Mixed Ownership Reform and Corporate Governance in China's State-Owned Enterprises

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ABSTRACT

This Article provides an early assessment of the impact on corporate governance of the most recent wave of reform of China's state-owned enterprises (SOEs) announced by the CCP in 2013, officially known as the mixed-ownership reform (MOR). It offers a comprehensive and detailed account of the background, policy and regulatory frameworks, and rationale of the MOR in light of the history of ownership reform in China. It also conducts empirical studies of the change in ownership and board composition in over 30 SOEs which have recently completed their MOR experiments, as well as several case studies. It observes that MOR's impact on SOE corporate governance has been embodied in the "retreat of the state," the "advance of the Chinese Communist Party" (the Party), and a limited yet emerging separation of power between the Party and the board in SOEs. To explain this observation, the Article argues that the MOR programme is driven by three current beliefs of the Chinese Party-state on the future of SOEs in China. First, ownership and ownership reform matter. Second, sharing control, rather than dominance by a single state shareholder, improves both the efficiency and governance of SOEs. Third, the MOR was designed to develop partnerships or alliances between the state shareholders and strategic investors in order to help the post-

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MOR state enterprises improve their efficiency and enhance market opportunities.

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I. INTRODUCTION

Ownership reform has been at the center of the economic reform programme of the People's Republic of China (PRC or China) since the early 1990s,[1] when the Chinese government decided to corporatise its state-owned enterprises (SOEs). This is understandable given the collectivization of property that was established after 1949, when the Chinese Communist Party (CCP, or "the Party") defeated the Kuomintang government. The PRC's first Company Law was adopted in 1993 to facilitate the fulfillment of this objective by establishing a legal framework to convert traditional SOEs into "modern enterprises."[2] These enterprises are corporate entities with systems of modern ownership and governance structures in which the decision-making powers are jointly exercised by the shareholders' meeting, the board of directors, the supervisory board, and the manager,[3] very much akin to how modern corporations are governed in other jurisdictions.

In China's historical transition from a Soviet-style planned economy to a market-oriented economy, ownership reform serves two functions. First, the policy to initiate ownership reform in China represented a fundamental breakthrough in China's socialist ideology. The planned "command economy," which China established and practiced between 1949 and 1979, was underlined by the Marxist economic ideology that the state "owns the means of production, and therefore controls the economy, and determines what to produce and who will receive what products at what levels according to the state plan."[4] Any attempt to break the state's monopoly in the economy would be considered a serious political challenge to the socialist Party-state itself. In this respect, the CCP's decision to launch ownership reform to transform the Chinese economy from complete public ownership to a mixed structure demonstrated a strong political will to depart from orthodox Marxist ideology. More significantly, it has offered legitimacy to all future mixed-ownership reform initiatives that

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1. *See* Sujian Guo, *The Ownership Reform in China: What Direction and How Far?*, 12(36) J. CONTEMP. CHINA 553, 553 (2003) (noting that "the ownership system, rather than market mechanism, is fundamental to China's economic transition").

2. JIANGYU WANG, COMPANY LAW IN CHINA: REGULATION OF BUSINESS ORGANIZATIONS IN A SOCIALIST MARKET ECONOMY 33 (Edward Elgar ed., 2014); *see also* OECD, CHINA IN THE WORLD ECONOMY 433 (2002).

3. *Id.* at 151–95.

4. Guo, *supra* note 1, at 554–55.

would not necessarily be considered ideological violations of China's socialism. The upper limit for such ownership transformation is officially described in the CCP's first decision in 1992 to establish a "socialist market economy with Chinese characteristics" under which the Chinese economy must be one that the public sector dominates, and various types of ownership systems coexist.[5]

Second, ownership reform also generated institutional reform in China, which created a common legal framework for both state and nonstate–business organizations, paving the way for corporatization and eventual privatization of SOEs.[6] The adoption of the Company Law in 1993, as mentioned, is a milestone in such institutional evolution.[7] The law provides a national basis for the establishment, organization, and operation of "limited liability companies" and "joint stock limited companies," which are separate and self-responsible legal entities able to operate independently under the law.[8]

The real effect of corporatization resulting from ownership reform on SOE governance has, however, been questioned. Two arguments have been advanced. In the first, Milhaupt and Zheng have called for the need to look beyond ownership when studying Chinese-state capitalism.[9] They call for attention to be paid to the institutional environment in China, which in practice makes the distinction between state ownership and private ownership less meaningful. In their own words, functionally, "SOEs and large POEs [privately owned enterprises] share many similarities in the areas commonly thought to distinguish state-owned firms from privately owned firms: market

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5. 中共中央关于建立社会主义市场经济体制若干问题的决定 [*Decision of the Central Committee of the Chinese Communist Party on Several Issues concerning the Establishment of the Socialist Market Economy System*], PEOPLE'S DAILY, http://www.people.com.cn/GB/shizheng/252/5089/5106/5179/20010430/456592.html (last visited Mar. 19, 2020) [https://perma.cc/2TEX-FQNZ] (archived Feb. 15, 2020).

6. Though it has famously been argued that China's SOE reform is "corporatization, not privatization", Donald C. Clarke, *Corporatisation, not Privatisation*, 7 CHINA ECON. Q. 27, 27–30 (2003).

7. The P.R.C. Company Law, or *Gongsifa*, was adopted by the National People's Congress Standing Committee December 1993 and amended respectively in December 1999, August 2004, October 2005, December 2003 and October 2018. P.R.C. Company Law (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 29, 1993, rev. Dec. 25, 1999, Aug. 28, 2004, Oct. 27, 2005, Dec. 28, 2013, and Oct. 26, 2018, effective Nov. 5, 2018), http://www.npc.gov.cn/npc/c12435/201811/68a85058b4c843d1a938420a77da14b4.shtml [https://perma.cc/43S3-A8WG] (archived Feb. 15, 2020) (China) [hereinafter P.R.C. Company Law].

8. BARRY NAUGHTON, THE CHINESE ECONOMY: TRANSITIONS AND GROWTH 301 (2007) [hereinafter NAUGHTON, THE CHINESE ECONOMY].

9. Curtis J. Milhaupt & Wentong Zheng, *Beyond Ownership: State Capitalism and Chinese Firm*, 103 GEO. L.J. 665, 669 (2015).

access, receipt of state subsidies, proximity to state power, and execution of the government's policy objectives."[10]

In a related argument, Wang has identified the "twin governance structures" in China's SOEs: one for legal governance and the other for political governance.[11] The legal governance structure, featuring the shareholders' meeting, the board of directors, the supervisory board, and the management team, is installed according to the PRC Company Law and represents the convergence of Chinese corporate governance with Western corporate law norms. On the other hand, political governance is "a CCP-dominated process that actually controls personnel appointments and decision-making in SOEs."[12] In such a case, as long as the board of directors is not given real power to run the company independently and the CCP organization is really in charge, the percentage of private ownership is more or less irrelevant in SOEs with mixed ownership.

Although both of the aforesaid arguments are powerful in their own ways, it would not be fair enough to reckon that ownership is totally irrelevant in the study of corporate governance in Chinese SOEs,[13] in part because of the two general functions of ownership reform that were discussed at the beginning of this Article. More specifically, ownership cannot be ignored because corporate decision-making eventually has to go through the legal governance structure, and hence has to follow the rules concerning decision-making in the PRC Company Law, as a matter of both principle and formality. Ownership in a Chinese company, be it state owned or privately owned, necessarily places power with shareholders to vote on all corporate matters that fall within the province of the shareholders' meeting, including the right through the voting process to select the directors and supervisors.[14] This is true even in any corporatized SOE with a Party cell.[15] That is, to the extent the Chinese Party-state wants to control SOEs, it understands that any move to increase private

10. *Id.* at 668.

11. Jiangyu Wang, *The Political Logic of Corporate Governance in China's State-owned Enterprises*, 47 CORNELL INT'L L.J. 631, 648–60 (2014).

12. *Id.* at 648.

13. *See* Milhaupt & Zheng, *supra* note 9, at 669 (emphasizing that they "do not argue that corporate ownership is completely irrelevant in China or that Chinese POEs are identical in all respects to SOEs.").

14. P.R.C. Company Law, *supra* note 7, at arts. 37, 97 (Article 37 notes the powers of shareholders in limited liability companies, which are functional equivalents of closed held corporations, and Article 97 notes granting shareholders in joint stock companies, which are the functional equivalent of public corporations, the same powers by making reference to Art. 37).

15. *See id.* at art. 19 (SOEs which are incorporated in the form of limited liability companies and joint stock companies must comply with the PRC Company Law, though Art. 19 of the Company Law requires companies with CCP committees must provide necessary conditions for the activities of the Party committees.).

ownership in SOEs will lead to the possibility that the private investor will demand more participation in corporate decision-making, which must be treated at least as a legal matter.[16] In a nutshell, though ownership may be subject to important constraints in China, and there is indeed a need to look beyond ownership to consider Chinese state capitalism as a whole, it is still important to pay due consideration to ownership change in an SOE and analyze how such a change may impact corporate governance in SOEs.

It is in such a context that we aim to provide an early assessment of the impact on corporate governance of the most recent wave of SOE reform announced by the CCP in 2013,[17] officially known as the mixed-ownership reform (MOR). The stated purpose of the MOR is to bring private-sector investment and management into SOEs to improve the efficiency and governance of the state sector.[18] Since 2016, China has launched four rounds of MOR reforms.[19] The first three pilot reforms included fifty SOEs, covering seven key sectors including electricity, oil, natural gas, rail transportation, civil aviation, and telecommunications.[20] The Chinese government nominated 160 SOEs for the fourth round of the MOR programme in May 2019, possibly in acknowledgment of the perceived success of the previous MOR reforms.[21] An official source suggests that by 2018, a total of 2,880 SOEs conducted MOR, which included 70 percent of the central SOEs.[22] Xiao Yaqing, Chairman of the state-owned Assets Supervision and Administration Commission of the State Council (SASAC),

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16. See WANG, *supra* note 2.
17. *See infra* notes 44-61 and accompanying text.
18. *See infra* note 61 and accompanying text.
19. Zhong Nan, *100 SOEs to Join 4th Round of Mixed Ownership Reform*, CHINA DAILY (Apr. 17, 2019), http://global.chinadaily.com.cn/a/201904/17/WS5cb67648a3104842260b697c.html [https://perma.cc/GT8U-6SWF] (archived Feb. 15, 2020).
20. 徐善长 [Xu Shanchang], *国有企业混合所有制改革的政策和实践* [*Policy and Practice of the Mixed Ownership Reform in China's SOEs*], 中国改革 [CHINA REFORM] (Oct. 27, 2018), http://www.chinareform.org.cn/forum/crf/84/speech/201810/t20181027_275799.htm [https://perma.cc/3GTM-6NCQ] (archived Feb. 15, 2020).
21. *China Approves 160 SOEs in Pilot Mixed-Ownership Reform*, XINHUA NEWS (May 17, 2019), http://www.xinhuanet.com/english/2019-05/17/c_138067229.htm [https://perma.cc/NM9R-GNA5] (archived Feb. 15, 2020) [hereinafter *China Approves 160 SOEs*].
22. *China Accelerates Mixed Ownership Reform of SOEs: Newspaper*, XINHUA NEWS (May 13, 2019), http://www.xinhuanet.com/english/2019-05/13/c_138055082.htm (last visited Mar. 19, 2020) [https://perma.cc/5DSF-YAWB] (archived Feb. 15, 2020). According to SASAC, this number included the second and third level subsidiaries of central SOEs and local SOEs. *See 国有企业混合所有制改革步伐加快* [*Mixed Ownership Reform Accelerated in SOEs*], XINHUA NEWS (Nov. 14, 2018), http://www.gov.cn/xinwen/2018-11/14/content_5340406.htm [https://perma.cc/NV53-PE3V] (archived Feb. 15, 2020).

expressed the hope that MOR would lead to breakthroughs in China's SOE reform but still warned that the MOR programme was not about privatization of China's massive public sector.[23]

The rest of the discussion proceeds as follows. Part II offers a detailed and comprehensive account of the background, proposed measures, and policy features of the MOR programme in light of the history of China's SOE reform. It also discusses two recent institutional changes in China's SOE policy that have accompanied the programme, namely the classification of SOEs into commercial entities and public services entities and the shift from asset management to capital management by inserting a layer between the government and the firms commercial SOEs.

Part III looks at MOR in practice. It begins with a survey of the trending change in shareholder ownership, board composition, important board positions, and board powers,[24] which is followed by several MOR case studies. Part III then discusses the changes brought to corporate governance of SOEs by the policy and regulatory initiatives on SOE reform as well as the emerging practices in implementing the MOR programme. It observes several trends in the corporate-governance framework of MOR firms. First, there is an obvious retreat of the Chinese state from SOE governance with the implementation of the shift from "asset management" to "capital management." On the other hand, the retreat of the state is accompanied by the strengthened involvement of the CCP in SOEs, as the firms have been asked to institutionalize the role of the Party in their articles of association. It is observed that there is a limited degree of separation of power between the Party committee and the board of directors. Based on this, that MOR has set out a new model of corporate governance in some of China's SOEs, which is styled here as a partnership-based, consultative-governance model. That is, on the condition that SOE ownership is diversified to include substantial nonstate ownership (with the state remaining a significant but not necessarily majority shareholder), decision-making power is shared

23. *See* 肖亚庆 [Xiao Yaqing], *混合所有制改革不是私有化 不可能"一混了之"、"一混就灵"* [*Mixed Ownership Reform is Not About Privatization, and It Is Unlikely that It Can Resolve and Close All the Problems*], XINHUA NEWS (Mar. 9, 2019), http://www.xinhuanet.com/politics/2019lh/2019-03/09/c_1210077198.htm [https://perma.cc/Q54U-3MDN] (archived Feb. 15, 2020) (press conference of SASAC at annual meeting of the National People's Congress); *see also* Qu Hui & Han Wei, *More State Enterprises Set for Mixed Ownership Reforms*, CAIXIN GLOB. (Mar. 29, 2019), https://www.caixinglobal.com/2019-03-29/more-state-enterprises-set-for-mixed-ownership-reforms-101398493.html [https://perma.cc/TF4J-8ZRB] (archived Feb. 15, 2020).

24. For example, whether the board of directors would be allowed to appoint senior executives.

between the Party organization and the board of directors (in which nonstate shareholders appoint the majority of the directors).

Part IV attempts to understand the rationale of MOR from both theoretical and practical perspectives and, on this basis, explain the internal factors that motivate the Chinese Party-state to pursue MOR. It argues that the MOR programme is driven by three current beliefs on the future of SOEs in China. First, it is clear that ownership reform matters. Empirical evidence about China's economic reform consistently suggests partially privatized SOEs, or SOEs with mixed ownership, exhibit higher productivity, better performance, and improved corporate governance than firms with complete or dominant state ownership. [25] This is consistent with the strong economic literature worldwide that privatisation leads to efficiency gains.[26] To the extent there are both ideological and rational constraints for China not to pursue full privatization of its state-backed economic entities, at least at this stage, "[p]erhaps the 'mixed economy' is a decent model of industrial organization after all [in China]."[27] The second belief is that sharing control, rather than dominance by a single state shareholder, improves both the efficiency and governance of SOEs. Third, the MOR was designed to develop partnerships or alliances between the state shareholders and strategic investors in order to help the post-MOR state enterprises improve their efficiency and enhance market opportunities.

