

Compare the Disclosures of U.S.-listed Chinese Companies with U.S.-based Companies

Jiongnan Wu^{1,a,*}, Fan Fei^{2,b}, Xutong Zhu^{3,c}, Weihang Lin^{4,d}

¹*Gabelli School of Business, Fordham-Rose Hill, New York, 10458, America*

²*Oakville Trafalgar High School, Oakville, L6J3L6, Canada*

³*University of California San Diego, La Jolla, CA, 92093, USA*

⁴*Rensselaer Polytechnic Institute, Troy, NY 12180, USA*

a. jwu297@fordham.edu, b. feryfan95@gmail.com, c. zxtcjs@gmail.com, d linw8@rpi.edu

**corresponding author*

Abstract: The purpose of this study is to compare the differences in disclosure quality between Chinese and American companies listed in the United States. Despite the fact that Chinese companies listed on a U.S. stock exchange are required to adhere to the same disclosure and financial reporting regulations as U.S. companies listed on that exchange, variations between the two persist. Consequently, this study seeks to explore and compare the specific disparities in disclosure quality between Chinese companies listed in the U.S. and American companies. The "use of proceeds" section of the initial IPO prospectus for both American and Chinese companies will be employed to assess the specificity of disclosure quality. Statistical data sampling and analysis will be conducted to compare their specificity of disclosure. Finally, a T-test will be employed to compare and contrast the results. Based on our research findings, it can be concluded that Chinese companies listed in the U.S. exhibit a significantly higher overall quality of information disclosure compared to domestically listed U.S. companies.

Keywords: prospectus, use of proceed, net of proceed, specificity

1. Introduction

In recent years, with the rapid development of the global economy, an increasing number of Chinese companies have opted to list on American stock exchanges. Although Chinese companies are also required to comply with the same information disclosure and financial reporting regulations as American companies, significant differences in disclosure practices persist between the two types of firms. These disparities may stem from a variety of factors, including divergent policy frameworks, cultural variations, and other factors.

Previous studies have shown that companies that voluntarily disclose information can reduce information asymmetry and improve the efficiency of capital markets [1]. It follows that higher-quality disclosure can directly impact a firm's market performance. However, prior research has primarily focused on the competition among domestic American companies. With the increasing number of multinational companies choosing to list in the United States, their disclosure quality differs significantly from domestically listed companies. These companies not only have to meet US disclosure requirements but also need to comply with the laws and regulations of their home countries.

These potential factors can create information asymmetry for investors in the financial disclosures of many multinational companies in the US market [2]. This study aims to further explore the differences in the disclosure quality of Chinese and American companies listed in the United States. Specifically, we will focus on the use of net proceeds in the prospectuses of these companies' first IPOs.

We compared the differences in information disclosure between listed companies in China and the United States. We explored the specific manifestations of these differences through data statistics and analysis. We adopted the measurement method of Leone, Rock, and Willenborg, obtaining the initial public offering (IPO) prospectus of each company from the public data of the Securities and Exchange Commission (SEC) and using the "use of Proceeds" section as a specific indicator to measure the quality of information disclosure [3]. Since the "use of Proceeds" section can inform investors how the company will use the net proceeds obtained, it is an essential indicator for evaluating the quality of a company's information disclosure. Furthermore, when selecting company samples, we made efforts to select companies with similar scales and industries to reduce the interference factors caused by characteristics such as company size and industry. Finally, we will use the T-test to analyze the results in order to compare further and clarify the differences in the information disclosure of listed companies in China and the United States.

In this study, we initially predicted that U.S. companies would exhibit the same level of quality disclosure as Chinese companies. However, upon comparing the data, we discovered that the majority of American companies had very low specificity in their disclosure of the use of proceeds, with some companies even reporting zero exposure. Only a few companies met our expectations. Conversely, most Chinese companies far exceeded our expectations in terms of disclosure performance. They provided clear statements regarding the use of net proceeds and the expected use ratio. Furthermore, our research results indicate that Chinese companies generally outperformed American companies in disclosing the use of capital in IPO prospectuses. Overall, our findings suggest that disclosures by firms vary in the context of cross-border comparisons and underscore the need for further research to better understand the underlying reasons for these differences. Such research can provide investors with a more reliable measure of the market.

