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China's "Corporatization without Privatization" and the Late Nineteenth Century Roots of a Stubborn Path Dependency

Nicholas Calcina Howson[*]

ABSTRACT

This Article analyzes the contemporary program of "corporatization without privatization" in the People's Republic of China (PRC) directed at China's traditional state-owned enterprises (SOEs) through a consideration of long ago precursor enterprise establishments—starting from the last Chinese imperial dynasty's creation of "government-promoted/-supervised, merchant-financed/-operated" (guandu shangban) firms in the latter part of the nineteenth century. While analysts are tempted to see the PRC corporations with listings on international exchanges that dominate the global economy and capital markets as expressions of "convergence," this Article argues that such firms in fact show deeply embedded aspects of path dependency unique to the Chinese context even prior to the fall of the Qing dynasty in 1911. To that end, this Article identifies commonalities between China's large-scale state (imperial court)-promoted or -operated enterprises after 1870 and the PRC's largest corporations and corporate groups that have grown since the early 1990s—commonalities which touch on the national development ambitions behind such firm establishments, financing, operations, monopoly franchise rights, corporate governance, relationship to law and domestic and transnational legal systems, the interaction between the state and other non-state sectors, and more. Conversely, the Article investigates key differences in the surrounding geopolitical, political, legal, economic, and market environments between the late nineteenth century and today, so as to explain how today's largest Chinese enterprises are, and will be, distinct from their nineteenth century ancestors. This Article does not address the extent to which China's corporatized, publicly held

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SOEs should be understood as "sovereign" for purposes of evaluating foreign sovereign immunity and the like. Instead, this Article aims to help policy makers, global capital markets participants, and even corporate governance specialists understand more concretely the underlying differences between modern China's apparently convergent corporations, on one side, and corporate enterprises operating and financed in other parts of the world, on the other. This analysis may, in turn, illuminate the future trajectory of the PRC and its rising corporate entities as global political and economic actors of abiding power and influence.

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I. CONVERGENCE, PATH DEPENDENCY, AND THE "CORPORATIZED" CHINESE STATE-OWNED ENTERPRISE (SOE)

For almost two decades, developed-world academic discourse on "the firm," corporate governance, and corporate and securities law has fixated on the possibility of global "convergence" and the continuing frustration of that possibility because of "path dependence."

On the one side, convergence with respect to firm organization and governance across distinct political, economic, and legal systems seemed assured given agreement on what kind of firm was most economically efficient—efficient in its productive tasks, but also what kind of firm (active in what kind of capital market) offered the best mechanism for the efficient allocation of capital. This, so argued the strongest proponents of convergence, was the Anglo-(US) American "shareholder-oriented" model of firm organization and governance: widely held companies with most or all of their shares publicly traded, featuring complete separation of ownership and management, all regulated by (i) enabling corporate law with a key role ceded to *ex*

post standard-applying common law-style judicial institutions,[1] and (ii) a securities regulatory system focused on mandatory information disclosure and strict prohibitions on insider and manipulative trading.[2] Emphasis on the way to best ensure the efficient allocation of capital allowed for the possibility of slightly weaker convergence but specifically with respect to the world's largest publicly listed companies, or a convergence driven by the shared expectations of the increasingly global capital markets and the impact of the securities law and regulation of those markets on the law of corporate organization and governance.[3] Perhaps the most penetrating vision of convergence identified national systems where *functional* convergence (sometimes effected simply by contract) might occur, notwithstanding apparently frustrated *formal* convergence.[4] Informing this side of the debate was a justified questioning of the viability and long term success of organizational and legal transplants from allegedly more mature political, economic, and legal systems (mostly Northern hemisphere Western, but usually including pre-Recession Japan) to "less developed" national systems.[5]

On the other side, academic analysts predicted not convergence, but stubborn and persistent "divergence," resulting from historical developments and political and ideological forces unique to the still-relevant national unit.[6] These path-dependent factors resulted not only in specific, and distinct, firm capital structures and legal and organizational norms, but also in insulation of certain national

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1. See, in particular, the "legal origins" law and finance literature, attempting to prove empirically that an Anglo-American, common law system is superior, at least in comparison to civil law systems and with respect to the creation of strong and efficient capital markets. These authors asserted that (i) common law jurisdictions are more protective of property rights generally, and specifically the rights of minority shareholders in corporate firms, and (ii) civil law systems "over-regulate" private economic activity, and private ordering in particular. *See* Rafael La Porta, Florencio Lopez-de-Silanes, Andrei Shleifer & Robert W. Vishny, *Legal Determinants of External Finance*, 52 J. OF FIN. 1131, 1149 (1997).

2. *See* Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439, 455–56 (2003).

3. *See* John C. Coffee, Jr., The Future as History: The Prospects for Global Convergence in Corporate Governance and its Implications, 93 NW. L. REV. 641, 707 (1999).

4. *See* Ronald J. Gilson, *Globalizing Corporate Governance: Convergence of Form or Function*, 49 AM. J. COMP. L. 329, 338 (2001).

5. *See* Hideki Kanda & Curtis J. Milhaupt, *Re-examining Legal Transplants: The Director's Fiduciary Duty in Japanese Corporate Law*, 51 AM. J. COMP. L. 887, 889 (2003); Curtis J. Milhaupt, *In the Shadow of Delaware? The Rise of Hostile Takeovers in Japan*, 105 COLUM. L. REV. 2171, 2208–09 (2005).

6. *See* Lucian A. Bebchuk & Mark J. Roe, *A Theory of Path Dependence in Corporate Ownership and Governance*, 52 STAN. L. REV. 127, 167–70 (1999); Mark D. West, *The Puzzling Divergence of Corporate Law: Evidence and Explanations from Japan and the United States*, 150 U. PA. L. REV. 527, 553–55 (2001) (noting divergence in Japanese and United States corporate law between 1950 and 2000 despite similar starting positions).

systems or practices from the global forces identified as the drivers behind hoped-for convergence—mostly the firm and capital allocation efficiency goals described above.[7]

In the almost two decades between the start of the convergence/ path-dependency debate and the present day, the globe has witnessed the rise of explicitly *corporate* behemoths from the People's Republic of China (PRC or China). These PRC-controlled firms, whether domiciled in the PRC "mainland"[8] or outside, now complete the largest initial public offerings (IPOs) and corporate finance transactions in history, dominate listings of the world's largest enterprises by market capitalization and revenues, have shares traded on both PRC exchanges and the major international stock exchanges, and act increasingly beyond China's national borders to acquire control of firms and assets positioned in other national jurisdictions, including many of China's erstwhile tutors in the arts of economic and legal system development.

Superficial analysis—not just from global underwriters managing and hard-selling gargantuan PRC-origin IPOs—has always explicitly trumpeted the PRC's new corporate entities and the corporate governance system within which they are situated as "convergent" in the terms described above.[9] After all, they say, the PRC's corporate firms feature every formal aspect of a "modern" corporation and corporate law system:

- legal personality for the firm;
- perpetual existence of the corporation;
- "owner-shielding" asset partitioning (i.e., limited liability for investor shareholders) coupled with "entity-shielding" asset partitioning (i.e., state-provided rules that protect the firm from the claims of creditors of the firm's investors or other entities in which such shareholders are invested);[10]
- formal separation of ownership (the shareholders) from management (the board of directors);
- centralized management (the board of directors, again) acting pursuant to a simple majority vote;

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7. *See* Bebchuk & Roe, *supra* note 6, at 150; West, *supra* note 6, at 601.

8. For the purposes of this article, the PRC means the PRC excluding the Special Administrative Regions of Hong Kong and Macao, and Taiwan/the Republic of China.

9. *See, e.g.*, Chao Xi, *In Search of an Effective Monitoring Board Model: Board Reforms and the Political Economy of Corporate Law in China*, 22 CONN. J. INT'L L. 1, 27 (2006) ("China's board reform strategy, featuring the mandatory independent director requirement for listed companies, clearly demonstrates a formal convergence toward the Anglo-American governance model.").