Part V concludes with several general remarks. It restates the central argument of this Article that MOR offers a practical approach at this stage of China's development which defines the role and operation of SOEs in the context of a socialist market economy in a single-party state. China should be encouraged to reduce state ownership in its SOEs through mixed ownership reform. The introduction of nonstate capital into SOEs has led to greater participation in corporate governance by nonstate investors, which is required by China's corporate law but also evidenced in practice by the empirical study of this Article. This development may be interpreted as that the Chinese Party-state has realized the benefit of "sharing control" in corporate governance. Nevertheless, the institutionalization

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25. See *infra*, footnotes 214–21 and the accompanying texts. See also the literature in, *infra*, note 225.

26. *See* William L. Megginson & Jeffry M. Netter, *From State to Market: A Survey of Empirical Studies on Privatization*, 39(2) J. ECON. LITERATURE 321, 381 (2001) ("privatization 'works,' in the sense that divested firms almost always become more efficient, more profitable, increase their capital investment spending, and become financially healthier"); *see also* WORLD BANK, WORLD DEVELOPMENT REPORT 1996: FROM PLAN TO MARKET 143 (1996) (noting the positive effects of privitisation in transition economies, including China).

27. Barry Naughton, *China's Distinctive System: Can It be a Model for Others?*, 19 J. CONTEMP. CHINA 65, 437, 442 (2010).

of the role of the Party in SOE corporate governance demonstrates the limit of such control sharing.

II. THE TOP-LEVEL DESIGN FOR MIXED-OWNERSHIP REFORM: POLICY, MEASURES, AND FEATURES

A. *Historical Development and Recent Institutional Reform in China's State Sector*

SOE reform in China has been a journey toward improving firm efficiency through interconnected ownership change and good corporate governance, but not rapid privatization.[28] The reform of China's state economy has lasted for four decades since the late 1970s. The SOE system, established and developed during the planned economy period (1950s to 1970s), featured state enterprises being administratively controlled and directly managed by the government at various levels.[29] In that system, a state enterprise, whatever it was called, was a work unit or *danwei*, which was part of the government with multiple roles and functions.[30] From the beginning, SOE reform has been oriented to address the soft budget constraint problems, increase enterprise autonomy, and improve corporate governance, with the view to transforming SOEs into commercially viable entities.[31] In this process, four modalities were used, at different stages of the reform, to achieve the aforesaid objectives: contracting, corporatization, ownership diversification, and creation of large enterprise groups.

The first stage of the SOE reform (1978-1992) introduced the contractual managerial responsibility system for the purpose of enhancing enterprise autonomy and granting market-based incentives to the state-appointed managers of the SOEs.[32] Under the contractual system, an SOE was allowed to ride on a unique system of dual-track pricing[33] and, on this basis, sign an agreement with the government

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28. Donald C. Clarke, *Law without Order in Chinese Corporate Governance Institutions*, 30 NW. J. INT'L L. & BUS. 131, 142–44 (2010).

29. OECD, REFORMING CHINA'S ENTERPRISES 51 (2002); *see* BARRY NAUGHTON, GROWING OUT OF THE PLAN: CHINESE ECONOMIC REFORM 1978-1993, at 97–136 (1995); WU JINGLIAN, UNDERSTANDING AND INTERPRETING CHINESE ECONOMIC REFORM 139–42 (2005).

30. *See* STOYAN TENEV ET AL., CORPORATE GOVERNANCE AND ENTERPRISE REFORM IN CHINA: BUILDING THE INSTITUTIONS OF MODERN MARKETS 10–11 (2002); *see also* JINGLIAN, *supra* note 29, at 140.

31. *See* NAUGHTON, THE CHINESE ECONOMY, *supra* note 8, at 301 (2007); JINGLIAN, *supra* note 29; TENEV ET AL., *supra* note 30, at 9–20.

32. *See* TENEV ET AL., *supra* note 30, at 13–14.

33. China adopted a dual-track approach to price liberalization in its transition from a planned to a market economy in the 1980s and 1990s. The government

agency in charge, through which the SOE ensured the government a fixed amount of profit, while retaining any surplus profit.[34] Ownership reform emerged in the second stage (1992-2003), known as *gaizhi* (ownership transformation).[35] Ownership diversification was the major theme in this period, leading to corporatization and a limited degree of privatization.[36] The promulgation of the PRC Company Law aimed to create an institutional framework for the modern enterprise system and paved the way for reorganizing the SOEs into Western-style corporations.[37] After the CCP adopted the policy of "grasping the large, letting go the small" (*zhuada fangxiao*) in 1995,[38] the Chinese government retained about five hundred to one thousand large enterprises and restructured other SOEs through sale or lease.[39] The third stage (2003-2013) carried on the corporatization programme and further institutionalized state-SOE relations with the creation of SASAC in 2003.[40] SASAC's emergence indicated for the first time that the Chinese state would behave as a shareholder in SOEs.[41] The continuing reform of SOEs under SASAC also resulted in the creation of large enterprise groups brought about through consolidation and restructuring of SOEs, leading to a significant reduction of the total number and a substantial increase in the average size of SOEs.[42] Meanwhile, the Chinese government placed emphasis on dominance of state ownership in strategic industries including, initially, high

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maintained price controls and quotas to some extent under the planned track, through which "economic agents were assigned rights to and obligations for fixed quantities of goods at fixed planned prices and quotas ." A market track was established simultaneously to allow economic agents to transact at "free market prices." Gradually, the price controls under the planned track was phased out. *See* Yingyi Qian, *The Institutional Foundation of China's Market Transition*, *in* ANNUAL WORLD BANK CONFERENCE ON DEVELOPMENT ECONOMICS 1999, 384 (Boris Pleskovic & Joseph E. Stiglitz eds., 2000).

34. JINGLIAN, *supra* note 29, at 146; *see also* Ligang Song, *State-Owned Enterprise Reform in China: Past, Present and Prospects*, *in* CHINA'S 40 YEARS OF REFORM AND DEVELOPMENT 1978-2018, 349–50 (Ross Garnaut, Ligang Song & Cai Fang eds., 2018).

35. Song, *supra* note 34, at 351. *See generally* ROSS GARNAUT ET AL., CHINA'S OWNERSHIP TRANSFORMATION: PROCESS, OUTCOMES, PROSPECTS (2005).

36. *See* SHAHID YUSUF ET AL., UNDER NEW OWNERSHIP: PRIVATIZING CHINA'S STATE-OWNED ENTERPRISES 105–14 (2006).

37. *See* TENEV ET AL., *supra* note 30, at 16–17.

38. This policy was formally approved as a state policy by the National People's Congress in 1997.

39. Song, *supra* note 34, at 352.

40. NAUGHTON, THE CHINESE ECONOMY, *supra* note 8, at 302–03.

41. Jiangyu Wang, *The Political Logic of Corporate Governance in China's State-Owned Enterprises*, 47 CORNELL INT'L L.J. 631, 648–60 (2014) (noting that SASAC was created "as a centralized representative of state investor" and, before SASAC's establishment, "the ownership of SOEs within the government was very fragmented, and many bureaucracies, from central ministries to departments of local governments, had control over SOEs").

42. Song, *supra* note 34, at 357–58.

technology, nonrenewable natural resources, public utilities and infrastructure services, and national security.[43]

Since 2013, SOE reform has entered its fourth stage, marked by a call for further action by a decision of the Third Plenum of the CCP in 2013.[44] One of the breakthroughs of the decision was its emphasis on the critical role of the private sector in the Chinese economy in that "both public and non-public sectors are key components of the socialist market economy."[45] As Zheng has put it, this may represent "a major shift in official ideology away from the superior status of the state sector"[46] and that "the Chinese government no longer insists on majority ownership, except for strategic industries."[47] In other words, as long as state assets in the SOEs continue to grow, "it is no longer imperative to maintain majority state ownership."[48]

The new wave of reform was put into operational policy design with the promulgation of a set of guidelines adopted by the CCP in August 2015,[49] which was followed by more detailed implementing measures issued by China's State Council, together with a series of supplementary policies and measures promulgated by the National Development and Reform Commission (NDRC), SASAC, and other relevant government agencies.[50] The guidelines have formed the new institutional background for the MOR programme. The following three new policy initiatives in the guidelines are particularly worth noting.

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43. *Id.* at 356.

44. Central Committee of the Communist Party of China [CCCPC], 中共中央关于全面深化改革若干重大问题的决定 [*Decision of the Central Committee of the Communist Party of China on Some Major Issues Concerning Comprehensively Deepening the Reform*] Part II, http://www.gov.cn/jrzg/2013-11/15/content_2528179.htm (last visited Mar. 19, 2020) [https://perma.cc/7YUP-K8TD] (archived Feb. 17, 2020), *translation available in* http://www.china.org.cn/chinese/2014-01/17/content_31226494_2.htm [https://perma.cc/S9KG-LZSG] (archived Feb. 17, 2020) [hereinafter CCCPC Reform Decision] (adopted at the Third Plenum of the 18th Party Congress).

45. *Id.*

46. Zheng Yu, *China's State-Owned Enterprise Mixed Ownership Reform*, 6 E. ASIAN POL'Y 4, 39, 41 (2014).

47. *Id.*

48. *Id.*

49. CCCPC, 中共中央、国务院关于深化国有企业改革的指导意见 [Guidelines of the CCP Central Committee and the PRC State Council to Deepen Reform of the State-owned Enterprises] (Aug. 24, 2015), http://www.gov.cn/zhengce/2015-09/13/content_2930440.htm [https://perma.cc/M8R5-YKM7] (archived Feb. 17, 2020) [hereinafter CCCPC Reform Guidelines].

50. State Council of the People's Republic of China [State Council], 国务院关于国有企业发展混合所有制经济的意见 [Opinions of the State Council on the Development of Mixed-ownership Reform in SOEs] (Sept. 23, 2015), http://www.gov.cn/zhengce/content/2015-09/24/content_10177.htm [https://perma.cc/7Q6Q-UF33] (archived Feb. 17, 2020) [hereinafter Opinions of the State Council].

First, Chinese SOEs, according to their nature, are to be classified into commercial SOEs (*shangyelei*) and public service SOEs (*gongyilei*).[51] Table 1 displays the different types of SOEs, their assigned objectives, and the respective measures proposed to reform them. Commercial SOEs would operate fully on a commercial basis with the for-profit purpose of enhancing efficiency and maximizing the valuation of state assets.[52] Such firms are all required to be restructured into modern stock corporations with a view to being listed on a stock market in the future.[53] The state can be the dominant controller, a majority shareholder, or even a minority shareholder in these firms.[54] On the other hand, the public service SOEs are expected to provide public goods and services in a price-regulated environment in order to enhance the Chinese people's standard of living.[55] Such firms can be solely owned by the state, and they will be evaluated by cost control, product quality, operational efficiency, and capacity in delivering the requisite product or service.[56]

Table 1: Classification and Functional Definitions of Chinese SOEs

Category	***Sub-Category***	***Defined by Sectors and Areas***	***Enterprise Objectives***	***Reform Measures***
Commercial SOEs	Tier 1	Fully competitive sectors and areas	Maximizing the value of state capital Operating on commercial basis Enterprise autonomy	Taking the form of joint stock companies Ownership diversification Private investors can be a majority shareholder Complete listing
	Tier 2	National security Important industries or key point areas in the commanding heights of	Safeguarding national security Ensuring the smooth operation of the Chinese economy Developing forward-looking, strategic industries	The state must maintain a controlling position in ownership Private investors can be minority shareholders

51. *See* CCCPC Reform Guidelines, *supra* note 49, at Part II.
52. *See id.* at Part II (5).
53. *Id.*
54. *See id.* at Part II (4)–(5).
55. *See id.* at Part II (6).
56. *See id.*; *see also* NAUGHTON, THE CHINESE ECONOMY, *supra* note 8.

		national economy Natural monopoly sectors Undertaking state-assigned significant projects	Harmonizing economic, social, and security interests	State-enterprise separation in natural monopolies
Public Interest SOEs		Public goods and services	Safeguarding people's livelihood Serving the society Prices of products or services can be adjusted by the government Market mechanisms encouraged to improve efficiency	Taking the form of wholly state-owned companies or more diversified ownership if conditions are met Private enterprises can be involved in the form of outsourcing, franchise, or agency by agreement

Second, the role of the state owner in enterprises, exercised by SASAC at the central and local levels, will shift from "asset management" to "capital management."[57] Specifically, state capital investment/management companies will be established to serve as the state shareholder in SOEs.[58] SASAC, in turn, will become the state shareholder in such capital investment/management companies. The rationale for creating such state capital companies is to establish a firewall between SASAC and the SOEs so as to stop the "tendency for SASAC to become increasingly involved in the business operation of

57. *See* Opinions of the State Council, *supra* note 50, at Part IV(9); *see also* 改革国有资本授权经营体制方案 [*Programme on Reforming the State Capital Authorization System*], STATE COUNCIL (Apr. 14, 2019), http://www.gov.cn/zhengce/content/2019-04/28/content_5387112.htm [https://perma.cc/TCX9-TVP4] (archived Feb. 17, 2020).

58. Numerous state capital entities have been established in recent years. China National Cereal, Oils and Foodstuffs Corporation (COFCO) and Chinese Investment Corporation (CIC) were the first pilot companies designated as state investment/management entities. The State Development & Investment Corp Ltd is the largest state-owned investment holding company for restructuring the state sector, but many capital investment and management companies have been established on a sectoral basis.

SOEs."[59] Arguably, this policy move brings China's SOE supervision model closer to Singapore's Temasek model.[60]

Third, the formation of the "modern enterprise system" is included as a key part of the reform, with the stated aim of establishing a modern corporation, preferably listed, with diversified shareholding and sound corporate governance.[61] The policy statement on SOE corporate governance embodies a wide range of objectives, which is discussed in Part II.C. Suffice it to say that the corporate governance system proposed for SOEs in the guidelines looks positive from the perspective of the convergence side of the global corporate governance debate, as it seems to allow board centrality and independence in corporate decision-making. Nevertheless, as discussed in Part IV.B, these objectives have to be read in tandem with the prescribed role of the CCP in SOEs.

B. *The General Policy Design for Mixed-Ownership Reform*

1. A Balanced Relationship between the State and the Market

The MOR is supposed to be a state-driven process. However, the Chinese government seemingly still intends for the MOR to take place in the marketplace in the process known as *zhengfu yindao, shichang yunzuo*.[62] This follows the spirit of the Third Plenum Decision that, for the first time, advocated for "the market to play a decisive role in the allocation of resources," and the state would refrain from exercising excessive intervention."[63] The state promises to "respect" the principles of the market economy and allow the enterprises to be the central players in the MOR process.[64] In addition, a vow is made to protect the property rights of all forms of ownership, enforce contracts,

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59. *See* CHUNLIN ZHANG, THE WORLD BANK IN CHINA'S STATE-OWNED ENTERPRISE REFORM SINCE THE 1980S 7 (2019), http://documents.worldbank.org/curated/en/828251550586271970/pdf/134778-World-Bank-in-China-SOE-reform-final-Feb-09-2019-En.pdf [https://perma.cc/SH5F-CSC3] (archived Feb. 17, 2020).

