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Corporate Governance Deficiencies and Financial Risk Outbreaks under the Registration-Based IPO System: A Case Study of China Huarong Asset Management Co., Ltd.

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Abstract: *The full rollout of the registration-based initial public offering (IPO) system has advanced the market-oriented transformation of China's capital market, while imposing stricter requirements on the corporate governance quality and financial risk management capabilities of listed enterprises. Centered on information disclosure as its core regulatory principle, the registration-based system has amplified the negative spillover effects of corporate governance defects on the market, making financial risk prevention and control a core concern for both enterprises and regulators. Drawing on principal-agent theory and information asymmetry theory, this paper constructs an analytical framework illustrating how corporate governance shapes financial risk. Taking China Huarong Asset Management Co., Ltd. as a typical case, it systematically explores the internal and external drivers of financial risk outbreaks among financial enterprises within the registration-based IPO context. The findings reveal that internal governance failures — including dysfunctional board oversight, unchecked management power, and ineffective internal controls — constitute the root causes of risk accumulation. Aggressive expansion strategies and distorted business philosophies further accelerate risk materialization. Externally, the inherent high-risk nature of the asset management industry and an increasingly stringent regulatory environment jointly serve as major external triggers for risk outbreaks. On this basis, this paper proposes targeted governance countermeasures from enterprise-level and regulatory perspectives, offering practical references for improving the governance quality of listed firms and preventing systemic financial risks under the registration-based IPO system.*

Keywords: *Registration-Based IPO System; Corporate Governance; Financial Risk; Asset Management Industry; Internal Control; China Huarong*

1. Introduction

The registration-based IPO reform represents a landmark initiative to improve the market-oriented operational mechanism of China's capital market. Shifting from substantive review to information-disclosure-oriented supervision, the reform has lowered enterprises' listing thresholds and stimulated market vitality. It has also raised higher standards for the standardized operation of listed companies. Under the registration-based system, the authenticity, accuracy and completeness of corporate information disclosure directly determine the efficiency of market resource allocation and the protection of investor rights and interests. As the institutional foundation for standardizing enterprise operations and guaranteeing information quality, corporate governance has become a pivotal factor influencing enterprise stability and the sound development of capital markets.

For financial enterprises, especially large asset-management institutions, their high-leverage business models, strong interconnectedness, and complex transaction structures mean governance defects may not only trigger operational crises within individual firms but also propagate systemic risks across financial market networks. In recent years, financial risk incidents at several large financial enterprises have laid bare the severe consequences of governance failures, highlighting the urgency of strengthening corporate governance and risk prevention amid registration-based reform.

As a central state-owned financial asset management enterprise, China Huarong Asset Management Co., Ltd. (hereinafter referred to as "China Huarong") once achieved ultra-rapid expansion through

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diversified operations. It subsequently suffered massive financial risks and severe financial irregularities, emerging as a representative case of governance failure in China's financial sector. Taking China Huarong as the research subject, this paper conducts an in-depth analysis of the internal logic linking corporate governance deficiencies and financial risk outbreaks under the registration-based IPO system and puts forward corresponding improvement measures. This research carries important practical implications for promoting standardized governance among listed enterprises, refining financial risk prevention-and-control systems, and fostering stable, healthy development of capital markets under the registration-based framework.

2. Theoretical Framework

2.1 Core Concepts and Theoretical Foundations

Corporate governance refers to a set of institutional arrangements that balance rights and responsibilities among shareholders, the board of directors, management and other stakeholders. Its core objective is to mitigate principal-agent problems and restrain management opportunistic behavior. Sound corporate governance can effectively oversee business decisions, enhance accounting information quality, and reduce the likelihood of financial risk accumulation.

Financial risk denotes the potential for economic losses arising from various uncertainties embedded in corporate financing, investment and operational activities. For financial enterprises, financial risks are typically characterized by strong concealment, rapid transmission and devastating impacts. When internal governance breaks down, irrational managerial decisions and improper operations continuously build up latent risks, which eventually materialize in the form of huge losses or financial fraud.

From a theoretical standpoint, principal-agent theory posits that the separation of ownership and management gives rise to information asymmetry between shareholders and management. Where governance mechanisms are defective, management may pursue private interests at the expense of corporate value — for instance, pursuing blind expansion to expand power or manipulating financial statements to mask underperformance — directly elevating financial risks. Information asymmetry theory further explains that under conditions of information opacity, enterprise internal control failures cannot be detected promptly by external investors and regulators. This delays risk intervention and allows risk-related losses to escalate continuously.

