

Research on Internet Financial Supervision System

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Abstract—With the development of information technology, the finance capitalizes on the internet and constantly creates new financial models, which constitutes the generalized Internet Finance. Without changing the nature of finance, the Internet Finance just improves its efficiency through the combination of new elements. This paper proposes the way to complement the Internet financial supervision system under the new situation. We analyze the challenges brought by the new Internet finance to the traditional supervision methods, and summarize their shortage. It suggested that the platform supervision system, investor protection system, small issue exemption system, and Internet financial supervision coordination mechanism should be established on the basis of philosophies such as principle supervision, restricted supervision, and bottom line supervision.

Keywords—*Internet Finance; Internet Finance Supervision; investor protection; regulation coordination mechanism*

I. INTRODUCTION

As the advancement of information technology leading the Internet 2.0 era, traditional financial service organizations have gradually moved their financial services onto the internet. At the same time, fueled by global financial technology innovations, a large number of Internet technology service companies have made progresses and innovations based on the traditional financial services and generated various innovative Internet financial services. These Internet-related financial service innovations can be defined as generalized Internet finance. While the Internet financial market is booming, the involvement of Internet information technology in traditional financial services brought new risks into the financial market. Issues like Information system reliability and data security exacerbated the operational risk in the original financial market. In addition, the Internet-related innovations in the financial services industry challenged the traditional financial regulation. In this context, based on the characteristics of Internet finance in the new era, and addressing the current regulatory experience and dilemma, this paper proposes to construct an Internet financial regulatory framework consistent with China's national conditions.

II. BASIC CONCEPTS OF INTERNET FINANCE

Judging from the function and the history of finance, the relationship between finance and currency, and financial risks, the essence of Internet finance is still finance. Specifically, Internet-enabled non-traditional financial services such as Peer-to-Peer lending and crowdfunding are fundamentally performing basic financial functions such as risk management, clearing and payment settlement, information disclosure. They have not changed the nature of finance, but the mode of

realizing the original functions. Internet finance adopts new technologies and methods to change the combination of the basic elements of the original financial system to provide new financial functions. It is created to improve efficiency by refactoring the mix of liquidity, profitability and security. In the Annual Report on China's Internet Finance Development (2014), Internet finance is referred as, in essence, a new type of financial service model that utilizes Internet technologies such as big data, cloud computing, social networks and search engines to realize financial communication.

III. THE OVERALL THINKING OF INTERNET FINANCIAL SUPERVISION

In light of China's Internet financial market characteristics and foreign countries' experience, we should first adjust the legislative concept, clarify the choice of supervision methods, and then construct a specific regulatory system, so as to ultimately maintain market order, control financial risks, and guide a sound development of the market.

In terms of the regulatory concept, we should first recognize the legitimacy of Internet finance, affirm its positive value, and give it legal status in law. Then, the integrated Internet financial legal regulation system should be improved to make up for the institutional mismatch and legal loopholes of the regulatory legislation, so that we can shift from the original dictation supervision to adjustment supervision. By adopting dynamic control measures, we can curb excessive innovation of the financial institutions. A mutual aspiration between financial regulation and financial innovation is to be expected.

Regarding the supervision methods, we need to consider the polymorphism of the Internet, and strike a balance between regulatory revenue and costs. The goal of Internet finance regulation is to promote development, rather than stifle financial innovation. Therefore, principle supervision, restricted supervision, and bottom line supervision have become the consensus of the academic community. Additionally, some scholars put forward incentive supervision or incentive compatibility. The concept is to stimulate the autonomy and consciousness of the Internet financial institutions by establishing an administrative guidance system, both positive and negative incentive mechanism and signing compliance.

IV. SUGGESTIONS FOR SPECIFIC SYSTEMS OF INTERNET FINANCIAL SUPERVISION

With regard to the Internet financial supervision system, the existing research results mainly spring from the perspective

of platform supervision and investor protection. It is proposed that we should encourage innovation and conduct moderate supervision, and explore the legal path of effective supervision, so shall be followed the two legislative principles of maintaining a balance between investor protection and the financial system, and combining entrepreneur support and financial operation efficiency. Also a system with diversified rules shall be established, and a three-fold protection of investor rights through civil, administrative and criminal liability provided. Last, in the institutional framework of China's Internet financial supervision, platform access system, platform behavior system, and investor protection/grading system should be included.

