

Alibaba and the Rise of Law-Proof Insiders

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10th Emerging Market Finance Conference
Mumbai, INDIA, December 12-14, 2019

Praises

- Paper raises three intriguing questions using Alibaba as the reference
 - ✓ CG rules seem to emphasize substance without much regard for enforcement when it comes to certain types of firms
 - ✓ CG rules have an inherent inequality in the treatment of domestic and foreign firms
 - with respect to disclosure and compliance requirement
 - with respect to ability of enforcement
 - ✓ Listing may not be a signal for bonding with higher CG standards but an effort to escape them
 - one needs to be watchful of foreign firms trying to list in domestic markets
- The paper provides a microscopic look
 - ✓ into ownership and governance structure of Alibaba
 - ✓ of the relevant US corporate and security laws governing listed firms
 - ✓ of facts related to enforcement → rules on the ground → lot to learn

Ability and incentives of CS to execute value reducing actions

- Value reducing actions
 - ✓ Unending dissipation
 - ✓ Rapacious tunnelling
- Ability to execute these actions
 - ✓ Action (a) requires controlling shareholders to be non-significant owners
 - thus other shareholders should be able to remove them
 - ✓ Action (b) requires pyramidal ownership structures
 - not prevalent in the US, but may be relevant for PRC
- Incentive of controlling shareholders not to execute value reducing actions
 - ✓ Large incentives to grow as they can amass more wealth through this than by simple stealing → why do these firms survive, why people subscribe to them
 - ✓ Reputation, especially for group firms

Law-proof insiders: which events?

- Laws for prosecution → extreme events
 - ✓ Misappropriation of assets
 - ✓ Frauds
 - ✓ Bankruptcy and distribution of assets

These may be difficult to legally pursue due to dual or multiple jurisdictions

- Laws for “daily” governance
 - ✓ Disclosure
 - Accounting rules
 - Listing rules
 - IPO rules
 - ✓ Market discipline
 - Voting through the feet
 - No new capital inflows

Troublesome observations of US Laws

- Disclosure and filing laws are diluted for foreign private issuers (FPI) like Alibaba
 - ✓ Financial information, Conflict information, Insider information
 - ✓ PCAOB requires home country's (PRC) approval for periodic scrutiny of FPIs (Alibaba)
 - ✓ Domestic issuers must file interim quarterly reports (10-Q) in specified formats while and FPI can furnish only a subset of this information → only annual report can be filed
 - ✓ Form 20-F exemptions for FPI with respect to declaration of material conflicts, and declaration of share ownership
 - ✓ IPO's rules are same though

How to design “good” laws?: substance vis-à-vis enforcement

- Should we frame the “first-best” laws and then try to enforce them, or
- Should we endogenize enforceability in the framing of the law itself → the “second-best” option
 - will this lead to design of laws which needs to be updated continuously
 - How can we harmonize cross border laws when enforcement varies across countries
- Challenging to design laws for specific structures (Alibaba and PRC),
 - ✓ structure evolve in response to laws, so presumably laws have to be designed at an absolute scale
 - ✓ laws which can handle specific structures may be in-optimal for others,
 - Type 1 error versus Type 2 errors → why do the Delaware Law and Cayman Law co-exist?
- Does the solution lie in having the “first-best” law, with inter-governmental cooperation, standardized disclosures, investor education, and market discipline

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- Enjoyed reading the paper and hope to see more debate on this issue