60. *See* Yu Hong, *China's Push for State-owned Enterprise Reform*, EAI BACKGROUND BRIEF NO. 1083 i (2015) (noting the "proposal to establish state capital investment corporations is viewed as a Singapore-inspired quest, modelled on Temasek Holdings"); Tan Cheng-Han et al., *State-Owned Enterprises in Singapore: Historical Insights Into a Potential Model for Reform*, 28 COLUM. J. ASIAN L. 61, 88–90 (2015) (The Temasek model is intended to create a level of separation between the Singapore government and government linked companies so as to facilitate commercial decision making that is insulated from the dictates of government policy.).

61. CCCPC Reform Guidelines, *supra* note 49, at Parts III(7)–(8).

62. Opinions of the State Council, *supra* note 50, at Point 2.

63. CCCPC Reform Decision, *supra* note 44, at Points 2–3; *see also* Sarah Y. Tong, *China's New Push to Reform the State Sector: Progress and Drawbacks*, 16(3) CHINA INT'L J., 35, 43 (2018).

64. Opinions of the State Council, *supra* note 50, at Part I(2).

and encourage fair competition.[65] On the other hand, the CCP has also stressed that the state sector should retain "dominance" (*zhuti diwei*) and play the leading role (*zhudao zuoyong*) by enhancing the "state sector vitality, controlling capacity and influence" in the Chinese economy.[66] In this spirit, the general policy design of the MOR programme suggests that the state sector can involve private investment. The Third Plenum Decision confidently stated this objective as follows:

> A mixed economy with cross holding by and mutual fusion between state-owned capital, collective capital and non-public capital is an important way to materialize the basic economic system of China. It is conducive to improving the amplification function of state-owned capital, ensuring the appreciation of its value and raising its competitiveness, and it is conducive to enabling capital with all kinds of ownership to draw on one another's strong points to offset weaknesses, stimulate one another and develop together.[67]

On this basis, the CCP declared that it "will allow more SOEs and enterprises of other types of ownership to develop into mixed enterprises" and "non-state-owned capital to hold shares in projects invested by state-owned capital," as well as "mixed enterprises to implement employee stock ownership plans (ESOP) to form communities of capital owners and laborers."[68]

2. Modes of Participation in MOR Firms

MOR has been planned to be conducted at two levels: the corporate group (parent/holding company) level and the subsidiary level.[69] The subsidiary SOEs are firms that engage in business, many of which are listed companies themselves. At the current stage, MOR is prioritized at the subsidiary level with the view of redefining the role of the state shareholder, in this case the parent/holding company, to ensure it functions as a shareholder in accordance with the PRC Company Law.[70] MOR at the parent/holding company level is permitted but will only be carried out on a larger scale at a later stage.[71] The nonstate capital entities allowed to acquire shares in SOEs include private investors, collectively owned enterprises,[72] and foreign investors

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65. CCCPC Reform Decision, *supra* note 44, at Point 5.
66. *Id.* at Point 2.
67. *Id.* at Point 6.
68. *Id.*
69. Opinions of the State Council, *supra* note 50, at Points 6–7.
70. *Id.* at Point 6.
71. *Id.* at Point 7.
72. *See* WANG, *supra* note 2, at 68 (giving the definition and functions of collectively-owned enterprises).

through a variety of means.[73] Table 2 exemplifies the general, top-level-designed requirements for the degree of state ownership in different MOR firms.

Table 2: MOR State Ownership Requirements in Different Categories of SOEs

Category	***Sub-Category***	***Sectors or Areas***	***Ownership Requirements***
Commercial SOEs	Tier 1	Fully competitive sectors or areas	Complete listing Ownership diversification
	Tier 2	Important telecommunication infrastructure, pivotal transportation infrastructure, water resources, and hydropower projects that control important rivers, and cross-basin diversion projects	Full or majority state ownership Nonstate enterprises allowed to participate through franchising or government procurement
		Exploitation and unitization of important water resources, forest resources, and strategic mineral resources	Full or absolute majority state ownership Minority nonstate ownership allowed
		Main river channels, main pipeline network of petroleum and natural gas, and main grid	Distinguishing between natural monopolies and competitive businesses Full or absolute majority state ownership for natural monopolies Competitive business areas
		Nuclear power, important public technology platform, basic data acquisition, and utilization involving meteorological mapping hydrology	Full or absolute state ownership Minority nonstate ownership allowed
		State reserve of strategic materials in grain, oil, and natural gas	Full or absolute state ownership
		National defense industries which are involved in research and development of strategic weapons and equipment, in strategic national security, or in core state secrets;	Full or absolute state ownership

73. CCCPC Reform Guidelines, *supra* note 49, at Points 16–18.

		Other national defense industries	Phased relaxation of market access to nonstate enterprises
Public Service SOEs		Public utilities including water, electricity, gas, heating, public transportation, public infrastructures	Diversified ownership permitted in firms which "meet conditions" Participation of nonstate investors through government procurement, franchising or agency by agreements

Specifically, MOR is achieved through any or a combination of the following modes of private participation:

> 1) The introduction of strategic investors who have extensive experience in reorganizing firms through investments in them, and in addition to capital, may provide management experience, industrial connections, market access, and experience with the stock market.[74]
>
> 2) Investments made by venture capital funds or industrial funds, many of which have been established by the Chinese government at central and local levels.[75] Known as state-controlled "guidance funds," they are designed to use government-allocated "seed money" to attract and direct private capital to invest in strategic sectors and areas.[76] In MOR projects with fund participation, an investment syndicate is organised in the form of a limited

74. *See* 德勤 [DELOITTE], 聚焦混合所有制改革 [Focus on Mixed-ownership Reform], 德勤国企改革系列白皮书第二辑 [Deloitte SOE Transformation White Paper] 11 (2015), https://www2.deloitte.com/cn/zh/pages/operations/articles/soe-transformation-whitepaper-issue2.html# [https://perma.cc/5ZEB-S8QT] (archived Feb. 17, 2020).

75. Emily Feng, *China's State-owned Venture Capital Funds Battle to Make an Impact*, FIN. TIMES (Dec. 24 2018), https://www.ft.com/content/4fa2caaa-f9f0-11e8-af46-2022a0b02a6c [https://perma.cc/X8PW-HRK2] (archived Mar. 19, 2020) (noting "China has claimed that it has amassed RMB12.5tn ($1.8tn) of state money across thousands of venture capital funds to achieve its goal of technological dominance by 2025.").

76. "Guidance funds" are defined as "policy funds which are established by the government but operate on market-based principles", with the main purpose of "directing social capital to innovative investment." *See* 中华人民共和国商务部，国家发展改革委员会 [MINISTRY OF FIN. & MINISTRY OF COMMERCE, NAT'L DEV. & REFORM COMM'N], 关于创业投资引导基金规范设立与运作的指导意见 [*Guiding Opinions on the Establishment and Operation of Guiding Funds for Innovative Investment*] Point 1 (Oct. 18, 2008), http://www.mofcom.gov.cn/aarticle/b/g/200812/20081205924175.html [https://perma.cc/P63G-CSPT] (archived Feb. 17, 2020); *see also* Song, *supra* note 34, at 48.

partnership, in which the guidance fund, as a limited partner,[77] contributes 10 to 20 percent of the total investment, and funds based on private or foreign capital make up the rest. The syndicate then invests, often through a special purpose vehicle (SPV), in SOEs which undergo MOR.[78] In this way, the limited investment of state capital will have significant leveraging effect to lure a large amount of private investment into MOR firms.

3) Employee shareholding schemes (ESC) are also utilized whereby employees who have made substantial contributions to the SOE's performance are allowed to acquire shares in the firm,[79] for the purpose of creating "a community of common interest for the owners of capital and labor."[80] Chinese authorities only permit ESC in commercial SOEs in fully competitive areas.[81]

Initial public offerings (IPOs) are an important mechanism that SOEs are encouraged to use.[82] A key advantage of going public is that it provides not only a legal regime that offers better protection of the SOE's property rights but also a more institutionalized framework to organize the SOE's corporate governance into standardized, transparent structures.[83] IPOs also offer an exit opportunity for strategic shareholders, as well as long-term incentives for employee shareholders.[84]

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77. China's partnership law does not allow SOEs to be general partners. *See* 合伙企业法 [Partnership Enterprise Law] (promulgated by the Standing Comm. Nat'l People's Cong., Aug. 27, 2006, effective June 1, 2007), art. 3, *translation available at* http://www.lawinfochina.com/display.aspx?id=1e2875e63e5b3de3bdfb&lib=law [https://perma.cc/AG9L-EE7L] (archived Feb. 17, 2020) (China) [hereinafter Partnership Enterprise Law].

78. *See* 德勤 [DELOITTE], *supra* note 74, at 10.

79. Opinions of the State Council, *supra* note 50, at Point 15.

80. CCCPC Reform Decision, *supra* note 44, at Point 6.

81. 关于国有控股混合所有制企业开展员工持股试点的意见 [*Opinions on Practising Employee Shareholding Scheme in State-Controlled Mixed Ownership Reform Enterprises on Pilot Basis*], STATE-OWNED ASSETS SUPERVISION & ADMIN. COMM'N OF THE STATE COUNCIL Part II (1) (Aug. 18, 2016), http://www.sasac.gov.cn/n2588030/n2588924/c4297190/content.html [https://perma.cc/XEV3-E863] (archived Feb. 17, 2020).

82. Opinions of the State Council, *supra* note 50, at Point 3.

83. *See* P.R.C. Company Law, *supra* note 7.

84. *See* Opinions of the State Council, *supra* note 50, at Point 8.

III. IMPLEMENTATION OF THE MIXED-OWNERSHIP REFORM: SEVERAL CASE STUDIES

This Part examines how MOR is conducted in reality through four case studies: China Unicom, China Eastern Logistics, Sinopec Marketing, and Yunnan Baiyao. It looks at the process of MOR in these cases, with a focus on the change in ownership, representation of state and private capital, and occupancy of important board positions.

A. *Change of Ownership and Board Composition in MOR Companies: A General Survey*

As previously noted, China has launched four rounds of mixed ownership reform, involving in total 210 SOEs, most of which are subsidiaries of centrally administered SOEs.[85] Official statistics revealed that, in 2018, two-thirds of such subsidiaries were already firms which had finished MOR.[86] In 2018, minority ownership equity in central SOEs was $7.2 trillion RMB, amounting to 36 percent of the total market capitalization of these SOEs.[87] According to SASAC, an overwhelming majority of the minority shareholders' equity interests were generated through MOR.[88]

In a typical MOR case at the subsidiary level, an SOE, often the holding company of a group, selects a subsidiary that owns an important unit of the group's business and sells a stake in that subsidiary to private/social investors, who may be allowed to possess about 30 percent to 45 percent of the subsidiary.[89] Such MOR can be realised in the following manner: restructuring; IPO; Employee Stock Ownership Plan (ESOP); introduction of investment funds; introduction of strategic investors; or a combination of some of these.

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85. The first three rounds involved fifty SOEs and the fourth round 160 SOEs. *See* Nan, *supra* note 19; 徐善长 [Shanzhang], *supra* note 20; *China Approves 160 SOEs in Pilot Mixed-Ownership Reform*, *supra* note 21.

86. *See 国新办就中央企业 2018 年前三季度经济运行情况举行发布会* [*State Council Information Office held Press Conference on the Economic Performance of Central SOEs in the First Three Quarters of 2018*], XINHUA NEWS (Oct. 15, 2018), http://www.xinhuanet.com/talking/20181015z/index.htm [https://perma.cc/GPW7-CEDD] (archived Feb. 17, 2020).

87. *See 中央企业混合所有制改革回顾* [*Review of the Mixed-ownership Reform of Central SOEs*], 普华永道 [PRICEWATERHOUSE COOPERS] (Apr. 5, 2009), https://www.pwccn.com/zh/blog/state-owned-enterprise-soe/review-on-the-reform-mixed-ownership-central-enterprises.html [https://perma.cc/A8UC-WRYB] (archived Feb. 17, 2020).

88. *Id.*

89. *See* Yang Ge, *5 Things to Know About China's Mixed-Ownership Reform*, CAIXIN GLOB. (Aug. 28, 2017), https://www.caixinglobal.com/2017-08-28/5-things-to-know-about-chinas-mixed-ownership-reform-101136807.html [https://perma.cc/MG4M-PMJA] (archived Feb. 17, 2020).

In selecting such private-sector investors, the SOE looks more at factors such as management experience, technology, or development of new products or markets, rather than financial investment.[90] In any event, MOR will lead to substantial reduction of state ownership in the SOE concerned. Table 3 shows the change in ownership and board composition in thirty-one SOEs, which covers most of the completed MOR programmes in SOEs selected by the Chinese government for such reform.[91]

Table 3: Change of Ownership and Board Composition in Selected MOR Cases[92]

MOR Company	Shareholding					Board Composition								Board Chair
	Pre-MOR		Post-MOR			Pre-MOR				Post-MOR				
	State Shareholding	Shareholding of Other Shareholders	State Shareholding	Shareholding of Private Strategic Investors	Employee Shareholding	State Representation	Private Strategic Investors Representation	Independent Director	Worker Representation	State Representation	Private Strategic Investors Representation	Independent Director	Employee Representation	
China Unicom	62.74%	37.26%	37.8%	35.19%		57.1% (4/7)	0%	42.9% (3/7)	0%	23.1% (3/13)	38.5% (5/13)	38.5% (5/13)	0%	State
Hefei Jianghang Aircraft Equipm	100%	0%	76%	24%		100%				57.1% (4/7)	42.9% (3/7)	0%	0%	State

90. Opinion of the State Council, *supra* note 50, at Points 9–15.
91. *See infra* Table 3.
92. Sources: Sina Finance, Xinhuanet, IDC News, Cailianshe, Diyicaijing, State-owned Assets Supervision and Administration Commission News, China Storage & Transport Magazine, CAAC News, Sunshine Law Firm, Cdmwjj News, PEdaily, Shanghai Securities News, QQ News, China Economic Net, JRJ.com, 21st Century Business Herald, China Venture Investment Consulting News, National Business Daily, Ping An Insurance (Group) Company of China News, Xintuoshop.com, CITIC-CP Asset Management Company News, EFN China, Jianshu, Everbright Securities Report, China Railway Engineering Consulting Group News, Tianjin Xintuo Zixun Menhu, Phoenix New Media Finance, Sina Medicine, Sohu News, MP Consulting Group, LexisNexis, Xuehua News, Wolters Kluwer, China Mining, Wsxm.net, People's Daily Online, Toushi Jinfu, Xunmeng News, Changjiang Securities Report, Time-Weekly, Qichacha.com, Hexun.com, Xinde Marine News, Ouyeel.com

ent Co., Ltd.														
Eastern Air Logistics	100%	0%	45%	45%	10%	No board of directors before MOR.				55.6% (5/9)	33.3% (3/9)	0%	11.1% (1/9)	State
Sinopec Marketing Co Ltd.	100%	0%	68.8%	31.2%						36.4% (4/11)	27.3% (3/11)	27.3% (3/11)	9.09% (1/11)	State
China Tea Co. Ltd.	100%	0%	40%	60%						42.9% (3/7)	42.9% (3/7)	0%	14.3% (1/7)	State
Datang Network Co., Ltd.	97.89%	2.11%	37.23%	62.77%						33.3% (2/6)				State
Changchun Faway Automobile Components Co., Ltd.			20.14%	79.86%		55.6% (5/9)				28.6% (2/7)				State
Sdic Taikang Trust Co., Ltd.	100%	0%	54.50%	45.5%		100%	0%	0%	0%	44.4% (4/9)	22.2% (2/9)	33.3% (3/9)	0%	State
Yunnan Baiyao Group Co Ltd	100%	0%	25.14%	55%		No board of directors before MOR.				40% (4/10)	30% (3/10)	30% (3/10)	0%	Strategic Investor
China Railway Engineering Consulting Group Co., Ltd.	100%	0%	70%	10%	20%					55.6% (5/9)	22.2% (2/9)	0%	22.2% (2/9)	State
Northern International	86.17%	13.83%	32.33%	50.07%						36.4% (4/11)	27.3% (3/11)	27.3% (3/11)	9.09% (1/11)	Vacant (Used to be from

