified products and delivering more sophisticated financial services. The Chinese banking industry itself has also expanded significantly in the last few years. **Chart 17.1** below illustrates the total assets and liabilities of banking institutions from 2003 to 2011. As at the end of end-2011, the total assets of China's banking institutions increased to RMB113.3 trillion; total liabilities rose to RMB106.1 trillion.[2]

Chart 17.1: Total assets and liabilities of banking institutions (2003-2011)



[2] CBRC Annual Report 2011, p. 24.

Source: CBRC [3]

The banking industry in China composes of different groups of banks. [4] The policy banks refer to the China Development Bank, Export-Import Bank of China, and Agricultural Development Bank of China. [5] The Industrial and Commercial Bank of China, Agricultural Bank of China, Bank of China, Bank of Communications, and China Construction Bank are the large commercial banks.[6] The joint-stock banks; for instance, the China Citic Bank Corporation, China Everbright Bank, Huaxia Bank, China Bohai Bank, and Shenzheng Development Bank and others are playing an increasingly important role in the national economy. Moreover, the rural banks and city commercial banks are important components of the Chinese banking industry. Furthermore, the Postal Banking of China provides various banking services.

Apart from the above, the foreign fund related banks actively participate in the Chinese economy; for example, the Standard Chartered Bank (China), HSBC Bank (China), Citibank (China), Deutsche Bank (China), BNP Paribas (China), Industrial Bank of Korea (China), etc. According to the China Banking Regulatory Commission (CBRC), as the end of 2011, there were 5 large commercial banks, 12 joint-stock commercial banks, 144 city commercial banks, 212 rural commercial banks, 190 rural cooperative banks, 2,265 rural credit cooperatives

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3 CBRC Annual Report 2011, p. 25.

4 The latest lists of domestic banking institutions can be found at China Banking Regulatory Commission website: http://www.cbrc.gov.cn.

5 The policy bank in China were established according to Decision of the State Council on Reform of the Financial System, in order to separate policy finance from commercial finance and to solve the problem of national specialized banks executing dual function. The National Development Bank，handles policy loans and discount business for key national construction projects (including capital construction and technical transformation). The Agricultural Development Bank of China (ADBC) to undertake policy loans for State reserve in grain, cotton and edible oil, for contract-purchasing of farm and sideline products, and agricultural development, and to appropriate fiscal funds for supporting agriculture and to supervise their use as an agent. The China Import-Export Credit Bank (CIECB) supplies buyer's and seller's credits for importing and exporting of large scale mechanical and electrical equipment, etc. See Decision of the State Council on Reform of the Financial System , Guofa [1993] No. 91, promulgated date: 25 December 1993, part 2.

6 "Commercial banks" means enterprise legal persons that are established in conformity with the law and take in deposits from the general public, grant loans, handle settlements, etc. See Law of the People's Republic of China on Commercial Banks, promulgated date: 10 May 1995, revised date: 27 December 2003, Article 2. According to Article 3 of this law, the commercial banks may engage in the following business: taking deposits from the general public; granting short-term, medium-term and long-term loans; handling domestic and foreign settlements; handling the acceptance and discounting of negotiable instruments; issuing financial bonds; acting as an agent for the issue, honouring and underwriting of government bonds; buying and selling government bonds and financial bonds; engaging in interbank lending; buying and selling foreign exchange and acting as an agent for the purchase and sale of foreign exchange; engaging in the business of bank cards; providing letter of credit services and guaranty; acting as an agent for the receipt and payment of money and acting as an insurance agent; providing safe deposit box services, etc.

(RCCs), 1 postal savings bank, 4 banking assets management companies, 40 locally incorporated foreign banking institutions, 66 trust companies, 127 finance companies of corporate groups, 18 financial leasing companies, 4 money brokerage firms, 14 auto financing companies, 4 consumer finance companies, 635 village or township banks, 10 lending companies and 46 rural mutual cooperatives.[7] These institutions together, facilitate the development of national economy.

17.3 The Legal Framework and Banking Regulators

The importance of the banking industry means that to achieve good corporate governance the best scientific methods and approaches have to be used. In the past few years, different approaches have been introduced to improve the corporate governance regime. In this part of the paper, the effects and implications will be examined with details.

