US financial regulation

SEC targets US firms tied to suspected Chinese 'pump and dump' scams

Regulators put accounting and underwriting groups in crosshairs after FT report on billions of dollars lost

Investors have in recent months lost billions of dollars betting on small Nasdaq-listed Chinese stocks that were heavily promoted on social media © Eric Thayer/Reuters

George Steer in New York

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US regulators have targeted professional services firms alleged to have ties to suspected Chinese "pump and dump" scams as part of a fresh crackdown on cross-border fraud.

A task force launched last week would take aim at US-based "gatekeepers, particularly auditors and underwriters" that facilitate "potential securities law violations related to companies from foreign jurisdictions such as China", the Securities and Exchange Commission said.

The regulator's announcement came a day after Nasdaq, the world's second-biggest stock exchange, outlined plans to tighten trading standards to combat a surge of suspected pump and dumps, in which people with a vested interest artificially inflate a company's share price before abruptly selling their own stake.

"[Regulators] are going to crucify the bilge bracket," said a person familiar with the SEC's thinking, referring to the small white-collar groups that act as a "conduit" for Chinese companies applying to list in the US, as opposed to the so-called bulge bracket of prestigious banks and law firms.

"This is a national security issue, that's what the SEC's focus is," the person added.

Investors have in recent months lost billions of dollars betting on a handful of small Nasdaq-listed Chinese stocks that were heavily promoted on social media, the Financial Times reported last month.

Analysts and academics have long highlighted that foreign companies used as vehicles for pump and dump scams typically gain access to US markets thanks to a group of small underwriters, auditors and law firms.

A 2023 study conducted by independent researcher Stephen Walker and Ian Gow of the University of Melbourne found Nasdaq initial public offerings involving a specific cluster of underwriters and auditors were associated with "substantially worse returns" for investors.

"If you want to clean up Wall Street, go after the auditors and underwriters who make the [pump and dumps] possible," Walker told the FT on Tuesday. "Billions have been incinerated."

Others argued the SEC, which has shed hundreds of staff in recent months, may not be up to the job.

Bill Singer, a lawyer and former regulatory attorney at the American Stock Exchange, said: "If you really want to go after misconduct and crime in the securities industry, perhaps the least effective way of doing it is by creating a task force. It dilutes everything. The best way to do it is to hire a veteran attorney and an investigator and let them build a case."

The chief executive of a small New York-based boutique bank said "more regulatory scrutiny" had in recent months made listing Chinese stocks more hassle than they were worth.

"It was becoming a headache," the person said. "We haven't got any more [Chinese IPOs] lined up."

A new Nasdaq rule stipulating that Chinese companies must have a minimum $25mn public offering size "will weed out the bullshit companies", they added.