Trust Co., Ltd.														the state)
Shaanxi Coal and Chemical New Energy Group Co., Ltd.	100%	0%	73.17%	17.07%	9.76%					42.9% (3/7)	28.6% (2/7)	14.3% (1/7)	14.3% (1/7)	
Harbin Pharmaceutical Group Co., Ltd.	45%	55%	38.25%	61.75%		(?/5)				33.3% (2/6)	66.6% (4/6)	0%	0%	Strategic Investor
Shandong Transportation Group Co., Ltd.	100%	0%	37%	33%	30%					57.1% (4/7)	28.6% (2/7)	0%	14.3% (1/7)	State
Tianjin Construction Group	100%	0%	35%	55%	10%					45.5% (5/11)	45.5% (5/11)	0%	9.09% (1/11)	State
Tianjin Seagull Watch Group Co. Ltd.	100%	0%	35%	65%						33.3% (3/9)	55.6% (5/9)	0%	11.1% (1/9)	Strategic Investor
Shenzhen Tefa Property Management Co., Ltd.	100%	0%	65%	20%	15%					80% (4/5)	20% (1/5)	0%	0%	State
Shanxi Xinghuacun Fen Wine Factory Co., Ltd.	69.97%	30.03%	58.52%	41.48%						25% (2/8)	25% (2/8)	50% (4/8)	0%	State
Beijing Qing-Feng Catering	100%	0%	91.58%	7%	1.42%					71.4$ (5/7)	14.3% (1/7)	0%	14.3% (1/7)	State

Management Co., Ltd.														
Anyang Anhua Maintenance and Installation Engineering Co., Ltd.	100%	0%	50.39%	33.59%	16.02%					60% (3/5)	20% (1/5)	0%	20% (1/5)	
Hebei Huabei Pharmaceutical Huaheng Pharmaceutical Co., Ltd.	100%	0%	96.762%	0%	3.238%					71.4% (5/7)	0%	0%	28.6% (2/7)	State
Chongqing Department Store Co., Ltd.	100%	0%	29.95%	74.86%						22.2% (2/9)	22.2% (2/9)	44.4% (4/9)	11.1% (1/9)	State
Shanghai Juss Intellisports Co, Ltd	Newly registered company		60%	34%	6%					50% (2/4)	25% (1/4)	0%	25% (1/4)	State
Greenland Holdings Corp., Ltd.	<80% (unclear)		46.37%	53.63%						33.3% (5/15)	33.3% (5/15)	33.3% (5/15)	0%	State
Guangdong Fenghua New Energy Co., Ltd.	100%	0%	80.5%	10.3%	9.15%					71.4% (5/7)	14.3% (1/7)	0%	14.3% (1/7)	State

Jiangsu Jinsili Pharmaceutical Co., Ltd.	100%	0%	62.71%	20.64%	16.65%					100% (5/5)	0%	0%	0%	State
Xi'an Municipal Construction Group Co. Ltd.	100%	0%	38.47%	32%	29.53%					50% (3/6)	33/3% (2/6)	0%	16.7% (1/6)	State
Ningxia Shenyao Technology Co., Ltd.	Newly registered company		35%	45%	20%					28.6% (2/7)	42.9% (3/7)	0%	28.6% (2/7)	State
Shanghai Pan Asia Shipping Co., Ltd.	100%	0%	82%	10%	8%					87.5% (7/8)	12.5% (1/8)	0%	0%	State
Shanghai Yangshupu Cultural and Creative Media Co., Ltd.	100%	0%	48.53%	46.6%	4.85%					60% (3/5)	20% (1/5)	0%	20% (1/5)	State
Ouyeel Co., Ltd.	100%	0%	72%	23%	5%					55.6% (5/9)	33.3% (3/9)	0%	11.1% (1/9)	State
Beijing Gouli Technology Co., Ltd	Newly registered company		65%	10%	25%					60% (3/5)	20% (1/5)	0%	20% (1/5)	State
Tianjin Hydraulic & Machine (Group) Co., Ltd.	100%	0%	40%	60%	0%					40% (2/5)	60% (3/5)	0%	0%	State

B. *MOR Case Studies*

1. China Unicom MOR

China Unicom, China's third largest and the world's fourth largest telecom operator (by number of subscribers), was among the first group of SOEs chosen by the Chinese government to undergo MOR.[93] China Unicom implemented a controversial MOR through its Shanghai-listed subsidiary, China United Network Communications (CUNC).[94] In August 2017 CUNC announced a sale of shares, representing 37 percent of the firm's shares, to fourteen strategic investors for ¥78 billion RMB ($11.7 billion USD). These investors, including several of China's star firms such as Alibaba Group, Tencent Holdings, Baidu Inc., JD.com, Inc., China Life Insurance, and a few private equity firms, can be classified into four categories: (1) internet companies in China; (2) leading companies in industry verticals; (3) financial institutions; and (4) specialist funds.[95]

As can be seen from Chart 1, before the implementation of MOR, the Unicom Group held 62.7 percent of the shares in CUNC, while the other 37.3 percent of the shares were held by public shareholders.[96] After the reform, the Unicom Group's shareholding decreased to 36.7 percent and the strategic investors held 35.2 percent of the shares.[97] The remaining shares are held by employees as employee incentive shares (2.7 percent) and public shareholders (25.4 percent).[98] China Unicom Group, while still the largest shareholder of CUNC, became a minority shareholder after the MOR.

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93. *See 19 家混改试点央企将引资 3000 亿元* [*Mixed-Ownership Reform of 19 State-owned Enterprises Expected to Draw 300bn Yuan*], 中国证券报 [CHINA SEC. DAILY] (Dec. 4, 2017), http://news.hexun.com/2017-12-04/191856565.html [https://perma.cc/4L79-VFFA] (archived Feb. 17, 2020); *see also* Clare Jim & Julie Zhu, *State-Owned China Unicom to Raise $12 billion from Alibaba, Tencent, Others*, REUTERS, Aug. 16, 2017, https://www.reuters.com/article/us-china-unicom-results/state-owned-china-unicom-to-raise-12-billion-from-alibaba-tencent-others-idUSKCN1AW0JP [https://perma.cc/F8P4-ZPVH] (archived Feb. 17, 2020).

94. Fan Feifei, *China Unicom Shakeup a Milestone in SOE Reform*, CHINA DAILY (Aug. 18, 2017), https://www.chinadaily.com.cn/business/tech/2017-08/18/content_30763797.htm [https://perma.cc/FR8H-36QV] (archived Feb. 17, 2020); *see also* Huang Kaixin et al., *China Unicom Dials Up Private Capital in Ownership Reform*, CAIXIN GLOB. (Aug. 27, 2017), https://www.caixinglobal.com/2017-08-27/china-unicom-dials-up-private-capital-in-ownership-reform-101136368.html [https://perma.cc/TT8P-NFUQ] (archived Feb. 17, 2020).

95. *See infra* Table 4.

96. *See* CHINA UNICOM (H.K.) LIMITED, 2017 CORPORATE SOCIAL RESPONSIBILITY REPORT 7 (2017), https://www.chinaunicom.com.hk/en/csr/reports/csr2017.pdf [https://perma.cc/ZML9-RHXU] (archived Feb. 17, 2020) [hereinafter UNICOM CORPORATE REPORT]; *see also* Kaixin et al., *supra* note 94.

97. UNICOM CORPORATE REPORT, *supra* note 96, at 7.

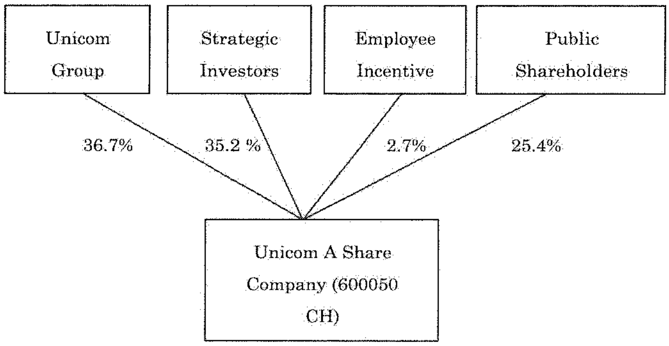
98. *Id.*

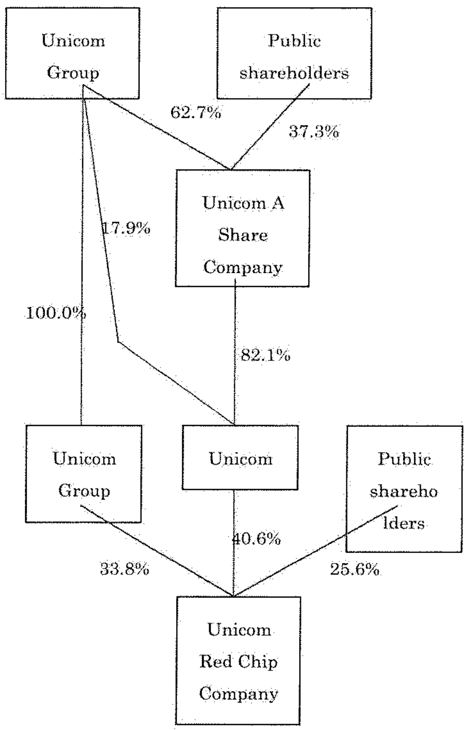
Chart 1: CUNC's Pre- and Post-MOR Equity Structure

Pre-MOR Structure

Shareholding

Unicom A Share Company's Post-MOR Shareholding Structure





- Strategic investors subscribed for about 9 billion new shares of Unicom A Share Company and purchased 1.90 billion shares of Unicom A Share Company from Unicom Group, representing in aggregate 35.2 percent of Unicom A Share Company's enlarged share capital, at a of price RMB 6.83 per share.
- Key employees were granted about 850 million restrictive shares of Unicom A Share Company at a price of RMB 3.79 per share.
- Total consideration was about RMB 78 billion.

Source: China Unicom[99]

99. See *混合所有制改革及 2017 年中期业绩* [*Mixed Ownership Reform and 2017 Interim Results*], 中国联通 [CHINA UNICOM] 6 (Aug. 21, 2017), http://www.chinaunicom-

The MOR led to the expansion of CUNC's board of directors from seven to thirteen members, in which five are independent directors. Among the eight nonindependent directors, only three were appointed by Unicom Group.[100] That is, the strategic investors, including China Life Insurance and the four tech giants, now have appointed five directors to the board.[101] According to CUNC's own announcement, the new board composition aimed to "establish sound and well-coordinated corporate governance with effective checks-and-balances" and to "strengthen the Board's authorities in critical decision-making, personnel selection and appointment and compensation allocation."[102]

Table 4: CUNC Board Composition before mixed ownership reform (as of August 12, 2016)[103]

Board of Directors		
	Name	Position/Other Info
Representing the State Company		
1	Wang Xiaochu (王晓初)	Chairman and Party Secretary of China Unicom
2	Lu Yimin (陆益民)	Vice Chairman/General Manager of China Unicom Group
3	Li Fushen (李福申)	Director/Chief Financial Officer
4	Shao Guanglu (邵广禄)	Director/Senior Vice President of China Unicom
Independent Directors		
5	Lu Tingjie (吕廷杰)	Independent Director/Professor at Beijing University of Posts and Telecommunications
6	Chen Yonghong (陈永宏)	Independent Director/Certified public accountant
7	Li Hongbin (李红滨)	Independent Director/Professor at Peking University

a.com/wcm/1/attachments/2017/8/21/1226/1503248411683.pdf [https://perma.cc/7GNH-G8DP] (archived Feb. 17, 2020).

100. *专访中国联通党组书记、董事长王晓初 联通混改实践两个一以贯之* [*Interview with Party Secretary and Chairman Wang Xiaochu of China Unicom*], XINHUA NEWS (Dec. 17, 2018), http://www.xinhuanet.com/info/2018-12/17/c_137679731.htm [https://perma.cc/RY9K-96PB] (archived Feb. 17, 2020).

101. *Id.*

102. *See* Wang Xiaochu, *Mixed-Ownership Reform & 2017 Interim Results Announcement Presentation Transcript*, CHINA UNICOM (Aug. 21, 2017), https://www.chinaunicom.com.hk/en/ir/transcript/transcript_17ir.pdf [https://perma.cc/23LD-NKQ5] (archived Apr. 26, 2020).

103. *See* TIANYANCHA, https://www.tianyancha.com/company/863877372 (last visited Aug. 12, 2019) [https://perma.cc/9XQR-H2NL] (archived Apr. 26, 2020) (providing registration information about China Unicom).

Table 5: CUNC Board Composition after mixed ownership reform[104]

Board of Directors		
	Name	Position/Other Info
Representing the State		
1	Wang Xiaochu (王晓初)	Chairman and Party Secretary of China Unicom
2	Li Guohua (李国华)	General Manager, Deputy Secretary of the Party Group, Director of China Unicom
3	Li Fushen (李福申)	Deputy Secretary and Director of the Party Group of China Unicom
Representing the strategic investors		
4	Liao Jianwen (廖建文)	Nonindependent Director/Chief Strategy Officer of JD.com
5	Yin Zhaojun (尹兆君)	Nonindependent Director/Chairman of China Life Investment Holdings Co., Ltd.
6	Lu Shan (卢山)	Nonindependent Director/Senior Executive Vice President and President of Technology Engineering Group of Tencent
7	Wang Lu (王路)	Nonindependent Director/Baidu Vice President
8	Zhang Jianfeng (张建锋) **Note**: 张建锋 replaced 胡晓明 on July 5, 2019.	Nonindependent Director/Alibaba Chief Technology Officer and President of Alibaba Cloud Intelligence Group
Independent Directors		
9	Wu Xiaogen (吴晓根)	Independent Director/Professor at the School of Accounting, Zhejiang Zhangzhou Economics University
10	Lu Tingjie (吕廷杰)	Independent Director/Professor at Beijing University of Posts and Telecommunications
11	Ma Shidong (冯士栋)	Independent Director/Engineer/ Previously a deputy secretary of State Development & Investment Corp.

104. *Management Profile: China Unicom*, EASTMONEY, http://f10.eastmoney.com/f10_v2/CompanyManagement.aspx?code=sh600050#glcjj-0 (last visited Mar. 19, 2020) [https://perma.cc/3CHP-NZP4] (archived Feb. 17, 2020) (providing a full biography of each director).