2.2 Impact of the Registration-Based IPO System on Corporate Governance and Financial Risk

The registration-based IPO reform has exerted profound influences on the corporate governance and risk management of listed enterprises, mainly reflected in three dimensions.

First, the reform strengthens information-disclosure-based constraints on corporate governance. Under the registration-based regime, regulatory authorities focus on examining the adequacy and standardization of information disclosure. This compels enterprises to enhance transparency regarding governance structures and operational decisions. Governance flaws and latent risks are more likely to surface via information-disclosure channels, raising the costs of governance misconduct.

Second, the market-oriented listing mechanism intensifies competitive pressure on enterprises and may incentivize short-termist behavior. Access to convenient financing channels and market-valuation pressure may drive some firms to excessively pursue scale expansion while neglecting risk control. This creates a mismatch between expansion speed and governance capacity and builds up latent financial risks.

Third, the reform imposes higher compliance requirements on enterprises. As regulatory systems keep improving and penalties for violations rise, enterprises with governance defects face heightened legal and regulatory risks. Pre-existing non-standard operational patterns and risk-control loopholes become unsustainable under the new regulatory framework, and previously hidden risks gradually come to light.

2.3 Corporate Governance Defects and Financial Irregularities

Corporate governance deficiencies constitute key drivers of financial irregularities such as accounting fraud and misleading information disclosure. Where boards of directors fail to perform supervisory duties and internal-control mechanisms malfunction, management may manipulate financial data by fabricating revenues, concealing liabilities, and abusing accounting estimates to mask operational difficulties and

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meet performance expectations.

Financial irregularities severely distort accounting information quality and mislead investor decision-making. They also camouflage underlying operational risks, causing enterprises to miss optimal risk-disposal windows. For listed enterprises under the registration-based system, financial irregularities may trigger administrative penalties and civil compensation, erode corporate reputation and market value, and in severe cases, even lead to delisting. Consequently, improving corporate governance represents a fundamental approach to standardizing information disclosure and mitigating financial risks.

3. Case Background

China Huarong Asset Management Co., Ltd., founded in 1999, is one of China's four major state-owned financial asset management companies. Its core businesses cover non-performing asset management, banking, securities, trust, leasing and other financial segments. Following its Hong Kong IPO in 2015, China Huarong entered a phase of rapid expansion. During Lai Xiaomin's tenure as chairman, the company adopted an aggressive diversification strategy, continuously broadened its business scope, and established numerous non-financial subsidiaries and overseas entities[1].

Between 2015 and 2017, China Huarong experienced explosive scale growth: its total assets surged from HK$5.37 billion to HK$46.32 billion, with its business footprint spanning multiple domestic and overseas sectors. Nevertheless, behind this rapid expansion, internal governance and risk-control systems failed to keep pace with corporate development, giving rise to abundant high-risk businesses and non-standard operations.

In 2018, following the investigation into Lai Xiaomin, China Huarong's internal problems gradually came to light. The company's performance plummeted sharply, recording net losses of HK$1.48 billion and HK$2.86 billion in 2018 and 2019 respectively. Subsequent regulatory investigations confirmed that during its expansion phase, China Huarong committed serious financial violations including fabricated revenues, concealed liabilities, inappropriate accounting estimates, and irregular related-party transactions. This case sent major shockwaves across the financial industry and fully demonstrates how destructive corporate governance deficiencies can be for financial-enterprise operations. Against the backdrop of deepening registration-based IPO reform, this case delivers important lessons for improving governance standards among listed financial enterprises and preventing financial risks.

4. Analysis of the Causes of Financial Risk Outbreak in China Huarong

4.1 Internal Governance Root Causes

4.1.1 Dysfunctional Board of Directors and Failure of Supervisory Mechanism

As the core of corporate governance, the board of directors is tasked with supervising business decisions and balancing management power. In China Huarong's case, the board failed to fulfill its supervisory obligations, and internal checks-and-balances completely collapsed. Chairman power became overly concentrated; major investment decisions and business arrangements were largely dictated by individual senior executives without rigorous board deliberation and risk assessment.

Board supervisory failure directly caused the company to lose control over its development trajectory. The board did not effectively curb the aggressive off-core-business expansion strategy, nor did it build matching risk-supervision mechanisms for fast-growing non-financial and overseas businesses. Such governance defects pushed corporate operations away from standardized development and allowed risk factors to accumulate persistently.