10. *See* Henry Hansmann, Reinier Kraakman & Richard Squire, *Law and the Rise of the Firm*, 119 HARV. L. REV. 1335, 1337–40 (2006) (examining entity shielding as a universal characteristic of modern business firms).

- indicia of a desirable "shareholder orientation" in the PRC's formal company law and securities regulation, including: a board of directors elected and removed by voting shareholders; officers appointed by a board of directors responsible to the shareholders; corporate fiduciary duties owed to the firm (and its shareholders) by orthodox fiduciaries (directors, supervisory board members, and officers) and even controlling shareholders; corporate law doctrines like "oppression" (to protect minority shareholders) and a corporate derivative action allowing minority shareholders to work around the board in suing breaching fiduciaries on behalf of the firm, etc.;
- free transferability of, often publicly-traded, share capital;
- veil piercing (to protect third party creditors in tort or contract), etc.

At the same time, there has been a good deal of writing by more discerning analysts identifying how the products of China's "corporatization without privatization" established in the political-legal system and corporate governance ecology unique to the post-1978 Reform-era PRC are anything but convergent and have a "Chinese characteristics"-hugging path dependency.[11] That path dependency is often understood as rooted in (i) China's post-1949 political and ideological settlement, or the basic tenets of Mao Zedong's elaboration of Marxist orthodoxy, which requires that ownership of the means of production be firmly vested in "the people"[12] as represented by the Chinese Communist Party (CCP)-controlled state (the PRC Party State), (ii) China's development model—increasingly called "state capitalism"[13]—and (iii) resistance

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11. *See, e.g.*, Donald C. Clarke & Nicholas C. Howson, *Pathway to Minority Shareholder Protection: Derivative Actions in the People's Republic of China in* THE DERIVATIVE ACTION IN ASIA: A COMPARATIVE AND FUNCTIONAL APPROACH 243, 245–47 (Dan W. Puchniak, Harald Baum & Michael Ewing-Chow eds., 2012); Donald C. Clarke, *Corporate Governance in China: An Overview*, 14 CHINA ECON. REV. 494, 494-95 (2003); Nicholas C. Howson, *Corporate Law in the Shanghai People's Courts, 1992-2008: Judicial Autonomy in a Contemporary Authoritarian State*, 5 E. ASIA L. REV. 303, 321-7 (2010); Nicholas C. Howson, *"Quack Corporate Governance" as Traditional Chinese Medicine – the Securities Regulation Cannibalization of China's Corporate Law and a State Regulator's Battle Against Party State Political Economic Power*, 37 SEATTLE U. L. REV. 667, 689–94 (2014) [hereinafter Howson, *"Quack Corporate Governance"*].

12. Note that for Mao and the CCP in 1949, the "people" was more than just the "proletariat" and included, at least initially, the "the workers, peasants and military," while excluding class enemies (landlords, capitalists, haute bourgeoisie, etc.), reactionary party members, spies, etc. This alternative formulation of who precisely the Chinese Communist Party, and the Chinese Marxist state it controls, represent has important implications for the contemporary corporatization program discussed here.

13. *See* Regulating the Visible Hand? The Institutional Implications of China's State Capitalism (Benjamin L. Liebman & Curtis J. Milhaupt eds., 2015).

against any alternative path arising from the power and interest of incumbent control parties which actually operate PRC firms.

Yet, even the most discerning analysts have rarely looked further back into history to understand how these same factors shaped China's nineteenth and early twentieth century "firms" and contributed to the same path dependency.[14] It is that underperformed glance into history that is the stimulus for this writing. Said another way, this Article proposes revived consideration of some of China's late nineteenth and early twentieth century firms—not as historical artifacts proving or denying the buds of a pre-Communist industrial capitalism[15] or as exotic curiosities demonstrating how late imperial China failed to understand the power of the British East India Company[16] (they did understand)—but as the precursors of, and in some ways determinative models for, the same massive PRC corporations that now stand astride the world.

Accordingly, this Article proceeds as follows. Part II describes in summary terms the genesis and fruits of the PRC's corporatization without privatization program, emphasizing the political, organizational, and legal ecologies in which China's corporatized SOEs function. Part III focuses on a lesser-known story—aspects of firm organization and governance norms in China from a time before the end of imperial rule in 1911, which have very strong resonance for today's PRC firms established in a radically different political, economic, and historical circumstance and informed by a completely different degree of transnational engagement. Part IV isolates common elements between the two generations of enterprise establishment in China, regardless in many cases of the governing (domestic or transnational) law, the surrounding political legal environment, and the degree of interaction with the world outside of China. This Part demonstrates aspects of firm organization and governance from more than a century ago that reveal the path dependencies working so strongly today in the PRC. Part V concludes with a consideration of the possible trajectory of the PRC and its

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14. Each of Ruskola, Kirby and Zelin have written extremely useful studies of China's pre-1980s firm establishments, but published this work before the PRC's "state capitalist"-model corporatized SOEs developed to the form we see today. Accordingly, their studies are useful as histories of institutional and legal (both statutory and contractual) developments, but do not look to those historical institutions and arrangements to understand similar kinds of institutions in the late 2010s. *See* William C. Kirby, *China Unincorporated: Company Law and Business Enterprise in Twentieth-Century China*, 54 J. OF ASIAN STUD. 43 (1995); Teemu Ruskola, *Conceptualizing Corporations and Kinship: Comparative Law and Development Theory in a Chinese Perspective*, 52 STAN. L. REV. 1599 (2000); Madeleine Zelin, *The Firm in Early Modern China*, 71 J. OF ECON. BEHAV. & ORG. 623 (2009).

15. *See, e.g.*, ALBERT FEUERWERKER, CHINA'S EARLY INDUSTRIALIZATION: SHENG HSUAN-HUAI (1844–1916) AND MANDARIN ENTERPRISE 250 (1958).

16. *See* JOHN MICKLETHWAIT & ADRIAN WOOLDRIDGE, THE COMPANY: A SHORT HISTORY OF A REVOLUTIONARY IDEA 7 (2005).

corporate entities as global actors of great and abiding influence and of whether, in this sphere at least, "law—Chinese or foreign—matters."[17]

II. THE STATE-CONTROLLED CHINESE CORPORATION AND ENTERPRISE IN THE LATE 2010S

This Part describes one form of the modern PRC enterprise legal person (or group of legal persons) as it (they) exist(s) today. To set up the desired comparison with Chinese firms of yesteryear, this Part must generalize a rather complex picture, but also focus on a particular form of Chinese corporation—the corporatized traditional SOE and its group of affiliated enterprises, the same entities and groups which presently occupy the heights of China's productive economy and not incidentally the global capital markets.[18] Accordingly, this Part mostly neglects the very large number of firms active in China that are not built upon the assets or franchise rights of former SOEs or government departments, small and medium enterprises which have grown from (often *local government*-owned) "collectively-owned" and "township and village enterprises", and the myriad of other successful enterprises in the Chinese landscape evidencing something closer to "private" rather than public ownership, including entities active outside of China but with only opaque relationships to the PRC Party State such as Anbang and Wanke.[19] The path dependencies this Article illustrates are most immediately identifiable when studying the PRC's present day corporate (and group) giants that have been erected on the foundations of China's traditional SOEs.

Donald Clarke and I, among others, have tried to explain China's Reform era "corporatization" program and its consequences for the Chinese firm and the nature of corporate law and corporate

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17. I should note that this particular writing does not address the ever-important question of how "sovereign" China's corporatized SOEs and SOE groups are for traditional or modern statutory sovereign immunity analysis. Nonetheless, I believe there are aspects of this analysis which will help observers understand the relationship of some of the world's largest enterprises with China's sovereign power.