12	Chen Jianxin (陈建新)	Independent Director/A retired director of the Finance Department of the General Office of the Chinese Ministry of Personnel
13	Xiong Xiaoge (熊晓鸽) **Note**: 熊晓鸽 tendered his resignation as director on July 5, 2019. There is no known replacement for him.	Independent Director

2. Eastern Air Logistics

Eastern Air Logistics Co., Ltd. (EAL) is the logistics arm of China Eastern Air Holding Company (China Eastern), one of China's biggest airlines.[105] It started MOR in June 2017, becoming the first SOE in the aviation sector to pursue such reform. Through the MOR, China Eastern sold almost half its equity stake in EAL to four strategic investors, namely Legend Holdings (20 percent), Global Logistic Properties (GLP) (10 percent), Deppon Logistics (5 percent) and Greendland Financial (5 percent). China Eastern kept a 45 percent stake in EAL. EAL's key employees were granted 10 percent of the firm's ownership.[106]

EAL's board of directors after the MOR comprised nine members, five of which were appointed by China Eastern, two by Legend Holdings, one by the Singaporean investor GLP, and the last one by the employee shareholders.[107] This ensured the state controlling shareholder, China Eastern, a simple majority while leaving the nonstate shareholders a veto power on the board on issues concerning

105. Air China, China Southern Air, and China Eastern are the three biggest airlines in China in terms of the possession of registered aircrafts and shipping capacity. *See* UNITED CREDIT RATINGS CO. LTD., *航空运输行业研究报告* [*Research Report of 2017 on the Air-Transport Industry*] (Dec. 2017), http://pdf.dfcfw.com/pdf/H3_AP201712141066423114_1.pdf [https://perma.cc/F59S-CR9N] (archived Feb. 17, 2020); *see also China Eastern Airlines Corp. Ltd. Profile*, REUTERS, https://www.reuters.com/companies/CEA (last visited Apr. 5, 2020) [https://perma.cc/P794-WD2X] (archived Feb. 17, 2020).

106. Of the four strategic investors, Legend Holding, parent of the personal computer giant Lenovo Group Ltd., is a private company, GLP is a Singaporean company, while Deppon Logistics and Greeland Financial are two private companies. Brenda Goh, *China Eastern Sells Stakes in Cargo Unit to Four Firms*, REUTERS, June 19, 2017, https://www.reuters.com/article/us-china-eastern-cargo-idUSKBN19A0WS [https://perma.cc/4EY7-8AFH] (archived Mar. 19, 2020).

107. 东方航空物流股份有限公司首次公开发行 A 股股票招股说明书（申报稿）[*Draft Prospectus of Eastern Air Logistics Co., Ltd. For Initial Public Offering of A Shares*] 228–30, http://www.csrc.gov.cn/pub/zjhpublic/G00306202/201907/P020190705571557486703.pdf (last visited Mar. 19, 2020) [https://perma.cc/QCR8-PJWS] (archived Feb. 17, 2020).

corporate investment and budgets, according to EAL's prospectus for initial public offering (IPO) in China's stock market.[108] In December 2018, EAL was entirely converted into a joint stock company, Eastern Air Logistics Co., Ltd., and added four independent directors to its board.[109]

3. Sinopec MOR

China Petroleum & Chemical Corporation, popularly known as Sinopec, is a Chinese central SOE headquartered in Beijing and one of the world's largest oil refining, gas, and petrochemical conglomerates.[110] Sinopec was included in the first batch of SOEs selected for MOR by Chinese authorities and hence was one of the earliest MOR cases.[111] In September 2014, Sinopec entered into a capital contribution agreement with twenty-five domestic and foreign investors to sell 29.5849 percent of its shares in Sinopec Marketing Co., a subsidiary then wholly owned by Sinopec.[112] After the MOR, Sinopec still held about 70 percent of the subsidiary's total shares.[113]

It must be noted that this MOR did not bring significant change in ownership in favor of private investment, because six of the strategic investors are state-owned companies (including China Life Insurance and China Tobacco) and eleven of the strategic investors are state-controlled asset management companies or private equity houses.[114] Real private and foreign investors only acquired 9.826 percent of the total shares in the MOR.[115] Moreover, critics have also pointed out that the twenty-five investors are sharing approximately 30 percent of the shares, and this means that each shareholder will hold no more than 2.8 percent of the shares.[116] However, changes in board composition do show an early sign of the trend that a larger representation could be given to investors introduced through MOR, which in many later MOR cases appeared to be nonstate investors. In the case of Sinopec

108. *See id.* at 67 (noting China Eastern owns forty-five percent of EAL).
109. *Id.* at 54.
110. *See generally About Us*, SINOPEC GRP., http://www.sinopecgroup.com/group/en/companyprofile/AboutSinopecGroup/ (last visited Mar. 19, 2020) [https://perma.cc/698T-GLYY] (archived Feb. 17, 2020).
111. Matthew Miller & Charlie Zhu, *China's Sinopec Sale Points to Next Round of State Privatization*, REUTERS, Mar. 4, 2014, https://www.reuters.com/article/us-china-parliament-soe/chinas-sinopec-sale-points-to-next-round-of-state-privatization-idUSBREA2223820140303 [https://perma.cc/P9J7-Z9J2] (archived Feb. 17, 2020).
112. Shirley Yam, *Sinopec Offers Master Class in SOE Mixed Ownership Reform*, S. CHINA MORNING POST (Sept. 20, 2014), https://www.scmp.com/business/china-business/article/1596467/sinopec-offers-master-class-soe-mixed-ownership-reform [https://perma.cc/2VKC-6ZME] (archived Feb. 17, 2020).
113. *See id.*
114. *See id.*
115. *See id.*
116. *See id.*

Marketing, before the MOR all the seven directors were appointed by the parent company, Sinopec Corporation. After the MOR, Sinopec Corporation appointed four of the eleven directors on the board.[117] However, all the other four nonindependent directors were appointed by state-linked shareholders.

Table 6: Sinopec Marketing Board before mixed ownership reform (as of March 30, 2015)

Board of Directors[118]		
	Name	Position/Other Info
Representing the State/ Sinopec		
1	Zhang Haichao (张海潮)	Director/Chairman and Secretary of CPC Committee of Sinopec Sales Co.
2	Lu Pin (吕品)	Director/Executive Deputy General Manager of Sinopec Sales Co./ General Manager of Sinopec Sales Hubei Branch
3	Zuo Xing Kai (左兴凯)	Director/Executive Deputy General Manager of Sinopec Sales Co.
4	Liu Xionghua (刘雄华)	Director/Executive Deputy General Manager of Sinopec Sales Co./ General Manager of Sinopec Sales Beijing Branch
5	Liu Quanying (刘全英)	Director/Employee's Representative Supervisor of Sinopec Corp.
6	Liu Zurong (刘祖荣)	Director/Chief Accountant of Sinopec Sales Co.
7	Zhao Jinhui (赵锦会)	An executive in Sinopec Sales Co. but no detailed information regarding his exact position

117. *See infra* Tables 6 and 7.
118. *See* QI XIN, https://www.qixin.com/company/9fc38553-c81a-489b-a374-001f7e87d945 (last visited Mar. 19, 2020) [https://perma.cc/B25K-9WSX] (archived Feb. 19, 2020).

Table 7: Sinopec Marketing Board after mixed ownership reform

Board of Directors[119]		
	Name	Position/Other Info
Representing the State/ Sinopec		
1	Zhao Rifeng (赵日峰) Note: Zhao Rifeng (赵日峰) replaced Zhang Haichao (张海潮) on January 29, 2018.[120]	Director/Chairman and Secretary of CPC Committee of Sinopec Sales Co.
2	Xia Shixiang (夏世祥)	Director/Vice Chairman/General Manager of Sinopec Sales Co.
3	Yu Renming (俞仁明)	Director/Employee's Representative Supervisor of Sinopec Corp.
4	Xu Weidong (许卫东)	Director/Executive Deputy General Manager of Sinopec Sales Co.
Representing the outside investors		
5	Lan Yunsheng (兰云升)	Vice Chairman of the China National Petroleum Corporation
6	Zhao Xuejun (赵学军)	Nonindependent Director/Secretary of the Party Committee of Harvest Fund
7	Zhang Yuling (张霱岭)	Nonindependent Director/Deputy General Manager of Huaxia Fund and CEO of Huaxia Fund Hong Kong
8	Wang Wei (王颢)	Nonindependent Director/Vice Chairman, President and Party

119. *See* IFENG, http://finance.ifeng.com/a/20151228/14139747_0.shtml (last visited Mar. 19, 2020) [https://perma.cc/VTH7-YBGS] (archived Feb. 24, 2020); ZHONGGUO PETROLEUM & CHEM. SALES CO. LTD., https://zdb.pedaily.cn/enterprise/show7895/ (last visited Mar. 19, 2020) [https://perma.cc/6YTF-B7CC] (archived Mar. 19, 2020); QICHACHA, https://www.qichacha.com/firm_b0335502875cd0358aab6722b44f8058.html (last visited Mar. 19, 2020) [https://perma.cc/EY3D-TV6L] (Feb. 27, 2020).

120. On January 29, 2018, Mr. Zhang Haichao resigned as director, member of Strategy Committee of the Board, and the Senior Vice President of Sinopec Corp. due to his age. *See* SINOPEC, ANNUAL REPORT AND ACCOUNTS 77 (2018).

		Secretary of PICC Asset Management
Independent Directors		
9	Hu Wenrui (胡文瑞)	Independent Director/China Petroleum Association President/ Chinese Academy of Engineering Academician
10	Zhou Guomin (周国民)	Independent Director/Chief Financial Officer of Houpu Investment
11	Ning Xiangdong (宁向东)	Independent Director/Professor at Tsinghua University School of Economics and Management

4. Yunnan Baiyao MOR

Yunnan Baiyao (YNBY) is a time-honoured pharmaceutical brand for traditional Chinese medicine based in Yunnan Province of Southwestern China. It existed, in legal form, as Yunnan Baiyao Group Co., Ltd. (YNBY Group) and its parent company Yunnan Baiyao Holdings (YNBY Holdings) under the umbrella of the Yunnan SASAC. Since 2016, YNBY Group and YNBY Holdings have undergone a two-stage MOR process.[121]

In the first stage, two major strategic investors were introduced as new shareholders of YNBY Holdings. In December 2016, YNBY Holdings issued new shares to Fujian-based private company, New Huadu Industrial Group (New Huadu), granting it 50 percent of YNBY Holdings' total ownership.[122] In April 2017, the board of directors of YNBY Holdings was reconstituted, and New Huadu and Yunnan SASAC each nominated two board members.[123] The chairmanship of the board went to Wang Jianhua, who was the former chairman of Zijin

121. *See* David Blair & Li Yingqing, *Traditional Pharma Firm Furthers Reform Efforts*, CHINA DAILY (Feb. 22, 2019), http://www.chinadaily.com.cn/a/201902/22/WS5c6f5c6aa3106c65c34eac72.html [https://perma.cc/HV57-UT2E] (archived Feb. 8, 2020); *see also Local SOEs and Mixed Ownership Reform to See More Progress*, XINHUA FIN. AGENCY (Aug. 14, 2017), http://en.xfafinance.com/html/Dont_Miss/2017/353884.shtml [https://perma.cc/G6FF-WP99] (archived Feb. 8, 2020).

122. *See 国企混改案例之云南白药* [*SOE's Mixed Ownership Reform: Yunnan Baiyao as a Case Study*] (Feb. 14, 2017), http://www.sohu.com/a/126242948_481495 [https://perma.cc/Q79F-LLSX] (archived Feb. 8, 2020).

123. *See 云南白药完成混改, 新华都陈春花入选董事* [*Yunnan Baiyao Completed Its MOR, Chen Chunhua from New Huadu Appointed a Director*] (Apr. 20, 2017), https://xw.qq.com/cmsid/20170420008301/2017042000830100 [https://perma.cc/EG8C-9ZA4] (archived Feb. 8, 2020) [hereinafter *Yunnan Baiyao Completed Its MOR*].

Mining, a private company in which New Huadu had substantial ownership.[124] The former chairman of YNBY Holdings, Wang Minghui, was subsequently appointed as the chairman of YNBY Group and the CEO of YNBY Holdings.[125]

To avoid a deadlock in decision making, a second sale, totaling 10 percent of YNBY Holdings' ownership, was made in June 2017 to Jiangsu Yuyue Technology Development Co. (Jiangsu Yuyue), a private manufacturer of medical equipment.[126] Consequently, the Yunnan Provincial Government and New Huadu each hold 45 percent of YNBY Holdings' total shares.[127]

Of the two strategic investors, New Huadu was expected to help establish market-based business models for Yunnan Baiyao, while Jiangsu Yuyue would help to improve the firm's corporate governance.[128] With a new board member nominated by Jiangsu Yuyue, the board of YNBY Holdings was expanded to five members.[129] The first stage of YNBY Holdings' MOR was thus completed, which resulted in several changes in its corporate governance, including, notably, the appointment of Chen Fashu, the founder and board chairman of New Huadu, as the board chairman of YNBY Holdings in July 2018.[130] Moreover, senior executives of YNBY Holdings would no longer be treated as government officials but would become "professional managers" (*zhiye jingliren*) as if they were hired from the labour market.[131]

The second stage of the MOR process involved the merger of YNBY Holdings into its listed subsidiary YNBY Group. The plan was announced in November 2018 and the merger was successfully completed through a share swap in July 2019.[132] The Yunnan SASAC, New Huadu, and Jiangsu Yuyue now own 25.14 percent, 24.37 percent, and 5.59 percent of the shares of YNBY Group, respectively.[133] The identity and information of board candidates of the new YNBY Group were released in August 2019, pending an election in the near future.[134] The new combined enterprise would be expected to have greater synergy in its business operations by consolidating YNBY

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124. *See id.*
125. *See id.*
126. *See* Blair & Yingqing, *supra* note 121.
127. *See id.*
128. *See id.*
129. *See* 云南白药控股有限公司关于完成工商变更登记的公告 [PUBLIC DISCLOSURE BY YUNNAN BAIYAO CO. LTD. ON CHANGE OF REGISTRATION INFORMATION] (2020).
130. 云南白药控股有限公司关于法定代表人、董事长及董事发生变动 [PUBLIC DISCLOSURE BY YUNNAN BAIYAO CO. LTD. ON CHANGE OF LEGAL REPRESENTATIVE, CHAIRMAN OF BOARD, AND DIRECTORS] (2017).
131. *Yunnan Baiyao Completed Its MOR*, *supra* note 123.
132. *See* Blair & Yingqing, *supra* note 121.
133. *See id.*
134. *See id.*

Holdings' financial resources and YNBY Group's expertise in product manufacturing, marketing, research and development, and human resources.[135]

IV. IMPACT OF THE MIXED OWNERSHIP REFORM ON CORPORATE GOVERNANCE IN SOEs

This Part analyses the change brought to corporate governance of SOEs by the MOR programme. The change is being driven by both policy/regulatory initiatives and emerging practices in implementing MOR. On MOR firms' corporate governance, the SOE Reform Guidelines set out a wide range of objectives that in summary aim to provide effective checks and balances, board independence, efficiency in decision-making, directorial accountability, and also Party control.[136] As a summary, the new governance framework has the following features:

1) The CCP is being institutionalized in the formal corporate governance mechanisms of SOEs;

2) The state/government has been asked to retreat from SOE governance and not to interfere with the day-to-day management at the firm level. A wide span of regulatory measures have been released to grant more autonomy to SOEs;

3) The SOE board is expected to exercise independent power in deciding issues concerning personnel appointments, performance evaluation, and staff salary.[137]

The puzzle now is how to make sense of these apparently self-contradictory corporate governance objectives. Based on the recent general policy design for SOE reform, regulatory measures, and governance practices at firm level, it is submitted that MOR is likely to generate a partnership-based consultative governance model, in which Party leadership coexists with a board that has a certain degree of independence in the decision-making process. Such a model will strengthen the Party committee's involvement in corporate governance, but does not necessarily undermine the autonomy of the SOE in making independent decisions if the following conditions are met: (1) the Chinese government stays away from the management of

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135. *See id.*

136. *See* Barry Naughton, *State Enterprise Reform Today*, *in* CHINA'S 40 YEARS OF REFORM AND DEVELOPMENT: 1978-2018, at 375 (Ross Garnaut et al. eds., 2018) [hereinafter Naughton, *State Enterprise*].