The enactment of the Company Law in 1993 and the Securities Law in 1998 provided principles and guidelines for corporate governance in China.[8] However, with the development and reform of the Chinese economy and financial system there were numerous new issues needed to be dealt with; among different matters, reduction of the Non Performing Loan (NPL) was one of the key concerns. According to the domestic accounting standards at that time, in 1998 the Chinese banking system had an NPL ratio of 25 percent, by international accounting standards this would have put the rate at higher than 40 percent.[9] This was a great cause of concern. Consequently in February 2002, the second National Financial Work Conference set out plans to strengthen financial supervision and to proceed with financial restructuring. [10] Following this, the Chinese government made plans to reform the financial institutions; the approaches adopted such as lowing NPLs, allowing foreign investment in the state banks as strategic investors, opening up

[7] CBRC Annual Report 2011, p. 24.
[8] Company Law, promulgation date: 29 December 1993, effective date: 1 July 1994, revised in 2005.
Securities Law, promulgation date: 29 December 1998, effective date: 1 July 1999, revised: 27 October 2005, effective date: 1 January 2006.

9 Xiaochuan Zhou (2007), Instability and Evolution of the Financial System, http://www.pbc.gov.cn/publish/english/956/1947/19476/19476_.html, last accessed: 28 April 2013.

[10] ibid.

the financial sector to foreign investors by the end of 2006, and listing state banks on exchanges, have all promoted the transformation towards good corporate governance.

It is impossible to develop the corporate governance regime without suitable regulators. Financial regulators play an important role with regard to the improvement of corporate governance in China. The People's Bank of China (PBOC) is the central bank in China. On 1 December 1948, the PBOC was established; and in September 1983, the PBOC's status was confirmed by the State Council; the Law of the People's Republic of China on the People's Bank of China legally confirmed the PBOC's central bank status.[11] Furthermore, the China Banking Regulatory Commission (CBRC) regulates and supervises banking institutions and their business operations.[12] Based on the Commercial Bank Law of the People's Republic of China,[13] the Regulation of the People's Republic of China on the Administration of Foreign-funded Banks[14], and other laws and regulations, these banking regulators oversee the activities of banking institutions.

17.4 Approaches Adopted to Enhance the Corporate Governance

The Chinese banking industry has attempted numerous methods of seeking a better governance structure; for instance, introducing and redefining the concept of corporate governance, promoting CSR, enhancing the corporate disclosure regime, reforming the ownership structure and improving supervision of the board directors and other senior executives. The ownership structure reform can be viewed as one of these important steps to improving corporate governance of banking institutions. The diversification of shareholders, through overseas listing

[11] See PBOC website, http://www.pbc.gov.cn/publish/english/952/index.html, last accessed: 11 July 2012. Law of the People's Republic of China on the People's Bank of China, promulgated date: 18 March 1995, effective date: 18 March 1995.

[12] The main functions of the CBRC are: to formulate supervisory rules and regulations governing the banking institutions; to authorize the establishment, changes, termination and business scope of the banking institutions; to conduct on-site examination and off-site surveillance of the banking institutions, and take enforcement actions against rule-breaking behaviours; to conduct fit-and-proper tests on the senior managerial personnel of the banking institutions; to compile and publish statistics and reports of the overall banking industry in accordance with relevant regulations; to provide proposals on the resolution of problem deposit-taking institutions in consultation with relevant authorities. See CBRC website, http://www.cbrc.gov.cn/english/info/yjhjj/index.jsp, last assessed: 17 July 2011.

[13] Adopted 10 May, 1995, amended on 27 December2003, and came into force on 1 February 2004.

14 Adopted on 8 November 2006, came into force on 11 December 2006.

and involvement of the foreign institutional investors, boosted the reform towards good governance. Though the actual impact of the foreign entry is still to be precisely determined from an economic perspective; there should be no doubts concerning the benefits on the aspect of enhancing corporate governance.