2. Literature Review

High-quality financial disclosures are an important part of financial reporting. By comparing the disclosure specificities of several U.S.-based and U.S.-listed Chinese companies, we conclude that accurate and comprehensive financial disclosure is critical for companies to make informed decisions and for stakeholders to assess the company's financial condition. However, it is impossible for companies to disclose all information, so companies need to consider market valuations and competition when disclosing material information. Therefore, partial financial disclosure is recommended as the ideal strategy.

Transparency is one of the key benefits of high-quality financial disclosures. Transparency in financial disclosures assists with promoting accountability, as stakeholders can hold companies accountable for any discrepancies or issues that arise. High-quality financial disclosures also ensure that businesses follow all applicable laws and accounting guidelines. Publicly traded companies are accountable to their shareholders and the broader public. Companies can prove their adherence to pertinent rules and regulations by presenting accurate and thorough financial information, which is essential for maintaining public trust and confidence in the financial markets. Investor trust is boosted by this compliance since they are assured that the business is acting morally and in accordance with predetermined standards. High-quality financial disclosure helps to prevent fraudulent activities as well; disclosure requirements force companies to provide accurate and complete financial information, which reduces the likelihood of fraudulent activities. By disclosing financial information, companies are subject to greater scrutiny and regulatory oversight, which helps to detect and prevent fraudulent

activities. This was demonstrated in the Enron scandal, where the lack of financial disclosure allowed the company to engage in accounting fraud, leading to its collapse [1]. It also resulted in enacting the Sarbanes-Oxley Act, which increased the accountability and transparency of public companies—in the case of Lehman Brothers, the company's lack of high-quality financial disclosures and accounting irregularities contributed to its collapse during the 2008 financial crisis. The scandal led to a loss of investor confidence and triggered a global recession. However, the lack of financial disclosure allowed the company to hide its activities, resulting in significant financial losses for the company and a decrease in consumer confidence.

Moreover, high-quality financial disclosures and increased specificity mean that there will be less asymmetry in the information about the company. Thus indicating that such disclosures are economically beneficial to the firm. In Jensen and Meckling, it was suggested that financial disclosure might allow potential investors to assess the effectiveness of management, performance, and fulfillment [4]. Additionally, through Sengupta's study, it was found that companies with higher disclosure quality ratings reduced the cost of debt and that financial disclosure is critical in situations of high market uncertainty [5]. Research suggests that increased disclosure can also reduce uncertainty about a firm's value. High levels of prospectus disclosure can reduce IPO underpricing [6]. Risk management is another crucial benefit of high-quality financial disclosures. By providing a detailed breakdown of a company's financial performance, stakeholders can identify areas of strength and weakness and take appropriate steps to mitigate risks and exploit opportunities. Disclosure and its relationship to the cost of equity capital is examined in Botosan, where the authors report that a firm's cost of equity capital decreases with increased disclosure and that the type of disclosure is also important, and show that increased financial disclosure reduces a firm's cost of capital [7].

3. Data Analysis

The "Use of Proceeds" section of the initial IPO prospectus was used to assess the specific differences in disclosure quality between US-listed Chinese companies and US companies. The level of specificity can be found within the use-of-proceed section by specifying what proportion of proceeds to use for certain purposes. Specificity can be measured from two main data, fraction of company IPO proceeds designated for debt repayment and for purposes other than debt repayment. The non-debt repayment includes fraction of expansion or M&A, R&D or product development, distribution to pre-IPO shareholders, advertising and marketing, working capital uses (other than debt), or other uses. And the level of specificity can be ranged from 0% (rare disclosure information on "Use of Proceeds") to 100% (outstanding disclosure information on "Use of Proceeds").

For data selection, a total of 260 Chinese companies listed in the US that are filed in the SEC are selected. And the companies are grouped into sectors defined by the Global Industry Classification Standards. There are 11 sectors in total—energy, materials, industrials, consumer discretionary, consumer staples, health care, financials, information technology, telecommunication services, utilities, and real estate. Then, each Chinese company listed in the US is paired with an equivalent US-based public company in terms of the same sector and market capitalization. In addition, factors such as similar industry, company structure, type of business, product, and size were taken into account. After careful consideration and selection, this paper is going to analyze 187 pairs excluding companies that fail to match with a corresponding US-based company and penny stocks that provide insufficient information.