18. *See Global 500,* FORTUNE, http://www.fortune.com/global500/list/ (last visited Aug. 23, 2017) [https://perma.cc/J732-DZU2] (archived Aug. 23, 2017) (listing three corporatized PRC SOEs in the top five companies worldwide (State Grid, China National Petroleum Corporation, and Sinopec) and eleven in the top fifty (in addition Industrial and Commercial Bank of China, China Construction Bank, Agricultural Bank of China, Bank of China, Ping An Insurance, China Mobile, and the Shanghai Automotive Industry Corporation)).

19. See, for example, my *Return of the Prodigal Form? – Partnerships and Partnership Law in the People's Republic of China, in* RESEARCH HANDBOOK ON PARTNERSHIPS, LLC AND ALTERNATIVE FORMS OF BUSINESS ORGANIZATIONS 390, 390–91 (Robert Hillman & Mark Loewenstein eds., 2016).

governance in the PRC.[20] The traditional PRC SOE—or in literal English translation of the Chinese term "enterprise under the system of ownership by all the people" (*quanminsuoyouzhiqiye*)—was not what many mistook it for, a legal person owned by a single shareholder: the state (on behalf of "all the people"). The traditional and pre-Reform era SOE was in fact a division or ring-fencing of productive and social assets by a given state administration, which did not grant separate legal personality or competence to that group of assets or to the SOE of which it was deemed to be part. Nor did the division or ring-fencing have the status of an independent accounting unit, and thus by the same token it did not have profits, losses, taxable gains, or any accountability for the same. Indeed, historically there was no enterprise income tax system for domestic SOEs and thus no enterprise income tax levied on the gross revenues of SOEs, which were thus solely cost centers. This made perfect sense when SOEs operated pursuant to a centralized state plan, using annual grants from the state to fund the purchase of inputs and to meet annual operating expenses and the cost of social services, with the mandate that all net earnings were returned to the funds-granting government. In China, the traditional SOE had Chinese Communist Party-appointed, non-business managers scaling the Party's *nomenklatura* personnel appointments system and thus moving through a defined bureaucracy into progressively more powerful political positions.[21] The traditional SOE did not issue ownership interests in itself, like stock or equity. The SOE "borrowed" from other traditional SOEs configured as "banks" (only after 1994 "commercial banks"—thus distinguished from "policy banks" which continued as channels for direct grants from the state), with such borrowings functioning as another vehicle for the infusion of state-provided funding outside of direct grants by the state to the enterprises. The "control" interest in SOEs (the right to appoint management and appropriate some portion of gross revenues, and once an enterprise tax system came into existence, net revenues) was vested in some identity of the state—often central-line ministries (e.g., the Ministry of Textile Industry) or ministry-type bodies transformed directly into SOEs (e.g., the Ministry of Petroleum Industry metamorphosed into the China National Petroleum Corporation (CNPC)), but also subordinate units of government such as local (usually provincial or large municipal-level) bureaus of the line ministries (e.g., the Jiangsu Bureau of Textile Industry) or

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20. *See* Howson, *"Quack Corporate Governance"*, *supra* note 11, at 690–94.

21. Nicholas C. Howson, *China's Restructured Commercial Banks: Nomenklatura Accountability Serving Corporate Governance Reform? in* CHINA'S EMERGING FINANCIAL MARKETS: CHALLENGES AND GLOBAL IMPACT 123, 152 (Zhu Min, Cai Jinqing & Martha Avery eds., 2011).

equivalent local-level People's Governments (e.g., the Jiangsu Provincial People's Government).

This was the *status quo ante* system for traditional SOEs addressed by the corporatization program that began, experimentally and without much central government sanction, in the mid-1980s. Corporatization, confirmed in (all-important) policy terms with the advent of the "modern enterprise system" articulated in Communist Party policy in the early 1990s, and in (far less important) legal terms with the 1994 PRC Company Law, sought to abolish the SOE as a non-law-based organizational form[22] by converting such SOEs, or parts of them, into a *legal* form under a "Company Law." That new legal form for SOEs governed by the Company Law could take one of three forms: (i) the company limited by shares (CLS) (*gufen youxian gongsi*) for widely held firms issuing stock with assumed separation of ownership and management;[23] (ii) the limited liability company (LLC) (*youxian zeren gongsi*) issuing less-liquid equity interests (formally "registered capital interests") for smaller and more closely knit groups of investors with less presumed separation of ownership and management;[24] and (iii) the wholly state-owned company (WSOC) sub-form of the LLC, for companies erected on the backs of traditional SOEs owned directly by state agencies with no shareholders' meeting and a merely optional board of directors.

This process of corporatization did not initially and to this day does not implicate "privatization" of the PRC economy or its traditional SOEs, much less any withdrawal of the PRC Party State from the same. Why? Because a controlling equity interest in the resulting corporate entity went to or was maintained by the incumbent Party State control party of the pre-conversion SOE, originally 100 percent, but diluted as the newly established corporate entity engaged, post-hiving off of the burdens connected to the SOE's traditional social assets, in the issuance of new capital to capital markets investors, with the equity control position decreasing to 70 to 80 percent.[25] (Over time, these absolute control positions have been further diluted with subsequent capital raisings, but never below a strong 50 to 60 percent).[26] Moreover, the prior bureaucratic channels

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22. Ironically, the SOE was only given a *post hoc* legal basis in 1988 with the promulgation of a "law" concerning SOEs, just as the PRC was intent on abolishing SOEs as an organizational and legal form.

23. Modeled on the German *Aktiengesellschaft* or "AG."

24. Modeled on the German *Gesellschaft mit beschränkter Haftung* or "GmbH."

25. *See* Howson, *"Quack Corporate Governance"*, *supra* note 11, at 691 ("[Corporatization] did not implicate privatization because a controlling equity interest in the converted SOEs went to or was maintained by state entities.").

26. Some analysts understand the "share split reform" (*guquan fenzhi gaige*) initiative of 2005 as a remedy to such overly concentrated capital structures at Chinese listed firms. That is a misconception. The share split reform sought to address market overhang and public equity valuation problems arising from the fact that the state's controlling equity positions in companies with listed shares were held *via* non-tradable

of control working on SOEs remain largely undisturbed by the change in organizational form from CCP Party State policy-authorized SOE to law-based corporate entity, in which continuing lines of authority and decision making subvert almost completely the overlay of public norms described in law and regulation.

To the present day, the PRC Party State remains absolutely committed to retaining control over converted enterprises in the broadest range of sectors—not just the usual suspects for state control (e.g., defense and national security, power generation, extractive industries, and key infrastructure), but also non-national security and non-key infrastructure sectors that are extremely profitable for central or local Party State insiders, especially when financed by largely passive and information-deprived public investors, Chinese and foreign.

Since the early 2000s, traditional SOE systems have increasingly used corporatization of specific assets to assemble corporate "groups" of legal person subsidiaries and non-legal person divisions under a core group holding company, which serves as either (i) the controlling shareholder of the group's legal person subsidiaries or (ii) the headquarters of the subordinate divisions, with those corporate subsidiaries—not the holding company positioned at the top—seeking finance from the Chinese and foreign capital markets.[27] These groups benefit from monopoly rights over a certain business sector (or operational or geographical subdivision of that sector) sometimes implemented as a duopoly or triopoly to create the impression of competition. The group's core holding company is "owned" on behalf of "all the people" entirely by a central government (State Council) agency now called the State-owned Assets Supervision and Administration Commission (SASAC). The core holding company of the enterprise group is usually organized as a WSOC, the wholly state-owned sub-species of the LLC described above, which has no shareholders' meeting and an optional board of directors The core holding company, managed by Party State *nomeklatura* appointees who rotate between central and local official posts and enterprise executive offices or directorships (and even between allegedly competing enterprise groups in a single monopoly or duopoly sector), coordinates the entire group's business activities.