137. *See infra* Parts IV.A, IV.B, IV.C.

the firm; (2) the role of the Party committee, institutionalized or not, does not emasculate the SOE in making decisions as a commercial entity as a whole; and (3) the board of directors is given a high degree of independence in making managerial decisions.[138]

The survey below indicates that, from policy and regulatory perspectives, the role of the Chinese government in SOEs is clearly undergoing dramatic transformation, and the state has been asked to refrain from directly interfering in SOE management. The involvement of the Party committee does not necessarily denote politicization of corporate governance in SOEs, but instead there generally appears to be cooperation, a separation of power, and responsibility in the relationship between the Party committee and the board.

A. *The State Retreats: Capital Management to Enable Enterprise Autonomy*

The essence of shifting from "asset management" to "capital management" requires the state to act generally as an owner of state capital and care mainly about the general direction of state investment and value appreciation of the state's wealth in SOEs.[139] This move involves redefining the role of the state as well as reasserting the autonomy of the SOEs to run their own businesses. Thus, from the state's perspective, it means "separation of government functions and enterprises" (*zhengqi fenkai*) and "separation of government functions and capital," as stated in the State Council's reform plan on state capital.[140]

Reform measures adopted since 2015 fairly suggest that the separation of the state (government) from the SOEs has been formalized from policy and regulatory perspectives. These measures form two major reform programmes: (i) creating state capital investment and operation companies to add a layer between SASAC

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138. In essence, the three conditions require, for the sake of effective corporate governance, an adequate separation of ownership and control while recognizing pragmatically the role of the CCP in SOEs.

139. 郝鹏 [Hao Peng], *加快实现从管企业向管资本转变，形成以管资本为主的国有资产监管体制* [*Accelerating the Change from Enterprise Management to Capital Management and Forming a New State Assets Regulatory Regime based on Capital Management*], STATE-OWNED ASSETS SUPERVISION & ADMIN. COMM'N OF THE STATE COUNCIL (Dec. 12, 2019), http://www.sasac.gov.cn/n4470048/n10286230/n12924139/n12924144/c12927371/content.html [https://perma.cc/3C4X-KYVA] (archived Feb. 8, 2020). Note the author, Hao Peng, is the Chairman of SASAC.

140. 改革国有资本授权经营体制方案 [*Notice by the State Council of Issuing the Plan for Reforming the State-Owned Capital Authorized Operation System*], PEKING UNIV. (Apr. 19, 2019), http://en.pkulaw.cn/display.aspx?cgid=c65426284846a8bcbdfb&lib=law [https://perma.cc/A2JV-CAB4] (archived Feb. 20, 2020) (China).

and SOEs and redefining the role and functions of SASAC and (ii) adopting a negative-listing approach in passing autonomy to SOEs while removing power from SASAC.[141]

1. Creation of State Capital Investment and Operation Companies and Redefining the Role of SASAC.

Since SASAC was established in 2003 as the modern "ownership agency" of China's state capitalism, it has been both the regulator of and the state investor in SOEs.[142] Flaws have been seen in both roles. As a regulator, its objective was very ambiguous. One may wonder whether there is any need for a regulator of SOEs, since no such specialized watchdog exists for privately owned enterprises. Probably for such reasons, SASAC is not treated officially as a ministry in China's bureaucratic structure. Rather, it is called a "specialized agency directly under the State Council" (*Guowuyuan Zhishu Tebie Jigou*),[143] indicating it is not unequivocally regarded as a state regulator, although it has certainly exercised regulatory powers in terms of making policies and conducting institutional consolidation for SOE reform since its creation.[144] But, as an owner, it was not put in the position to properly exercise the two main functions of ownership: receiving dividends and voting as a shareholder.[145] That is, SOEs do not pay dividends to SASAC, and SASAC does not hold the appointment power for senior positions in SOEs because the appointment power is exercised by the CCP in practice.[146]

The 2015 SOE Reform Guidelines proposed to redefine SASAC–SOE relations by adding an additional layer between SASAC and the

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141. *See* 国务院国资委以管资本为主推进职能转变方案 [*Programme of the State Council on Functional Transformation of the Role of the SASAC to Capital Management*], GEN. OFFICE OF THE STATE COUNCIL, Part II:3 (Apr. 27, 2017), http://www.gov.cn/zhengce/content/2017-05/10/content_5192390.htm [https://perma.cc/AF5Q-B76J] (archived Feb. 8, 2020) [hereinafter SASAC Reform Programme] (providing that the SASAC would not directly regulate the behavior of the state shareholder in listed companies).

142. WANG, *supra* note 2, at 652–53; *see also* Barry Naughton, *The Transformation of the State Sector: SASAC, the Market Economy, and the New National Champions*, *in* STATE CAPITALISM, INSTITUTIONAL ADAPTATION, AND THE CHINESE MIRACLE 46, 48 (Barry Naughton & Kellee S. Tsai eds., 2015).

143. *See* *国务院组织机构* [*Organizational Structure of the State Council*], http://www.gov.cn/guowuyuan/zuzhi.htm (last visited Mar. 19, 2020) [https://perma.cc/E89Y-LX98] (archived Feb. 8, 2020).

144. *See* Barry Naughton, *SASAC and Rising Corporate Power in China*, 24 CHINA LEADERSHIP MONITOR 1 (discussing SASAC's roles as an owner and regulator); *see also* ORG. FOR ECON. COOPERATION & DEV., CHINA IN THE GLOBAL ECONOMY: GOVERNANCE IN CHINA 311 (2005) [hereinafter OECD, GOVERNANCE IN CHINA] (explaining the portfolio of SASAC's original regulatory powers).

145. *See* NAUGHTON, THE CHINESE ECONOMY, *supra* note 8, at 59.

146. *See id.* at 59–61.

SOEs with the creation of state capital investment and operation companies (SCIOs).[147] The SCIOs are either state capital investment companies (SCIs) or state capital operation companies (SCOs).[148] Established under the auspices of SASAC or directly under the government, the SCIOs are authorized to act in the capacity of the state shareholder in state-invested firms.[149] The SCIOs are required to behave as shareholders in accordance with the PRC Company Law and related regulations, and participate in the governance of the SOEs through nominating directors and supervisors and voting in shareholders' meetings.[150] In addition, they are expected to be financial investors mainly concerned with financial returns rather than management.[151]

The role of SASAC is thus modified to be the special agency authorized by the State Council to function as the ultimate state investor to manage state capital and oversee state investments.[152] It is the state shareholder in many of the SCIOs.[153] However, it is those SCIOs which will be the investors/owners on behalf of the state in

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147. *See* NAUGHTON, THE CHINESE ECONOMY, *supra* note 8, at 297–328.

148. The state capital operation companies (SCOs) are entrusted to manage state capital, i.e. state shareholding in companies, with the view to maximizing the value of state assets. They are expected to serve as financial investors in SOEs or non-SOEs which operate on commercial basis. State capital investment companies (SCIs) are basically industrial investment funds which invest on behalf of the state in sectors "relating to national security or the commanding heights of the national economy" presumably for the purpose of promoting industrial policies. *See* 国务院关于推进国有资本投资、运营公司改革试点的实施意见 [*Opinions of the State Council on Implementation of Pilots of State Capital Investment and Operation Companies*], STATE COUNCIL Part II (July 14, 2018), http://www.gov.cn/zhengce/content/2018-07/30/content_5310497.htm [https://perma.cc/87HP-4F6N] (archived Feb. 8, 2020).

149. 国务院关于改革和完善国有资产管理体制的若干意见 [*Several Opinions of the State Council on Reforming and Perfecting State-owned Assets Management System*], STATE COUNCIL Points 8–9 (Oct. 25, 2015), http://www.gov.cn/zhengce/content/2015-11/04/content_10266.htm (last visited Mar. 19, 2020) [https://perma.cc/3JDW-WLXH] (archived Feb. 8, 2020).

150. *Supra* note 49, at Part II.5.

151. *Supra* note 149, at Point 9. One of the two centrally created state capital operation companies is China Reform Holdings Corp. Ltd., known as "Guoxin." *See* Naughton, *State Enterprise*, *supra* note 136, at 386. Surveying the investment practice of Guoxin, Barry Naughton observed that Guoxin exercised "a financial ownership stake in many firms without having the additional regulatory and command-and-control functions that SASAC had." *Id.* at 387.

152. *See* SASAC Reform Programme, *supra* note 141, at Part I.2.

153. 王绛 [Wang Jiang], *当前国有资本投资、运营公司运行特点及改革趋势* [*A Contemporary Survey of the Operational Features State Capital Investment and Operation Companies and the Prospect for Future Reform*], ECON. OBSERVER (Aug. 10, 2019), http://www.eeo.com.cn/2019/0810/363306.shtml [https://perma.cc/R83K-ZY5D] (archived Feb. 8, 2020) (noting nineteen state capital management companies and two state capital operation companies were established under the umbrella central SASAC and a total of 142 SCIOs were established by local SASACs).

SOEs. As a result, a layer between SASAC and the SOEs is established. Thus, the SASAC is now neither a regulator which performs public administrative functions, nor a direct shareholder in the SOEs. It is explicitly disallowed by the State Council to interfere with the independence and autonomy of SOEs.[154]

2. A Negative-List Approach to Grant Autonomy to SOEs

One of the mysteries about state–business relations in China is what oversight powers SASAC has over SOEs. As noted, SASAC was launched as an ownership agency with the "core mission . . . to carry out the government's functions as investor and owner of state assets, and thus separate these tasks from the government's role as public manager of society as a whole."[155] Before the recent round of SOE reform, SASAC's original duties included: (i) functioning as the state investor in SOEs; (ii) representing the state on the supervisory board of large SOEs; (iii) appointing, dismissing, and assessing senior executives;[156] (iv) monitoring the change of value in state assets in SOEs; (v) drafting regulations and rules on the administration of SOEs; and (vi) directing and advising SOEs under local ownership.[157] This ambiguous portfolio demonstrates that SASAC was powerful, even though SASAC rarely exercised such powers. Quite ironically, the 2017 SASAC Reform Programme, which was supposed to grant enterprise autonomy back to state firms, tellingly revealed how all-embracing and intrusive SASAC's powers were in theory.[158] For instance, the Programme displayed forty-three items which represented the powers to be given to SOEs, of which twenty-six items concerned the powers which SASAC had given up.[159]

Furthermore, through the Reform Programme SASAC decided to authorize the boards of central SOEs to exercise powers including formulating the firm's five-year plan for strategic development and the annual investment plan, appointing the members of the firm's managerial team, evaluating their performance, determining their salaries, and approving the gross payroll of the firm, among others.[160] Implicitly, the fact that SASAC explicitly gave up those powers now indicates that they were originally held by SASAC in the first place.

In April 2019, the State Council decided to adopt a negative-list approach (*qingdan guanli*) to transfer to SOEs authority to exercise

154. *See* SASAC Reform Programme, *supra* note 141, at Part I.2.

155. NAUGHTON, THE CHINESE ECONOMY, *supra* note 8, at 316.

156. Note this was more of a power on paper, as the appointment power for senior positions in an SOE is always exercised by the CCP.

157. OECD, GOVERNANCE IN CHINA, *supra* note 144, at 311.

158. *See* SASAC Reform Programme, *supra* note 141.

159. *See id.*

160. *See id.* at Part III of the Appendix.

powers which belonged to them according to the PRC Company Law and would no longer be within SASAC's province.[161] The essence of the approach is that SASAC would produce a list of powers and responsibilities (*quanli zeren qingdan*) which would *inter alia* specify which powers will be returned to the central SOEs.[162] More importantly, the SOEs will hold the residual powers (i.e., any power which is not included in the list will be regarded as, by default, belonging to the companies rather than SASAC).[163] The guiding principle for the list is that the SOEs will eventually regain, through the list, the autonomy legally conferred upon them by the PRC Company Law and other laws.[164] Under the list, the state shareholders' reach does not go beyond the board of directors and is explicitly not allowed to touch on the management of the companies.[165] The first negative list, the SASAC Power Authorization List (2019), gave twenty-one powers back to central SOEs.[166] Significantly, the SOEs have been allowed to decide on issues concerning MOR of subsidiaries, asset restructuring of subsidiaries, shareholding change in nonlisted subsidiaries, bond issuances, hiring of managerial personnel on market-based principles, approving the dividend distribution plans of subsidiaries involved in high-tech industries, extension of business to other areas, etc.[167]

B. *The CCP Advances: The Role of the Party Organization in SOE Governance*

The retreat of the Chinese government from SOEs, as discussed above, must be understood in tandem with the fact that the role of the Party in SOEs has been strengthened and institutionalized in the new round of SOE reform. Though the Party committee (*Dangweihui*) is always a significant part of an SOE's corporate governance according to official CCP policy as well as the PRC Company Law,[168] in reality, while the CCP had "maintained representative committees inside

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161. *See* 中央企业混合所有制改革回顾 [Review of the Mixed-ownership Reform of Central SOEs], *supra* note 87, at Part II.2.

162. The list is "negative" in the sense that SASAC would not exercise any power which is not explicitly provided in the portfolio of powers reserved for it.

163. *See* SASAC Reform Programme, *supra* note 141.

164. *See id.*

165. *See id.*

166. *See* 国务院国资委授权放权清单 [*SASAC of the State Council List on Power Authorization and Release*], STATE-OWNED ASSETS SUPERVISION & ADMIN. COMM'N OF THE STATE COUNCIL (June 3, 2019), http://www.sasac.gov.cn/n2588030/n2588924/c11421043/content.html [https://perma.cc/K8M2-9DYN] (archived Feb. 20, 2020).

167. *See id.*

168. *See* Wang, *supra* note 11, at 655–56.