A sample of the result can be seen on Table 1. Specificity-Debt stands for a fraction of company IPO proceeds for which amounts are designated for debt repayment. Specificity-NonDebt stands for a fraction of company IPO proceeds for which amounts are designated for other purposes than debt repayment. Specificity-NonDebt includes Specificity-ExpAcq, Specificity-R&D, Specificity-Shrhlds, Specificity-AMPS, Specificity-WC, Specificity-Other. Specificity-ExpAcq stands for a fraction of

company IPO proceeds for which amounts are designated for expansion or mergers and acquisitions. Specificity-R&D stands for a fraction of company IPO proceeds, for which amounts are designated for research or product development. Specificity-Shrhkds stands for a fraction of company IPO proceeds for which amounts are designated for distribution to pre-IPO shareholders. Specificity-AMPS stands for a fraction of company IPO proceeds, for which amounts are designated for advertising, marketing, promotions, or sales. Specificity-WC stands for a fraction of company IPO proceeds for which amounts are designated for particular working capital uses. Specificity-other stands for a fraction of company IPO proceeds for which amounts are designated for general purposes other than the aforementioned designations. N/A indicates that either the use of the proceeds section is not presented or specified in the IPO prospectus as it was not required for companies filed before the year 2000, or the IPO prospectus (424B4 or S-1 form) cannot be found.

Table 1 indicates that the overall specificity of Chinese companies' use-of-proceed is higher than that of the US-based companies [8,9]. Also, Chinese companies have specified the fractions of proceed purposes, thus ruling out the possibility that the company might say, 'all (100%) of the proceeds is going to be used for general purposes', which is also a low-level of disclosure.

Table 1: A Sample (telecommunication service sector) of a full list of Chinese companies listed in the US and corresponding US companies and specificity tests.

Company	Specificity-Debt	Specificity-NonDebt	Specificity-ExpAcq	Specificity-R&D	Specificity-Shrhlds	Specificity-AMPS	Specificity-WC	Specificity-Other	Specificity in total
Chinese company-communication services									
Blue Hat Interactive Entertainment Technology		80.00 %		40.00 %		40.00 %			80.00 %
Kanzhun Limited		90.00 %		40.00 %		35.00 %	15.00 %		90.00 %
Pop Culture Group		85.00 %	21.00 %	21.00 %		14.00 %	29.00 %		85.00 %
Douyu		80.00 %	35.00 %	30.00 %		15.00 %			80.00 %
Phoenix New Media Ltd.		97.00 %	44.00 %	31.00 %		22.00 %			97.00 %
Greenpro Capital Corp.		100.00 %		57.00 %		14.00 %	15.00 %	14.00 %	100.00 %
Zhihu		90.00 %	35.00 %	25.00 %			30.00 %		90.00 %
HUYA Inc.		85.00 %	35.00 %	35.00 %		15.00 %			85.00 %
iClick Interactive Asia Group Ltd.		69.00 %		47.00 %		22.00 %			69.00 %
iQIYI Inc.		110.00 %	10.00 %	50.00 %			40.00 %	10.00 %	100.00 %
9F Group		90.00 %	45.00 %	20.00 %		25.00 %			90.00 %

Table 1: (continued).

36Kr	100.00 %	40.00 %	15.00 %		25.00 %	20.00 %	100.00 %
Hello Group Inc.	63.00 %		28.00 %	35.00 %			
Qutoutiao	67.00 %	40.00 %	27.00 %				67.00 %
Sohu.com Ltd.	0.00%						N/A
SoYoung Technology	80.00 %	20.00 %	30.00 %	20.00 %		10.00 %	80.00 %
Tencent Music Entertainment Group	100.00 %	15.00 %	30.00 %	15.00 %	40.00 %		100.00 %
JOYY Inc.	63.00 %	21.00 %	21.00 %	21.00 %			63.00 %
US company-communication services							
Snap Inc.	8.00%					8.00%	8.00%
ZipRecruiter Inc.							0.00%
Funko Inc.	100.00 %					100.00 %	100.00 %
DraftKings Inc.							N/A
Gray Television							N/A
Apollo Global Management							0.00%
Roku Inc.							0.00%
Sea Ltd.							0.00%
Trade Desk Inc.	5.00%					5.00%	5.00%
LendingClub Corp.							0.00%
Motley Fool Holdings Inc.							N/A
Pinterest Inc.							0.00%
Teladoc Health Inc.							0.00%
Spotify Technology							0.00%
Twitter Inc							N/A
ViacomCBS Inc.							0.00%