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shares. Under this 2005–6 share split reform initiative, holders of non-tradable shares (the state and legal person shareholders holding equity on behalf of the state) were given the right to sell their shares on PRC exchanges in return for present compensation payable to the suddenly diluted shareholders of the public float. While this reform did make state and legal person shares liquid, and there was some moderate selling down of the state's interest in listed firms, the program only reduced very moderately the Party State's controlling position in listed firms. *See* Andrea Beltratti et al., *The Stock Market Reaction to the 2005 Non-Tradeable Share Reform in China* 5–6 (Working Paper Series no. 1339, 2011).

27. Li-Wen Lin & Curtis J. Milhaupt, *We are the (National) Champions: Understanding the Mechanisms of State Capitalism in China*, 65 STAN. L. REV. 679, 717 (2013).

They do this in the interest, above all, of state industrial policy, and certainly with a preference for such national policy over what might be in the interest of shareholder wealth maximization for the non-group, minority shareholders invested in the individual legal person subsidiaries often through the public capital markets.

Almost on a level with the group core holding company is a group "finance holding company," which directs *group internal* revenue streams to *group internal* subsidiary enterprises or divisions, without much concern for the boundaries of distinct legal entities, much less the basic creditworthiness of *group internal* recipient entities. In short, the finance holding company entity allocates finance and investment strictly among its subsidiaries and affiliates, and it serves the group's controlled entities, with no concern whatsoever for the financing of external entities, much less the ultimate formal "owner" of the group, the state (acting through SASAC).[28]

SASAC is an empty bureaucratic box or a proxy for the state's (or "all the peoples'") majority ownership interest in the nation's productive assets. SASAC is thinly staffed, has little or no political heft when not the cat's paw of powerful State Council or Politburo actors, and exercises no control over its "owned" core holding companies positioned at the top of various groups. As such, SASAC continues as the long-standing "absent principal" in the Chinese corporate governance scheme formerly known as the "state" or "all the people" represented by the state, just under a different name or institutional title. PRC corporate groups, and by extension their subsidiaries and divisions, are therefore actually controlled by Party State *nomenklatura* insider appointees working at the core holding company level, and as directors and officers of the subsidiary entities controlled by the core holding company. As Party State bureaucratic political actors seeking advancement in the Party system, these individuals are perfectly responsive to Party State policy (which necessarily includes national industrial policy), while at the same time they are content to ignore the interests of external minority shareholders in the listed subsidiaries they formally manage.

To give a concrete illustration of how this structure works, consider a slightly anachronistic vision of the China National Petroleum and Chemical (Sinopec) Group,[29] anachronistic only because some of the elements described together below were not in place concurrently. Posit that Sinopec has a monopoly on all downstream hydrocarbons businesses in China, thus gas stations,

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28. *See id.* at 717–21.

29. *See* SINOPEC, http://www.sinopecgroup.com/group/en/ (last visited Aug. 26, 2017) [https://perma.cc/7UXH-7WV4] (archived Aug. 26, 2017) (Sinopec Group's website in English); SINOPEC, http://www.sinopec.com/listco (last visited Aug. 26, 2017) [https://perma.cc/8648-9Z7Y] (archived Aug. 26, 2017) (China Petroleum and Chemical Co. website in Chinese).

refining, petrochemicals, etc.—everything separate from exploration, development and production, and energy transportation businesses, all of which are the province of other enterprise groups (here, the separate families of companies under the CNPC and China National Offshore Oil Corporation (CNOOC) groups). There is a Sinopec core holding company at the center of this group—the "Sinopec Group Holding Company", which is a WSOC 100 percent "owned" by a State Council department now called SASAC. A majority-controlled subsidiary, department, or affiliated entity would function as a dedicated "finance holding company" necessary for the allocation of funds and finance to and among operations and entities included in the Sinopec Group. Sinopec Group Holding Company, explicitly permitted in its business license to invest in other entities, in turn owns a vast number of only Sinopec business-related subsidiaries, each with a business scope allowing it to operate in a defined sector within the group's larger monopoly (e.g., oil refining, gas stations, or petrochemicals) or defined geographical areas (e.g., just Jiangsu Province, or just three southern coastal provinces). Those subsidiaries will always show majority equity ownership in the hands of the Sinopec Group Holding Company or one of its controlled subsidiaries, but they can be financed directly by bank loans, minority non-public investment, or the public capital markets (domestic or foreign). Thus, for example, this Sinopec Group might seek to reorganize a traditional SOE grouping of productive and social assets conducting a petrochemicals business in the Shanghai suburbs of Jinshan District into a Sinopec Group Holding Company-controlled company called "Sinopec Shanghai Petrochemical Company Limited," which could complete an IPO on the PRC domestic or foreign capital markets. After the IPO, issuer Sinopec Shanghai Petrochemical Company Limited would still be dominated absolutely by the core holding company via an 80 percent equity stake and its power to appoint all directors and officers of the listed subsidiary. Moreover, Sinopec Shanghai Petrochemical Company Limited would benefit from well-advertised preferences critical to its commercial success, preferences relating to regulatory breaks, supply or other inputs, availability or pricing, or exclusive access to certain markets at preferred (higher) prices, importantly preferences delivered not just by other Sinopec Group affiliates but even by other Party State-controlled competitors (e.g., the supply of crude oil for refining from CNPC).[30]

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30. This is not a fanciful example, and tracks exactly the first IPO of a PRC-domiciled issuer on the Hong Kong Stock Exchange in 1992 and indirectly via American Depositary Shares and Receipts (ADRs) on the New York Stock Exchange (NYSE). *See* SINOPEC, http://www.sinopec.com/listco/en/about_sinopec/subsidiaries/subsidiaries_joint_ventures/20161109/news_20161109_400111388102.shtml (last visited Aug. 29, 2017) [https://perma.cc/K9BT-AGVM] (archived Aug. 29, 2017) for the Sinopec Shanghai Petrochemical Company Limited website, which trades on the Hong Kong Stock Exchange (under "SEHK"), the New York Stock Exchange (American

The negative effects of such a "corporatization without privatization" program on corporate governance and productive efficiencies—at least with respect to the controlled subsidiary firms that have a public float—have been well aired in the literature. Suffice it to say that the result has been a keen horizontal, not vertical (i.e., minority shareholders versus controlling shareholders, not general shareholders' meeting versus board of directors), agency problem, where the party able to extract the private (here the better word is "specific" or "tunneled") benefits of control of the enterprise and expropriate returns from and otherwise oppress the minority (often) public shareholders is far more than a run-of-the-mill control party. It is instead a legal person or natural person identity of the Party State (central or local), giving it or them a potent mix of political and economic power, especially against disaggregated, non-politically privileged minority shareholders. The result was and is as to be expected: an unconstrained opportunity for control parties *qua* controlling shareholders to engage in oppression of minority shareholders, tunneling, and outright expropriation, where other state institutions (i.e., the judiciary or agencies) that might act as a check against such control parties are politically conflicted, burdened with limited bureaucratic autonomy, or suffering from competency constraints.

Notwithstanding that expected result, however, and perhaps most important for the current analysis, China's largest corporate issuers continue to attract ready purchasers on the PRC's domestic capital markets and on global exchanges, even when the underlying business and assets are in very bad shape.[31] Said another way, if corporatization without privatization was, at least in part, about financing money-losing state assets through the public capital markets—i.e., gaining finance through legal forms recognized across the world whereby (i) the incumbent control party's absolute control of the assets remains undisturbed, (ii) state banks do not have to pile

Depositary Receipts, "SHI") and the Shanghai Stock Exchange (A shares, under "SSE"). It has long been rumored that this long-ago initial listing vehicle for the Sinopec Group will be "privatized," meaning the public investors in this Shanghai subsidiary will be bought out, so that the later (2000–1)-appointed Sinopec group listed subsidiary, China Petroleum & Chemical Company Limited (also trading on the Shanghai, Hong Kong and New York exchanges), will stand alone as Sinopec Corp's finance window on the domestic and international capital markets.