Nevertheless, although there have been substantial developments, problems such as the lack of protection for minority shareholders, absence of transparency and inaccurate corporate disclosure, have attracted numerous criticisms. A call for further scientific and responsible improvement has emerged; for instance, to address the financial inclusion and CSR. In this part of the paper, selected issues on promoting good corporate governance will be examined.

17.4.1 A New Concept of Corporate Governance

After the recent financial crisis, it has been broadly accepted that corporate governance is one of the essential methods to maintain financial system stability. However, as a concept, there has not been a universal definition on what is corporate governance. Corporate governance involves different elements; for instance, the regulatory and market mechanisms, the relationships between a company's management, its board, its shareholders and other stakeholders, and the goals and aims for which the corporation is governed.

In 2004, the Guidance on the Corporation Governance Reform and Supervision of Bank of China and China Construction Bank set out requirements for corporate governance: the two pilot banks shall establish a standard shareholders' general meeting, a standard board of directors, a standard supervisory board and a standard system of senior management respectively; the shareholders' general meeting, board of directors, supervisory board and the system of senior management of the two pilot banks shall be established upon the principles of separate establishment, separation of the three powers, effective constraint and coordinated development in accordance with the requirements of a modern corporate governance structure.[15] This Guidance primarily illustrates the scope of corporate governance for banking institutions.

Problems identified from the recent financial crisis, for instance, inadequate risk management, opaque bank organizational structures and activities, and lack of oversight of the senior

[15] CBRC, 11 March 2004. Article 4.

management have resulted in a searching for a new improved definition of corporate governance. Drawing on the experiences from international best practices the Chinese government and banking regulators have numerous inputs on the developing of corporate governance. One of the key concerns in China is improving the corporate governance of banking institutions from a framework building-up to a more advanced level with a feature of clear structure, responsibilities and accountability.

A newly developed recognition is contained in the Guidelines on Corporate Governance of Commercial Banks (Consultative Version)[16]. In this consultative document, "corporate governance of commercial banks" is defined as the relationships among the general meetings of shareholders, the Board of Directors, the Supervisory Board, senior management, shareholders and other stakeholders, which includes "checks and balances" mechanisms as part of the organizational structure, division of responsibilities and duty requirements, as well as such operating mechanisms as the decision-making, implementation, monitoring and incentives and disciplines.[17] It further states that to establish a sound corporate governance of a commercial bank, at least the following shall be consisted: a complete organizational structure; clear division of responsibilities; scientific development strategy; values and codes of conduct as well as social responsibilities; effective risk management and internal control; rational incentives and discipline mechanisms; and a well-established information disclosure system.[18] Clearly, this consultative version, take reference from the OCED and Basel Committee principles, which introduced a new concept of "corporate governance" with the notion of "stakeholders"; therefore, it can better reflect the banks' duty of protection of the depositors and banking employees.[19]

17.5 Corporate Social Responsibility

The CSR has been addressed by the Chinese banking industry gradually. While this issue has been recognized earlier in other countries, it has been argued that the literature on CSR in China

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[16] CBRC, 25 July 2011, consultative version.
[17] ibid, Article 3.
[18] ibid, Article 7.
[19] CBRC Answering the Questions about Guidelines on Corporate Governance of Commercial Banks (Yinjianhui jiu 'Shangye Yinghang Gongsi Zhili Zhiyin' Dawen), 26 July 2011, http://www.gov.cn/gzdt/2011-07/26/content_1914435.htm, last accessed: 6 April 2012.

or on CSR from a Chinese perspective is rather limited. [20] However, this has changed significantly. Law and regulation have put more emphasizes on this issue; Company Law Article 5 promulgated that when undertaking business operations, a company shall comply with the laws and administrative regulations, social morality and business morality; it shall act in good faith, accept the supervision of the government and the general public, and bear social responsibilities.[21] This is the first time that Chinese law addressed the CSR issue, before the enforcement of this law the concept of CSR was not clearly presented.