Then a t-test would be used to determine whether there is a significant difference between the means of specificity of two groups to test the hypothesis of whether Chinese companies listed in US and US-based public companies have different disclosure levels. The t-test is appropriate in this context because it is a simple and widely used statistical test that is appropriate for comparing the means of two groups. Additionally, the t-test assumes that the data is normally distributed and that the variances of the two groups being compared are roughly equal. If these assumptions are met, the t-test can provide a reliable measure of whether the observed difference in means is statistically significant, meaning that it is unlikely to be due to chance or random error. Also, two-sample t-test assuming unequal variances will be used: this test is used to determine whether the means of two independent samples are significantly different assuming unequal variances.

Table 2: Two-sample t-test assuming unequal variances of all Chinese companies listed in US and corresponding US companies.

	Chinese	US
Mean	0.75413548	0.1295952
Std	0.13308509	0.1043286
Observation	62	62
Hypo	0	
df	120	
t Stat	10.0926092	
p one-tail	5.145E-18	
t one-tail margin	1.6576509	
p two-tail	1.029E-17	
t two-tail margin	1.9799304	

Overall, by conducting a t-test, a p-value of $< 5\%$ rejects the null hypothesis and concludes that the difference between the specificity of use-of-proceed of Chinese companies listed in the US and specificity of use-of-proceed of US-based public companies is statistically significant. Same result can be found within each sector (table 2-7). Conclusively, a large proportion of US companies provided vague or no disclosure regarding the use of proceeds, with only a few companies meeting our expectations. In contrast, Chinese companies displayed a higher level of information disclosure, providing specific details on the use of net proceeds and expected proportions of use. Ultimately, our research findings suggest that Chinese companies generally exceed US companies in disclosing the use of proceeds in their IPO prospectuses.

Table 3: Two-sample t-test assuming unequal variances of all Chinese companies listed in US and corresponding US companies in telecommunication service sector.

	Chinese	US
Mean	0.88833333	0.09416667
Std	0.00930606	0.0820447
Observation	12	12
Hypo	0	
df	13	
t Stat	9.10219638	
p one-tail	2.649E-07	
t one-tail margin	1.7709334	
p two-tail	5.298E-07	
t two-tail margin	2.16036866	

Table 4: Two-sample t-test assuming unequal variances of all Chinese companies listed in US and corresponding US companies in customer discretionary sector.

	Chinese	US
Mean	0.68395	0.17140313
Std	0.19970154	0.13806126
Observation	32	32
Hypo	0	
df	60	
t Stat	4.98887558	
p one-tail	2.7538E-06	
t one-tail margin	1.67064886	
p two-tail	5.5075E-06	
t two-tail margin	2.00029782	

Table 5: Two-sample t-test assuming unequal variances of all Chinese companies listed in US and corresponding US companies in energy sector.

	Chinese	US
Mean	0.65666667	0.29333333
Std	0.17543333	0.06943333
Observation	3	3
Hypo	0	
df	3	
t Stat	1.27174792	
p one-tail	0.14654966	
t one-tail margin	2.35336343	
p two-tail	0.29309933	
t two-tail margin	3.18244631	

Table 6: Two-sample t-test assuming unequal variances of all Chinese companies listed in US and corresponding US companies in consumer staple sector.

	Chinese	US
Mean	0.87	0.284
Std	0.027	0.19328
Observation	5	5
Hypo	0	
df	5	
t Stat	2.79186931	
p one-tail	0.01918004	
t one-tail margin	2.01504837	
p two-tail	0.03836008	
t two-tail margin	2.57058184	

Table 7: Two-sample t-test assuming unequal variances of all Chinese companies listed in US and corresponding US companies in financials sector.