31. See, for example, the 2010 US $22.1 billion IPO by the Agricultural Bank of China, still the largest IPO in world history, but one completed with respect to a vastly underperforming "bank" entity. *See* Michael Wines, *China Bank IPO Raises $19 Billion*, N.Y. TIMES (July 6, 2010), http://www.nytimes.com/2010/07/07/business/global/07ipo.html (subscription required) [https://perma.cc/Y6BF-E4FP] (archived Aug. 26, 2017) (detailing 2010 IPO effected after purchase of $60 billion in non-performing loans in the late 1990s, the revelation of $7.5 billion of fraudulent loans in 2006, a 2008 $19 billion recapitalization of the bank when 25% of its loans were non-performing, and another purchase of bad debt of US$120 billion just before the IPO, leaving the bank, at the time of the IPO, with almost 3% of its loans as non-performing – the highest of any reporting bank *in the world*).

in more money from the PRC state treasury, and (iii) the investors are assuredly passive, and uniquely information- and collective action-challenged—then it has been an undiluted success. However, for those Chinese policymakers who saw corporatization without privatization as the way to separation of ownership and management, and to the possibility of some effective monitoring of and accountability for firm managers in the service of economically efficient (shareholder wealth-maximizing) firms, the process has proven almost irrelevant.

It bears emphasizing that the process outlined above, or the track whereby SOEs "owned" and operated directly by the Party State have been corporatized but not privatized, is not the entire picture of what has happened in the PRC over the past several decades. Indeed, very often after corporatization of traditional PRC SOEs but maintenance of the Party State's—central or local level—control position, real control is in fact given over to insiders who increasingly act in their own interest or in the interest of their "system" (*xitong*).[32] As will be explained below, this fuller process has distinct similarities to what occurred in China in the late nineteenth and early twentieth centuries during the transitions of Qing enterprise from (i) state-financed and -operated to (ii) state-promoted but privately financed and operated to (iii) state private co-operated and finally to (iv) (present or former) state official-operated but in the private interest of those state officials upon whom control is bestowed. An example of how this has occurred in modern China comes from the early and mid-1990s. At that time, then CCP General Secretary Jiang Zemin directed the military (the People's Liberation Army (PLA))—the third and roughly co-equal silo of institutional power in the PRC Party State, alongside the CCP and the state—to remove itself from industry and commerce, which it had entered from the earliest days of the Reform era. The PLA formally complied, but not by withdrawing from industry. Instead, the PLA, or more specifically departments of the PLA, established holding companies separate from the PLA with national and international investments (e.g., China Northern Group (Norinco), China Southern Group, Poly Group) operated by PLA "system" insiders. Or, in many cases, PLA personnel who had been managing significant groups of assets controlled by the military simply retired from their military positions to become full-time civilian directors or officers (e.g., Huawei). So, instead of the PLA withdrawing from industry, PLA assets were withdrawn from the PLA (and aggregated under corporate groups run by civilians), or PLA officers themselves withdrew from the military to continue to engage in industrial pursuits (and to act on behalf of their former military masters). The same process is also identified in

32. *See* KENNETH LIEBERTHAL, GOVERNING CHINA: FROM REVOLUTION THROUGH REFORM 218–19, 232–33 (2nd ed. 2003).

the recent rise of new PRC conglomerates like Anbang Insurance and Ping An Insurance, huge groups operating in sectors that did not exist in the planned economy of the pre-Reform era, but with the benefit of Party State networks and patronage, and under the direction of individuals closely connected to the Party State.

The foregoing is, admittedly, a rather superficial and generalizing picture of the PRC's policy-driven corporatization without privatization process over several decades. With an eye to understanding the deeper historical roots of this program and outcomes, below are the basic policy imperatives that have caused a system like this to come into being, followed by a list of some of the key resulting characteristics of those outcomes (including the fact that "law" seems to have little relation to the process).

First, consider some of the key policy imperatives supporting a program of "corporatization without privatization" and Party State-"owned" groups:

- Whatever organizational adjustments are made with respect to the institutions governing accumulations of productive assets or sectors of economic activity, the state and its agents remain in control, at least formally (at inception), and then over time, functionally;
- The PRC needs large amounts of capital for projects designed to make China "rich and powerful";
- The government of the PRC seeks protection against—and the creation of domestic (and eventually global) competitors for—capital- and technology-rich foreign invested enterprises, in China or (eventually) globally, especially in a period where foreign trading inside China and/or foreign investment in China benefits from capital endowment and (foreign) market access advantages, and/or regulatory protection or preferences;
- The PRC state treasury is unable or unwilling to continue—or wants to minimize—unrecoverable funding of the operation of productive assets and their related enterprises, whether by direct grants, loans, or other expenditures;
- The government of the PRC seeks to utilize idle Chinese savings and to employ that liberated investment capital on Chinese national economic development, while at the same time stopping or dissuading the flight of available domestic capital to finance development external to China;
- The government of the PRC seeks to use global capital markets to finance the development of its industrial firms, but in a way that cedes little or no governance

role for, or accountability to, such foreign providers of capital;

- If absolute state "ownership" of key productive assets cannot be maintained, then at least absolute state "control" must be maintained; and
- Whatever mechanism for the financing of state-owned assets is employed, it must conform to what is perceived of as "modernity" and "global practice" and eventually must comply with transnational public and private law norms and obligations, and thus—if only for an initial appeal to global capital markets—cannot be too exotic or *sui generis*.

Second, consider some of the key elements of the resulting architecture put in place to serve the above-described policy aspirations (and "enterprise" here should be read to include "enterprise group"):

- Promotion of the enterprise by the state, using generally applicable state legal norms, but those which apply only to state controlled investments (the WSOC form), or if others (the PRC Company Law) with an underlying capital structure that directly enables the state's maintenance of its incumbent control position and the open exploitation of minority investors;
- Donation of hard assets to the enterprise by the state in exchange for a controlling equity position in the new enterprise and monopoly franchise or extraction rights conferred on the enterprise to ensure revenues and the exclusion of competitors, domestic or foreign;
- Direct financial support from the state to the enterprise via additional equity capitalization (e.g., the successive recapitalizations of PRC commercial banks and the transfer of non-performing loans to the balance sheets of Asset Management Companies (AMCs)), loans by state controlled lenders (which ripen into grants, or are transferred off balance sheet as non-performing loans for AMCs), direct grants, subsidies, regulatory (or tax) exemptions, preferential prices for inputs provided by other state-controlled enterprises, etc.;
- Management of enterprises by Party State *nomenklatura* personnel who are not appointed because of expertise in the specific industrial or service provision sector and respond to national development plans and priorities rather than enterprise efficiency or investor wealth maximization,

all as they seek bureaucratic (Party State) advancement, for which enterprise efficiency or productivity is mostly irrelevant;

- Raising equity investment from a body of widely dispersed, passive, and information-deprived investors via domestic and global capital markets, with initial assurances: (i) for domestic and global investors, that the enterprise is too important to fail and will benefit from continuing state protection and support; and (perhaps contrarily) (ii) for foreign investors, that the state will stand back from undue intervention in enterprise operations management, notwithstanding the state's role in promotion of the enterprise, the ceding of monopoly or exclusive franchise rights grants, direct subsidies or soft loans, etc.;
- The promise, and enforcement of, monopoly franchise rights over (or participation in a monopoly covering) a certain activity or revenue stream, and strict prohibition against new entrants, domestic or foreign;
- Something like a guaranteed return for non-state investors, at least in terms of equity appreciation (and if the capital markets betray that promise, direct intervention in those markets to support equity prices); and
- After establishment and capital markets financing gained on promises of lack of state intervention, migration back towards state- (or Party State insider) dominated governance of the enterprise.