The Opinions on Strengthening the Social Responsibility of Banking Financial Institutions is one of the important legal documents in this area.[22] It pointed out that the banking financial institutions' fulfillment of their social responsibility is a must for building a harmonious society;[23] fulfilling social responsibility is an important path for banking financial institutions to improve their competitiveness.[24] It also requires that all banking institutions shall adopt appropriate forms to issue social responsibility reports in light of their actualities; major banking financial institutions shall issue annual social responsibility reports on a regular basis.[25] In this Opinion it also sets out the general requirements for the social responsibility of banking institutions, including: protecting the legitimate rights and interests of shareholders and treating all shareholders equally, maintaining to the people-oriented principle and attaching importance to and protecting the legitimate rights and interests of employees; operating the business in good faith and protecting the legitimate rights and interests of financial consumers; combating against unfair competition, commercial bribery and money-laundering activities and creating a good market competition order; saving resources, and protecting and improving the natural ecological environment; improving community-based financial services and enhancing community development; and caring for social development and supporting the public welfare undertaking. [26] **Chart 17.2** below gives an example of the CSR report for a Chinese banking institution. It

[20] Whelan, G. (2007), "Corporate Social Responsibility in Asia: A Confucian Context", in May, S.; Cheney, G.; Roper, J. (ed.) The Debate over Corporate Social Responsibility, pp. 105-118, New York, Oxford University Press.
[21] Company Law of the People's Republic of China, promulgation date: October 27, 2005; effective date: January 1, 2006.
22 No.252 [2007] of the General Office of China Banking Regulatory Commission, issued date: 5 December 2007, effective date: 5 December 2007.
23 ibid, Part 1
24 ibid, Part 2
25 ibid, Part 3.
[26] ibid, Part 3.

can be seen from the chart that the key contents of this report have broad coverage with the emphasis on the economic, environment and social performance.

Chart 17.2: Section of 2011Corporate Social Responsibility Report of the Industrial and Commercial Bank of China Limited[27]

[27] Directory of the 2011Corporate Social Responsibility Report of the Industrial and Commercial Bank of China Limited.

Strategy and Profile

Overview of ICBC
Responsibility Brand
Milestone in Responsibility
Responsibility Promotion
Responsibility Exchanges
2011 Highlights
Assessment from Third Parties

Economic Performance

Operating Results and Value Creation
Promoting Steady and Healthy Development of the Real Economy
Supporting the Coordinated Development of Regional Economies
Supporting the Strategic Key Industries of the State
Boosting the Development of Small and Micro Enterprises
Enhancing the Financial Services Related to "Agriculture, Rural Areas and Farmers"
Promoting the Economic Development in Ethnic Minority Regions
Serving the Construction of Low-income Housing
Speeding up Overseas Expansion, Enhancing Global Services

Environmental Performance

Promoting Green Credit, Supporting Low-carbon Economy
Advocating Green Finance, Promoting E-banking
Implementing Green Office, Promoting Energy Saving and Consumption Reduction
Promoting Green Concept, Boosting Environmental Protection Cause

Social Performance

Dedication to Repaying Society to Build a Charity Bank
Caring for Employees to Build a Harmonious Bank
Operating with Good Faith to Create a Creditworthy Bank
Vigorously Serving Customers to Build a Brand

Along with the banking regulators, the self-regulatory body plays an important role in this aspect too. To date the China Banking Association (CBA) has published the Social Responsibility Report of China's Banking Sector for 4 consecutive years.[28] On 5 December 2008 the CBA issued the first-ever social responsibility report of China's banking sector. CBA's Guidelines on the Corporate Social Responsibility of Banking Institutions of China set out more detailed

[28] The reports can be found at CBA website, http://www.china-cba.net/list.php?fid=65. Last accessed: 12 December 2012. The CBA is the self-regulatory organization for the Chinese banking institutions. It was established in 2000. At the end of November 2012, the CBA has 168 member banks and 2 observer banks.