SOEs for decades, . . . they were often moribund bodies."[169] SOE reform since Chinese President Xi Jinping took power in 2012 has however witnessed the revived role for Party leadership in the formal corporate governance mechanism of SOEs.[170] The SOE Reform Guidelines officially required "legalization of the status" (*fadinghua*) of the CCP committee by mandating that "Party-building work" be included in the SOEs' articles of association and the legal status of the CCP is explicitly provided in the enterprise's corporate governance structure.[171] Significantly, the "leadership system" in the SOE will follow the principle of "two-way access and cross-holding of positions" (*shuangxiang jinru, jiaocha renzhi*), which means candidates appointed by the Party organization in the SOE will be allowed to hold positions on the board of directors, the supervisory board, and the management team, while members of the aforesaid corporate governance institutions may be selected to be leaders of the Party organization in the firm.[172] In particular, the guidelines demand separation of the chairman of the board of directors and the general manager (CEO), but suggest that the chairman of the board of directors and the Party secretary in the company may be the same person.[173]

Numerous Chinese SOEs, including those listed in Hong Kong, have made provisions for the role of the CCP in their company constitutions or articles of association.[174] The relevant articles, which were added to the corporate constitutions by special resolutions of the shareholders' meetings, often described the Party committee as playing a core role in "an organized, institutionalized and concrete

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169. Tom Mitchell, *China's Communist Party Seeks Company Control Before Reform*, FIN. TIMES (Aug. 15, 2017), https://www.ft.com/content/31407684-8101-11e7-a4ce-15b2513cb3ff [https://perma.cc/FK9X-MHF9] (archived Feb. 8, 2020).

170. *See* Richard McGregor, *How the State Runs Business in China*, GUARDIAN (July 25, 2019), https://www.theguardian.com/world/2019/jul/25/china-business-xi-jinping-communist-party-state-private-enterprise-huawei [https://perma.cc/4TNS-P623] (archived Feb. 8, 2020).

171. NAUGHTON, THE CHINESE ECONOMY, *supra* note 8, at Part VII (24).

172. *Id.*

173. *See id.*

174. *See* Jennifer Hughes, *Chinese Communist Party Writes Itself into Company Law*, FIN. TIMES (Aug. 14, 2017), https://www.ft.com/content/a4b28218-80db-11e7-94e2-c5b903247afd [https://perma.cc/EGF2-S9P3] (archived Feb. 8, 2020); Yu Nakamura, *More Companies Are Writing China's Communist Party into Their Charters*, NIKKEI ASIAN REV. (Aug. 24, 2017), https://asia.nikkei.com/Politics/More-companies-are-writing-China-s-Communist-Party-into-their-charters [https://perma.cc/XFQ9-KGZ6] (archived Feb. 8, 2020) (reporting that 288 of the 3314 companies on the Shanghai and Shenzhen stock exchanges included provisions reflecting the CCP committee's preferences). By September 2018, 123 Chinese state-invested companies had revised their articles of association to include provisions for such purpose. *See* LI YAO, CHINESE COMMUNIST PARTY'S GROSS-ROOTS ORGANISATIONS IN STATE-OWNED ENTERPRISES: EAI BACKGROUND BRIEF NO. 1462, i (2019).

way" and "providing direction [and] managing the overall situation."[175] Significantly, it was a change that placed "the party, rather than the Chinese state, at the heart of each [SOE]."[176] The provisions in the Articles of Association of ICBC offer a standard formula to illustrate this change:

> **Article 13** In accordance with the relevant regulations of the Constitution of the Communist Party of China and the Company Law of China, organizations of the Communist Party of China (hereinafter the "Party") shall be established; the Party Committee shall play the core leadership role, providing direction, managing the overall situation and ensuring implementation. . .
>
> **Article 52** The Committee of the Communist Party of China of Industrial and Commercial Bank of China Limited (hereinafter the "Party Committee") shall be established within the Bank. The Party Committee shall consist of one secretary, two deputy secretaries and several other members. The chairman of the board of directors of the Bank and the secretary of the Party Committee shall be the same person, and one deputy secretary shall be designated to assist the secretary in carrying out Party-building work. Eligible members of the Party Committee can join the board of directors, the board of supervisors and the senior management through legal procedures, while eligible members of the board of directors, the board of supervisors and the senior management can also join the Party Committee in accordance with relevant rules and procedures. Meanwhile, commissions for discipline inspection shall be established in accordance with relevant requirements.
>
> **Article 53** The Party Committee shall, in accordance with the Constitution of the Communist Party of China and other internal laws and regulations of the Party, perform the following duties:
>
> 1) Ensure and supervise the Bank's implementation of policies and guidelines of the Party and the State, and implement major strategic decisions of the Central Committee of the Party and the State Council, as well as important work arrangements of higher-level Party organizations;
>
> 2) Strengthen its leadership and gatekeeping role in the management of the process of selection and appointment of personnel . . .
>
> 3) [S]upport the shareholders' general meeting, the board of directors, the board of supervisors and the senior management of the Bank in performing their duties in accordance with law and support the Congress of Employees in carrying out its work;
>
> 4) Assume the primary responsibility to run the Party comprehensively with strict discipline . . . and support the Party discipline inspection commissions in earnestly performing its supervisory responsibilities;

175. Hughes, *Chinese Communist Party Writes Itself into Company Law*, *supra* note 174.
176. *Id.*

> 5) Strengthen the building of the Bank's grassroots Party organizations and of its contingent of Party members . . . and unite and lead officials and employees bank-wide to devote themselves into the reform and development of the Bank;
>
> 6) Other material matters that fall within the duty of the Party Committee.[177]

The role of the Party in SOEs has always been the least understood feature in SOE governance. A 2017 survey of foreign institutional investors by the Asian Corporate Governance Association disclosed that 61 percent of the 152 foreign fund managers surveyed indicated they did not find a "clear and accountable" role of the CCP in listed companies, but 21 percent were not even aware of the Party committee's existence in the firms.[178] The aforesaid lengthy provisions in the Articles of Association of ICBC do not provide sufficient clarity for outsiders to understand what exactly the Party organization does in SOEs.[179] However, based on this Article's examination of the policy and regulatory measures, as well as amendments to the articles of association of listed SOEs relating to the role of the CCP within these SOEs, the following points with respect to the role of the Party committee in SOE governance have become fairly clear: (i) the role of the Party committee should be provided in the articles of associations of SOEs; (ii) following the principle of Party Control Cadres in the political system of China's Party-state, the Party committee reserves the authority to recommend and select top level personnel for the firm; (iii) there should be cross-holding of offices by Party committee members and members of the firm's senior personnel; and (iv) the Party committee should lead and strengthen the Party-building work in the firm. What is unclear now is to what extent and at what stage the Party committee is involved in the firm's decision-making, and whether this involvement undermines the firm's ability to make decisions on a commercial basis.

C. *Separation of Power between the Party and the Board*

With the above discussion about the extensive and growing power of the Party committee in SOEs, it would sound somewhat ironic to start any conversation about "board independence" in Chinese SOEs. As alluded to in the previous discussions, the official documents issued by the CCP Central, the State Council, and ministries of the Chinese

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177. ARTICLES OF ASSOCIATION OF INDUSTRIAL AND COMMERCIAL BANK OF CHINA LIMITED, INDUS. & COMMERCIAL BANK OF CHINA 3, 14–15 (2017), http://v.icbc.com.cn/userfiles/Resources/ICBCLTD/download/2017/gszc_en.pdf [https://perma.cc/3VN5-AD8D] (archived Feb. 20, 2020) (emphasis added).

178. JAMIE ALLEN & LI RUI, AWAKENING GOVERNANCE: THE EVOLUTION OF CORPORATE GOVERNANCE IN CHINA 39 (Asian Corp. Gov. Assoc. 2018).

179. *See supra* note 177 and accompanying text.

government in relation to the recent round of SOE reform, including MOR, have raised two apparently contradictory objectives. Namely, the MOE is expected to both ensure that the board is able to exercise its powers of management[180] and to allow the Party organization to "play the role of political core" in the SOE and exercise powers in personnel appointment and other matters.[181]

It is thus obvious that the Party-state has established two "supremes" in corporate governance, since both the board of directors and the Party organization are prescribed to be the decision-making bodies in the SOEs.[182] The question then is whether there is any separation of power, or at least division of labour, between the two. On personnel management, official policy suggests the Party committee should be in charge of forming the "leading body" (*lingdao banzi*) of the SOE, understood as a group of top leaders of the firm including the chairman of the board, the general manager (Chief Executive Officer), important deputy general managers, key senior executives, and important Party committee leaders.[183] The essence of this policy is that the board of directors is allowed to appoint members of the managerial team (who are however not members of the leading body),[184] including the middle-level corporate officers such as leaders of the various departments in a company. The board is also the principal body involved in the day-to-day management of the SOEs even though there

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180. *See* NAUGHTON, THE CHINESE ECONOMY, *supra* note 8, at 179–208.

181. *See id.* at Points 24–5.

182. It is also known as the "twin governance structures" in SOEs. *See* Wang, *supra* note 11, at 648–59.

183. For instance, the "leading body" of China Railway Group Limited comprised seven leaders, including the Chairman of the Board of Directors who was also the Secretary of the Party Committee, the General Manager who was the Deputy Party Secretary, a Deputy General Manager, a specialized Party committee members, the Secretary of the Party's Disciplinary Inspection Committee, the company's Chief Financial Officer, and the company's General Counsel. *See* CHINA RY. GRP. LTD., *公司领导班子* [*Leading Body of the Company*], http://www.crecg.com/chinazt/1116/1120/31752/index.html (last visited Mar. 19, 2020) [https://perma.cc/55F9-WV6Q] (archived Feb. 8, 2020).

184. *See 关于在深化国有企业改革中坚持党的领导加强党的建设的意见* [*Certain Opinions of the General Office of the CCP Central Committee on Upholding the Party's Leadership and Strengthening Party Building in Deepening the Reform of State-owned Enterprises*] (these Opinions were known to be issued through press release but have not been fully made public); *see also* 中共中央办公厅印发《关于在深化国有企业改革中坚持党的领导加强党的建设的若干意见 [*The General Office of the CCP Central Committee Issued Certain Opinions on Upholding the Party's Leadership and Strengthening Party Building in Deepening the Reform of State-owned Enterprises*], (Sept. 20, 2015), http://www.gov.cn/xinwen/2015-09/20/content_2935593.htm [https://perma.cc/NW9X-NVUP] (archived Feb. 8, 2020) (an unofficial version of the Opinions can be found at http://xtkg.hnfun.com/upload/files/2016/6/2916421140.docx [https://perma.cc/P56P-3XYL] (archived Mar. 19, 2020)).

may be overlapping appointments in the Party committee and the board.

D. *An Emerging Partnership-Based Corporate Governance Model?*

The MOR, together with other related reforms launched by the Chinese Party-state in recent years, has brought certain changes, some of which are rather fundamental, to the corporate governance structure in Chinese SOEs. It is argued in this Article that all the reforms are pushing SOE governance towards a partnership based, control-sharing model, especially in MOR firms, in which the Party representatives work together with private investors and share the authority to govern.

First, MOR has resulted in significant reduction of state ownership in MOR firms.[185] Although the state still remains the largest shareholder and is usually in a controlling position, the authors of this Article observe a clear tendency toward less state-ownership concentration in MOR enterprises, measured by the transfer of roughly 15 percent to 45 percent of state-owned equity to other investors, though some of these investors may be state entities.[186]

Second, through the reforms, the boundary between the Chinese government and SOEs has been noticeably drawn and the separation of power herein is more institutionalized. As discussed previously, SOEs are evidently acquiring more enterprise autonomy from the Chinese state because of the negative-list approach. Further, there are now explicit provisions on the separation of power between the state and SOEs, which provide that the state shareholders shall exercise their rights and powers in accordance with the Company Law and other relevant laws like any other shareholder.[187] This significant move paves the way for Chinese corporate law, which is still ownership neutral, to apply more or less equally to SOEs and private firms. As ownership in a firm is proportionally associated with power and influence,[188] the shrinking state ownership in the MOR enterprises has made it possible—and even necessary in many cases—for a coalition-based governance structure to be established for the state shareholders and private shareholders to share power.

Third, the participation of the Party committee in SOEs has certainly been more institutionalized in the sense that the role of the Party is now clearly required to be provided in the articles of association.[189] This is certainly not positive news for those who wish

185. *See supra* Table 3.
186. *See id.*
187. *See supra* Part IV.A.
188. *See supra* notes 14, 15, 16 and accompanying text.
189. *See supra* Part IV.B.

for complete separation of the Party-state from the SOEs. The flipside of this change is that clarifying the role of the Party committee in the articles of association can improve transparency in SOE governance.[190] More significantly, the division of labor between the Party committee and the board of directors has been clarified, which leaves room for the board to maintain a limited degree of independence in making personnel decisions, in addition to the business operation decision-making powers, which already fall within the purview of the board.[191]

Fourth, the MOR practice of several significant SOEs demonstrates that shareholder representation on the board of directors has been improved, and power-sharing among shareholders in the shareholders' meeting and board of directors has begun to occur.[192] The fact that the state shareholder maintains a less than simple majority in representation on the board, coupled with a certain degree of independence reserved for the board in the new setting with more institutionalized and transparent participation of the Party committee, makes it not only possible but also inevitable for the controlling state shareholders to share power in decision making with other shareholders in SOEs with more diversified ownership structures.

IV. UNDERSTANDING MIXED-OWNERSHIP'S IMPACT ON SOE GOVERNANCE: THE BENEFIT OF SHARING CONTROL

This Part offers explanations about some of the reasons behind the MOR drive. It argues that, among other reasons, the MOR is inspired by the benefits of improved corporate governance and performance in SOEs through sharing of control between the controlling state shareholder and large nonstate shareholders (or even other state shareholders in some cases).

This rationale starts with the conventional wisdom that ownership matters. As Sanford J. Grossman and Oliver D. Hart argued, the value of ownership in a firm lies in the benefits of control which are not able to be enjoyed by outside investors through contracts.[193] That is, "contractual incompleteness" entails that,

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190. *See Interview: 'Moving Party committees in front of the curtain'* and *Interview: 'Specifying the Party's role will improve transparency'*, *in* AWAKENING GOVERNANCE: THE EVOLUTION OF CORPORATE GOVERNANCE IN CHINA, *supra* note 178, at 49–50 (noting the amendment of articles of association in relation to the role of the CCP "means that the Party committee moves from behind the scenes to the front of the curtain, increasing transparency").

191. *See supra* Part IV.C.

192. *See supra* Part III (regarding the empirical and case studies).

193. *See* Sanford J. Grossman & Oliver D. Hart, *The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration*, 94 J. POL. ECON. 691, 691–92 (1986).

because it is either impossible or "too costly for one party to specify a long list of the particular rights it desires over another party's assets,"[194] it may be optimal for that party to purchase all the rights not specified in the contract. In other words, ownership "is the purchase of these residual rights of control,"[195] which has positive efficiency consequences as compared to the permanently incomplete contracts. Thus, ownership always matters because it brings about the benefit of control, and change in ownership often leads to adjustment in control rights. This is certainly the case in the Chinese context, evidenced characteristically by the provisions in the PRC Company Law, which, in principle, allocate voting power on the basis of equity ownership in a firm.[196]

Mike Burkart, Denis Gromb, and Fausto Panunzi, however, observe that ownership structure involves a trade-off between control and managerial initiative, and "a concentrated ownership structure induces high levels of monitoring and control but renders management less active."[197] In other words, dominant control of ownership may reduce incentives and result in inefficiency. Marco Pagano and Ailsa Roell suggest that, from the viewpoint of an initial owner who takes into account "his own future private benefits," he would choose to have the ownership of the firm "sufficiently dispersed to ensure the optimal degree of monitoring," often through going public.[198] On the other hand, Armando Gomes and Walter Novaes identified "sharing control," which occurs when a single shareholder cannot make unilateral decisions in a company, as a new corporate governance mechanism.[199] They maintained that, in a firm with multiple controlling shareholders, the disagreements among those shareholders may prevent major corporate decisions from harming minority shareholders, thus improving corporate governance while preserving private benefits of control.[200] This is because the control is still shared within the control groups which can internalise firm value to a greater extent than in a situation where shares are sold largely to minority shareholders.[201] Furthermore, because of the *ex post* bargaining problems among controlling shareholders, sharing control "provides a compromise between the excessive monitoring of an outside investor

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194. *Id.* at 692, 717.