III. THE FIRM IN CHINESE HISTORY

The immediately preceding Part II has generalized the structures and key elements shared by the products of the PRC's post-1980 "corporatization without privatization" project. Part III lays out some of the structures and key elements seen at Chinese firms or proto-firms from a much earlier time, specifically after the mid-nineteenth century, a period in which Chinese imperial rule ended forever, and the Chinese nation endured almost half a century of intense political instability, warlord contest or civil war, foreign intervention, and eventually invasion.

Specifically, Part III describes the following kinds of firm or enterprise organization in China from the late nineteenth and early twentieth centuries: (i) the *guandu shangban* ("official-promoted, merchant-operated") enterprises (transitioned to *guanshang heban* ("official and merchant jointly operated") enterprises) from the latter

part of the nineteenth century; and (ii) so-called regional enterprises like former Qing official Zhang Jian's government-promoted but finally privately operated Da Sheng textile group of enterprises.

Regrettably, Part III does not address other important commercial establishments in Chinese history, namely: (i) large enterprises with national scope that were not promoted or maintained by the court or state, and/or understood as "family" enterprises; and (ii) so-called charitable trusts, an innovation stretching back to the Song Dynasty. This exposition unavoidably relies upon the excellent scholarship of a number of modern China historians[33] but also focuses upon select elements that correlate well to the PRC's Reform era corporate enterprises, the real focus of this Article.

There are, however, two things to note at the outset. First, it may be deeply misleading to refer to firm establishments in Qing, Provisional Republican, Beiyang Government, *Guomindang* (KMT) Republican, pre-Great Proletarian Cultural Revolution, or post Third Plenum, pre-1992 Communist Party-ruled China as "companies" or "corporations," etc. That terminology may cause a misapprehension for readers, who will map the broader meanings of those essentially Western and legal terms of art—or the specific accepted elements of the corporate form (limited liability, centralized management, separation of ownership and managements, perpetual life, freely transferrable share capital)—onto radically different enterprise structures and groups. As noted below, many of the *guandu shangban* enterprises are commonly translated as the "XXX *Company*," even though there was no company law or regulation in existence at the time and thus no legal basis for the form. These entities did not have distinct legal personality or limited liability and indeed used a Chinese character in their name (*jü*), indicating that they were more closely akin to a government department used as a vehicle to match something like private investment and management alongside state investment. While Chinese intellectuals and officials have certainly appreciated the Western model of the corporate enterprise, what has

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33. *See* WELLINGTON K.K. CHAN, MERCHANTS, MANDARINS AND MODERN ENTERPRISE IN LATE CH'ING CHINA (1977); SHERMAN COCHRAN, BIG BUSINESS IN CHINA: SINO-FOREIGN RIVALRY IN THE CIGARETTE INDUSTRY, 1890–1930 (1980) [hereinafter Cochran, 1980]; SHERMAN COCHRAN, ENCOUNTERING CHINESE NETWORKS: WESTERN, JAPANESE AND CHINESE CORPORATIONS IN CHINA, 1880–1937 (2000) [hereinafter COCHRAN, 2000]; DOU JIANMIN, ZHONGGUO GONGSIZHI SIXIANG YANJIU (1842–1996) [A STUDY OF CHINA'S COMPANY SYSTEM THOUGHT - 1842–1996] (1999); ELIZABETH KÖLL, FROM COTTON MILL TO BUSINESS EMPIRE – THE EMERGENCE OF REGIONAL ENTERPRISES IN MODERN CHINA (2004); Chi-Kong Lai, *The Qing State and Merchant Enterprise: The China Merchant's Company, 1872–1902*, *in* TO ACHIEVE SECURITY AND WEALTH: THE QING IMPERIAL STATE AND THE ECONOMY, 1644–1911, at 139 (1992); Kenneth Pomeranz, *"Traditional" Chinese Business Forms Revisited: Family, Firm and Financing in the History of the Yutang Company of Jining, 1779–1956*, *in* 18 LATE IMPERIAL CHINA 1 (1997); Kirby, *supra* note 14; Zelin, *supra* note 14.

appeared through history in China is an enterprise form that is decidedly not a transplant and is utterly distinct from those models, except with respect to certain mechanisms deemed useful—e.g., widely dispersed investment to accumulate funds on a large scale and from a relatively disempowered and collective action-challenged body of participants.

Second, many of the enterprise structures described below had little engagement with "law" *per se*; instead, they were structures that existed and occasionally thrived either without the benefit of authorization in state law or in direct contravention of state law when it was enacted. As historian Bill Kirby has recited in detail,[34] China only gained its first analogue to a company law statute near the end of imperial rule (the Qing court's *Gongsilü* of 1904), a specific and explicitly legal norm hardly used in practice. Much the same fate awaited successor company laws and regulations (of 1914, 1929, and 1946 under Beiyang Government and pre- and post-Anti-Japanese War KMT governments respectively)[35] that the state, company promoters, and entrepreneurs certainly engaged with more fully than at any prior time in Chinese history, but not in the ways another political-legal system might dictate.

At least for the Chinese sector of the economy, the state (at that time, the Qing court) led new industrial development in the nineteenth century.[36] Most historians of China tie the outsized role of the state in matters pertaining to economic development, and a minimal private sector, to a Confucian (*rujia*) orthodoxy hostile to commerce and trade. While this Article recognizes the rhetorical power of that oft-articulated Confucian hostility, the greater and determinative power of a surviving Legalist (*fajia*) obsession with the state's pursuit of "wealth and power" was the wellspring of heavy state involvement in first agricultural and then industrial and commercial pursuits, and certainly large scale projects critical to national economic development and rearmament against foreign threats.[37] Indeed, in the long course of Chinese imperial history, it

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34. *See* Kirby, *supra* note 14, at 44 (explaining that prior to 1904, China had no commercial code, nor civil code, and could regulate economic activity only through the Great Qing Code, which was primarily a penal code).

35. *Id.*

36. Before the Sino-Japanese War and the Treaty of Shimonoseki in 1895, foreigners were not permitted to establish manufacturing enterprises in China (even in the so-called "Treaty Ports" where the rights granted to foreign powers were "trading" rights). The weakened Qing government ignored small-scale foreign-owned enterprises in non-essential sectors (*e.g.*, shipbuilding and repair), but was strict in enforcing the ban on large, capital-intensive industry (*e.g.*, cotton spinning and weaving). The Treaty of Shimonoseki, and rights therafter gained by other foreign powers (and their agents) as a result of "most favored nation" clauses in the prior Qing treaties, changed all of that.

37. *See generally* HAN FEIZI, HAN FEIZI (Burton Watson ed., trans., Columbia University Press 2003) (280-233 BCE); BENJAMIN I. SCHWARTZ, THE WORLD OF

seems that few have seriously questioned the necessity of an active and interventionist state, with the governing elite, Han or foreign (Mongol or Manchu), instead questioning the nature and extent of such state involvement. So it was that by the middle and late nineteenth century, after the serial trauma of the "unequal treaties" resulting from the Opium Wars and the Taiping Rebellion, etc., no official could consider expansion of the economy and industrial development except under close state supervision. This basic assumption gave rise to at least two important premises which have continued life more than a hundred years later and in a vastly different global circumstance: (i) that the state had the right to run, or at least intervene in, the affairs of any major business enterprise, and (ii) that the state and ultimately its officials had a preferred right over the returns from such an enterprise (certainly over non-state providers of capital).