requirements for the banking institutions.[29] It states that the Guidelines is applied to the banking institutions which have the corporate status in China, including commercial banks, urban credit cooperatives, rural credit cooperatives and other financial institutions that are legally established within the territory of the People's Republic of China and receive public deposits; policy banks; financial assets management companies; petty loan companies, etc.[30] It further defines the concept of "Corporate Social Responsibility", i.e., the economic, legal, ethical and charitable responsibilities that the banking institutions shall bear to their shareholders, employees, consumers, business partners, government, communities and other interested parties and for enhancing the sustainable development of society and the environment. [31] Article 3 also elaborates that the CSR of banking institutions shall at least cover the following aspects: economic responsibility, which requires the institutions to maintain a fair, safe and stable competition order and use high-quality professional operations to continually create economic values for the country, shareholders, employees, customers and the general public, conditioned upon abiding by the law; social responsibility, which requires the institutions to follow the business operation notions meeting the requirements of social ethics and public welfare, actively protect the public interests of consumers, employees and community members, advocate charitable responsibility, actively dedicate themselves to activities for the public good, build up social harmony and promote social development; and environmental responsibility, which requires the institutions to support the industrial policies and environmental protection policies of the state, save resources, protect and recover the ecological environment and support the sustainable development of the society.[32]

The above legal requirements which aim to promote a scientific development and enhance the harmonious and sustainable growth of the economy, society and the environment, have significantly encouraged responsible business in the banking industry. The Shanghai Pudong Development Bank voluntarily published the first corporate social responsibility report in 2006; in 2008 the American Chamber of Commerce in Shanghai awarded this bank A Special

29 China Banking Association, issued date 12 January 2009, effective date: 12 January 2009.

30 ibid, Article 2.
31 ibid, Article 3.
32 ibid, Article 3.

Recognition for Exceptional and Longstanding CSR Achievements from 2006-2008.[33] Another example is the Industrial Bank which became China's first “Equator Bank” in October 2008, and took the lead in the promotion of rational and sustainable development.[34] Industrial and Commercial Bank of China has been awarded the Best Social Responsibility Organization of the Year and Best Green Finance of the Year by the CBA in 2011.[35] In 2011 the CBRC also actively communicated with the United Nations Environment Program Finance Initiative and IFC's Environment and Social Development Department.[36]

It can be seen from the above analysis that the CSR has been steadily addressed by the Chinese banking industry. However, it must be admitted that, there are some cases in China where the fulfillment of CSR has been questioned; in particular, with regards to issuing loans to projects which may have a high environmental risk. The CSR is not merely a legal responsibility, but also an ethical one requiring co-operation from different sectors. For the next step for further developing the corporate social responsibility in China, a focus on green credit and financial inclusion is needed. A further development shall balance shareholder value and public welfare. Appropriate facilitation shall be given to the enhancement of the financial service in rural branches, in order to ensure customers in the remote rural areas have access to the services. The CBRC is currently drafting of Administrative Measure of Implementing Corporate Social Responsibility by the Banking Institutions; CSR will be included in the supervision system.[37] A new regime is under construction.

17.6 Corporate Disclosure

20. See Shanghai Pudong Development Bank website, http://www.spdb.com.cn/docpage/c511/200605/0519_511_13975.aspx, last accessed: 5 April 2013.

[34] “IB Becomes the First Chinese Bank to Adopt the Equator Principles”. Industrial Bank was established in August 1988 and headquartered in Fuzhou City. See http://www.cib.com.cn/netbank/en/Sustainability/Sustainable_Finance_News/20081031_1.html, last accessed: 4 April 2013.

[35] See ICBC website, http://www.icbc-ltd.com/ICBCLtd/About%20Us/Awards%20%20Rating/2011/, last accessed; 4 April 2013.

[36] CBRC, 2011 Annual Report, Part 7.

[37] “Conference on Corporate Social Responsibility of Banking Industry and Central Stated Owned Enterprises Held in Beijing, Representatives from Global Financial Institution Discussed the Corporate Social Responsibility (Yinhangye yu Yangqi Shehui Zeren Yantaohui zai Jing Zhaokai Quanqiu Jinrong Daibiao Gongshang Qiye Shehui Zeren)”, *Legal Daily (Fazhi Ribao),* 10 January 2012.

Corporate disclosure is one of the core issues of corporate governance. This area has been significantly improved in China along with the development of the Chinese financial system. George A. Akerlof discussed the theory of information asymmetry, which occurs when the seller has more information about a product than the buyer.[38] Under this theory, the banks possess more information than the general public, bank customers, and other stakeholders. It is necessary to have adequate information available which aims to eliminate this imbalance. Therefore, a commercial bank should be adequately transparent to its shareholders, depositors, stakeholders and other market participants, in order to maintain financial stability.