195. *Id.* at 692.

196. *See* WANG, *supra* note 2, at 156–60.

197. Mike Burkart, Denis Gromb & Fausto Panunzi, *Large Shareholders, Monitoring, and the Value of the Firm*, 112 Q.J. ECON. 693, 694 (1997).

198. Marco Pagano & Ailsa Roell, *The Choice of Stock Ownership Structure: Agency Costs, Monitoring, and the Decision to Go Public*, 113 Q. J. ECON. 187, 215 (1998).

199. *See generally* Armando Gomes & Walter Novaes, *Sharing of Control as a Corporate Governance Mechanism* (Rodney L. White Ctr. for Fin. Research, Working Paper No. 09-01, 2000).

200. *See id.* at 1.

201. *See id.* at 1–2.

who does not internalize the private benefits and the excessive discretion of an unchecked controlling shareholder."[202]

Overmonitoring problems and undermonitoring problems exist in Chinese SOEs, though they come from the same controlling shareholder, the state. Lay-Hong Tan and Jiangyu Wang observed that there are two types of idiosyncratic problems in China's SOEs.[203] The first one, the undermonitoring problem, stems from the phenomenon of "strong managers, weak owners" caused by the dominant position of state shareholding coupled with the absence of state monitoring in SOEs.[204] As the state was little more than an abstract owner, it had to act through appointed agents, which in many cases were civil servants and government officials whose interests were not always aligned with the state, leading to a situation where "the principal is virtually non-existent" and a model of insider control which is called "*guanjianren kongzhi* (key-person-control)."[205] In this undermonitoring model, such a key person, who is usually the SOE's general manager (chief executive officer or CEO) or the chairperson of the board of directors, becomes "the super-sovereign and the sole commander of the company."[206] The key persons would disregard the property rights of the company as well as that of both the state and nonstate shareholders in the SOE.[207] The rampant corruption in SOEs demonstrated that, in many firms, SOE key persons were out of control, even from the hands of the state, and represented only their personal interests rather than being a loyal agent to the state.[208] As Chen Gang pointed out, Chinese President Xi Jinping's anticorruption drive against SOE officials in the 2013–2014 period, in the form of the inspection of fourteen major SOEs by the CCP's Central Commission for Discipline Inspection, led to the fall of over seventy SOE executives. These executives were found to be involved in "accepting bribes in procurement, buying and selling of official positions, wining and dining at public expense and assisting relatives in starting business with returns."[209] The behaviour of these key persons certainly harmed the interests of the minority shareholders, but they also undermined the interests of the controlling state shareholder.[210] In short, the dominant

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202. *Id.* at 2.

203. *See generally* Lay-Hong Tan & Jiangyu Wang, *Modelling an Effective Corporate Governance System for China's Listed State-owned Enterprises: Issues and Challenges in a Transitional Economy*, 7 J. CORP. L. STUD. 143 (2007).

204. *See id.* at 149.

205. *Id.* at 149–50.

206. *Id.* at 150.

207. *See id.*

208. *See id.* at 150.

209. CHEN GANG, CHINA'S GRAFT BUSTERS TARGET STATE-OWNED ENTERPRISES: EAI BACKGROUND BRIEF NO. 1058, 1–2 (2015).

210. This is because the key persons put their own interest above the interest of all shareholders, including the state.

but abstract position of state ownership in SOEs caused, in many cases, an undermonitoring problem which left the companies in the private hands of a few individuals.

There are also problems resulting from overmonitoring and excessive intervention from the state shareholder at the expense of the SOEs and its minority shareholders. Tan and Wang observed that "[m]any SOEs are debt-ridden enterprises 'repackaged' for listing and continue to be controlled by their parent companies who, having successfully seen to their IPO, look towards them as cash cows for ready milking."[211] Tunneling by controlling shareholders is pervasive in both SOEs and privately owned companies (POEs).[212] Further, the overmonitoring problems caused by the parent also bred weak managerial incentives in some instances because the appointments to managerial positions in SOEs were politically determined.[213]

The MOR, which is essentially partial privatization, thus offers a practical solution to the undermonitoring and overmonitoring problems in Chinese SOEs—by establishing a partnership-based, sharing of control governance model. Through the MOR, nonstate social/private capital is introduced into the SOEs to effect ownership change and diversified board composition by giving nonstate shareholders a larger representation on the board. This change is tied in with other institutional changes, which further strengthen control sharing as described above, including shifting the regulatory philosophy of the state shareholder from asset management to capital management and the release of powers from SASAC to SOEs.

Findings in the empirical and econometric literature on corporate governance in China consistently support the idea that Chinese SOEs with a certain degree of mixed ownership produced the most optimal performance results in the current political setting, which arguably strengthened the Chinese Party-state's political will to promote the MOR.[214] An earlier study by Qian Sun, Wilson H. S. Tong, and Jing Tong surveyed the firm performance of all companies listed on the Shenzhen Stock Exchange (SZSE) and Shanghai Stock Exchange (SSE) and found a positive correlation between government ownership and firm performance.[215] In other words, "partial government

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211. Tan & Wang, *supra* note 203, at 150–51 (noting a listed SOE, Luoyang Chundu, had to go bankrupt because its parent company borrowed and did not repay RMB 330 million after its IPO in 1998).

212. *See* Guoping Li, *The Pervasiveness and Severity of Tunneling by Controlling Shareholders in China*, 21 CHINA ECON. REV. 310, 311 (2010) (noting "tunneling by controlling shareholders is widespread and severe").

213. *See* Cyril Lin, *Corporatisation and Corporate Governance in China's Economic Transition*, 34 ECON. PLAN. 5, 7–8 (2001).

214. *See infra* notes 214–221 and accompanying text.

215. *See* Qian Sun, Wilson H. S. Tong & Jing Tong, *How Does Government Ownership Affect Firm Performance? Evidence from China's Privatization Experience*, 29 J. BUS. FIN. & ACCT. 1, 3 (2002).

ownership has a positive impact on SOE performance."[216] The authors, however, discovered that the relationship was nonlinear and followed "an inverted U-shape" pattern.[217] To wit, "100% government ownership is not good, but no government ownership is not good either. The optimal government ownership may be somewhere in between,"[218] though the authors did not address what was the "optimal" percentage of state ownership. In any event, as Gary H. Jefferson and Jian Su suggested, the conversion of SOEs to shareholding companies incorporated under the Company Law "contributes to overall increases in both current productivity and innovative effort."[219]

More recently, Guy S. Liu, John Beirne, and Pei Sun observed that "partial privatization, which leads to mixed ownership, can be an optimal form of privatization in the context of China's political system which is characterized by state capitalism" in investigating the performance of 1,184 firms in China, which underwent ownership transformation over the period of 1997 to 2003.[220] The authors concluded that ownership restructuring, particularly that which brought private investment to state firms, was the most appropriate approach to reforming SOEs and also enabled firms to gain favourable synergy gains from both the government and private sector.[221]

Apart from benefiting from sharing control, it is increasingly clear that the MOR also functions as industrial policy for the Chinese state to make use of private resources—which include not merely capital—to help SOEs grow stronger. The more important resources are the technologies, talents, and market networks owned by the potential private strategic investors. In the case of China Unicom's MOR, the intention was announced at the planning stage of the MOR that China Unicom would choose to sell stakes to potential shareholders, which were referred to by China Unicom as "cooperation partners" (*hezuo huoban*), on the condition that they could complement China Unicom's business, especially in the Internet industry.[222] Soon after, China Unicom announced strategic cooperation plans with Alibaba and Tencent, China's e-commerce giants which were also the leading

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216. *Id.* at 22.

217. *Id.* at 19.

218. *Id.*

219. Gary H. Jefferson & Jian Su, *Privatization and Restructuring in China: Evidence from Shareholding Ownership, 1995-2001*, 34 J. COMP. ECON. 146, 146 (2006).

220. Guy S. Liu, John Beirne & Pei Sun, *The Performance Impact of Firm Ownership Transformation in China: Mixed Ownership vs. Fully Privatised Ownership*, 13 J. CHINA ECON. BUS. STUD. 197, 198 (2015).

221. *See id.* at 212.

222. *See 联通混改将选择互补性强合作方* [*China Unicom's MOR Would Target Cooperation Partners which Strongly Complement its Business*], CHINA SEC. DAILY (Nov. 5, 2016), http://finance.ifeng.com/a/20161105/14986787_0.shtml [https://perma.cc/2TBB-VAZG] (archived Feb. 11, 2020).

private investors in the Chinese Unicom MOR programme.[223] The agreement with Tencent was presented as the "first major business cooperation with strategic investors after China Unicom's [MOR] proposal was approved," in which the two shareholders of post-MOR CUNC committed to cooperate and share resources to build a new internet–industry ecosystem platform.[224]

V. CONCLUSION

There is a body of literature that has found that in general the profitability and efficiency of resource allocation in SOEs are lower than in private firms.[225] This recognition has led to attempts by various countries from time to time to reform their SOEs, and China is only one example. However, the reform of SOEs is not without its challenges. For example, A. Musacchio, E.I.P. Ayerbe, and G. Garcia explored the challenges that certain Latin American countries faced when attempting to reform their SOEs.[226] In particular the authors pointed to the corporate governance problem and the fiscal governance problem.[227] To overcome these problems, they advocated that governments should design governance mechanisms that rely on the market, on *ex ante* administrative controls, or on hybrid solutions.[228] The mechanisms should be designed on a case by case basis that suit

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223. *See China Unicom Announces Cooperation with Tencent and Alibaba Following Mixed-Ownership Reform*, TELECOM REVIEW ASIA (Oct. 24 2017), https://www.telecomreviewasia.com/index.php/news/industry-news/814-china-unicom-announces-cooperation-with-tencent-and-alibaba-following-mixed-ownership-reform [https://perma.cc/5D6Z-B5PV] (archived Feb. 11, 2020).

224. Press Release, China Unicom Ltd., China Unicom's Mixed-Ownership Reform Leaps Forward in Business Cooperation with Tencent (Oct. 23, 2017) (on file with author).

225. *See generally* Anthony E. Boardman & Aidan R. Vining, *Ownership and Performance in Competitive Environments: A Comparison of the Performance of Private, Mixed, and State-Owned Enterprises*, 32 J.L. & ECON. 1 (1989); Kathryn L. DeWenter & Paul H. Malatesta, *State-Owned and Privately Owned Firms: An Empirical Analysis of Profitability, Leverage, and Labor Intensity*, 91 AM. ECON. REV. 320 (2001); Yuan Ding, Hua Zhang & Junxi Zhang, *Private vs. State Ownership and Earnings Management: Evidence from Chinese Listed Companies*, 15 CORP. GOV. 223 (2007); Eski Goldeng, Leo A., Grunfeld & Gabriel R. G. Benito, *The Performance Differential between Private and State Owned Enterprises: The Roles of Ownership, Management, and Market Structure*, 45 J. MGMT. STUD. 1244 (2008); David A. Ralston, et al., *Today's State-Owned Enterprises of China: Are They Dying Dinosaurs or Dynamic Dynamos?* 27 STRATEGIC MGMT. J. 825 (2006); Andrei Shleifer, *State versus Private Ownership*, 12 J. ECON. PERSP. 133 (1998); Aidan R. Vining & Anthony E. Boardman, *Ownership versus Competition: Efficiency in Public Enterprises*, 73 PUB. CHOICE 205 (1992).

226. *See generally* Aldo Musacchio, et al., *State-Owned Enterprise Reform in Latin America: Issues and Possible Solutions* (Inter-American Dev. Bank, Discussion Paper No. IDB-DP-401, 2015).

227. *See id.* at 3–4, 9–16.

228. *See id.* at 17–41.

the circumstances.[229] Similarly, Stefano Clò, *et al.* found from their study of the reforms in ten major Italian SOEs from 2004 to 2013 that listed SOEs that operated in liberalized markets gained higher profits and dividends, while unlisted SOEs operating in noncompetitive markets that are compelled to maintain an informal public mission often incur economic losses.[230]

Similarly, the MOR programme is the Chinese government's attempt to further expose its SOEs to market forces, while at the same time subject governance to greater scrutiny and supervision. In the absence of large institutional investors across China's capital market, the strategic investors can play such a role. Indeed, the scale of this type of investment in the SOEs, coupled with the strategic investors' accountability to their own shareholders, provides the investors with the incentive to monitor management. Arguably, their ability to do so is enhanced by the board seats that many of the strategic investors hold, unlike many institutional investors. As Table 3 shows, of thirty-three SOEs surveyed, sixteen have outside directors that constitute a majority of the board.[231] It must also be recognized that many if not all the strategic investors have strong links to the Party-state itself. This is true not only for the state-owned strategic investors but also the large private ones as well, given that links with the Party-state have hitherto been important for commercial success. It will, therefore, be much more difficult today for powerful managers to abuse their positions for personal gain.

At the same time, the clearer mandate within the corporate constitution of the party committee potentially acts as another check on management abuse as one of the key roles of the committee is to ensure discipline on the part of Communist Party members, which is still an essential requirement for advancement to the higher levels of management. Through its control of personnel appointments and responsibility for discipline, it is in a position to remove senior managers who abuse their positions. This aspect of the MOR programme can be seen as a logical extension of President Xi Jinping's drive to root out corruption within the Party-state.

While the desire for SOE reform appears strong, it remains to be seen how such reform tendencies can be sustained and institutionalised as opposed to being the personal initiative of the current, strong leader. In countries with a competitive democratic system, the need to establish legitimacy at each election cycle can act as a constraint on the ruling party of the day. This certainly was the Singapore experience in the 1950s and 1960s when a weak People's

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229. *See id.* at 1.

230. *See* Stefano Clò, et al., *Italian State-Owned Enterprises After Decades of Reforms: Still Public?* 4 (CIRIEC, Working Paper No. 19, 2015).

231. *See supra* Table 3.

Action Party (PAP) government relied on sound economic management, including the management of Singapore's SOEs, to deliver tangible benefits to the public and thereby cemented its support over time. This narrative on the part of the PAP, coupled with the need to win a mandate every four to five years, continues to act as a constraint on the PAP.[232] It is not clear that the Chinese Party-state, which is itself above the law, faces sufficient institutional constraints to ensure a deep rooted commitment to good governance in SOEs.

232. *See* Tan Cheng-Han, *The Beijing Consensus and Possible Lessons from the "Singapore Model"?* 15–17 (Nat'l Univ. of Sing., Working Paper No. 001, 2016); Tan et al., *supra* note 60, at 85.

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