Thus, the need for huge amounts of capital for projects designed to make China "rich and powerful" (again), the government's inability or unwillingness to provide that capital, the desire to protect against incursion by capital-rich, foreign-run enterprises, and the aim of employing idle Chinese capital or constraining its flight to fund external development, all spurred the Qing court—but really individual state officials—to create or allow new investment and business structures, chief among them the joining of official promotion and private investment known as "*guandu shangban*" or "official-promoted, merchant-operated."[38]

The *guandu shangban* enterprises started in the 1870s actually have their roots in entirely government-funded and -managed—thus "*guanban*"—operations of the 1860s in sectors directly relevant to what is now called national security—e.g., shipyards and arsenals. The new enterprises of the 1870s were designed to be active in areas traditionally occupied by some level of private entrepreneurs (Chinese and foreign)—e.g., textiles and shipping—and where there was an established state interest or monopoly—e.g., mining.[39] Li Hongzhang, for a time the most powerful Qing official and the political mastermind behind the first *guandu shangban* firm, China Merchants' Steam Navigation Company (*lunchuan zhaoshangju*) (CMS), neatly merged two ideas—the established imperial Chinese

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THOUGHT IN ANCIENT CHINA 321-349 (Belknap Press 1985); SHANG YANG, THE BOOK OF LORD SHANG (J.J.L. Duyvendak ed., trans., The Lawbook Exchange, Ltd. 2011) (390-338 BCE).

38. I differ here from the accepted English translation of "*guandu shangban*," usually rendered as "government supervised-merchant managed," because that translation implies more ongoing state supervision – rather than initial promotion – than I think was originally envisioned. However, as there was constant flux in the balance between state involvement and enterprise (investor) autonomy *per* both state policy and the identity of the officials or managers involved, my term may over-privilege Li Hongzhang's original rhetorical promise for these enterprises.

39. *See* CHAN, *supra* note 33, at 70.

bureaucratic construct utilized in the salt monopoly (actually called *guandu shangban*) and a very partial model of the Western European joint stock company—to advocate for a new kind of enterprise in the late Qing.[40] The salt monopoly program was useful because it showed a precedent for co-opting wealthy "merchants" (non-officials with private capital and business experience) to provide capital and management skills.[41] The joint stock model—a relatively new Western legal mechanism then much encountered at the hands of European companies active on the China coast (e.g., British American Tobacco) but also known domestically and from Chinese diaspora enterprises[42]—was deemed useful as a vehicle for raising huge amounts of capital from a large number of dispersed investors (without, it is important to note, any vision of shareholders' meetings, a centralized and elected board of directors with fiduciary duties to the merchant investors, or (merchant-representing) board appointed senior management, etc.).[43]

Notwithstanding this state (at this time, "court") innovation, a bedrock fact of industrial development in pre-1895 China remained—no moderate- to large-scale manufacturing enterprise could be established without the approval and support (which, as described below, took many forms) of a senior official. So it was that the first new large-scale industrial enterprises established in China with any private involvement, such as those seen in armaments, mines, shipping, and shipyards, were created under government sponsorship and the imprimatur of a specific court official. There are many examples of the so-called *guandu shangban* enterprise establishments in the nineteenth century, including the Hanyeping Company, the Hengfeng Spinning Mill, the Shanghai Cotton Cloth Mill, the Kaiping Mining Company, and CMS, all of which were created without sanction in state law, regulation, or indeed any formal utterance from the Qing court or bureaucracy, but each of which is identified with the concrete patronage of a specific government personality.

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40. *See id.*

41. The imperial salt administration's policy construct allowed the appointment of wealthy merchants to act as "chief merchants" (*zongshang*), which merchant managers were actually given official (government) rank to run operations with broad administrative power over both lesser private salt shippers but even other officials administering the same network. CHAN, *supra* note 33, at 71.

42. *See* COCHRAN 2000, *supra* note 33, at 58; Pomerantz, *supra* note 33, at 2.

43. Traditional enterprises in China that correlated with at least the possibilities inherent in the joint stock form at this point were smaller in scale, usually dependent upon the resources of an extended family or a few partners, and – importantly – managed by hired (non-family) managers. The formal owners or investors in such enterprises ceded a great deal of control to the hired managers, with little intervention in enterprise management or reporting demands. If the hired managers failed, they could be fired, but replaced by new stranger managers with the same management independence and power. *See* Chan, *supra* note 33, at 71.

The traditional view of the *guandu shangban* establishments in the late Qing was that they suffered from "state" (court) interference, notwithstanding real indications of growth in China's late nineteenth century productive economy and a lack of substantial impact by the state generally in that growth story.[44]

To understand the specific role of the state vis-à-vis such firms, and to be able to compare the role of the state with respect to such nineteenth century firms and the PRC's corporatized SOEs of today, it is useful to analyze in granular detail the state policy framework for the creation—really court permission for the allowance—and operation of such entities and how that changed over time.

As noted above, the *guandu shangban* firm establishments were occasioned by the following imperatives:

- The need for large amounts of capital for projects designed to make China "rich and powerful";
- The government's inability or unwillingness to provide that needed capital;
- The protection against, and the creation of competitors for, capital- and technology-rich foreign invested enterprises with their eyes on China's domestic markets and pre-established dominance of external markets; and
- The employment of idle Chinese capital on domestic infrastructure projects (and/or stopping the flight of domestic capital to finance development projects external to China).

Or as the CMS patron Li Hongzhang wrote in a December 1872 letter to a comrade official Zhang Shusheng about the promotion of CMS explicitly dismissing the importance (for the state) of its monopoly over domestic waterways transport of tribute rice:

> The use of steamships for the transport of tribute rice by sea route is but a minor consideration. The project will open up new prospects for the dignity of the state, for commerce, for revenue, and for military strength for China for hundreds of years to come.[45]

What characterized the organization and operations of the *guandu shangban* and the relationship of the state to these enterprises? Here, one needs to understand different phases of the *guandu shangban* style of enterprise, different phases that are identifiable even before the increasingly desperate Qing state (and its officials) reversed course and pushed their way back into direct involvement in the operation of these enterprises for what became

44. *See, e.g.*, Lai, *supra* note 33, at 139–40.
45. *Id.* at 142.

known as *guanshang heban* (or "co-operation by merchants and the state") and the choice between final retrenchment to pure state ownership and operation (*guanban*) or total letting go to entirely merchant-operated (*shang ban*) structures. In the initial phase of the initiative, one can identify the following:

- The promotion of the enterprise by the Qing court, and a powerful individual official connected to the court, all without authorization in public legal or regulatory norms (as compared to firm internal regulations, or written "instructions" from the promoting official);[46]
- The donation of hard assets (e.g., steamships, factories, etc.) or franchise or extraction rights (e.g., coastal shipping or coal mining, etc.) by the state to the firm, *gratis*, as a loan ripening into an outright grant, for a fixed (and low) use fee, or in exchange for an equity interest in the firm held by the court, or more likely the powerful official or his confederates as proxies;[47]
- The raising of finance from domestic capital (merchant) sources,[48] with a preference for state co-investment via loans instead of equity, with the promise *ex ante* that the Qing court would stand back on management and operations notwithstanding its promotion, monopoly grants, direct subsidies, or loan-funding;
- The promise, and subsequently grant of, subsidies to the enterprise by the state, which might come in the

46. For example, after 1873, CMS had rules (*jugui*) and regulations (*zhangcheng*) which operated much as modern "articles of association" or By-Laws do, and CMS was the subject and recipient of hundreds of "instructions" from Li Hongzhang, all at a time when there was no statutory basis for the firm, and Li also appointed top management of the firm. *See* Lai, *supra* note 33, at 144–45.

47. Sheng Xuanhuai's April 1872 scheme for the promotion of CMS proposed that the future firm acquire steamships from the state shipyard at a fixed, preferential rental, and attract merchant participation by giving the new firm (and by extension its private investors) a participation in what had previously been the state monopoly on transportation of tribute rice. *See id.* at 143–44.