4.1.2 Unconstrained Management Power and Aggressive Expansion Strategy

Under an insider-controlled governance structure, management prioritized scale growth and private interests over sustainable corporate development. During Lai Xiaomin's tenure, China Huarong pursued reckless, disorderly expansion, extensively venturing into non-financial sectors unrelated to its core asset-management business. The number of subsidiaries and the scale of overseas assets rose drastically. Such reckless and disorderly expansion has driven drastic shifts in the company's financial position. Table 1 below sets out China Huarong's key financial indicators for 2015–2019, which quantitatively reflect both the rapid scale surge in the expansion phase and the sharp performance reversal after risks came to light.

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Table 1: Key Financial Indicators of China Huarong (2015-2019), Unit: Thousand HKD.

Year	Total Assets	Total Liabilities	Net Profit	Operating Cash Flow	Investing Cash Flow	Financing Cash Flow
2015	5,369,271	4,634,116	(66,630)	(1,456,252)	53,261	4,260,387
2016	22,284,727	21,000,000	550,914	(10,465,613)	(5,016,283)	13,398,248
2017	46,324,769	42,226,195	1,005,643	(612,186)	(11,311,927)	14,346,512
2018	35,023,844	32,950,000	(1,482,139)	3,342,694	3,040,666	(7,412,196)
2019	22,930,000	20,320,000	(2,860,000)	8,678,673	1,568,105	9,687,662

Note: Based on China Huarong's annual financial statements (2015–2019). Parentheses denote negative figures.

As Table 1 illustrates, corporate total assets expanded more than seven-fold between 2015 and 2017, accompanied by simultaneous liability growth. This reckless expansion, outpacing risk-control capacity, drove sustained deterioration in asset quality and built up substantial impairment risks. When market conditions shifted, risks accumulated during expansion materialized collectively and inflicted massive corporate losses.

4.1.3 Ineffective Internal Control and Distorted Accounting Information

Robust internal controls constitute a critical institutional safeguard for enterprises to mitigate risks and guarantee the authenticity of financial information. In China Huarong's case, internal-control systems were severely impaired; control procedures governing major businesses, related-party transactions and accounting estimates became virtually ineffective.

To conceal risks accumulated during expansion and sustain superficial performance growth, the firm deployed multiple financial-manipulation tactics: fabricating revenues via sham transactions, hiding real liabilities through off-balance-sheet arrangements, and manipulating profits through inappropriate accounting estimates. Distorted accounting information misled external investors. It also prevented internal management from obtaining an accurate picture of actual risk conditions, further fuelling risk accumulation and eventual outbreak.

4.2 External Environmental Drivers

4.2.1 Inherent High-Risk Nature of the Asset Management Industry

The asset-management industry is inherently characterized by high leverage, intricate transaction structures and numerous connected entities, yielding substantially higher baseline risk levels than most ordinary industries. Asset-management firms engage in asset acquisition, restructuring, disposal and investment. Underlying-asset valuation carries considerable subjectivity, creating room for accounting manipulation and risk concealment.

Furthermore, the high interconnectedness of financial businesses means risks originating in one institution can spread rapidly across the financial system. As a full-license large financial institution, China Huarong maintained complex business ties with banks, securities firms, trusts and other entities. The interplay of industry-specific attributes and scale effects amplified the negative fallout of its governance defects and strengthened risk contagion.

4.2.2 Increasingly Stringent Regulatory Environment amid Registration-Based Reform

In recent years, alongside the steady advancement of the registration-based IPO reform, financial and accounting supervision across China has been continuously strengthened. In 2022, the Ministry of Finance issued the Measures for the Supervision and Inspection of Accounting Firms. In February 2023, the General Office of the CPC Central Committee and the General Office of the State Council jointly released the Opinions on Further Strengthening Financial and Accounting Supervision. Such policy releases mark notable improvements in the standardization and stringency of China's financial supervision[2].

Under stricter supervision, enterprises' previous room for regulatory arbitrage keeps shrinking. Non-standard operations and hidden risks formed during extensive development can no longer persist. China Huarong's financial irregularities were uncovered and investigated in this tightening-supervision context. This demonstrates that improving regulatory frameworks under registration-based reform imposes strong external constraints on corporate operations and significantly increase the probability of detecting and rectifying enterprise governance flaws and risk concerns[3].

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4.2.3 Insufficient External Market Discipline

Under the registration-based system, markets are expected to play a more prominent role in disciplining corporate governance. In practice, however, external-restraint mechanisms such as investor oversight and intermediary discipline have not been fully functional. On the one hand, the complexity of financial-enterprise operations makes it difficult for ordinary investors to accurately identify underlying governance defects and latent risks solely from public disclosures. On the other hand, corporate information disclosure lacks sufficient transparency; disclosures covering governance structures, risk exposures and other key items remain relatively vague, undermining market-supervision efficiency. Weak external market discipline prevented timely market-driven correction of governance defects and enabled continuous risk build-up.