	Chinese	US
Mean	0.4	0
Std	0.26666667	0
Observation	10	10
Hypo	0	
df	9	
t Stat	2.44948974	
p one-tail	0.01839375	
t one-tail margin	1.83311293	
p two-tail	0.0367875	
t two-tail margin	2.26215716	

4. Fact that Causes the Difference

Several facts might have contributed to the differences in disclosure quality during the IPO period for US and Chinese Companies. We hypothesize three main factors.

First, US companies disclose usable information in their annual report. In contrast, Chinese companies rarely do so, leading to a situation in which further information from Chinese companies is needed during an IPO for investors to have a wider lens into the financial and management status. This is compared to the US, where companies abide by strict corporate laws with Form 10-K, Form 8-K, etc. [10]. that companies need to fill, China Company Law is still an ongoing process and sometimes fails to impose strict regulations on companies' annual reports. A 2022 article analyzed hundreds of annual reports of Chinese companies [11]. It concluded that Chinese companies engaged in risk-related activities would provide a narrow and general statement of their activities in their annual report to meet the annual report requirement without disclosing the actual situation of the companies' financial status and the risks they are facing. Chaowang Ren and Xiaofen Lu also concluded in their linguistic article that the language used in annual reports generated by Chinese companies tends to be less explicit [12]. Therefore, it would be easier for management to hide specific facts or actual events from the general public. In addition, the China Company Act, for a long time, has neglected the right of minor shareholders to fully understand the financial, management, and risk-related situations of a company they are investing, so Feinerman called it a potential new hope for corporate governance in China when China eventually tried to address this problem in 2007 [13]. For investors, especially new investors, since they cannot know how a Chinese company is doing by reading through all the annual, semi-annual, or quarterly reports, there must be another way for Chinese companies to disclose the necessary information. To make up for the lack of explicit and readable information in the annual report, a higher quality of information disclosure is needed during the IPO period for Chinese companies.

Moreover, the US company act also requires companies to disclose details regarding talks regarding acquisition and merger, whereas, in China, company acquisition and merger are typically only publicly known until the acquisition is made. Of course, the business insiders and major shareholders would know, but minor shareholders and potential investors often would only know once the news media reported the deal. For example, Elon Musk's acquisition of Twitter was in the news long before the deal was settled when it was still in the review period. However, the recent acquisition of LELECHA, a once trendy bubble tea brand, by NAIKUE, one of China's top three bubble tea brands, was only reported after the acquisition was approved. This lack of transparency in

essential business activities also leads to the higher disclosure requirement during the IPO period if Chinese companies want to go public in the US.

In addition, the possibility of the Chinese government playing a role in business decisions could also have leveled up the disclosure requirement for Chinese companies during the IPO. As is widely known, China's government has a higher administrative power over companies than the US government. Also, it is common for the Chinese government to hold some shares in some companies to ensure the stability of prices and its country's safety. It could be a potential risk for potential minor investors. Without knowing how the previous money was spent and without knowing what the potential influences of the business decisions are, investors can hardly be sure that the money that they intended to invest in this particular company would not be used for some other purposes or whether political influence, rather than considerations from business scope, would affect their investment.

There sure are many other facts that may have led to the higher level of information disclosure of Chinese companies during the IPO period if they want to go public in the US compared to the level of disclosure quality those US-based companies need to achieve, including some subtle factors such as distrust or discrimination. However, those factors are impossible to visualize and exemplify, at this moment, not explicitly discussed.

5. Conclusion

Though going public in the US has become a popular choice among companies around the world, the IPO prospectuses for companies from companies based in different countries show wide discrepancies in the quality of information disclosure. In this article, we compared the differences in information disclosure between listed companies in China and the United States. Through careful analysis and validation, we conclude that Chinese companies in the US stock market are more likely to have a higher disclosure quality. Several factors might have led to this difference in disclosure quality, including Chinese companies' lack of transparency in annual reports and important business events and potential influence from China's national government. Further case studies comparing the disclosure qualities of annual reports from US companies and Chinese companies need to be conducted to validate our hypotheses about the gap in disclosure quality.

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