In practice, banks should disclose relevant and valuable information that supports the key areas of corporate governance. This issue has been addressed in different economies and internationally. The Organization for Economic Cooperation and Development (OECD) Principles of Corporate Governance established the general guidelines for disclosure and transparency. The 1999 Principles set down a framework for the disclosure issue; for instance, the basic contents of disclosure: the financial and operating results, the company objectives, foreseeable risk factor, etc.[39] However, it has been argued that the follow up work to implement the principles was confined to the developing and transitional countries.[40] The Principles of 2004 have improved the regime, these set down the disclosure principles: the basic contents of disclosure; information should be prepared and disclosed to high quality standards; an annual audit should be conducted by an independent, competent and qualified auditor; external auditors should be accountable to the shareholders and owe a duty to the company to exercise due professional care; disseminated information should be provided equally, in a timely and be cost efficient manner; corporate governance framework should be complemented by an effective approach designed to ensure that there are no material conflicts of interest.[41]

Today the general disclosure requirements for commercial banks should not be mainly concentrated on the asset side, detailed organizational and governance structures, operational

[38] George A. Akerlof (1970), "The Market for 'Lemons': Quality Uncertainty and the Market Mechanism", *The Quarterly Journal of Economics*, Vol. 84, No. 3, p. 488-500.
[39] The OECD Principles of Corporate Governance 1999.
[40] TUAC Secretariat (October 2004), The OECD Principles of Corporate Governance, An evolution of 2004 Review, www.tuac.org.
[41] The OECD Principles of Corporate Governance 2004.

policies, ownership, voting rights, and related party transactions should be included. The lessons learned from the latest financial crisis have put more focus on transparency and disclosure. To improve risk management and governance and strengthen transparency and disclosure regime has become more important. In 2011 the Basel Committee on Banking Supervision issued the Pillar 3 Disclosure Requirements for Remuneration to support an effective market discipline, to allow market participants to assess the quality of a bank's compensation practices, and to contribute to promote a greater convergence and consistency of disclosure on remuneration.[42]

The Chinese disclosure regime for the commercial banks has been set up under different legal documents. Interim Measures for the Information Disclosure of Commercial Banks established earlier requirements.[43] It required that commercial banks had to disclose information in the light of the principle of truth, accuracy, completeness, and comparability.[44] As for content, it required that the commercial banks should disclose their financial statements, all kinds of risk management conditions, corporate governance, and annual major matters.[45] Furthermore, the commercial bank's financial statements should consist of accounting statements, notes to accounting statements, and financial situation statements.[46] Moreover, the accounting statements disclosed by a commercial bank should consist of the statement of assets and liabilities, the profit statement (profit and loss statement), the statement of owners' equities change, and other relevant supplementary statements.[47] As can be seen from these requirements, the document built the fundamental structure of the disclosure regime for commercial banks.

Measures for the Information Disclosure of Commercial Banks further enhanced the disclosure requirements.[48] It requires the commercial banks to disclose credit risk status, liquidity risk status, market risk status, operating risk status etc.[49] Furthermore, each type of risk shall be illustrated by commercial banks in four aspects: risk monitoring ability of the board of directors and senior management; policy and procedure of risk management; system of risk measurement,

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[42] See BIS website, http://www.bis.org/publ/bcbs197.htm. Last accessed: 12 May 2013.
[43] PBCO, [2002] No. 6, promulgated date: 15 May 2002, repealed on 3 July 2007.
[44] ibid, Article 5.
[45] ibid, Article 8.
[46] ibid, Article 9.
[47] ibid, Article 10.
[48] CBRC, [2007] No. 7, promulgated date: 3 July 2007.
[49] ibid, Article 19.