A. Platform supervision system

In the Internet financial transaction, the platform serves as an intermediary platform with standard process of the transaction for the two parties, and also facilitates information acquisition and communication. It reduces the transaction costs and risks of both parties, and can also establish more trust between the parties. In terms of platform access, we need to establish an approval system for the administration of platform qualifications, and a registration system with the information disclosure system as the core. When implementing these systems, we should distinguish the pure information intermediary platform and the quasi-credit intermediary platform. While the former one is approved if it is registered or filed in the industry association, the latter should be regulated with the prudential supervision of banking financial supervision, as it is equivalent to the quasi-financial institution. At present, Chinese government has adopted an approved license management system for third-party payment institutions. The access to the online lending platform is approved mainly with the local financial regulatory authorities. And the access to the equity-based crowdfunding platform requires one to be filed in the industry association.

B. Investor/financial consumer protection system

In the investor/financial consumer protection system, we need to strike a balance between capital formation and investor protection in Internet financial regulation. First, it is necessary to establish an investor classification and quota system to ensure that investors have the corresponding investment capacity and risk-undertaking ability, as the financing parties are mainly small and medium-sized enterprises and start-up projects which have hidden risks of investment failure. Therefore, all countries in the world have set requirements or restrictions on investors who can be accepted in Internet financial investment activities. In particular, in the equity-based crowdfunding transactions, the UK and US limit the amount of investment that ordinary investors can make each year by legislation. In China, investors are classified into immature investors and mature investors by the Internet finance legislation. The total investment of immature investors should not exceed the specific limit of their net assets. And the immature investor is subject to the upper limit of the investment for a single financier in a 12-month period. At the same time, professional investors, high net value investors and institutional investors should be allowed to participate in the investment as mature investors.

C. Small issue exemption

In addition, a small issue exemption system should also be established. With the renewal of the financing model in the Internet era, the way to divide public offering and private equity has gradually become outdated, and the protection of it by securities law and securities regulators is likely to be eliminated. Moreover, the equity-based crowdfunding on the internet platform should be listed in the exemption system as it can save investors information costs so as to improve their self-protection ability. The small issue exemption system is an effective path for the legalization of equity-based crowdfunding. A small-scale public offering system can be established in the *Securities Law*. That is to say, for those need small scale public offering, approval or registration of the CSRC can be exempted without issuing detailed prospectuses and audit reports. It is worth noting that the implementing the small issue exemption system can maintain the financing efficiency of equity-based crowdfunding. However, we should be cautious of the potential investment risks of investors. Therefore, we should strengthen the management of the platform, specify the responsibility of the platform, claim information disclosure obligations and establish a qualified investor system simultaneously alongside the implementation of the micro-exempt system.

D. Internet finance regulatory coordination mechanism

Under China's current financial regulatory reform, the issues of financial regulatory coordination have also included the coordination of the micro-prudential regulatory responsibilities of various financial sectors and the People's Bank of China, in addition to the function distribution and communication between the central financial regulatory authorities and local financial regulatory authorities. In China's 13th Five-Year Plan for modern financial system, Internet finance has also been incorporated into the macro-prudential management of the central bank. By coordinating the central bank's comprehensive supervision and the supervision functions of the CBRC, CSRC and CIRC, we can address the regulatory gap and regulatory duplication under the original dividing supervision system. By coordinating the central bank's policy formulation and the policy implementation of the CBRC, CSRC and CIRC, we can ensure the consistency and sustainability of Internet financial policies. However, at present, China's financial regulatory system reform has not been accomplished with a large number of financial regulatory rules and legal systems need to be adjusted. The original regulatory rules may no longer be applicable for the future financial regulatory system, and it is necessary to make forward-looking design of the Internet financial regulatory system.

V. CONCLUSION

In the institutional framework of Internet financial supervision in China, there should be platform access system and investor protection/grading system. In terms of platform access, we suggest the establishment of an approval system for the administration of platform qualifications, and a registration system rooted in information disclosure. For investor protection, protective measures should correspond with investor's classification and situation. As for small issue

exemption, we set the upper limit amount of small-scale public offerings, under which are possible to be exempted from approval or registration in CSRC, issuing detailed prospectuses and audit reports, etc. With respect to the Internet financial regulatory coordination mechanism, we should strike a balance between the policy formulation of the People's Bank of China and the policy implementation of the CBRC, CSRC and CIRC so as to ensure the consistency and sustainability of Internet financial policies.

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