5. Governance Approaches to Financial Risk under the Registration-Based IPO System

5.1 Improving Enterprises' Internal Governance Systems

Enterprises should start with optimizing board governance structures and reinforcing checks and balances: refine board composition, raise the share of professionally qualified independent directors to ensure they can perform supervisory duties autonomously, clarify the division of decision-making authority among the board of directors, board of supervisors and management, and formalize procedures for major decisions to prevent excessive concentration of power in individual hands. Building on this foundation, they need to strengthen internal control frameworks and implement full-process risk management by establishing comprehensive internal control systems covering all business workflows, tightening oversight of high-risk activities such as large-scale investments, related-party transactions and accounting estimates, conducting regular internal control evaluations and defect remediation, giving full play to internal audit functions, enhancing the independence of internal audit departments, and promptly identifying and correcting operational irregularities and latent risks. To complete the internal governance system, enterprises shall also refine performance evaluation mechanisms to steer management toward high-quality development, adopt appraisal systems that balance scale and quality as well as short-term and long-term interests, avoid over-incentivizing scale expansion, guide management to prioritize core business operations and risk control, strengthen accountability for flawed strategic decisions, and enforce lifelong accountability for major high-risk decisions.

5.2 Optimizing Development Strategies and Risk-Management Capabilities

First, maintain core-business orientation and refrain from blind diversified expansion. Enterprises shall clarify strategic positioning and concentrate resources on competitive core businesses. Cross-sector expansion must undergo adequate demonstration and risk assessment. For financial enterprises, risk control must serve as the precondition for business growth, ensuring expansion speed matches risk-management capacity.

Second, build comprehensive risk-management architectures. Establish multi-dimensional risk identification, assessment and early-warning mechanisms, dynamically monitor credit, market, liquidity and operational risks, and enhance emergency-response capacity for sudden risk events. Strengthen supervision over subsidiaries and overseas affiliates, implement penetrating risk-supervision frameworks, and curb cross-business-segment risk contagion.

Third, upgrade accounting-information quality and boost internal-external transparency. Strictly enforce accounting standards and standardize accounting treatments to guarantee the truthfulness, accuracy and completeness of financial information. Improve internal information-transmission channels so that decision-makers can obtain timely, accurate information on real-time operational and risk conditions.

5.3 Enhancing External Supervision and Market-Discipline Mechanisms

Primarily, refine registration-based-system information-disclosure standards. Further specify disclosure requirements for listed enterprises, and formulate more granular disclosure standards specifically for financial enterprises regarding governance structures, risk exposures, asset quality and other critical dimensions to improve operational transparency.

Subsequently, advance cross-department collaborative supervision. Build coordinated supervision

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mechanisms connecting financial regulators, fiscal authorities and securities regulators, strengthen information sharing and coordinated law-enforcement, and generate combined supervisory momentum. Step up supervision and inspection targeting key financial enterprises, and rigorously investigate financial irregularities and governance deficiencies.

Ultimately, raise violation costs and strengthen deterrence. Impose severe sanctions on firms and responsible individuals involved in accounting fraud and disclosure violations; improve civil-compensation regimes to lift legal costs for misconduct. Strict supervision and heavy penalties will push enterprises to standardize governance practices and proactively guard against financial risks.

6. Conclusion

Full implementation of the registration-based IPO system imposes higher standards of corporate governance and risk management for listed enterprises. Taking China Huarong as a case, this paper systematically analyzes the formation mechanism behind financial-risk outbreaks from internal-governance and external-environment perspectives. The study finds that board dysfunction, out-of-control management power and ineffective internal controls constitute internal root causes of risk accumulation. High-risk industry attributes, tightening regulatory regimes and insufficient external market discipline represent key external drivers for risk materialization.

Addressing financial-risk challenges under the registration-based IPO system requires multi-dimensional collaborative governance. At the firm level, enterprises ought to upgrade governance structures, reinforce internal controls, adhere to core-business-oriented strategies, and comprehensively strengthen risk-management competencies. At the regulatory level, authorities shall refine information-disclosure standards, promote collaborative supervision, and increase penalties for violations to build effective external-discipline mechanisms.

This paper relies on a single financial-enterprise case study, so the generalizability of its findings is limited. Future research could expand industry samples and adopt quantitative empirical methods to test the linkage between corporate governance and financial risks more comprehensively, generating richer empirical evidence for risk prevention and control under the registration-based IPO system. In the long run, continuous improvement in listed-enterprise corporate governance and sound financial-risk-prevention frameworks will unlock the capital-market functions of the registration-based system and foster high-quality development of China’s capital market.

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