inspection, and information management; and information of internal controls and overall audit.[50] Regarding the corporate governance, the Measures states that, the general meeting of shareholders during the year, structure of the board of directors and its working performance, structure of the board of supervisors and its working performance, structure of the senior management and members' profiles, and the layout of bank departments and branches shall be disclosed; meanwhile, the work of independent directors shall be separately disclosed by commercial banks.[51] Furthermore, the Measures requires that at least the following contents shall be included in the annual material events disclosed by commercial banks: the names of the ten major shareholders and changes thereof within the report period; any increase or decrease of registered capital, division or merger; and other important information that should be known to the general public.[52]

It should be noted that the financial regulators in China adopt a mandatory disclosure system in different dimensions for the listed companies; for instance, in terms of internal control. Compilation Rules for Information Disclosure by Companies Offering Securities to the Public No.26 - Specific Provisions on Information Disclosure by Commercial Banks set out the requirements for the listed commercial banks, which they are required to comply with, in addition to the provisions set by the China Securities Regulatory Commission on information disclosure concerning the relevant periodic reports, interim reports, etc.[53] According to Article 3 in a periodic report a commercial bank shall disclose its main accounting data over the previous three years by the end of the reporting period, including the total assets and their structure, total liabilities and their structure, total deposits and their structure, total loans and their structure, inter-bank borrowings, net capital and its structure (including core capital and subsidiary capital), net risk-weighted assets, and loan loss reserves.[54] Article 4 requires that in a periodic report a commercial bank shall disclose the main financial indexes over the previous three years by the end of the reporting period, including the asset profit margins, the capital profit margins, the capital adequacy, the core capital adequacy, the non-performing loans ratio, the ratio of deposits to loans, the liquidity ratio, the loan ratio of a single top client, the loan ratio of the top ten

[50] ibid, Article 20.
[51] ibid, Article 21.
[52] ibid, Article 22.
[53] Promulgated date:
[54] ibid, Article 3.

clients, the migration ratio of pass loans, the migration ratio of OAEM loans, the migration ratio of substandard loans, the migration ratio of doubtful loans, the provisioning coverage ratio, and the cost-income ratio.[55]

Risk disclosure is an important part for promoting the good corporate governance. Under this document a commercial bank is required to disclose the following information in a periodic report: credit risk status, liquidity risk status, market risk status, operating risk status etc.[56] The Rules also requires that in the event of any change of the risk status of a commercial bank that has a significant effect on the business operation or profitability of the company, the commercial bank shall timely make an announcement. [57]

It can be seen from the above analysis that the disclosure regime for the Chinese banking institutions has been primarily established and performs important roles. On the other hand, after the recent financial crisis regulatory structure has been enhanced; for instance, risk management has been put in a highly important position. In 2010 the Basel Committee on Banking Supervision issued the Principles for Enhancing Corporate Governance in the banking sector.[58] These principles draw on experiences from earlier lessons and are intended to assist banking organizations in enhancing their corporate governance frameworks and assist financial supervisors in supervising the banking institutions. The principles revised previous guidance and focus on the areas such as board practices, senior management, risk management and internal controls, compensation, complex or opaque corporate structures, and disclosure and transparency. Together with the improvement of the Chinese banking industry the Chinese banking regulators may base on the latest development and international best practices, design and adopt a new set of principles.

17.7 **Conclusion**

[55] ibid, Article 4.
[56] ibid, Article 16.
[57] ibid, Artilce 25.
[58] Issuing date: 4 October 2010.

In the last 30 years, the Chinese banking industry has made rapid progress. Nevertheless, some problems remain, which mainly concentrate on: a limited degree of marketization, low competitiveness of the industry, imbalance of the development of different banking groups and a weak rural banking system. Focusing on the corporate governance, internal control, risk management, and transparency should be further improved and enhanced.

It can be seen in the paper, that with the gradual improvement of the socialist market economy and the deepening of the economic reform, the corporate governance of the banking industry is being further enhanced. Various approaches have been introduced; for instance, reforming the ownership structure, defining the concept of corporate governance, promoting corporate social responsibility and enhancing the information disclosure regime. Nevertheless, the establishment of a framework is not of itself sufficient. Importantly, to fulfill the legal requirements, a strong enforcement system and compliance culture is needed. Another important issue is that the Chinese banking industry should aim towards the long term development and combine their local specification with international best practices.

17.8 References

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