48. Those who understand Chinese will comprehend this aspect of the *guandu shangban* firm immediately from the formal Chinese name for CMS, which name has *nil* connection with the common English name used for the enterprise—"China Merchant Steam Navigation Company, Ltd." The Chinese term, *lunchuan zhaoshangju*, indicates that the firm is: the "[government] department" (*jü*) for attracting (*zhao*) investment from non-state sources (*shang*) for steamships (*lunchuan*)." Most of the other *guandu shangban* establishments referred to here also used the Chinese character "*jü*" for "[state] department," for example the Kaiping Mines (*Kaiping Kuangwuju*) and the Mohe Gold Mine (*Mohe Jinkuangju*).

form of loans at preferential interest rates[49] or no interest (the proceeds of which might often be used to pay down higher interest private extensions of credit),[50] with no expectation of repayment of principal or a concrete understanding that interest would be forgiven,[51] or the lease of hard assets from the state at a fixed (and low) price, etc., all justified because these apparently merchant- or privately operated and benefiting firms had an important public and not just commercial function (e.g., coastal shipping, mining, armaments);

- The promise, and enforcement of, monopoly franchise rights over (or participation in a monopoly covering) a certain activity or revenue stream, and strict prohibition against new entrants, domestic or foreign;[52]
- The operational management of the enterprise left in the hands of non-officials (merchants) after promotion;[53]
- The guaranteed, and government-enforced, preferential revenue rate for firm business, often with that preferred return from the firm arising in an area

49. The interest rate on the abundant state loans directed to CMS (more than half of the firm's borrowings) paid out between 7–10%, always lower than the guaranteed dividend paid to merchant investors of 10%. Lai, *supra* note 33, at 145.

50. With respect to CMS specifically, see *id.* at 144–46 (detailing how CMS was originally promoted in October 1872 with a government loan sourced in the appropriation by Li Hongzhang of 135,000 taels of *Zhili* military funds, and showing at least 18 state loans subsequently to CMS before 1885, all a result of pressure brought to bear on officials in Jiangsu, Zhejiang and Hubei, and customs officials in Tianjin and Shanghai); indeed, Lai's study shows that before 1882, CMS' state loans were much larger than the firm's actual paid-in capital (2.2 times larger than the maximum paid in capital).

51. For CMS, in 1877 Li Hongzhang obtained the permission of the Qing court to suspend interest payable on government loans for 3 years, and in the event, no interest whatsoever was paid on these loans between 1882 and 1885, the foregone interest equaling almost half of CMS' paid-in capital between 1882 and 1893. *Id.* at 145–46.

52. For instance, Li Hongzhang pressured Qing officials to consign a portion of the annual shipment of tribute rice to CMS, and, as noted *infra*, at a rate two to three times higher than the rate charged even by foreign steamship companies hauling ordinary freight. *Id.* at 146–47.

53. This was always deemed to be a critical proffer on the part of the Qing court, as demonstrated by Li Hongzhang's failure to successfully promote CMS in October 1872 because of appointment of an official to management (Zhu Qiang), and then successful promotion of the firm once two comprador-merchants Tang Jingxing and Xu Run were installed as the top managers (which function they performed until 1884). *Id.* at 144.

of business closed to other commercial firms, domestic or foreign;[54] and

- The guaranteed, preferred, "above the line" return to "merchant" equity investors, thus regardless of any net profits from the enterprise.[55]

In 1883, Qing court policy changed significantly, such that the state effectively replaced merchant management (the "*shangban*" part of "*guandu shangban*") with bureaucratic or state management (or "*guanban*").[56] A decade later, after the 1895 Treaty of Shimonoseki and the serious challenge presented by foreign industrial firms permitted to undertake manufacturing operations on Chinese soil, circumstances changed even more radically and private Chinese involvement in industry became far more active. While some purely private (*shangban*) enterprises and wholly state-owned (*guanban*) enterprises continued to exist, for enterprises involving the state late period Qing officials made increasing use of an enterprise form giving the state more power than it notionally possessed under the *guandu shangban* model: the "state and merchant co-operated" (*guanshang heban*) enterprise.[57] The new form was either promoted initially as such or developed on the framework of a prior *guandu shangban* enterprise where the state or "official" side encroached on the "merchant" side.

Indeed, this is part of the story for Li Hongzhang's CMS, which after the 1880s saw diversion of firm revenues to activities of a decidedly non-commercial nature and increasing official involvement, leading to merchant rejection and then privatization but with ownership and management ceded into the hands of former officials (or incumbent officials acting in their private interest). So, CMS, which had inaugurated government business cooperation in 1872, was successfully operated with real commercial autonomy until 1884 but was then subject to dominating government influence and direction from 1884 to 1895.[58] Initially, Qing officials proposed that the government take over CMS not because it was failing, but because it was making such a profit for its merchant investors (benefiting from the subsidies, monopoly rights, and preferences

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54. For instance, the rate CMS was able to charge for the transport of tribute rice forced upon local officials, a rate rewarding the most expensive provider, or two to three times higher than the rate charged even by foreign steamship companies hauling ordinary freight. *Id.* at 146–47.

55. For example, the initial (and very generous) 10% fixed annual dividend offered to CMS investors in that firm's promotion stage. *Id.* at 144.

56. Zelin, *supra* note 14, at 632.

57. *See* CHAN, *supra* note 33, at 238–39 (discussing the shift to the *guanshang heban* model).

58. *See id.* at 17 (citing research indicating that CMS tried to consolidate government-business cooperation between 1972 and 1884, but remained under government influence in following years).

detailed above).[59] Indeed, there was significant pressure from high Qing level officials for a government takeover of CMS as early as 1877 (by Shen Baozhen, governor general of Liangjiang),[60] 1879 (by Ye Tingjuan, a tribute-grain manager inside CMS but also an official (a Shanghai *daotai*)),[61] and 1881 (by Liu Kunyi, successor to Shen as governor-general of Liangjiang).[62] All of these efforts were successfully resisted, and the government-appointed comprador-background managers of CMS (Xu Run and Tang Tingshu) became the most significant shareholders of CMS in the late 1870s and early 1880s.[63] However, these forays by powerful officials in the direction of state takeover certainly altered the merchant (now non-manager investor) view of the viability of CMS and its future autonomy. By the early to mid-1880s, the failure of the Cixi Dowager Empress to invest in the Qing empire's defenses, the weakening of Li Hongzhang's political position, and the financial crisis of 1883 made it very difficult for the court to support a non-state operated enterprise like CMS. Accordingly, the CMS merchant managers were replaced by sitting officials, and the enterprise was used by the state for its own, often non-commercial, purposes (such as funding the Beiyang defense forces, even transferring shipping personnel from CMS to the Beiyang Navy).[64] This change was clearly signaled to China's non-state affiliated, private or "merchant" investors by the alteration in the Chinese language names given the newly-appointed managers. Whereas comprador Tang Tingshu was called "chief manager" (*zongban*) of both CMS and the Kaiping Mining Company—an appellation with slight color of official status—when he was succeeded by Sheng Xuanhuai (still a sitting government official) and later by Qing bannerman (and also sitting official) Zhang Yanmo at the Kaiping mines, the "chief manager" title was discontinued, and instead Sheng and Zhang were called "director generals" or "*du ban*," a Chinese language title which in the imperial era clearly indicated a government status and role.[65] That shift in turn led to a rise in corruption and poor performance at CMS, as the enterprise was unable to resist significant government intervention. After 1885, and following the financial crisis in Shanghai of 1883, CMS was effectively reorganized, with Sheng Xuanhuai—always a sitting official (*daotai* of Chefu and Tianjin at different times) but by 1885 the largest shareholder of CMS—appointed director general of the firm.[66] At the same time, all merchant or investor directors were

59. Lai, *supra* note 33, at 147.
60. *Id.*
61. *Id.*
62. *Id.*
63. *Id.* at 144.
64. *Id.* at 150; Zelin, *supra* note 14, at 632.
65. CHAN, *supra* note 33, at 75.
66. *Id.* at 74–75.

removed from their positions (in part because they had lost their capital during the 1883 crash), and Sheng appointed *his* insiders (mostly officials) to the company directorate.[67] Finally, and somewhat ironically, CMS was facially "privatized"—with control ceded to Sheng Xuanhuai and his group and removed from Li Hongzhang and his "merchant" managers—but in fact taken over by bureaucratic officials acting in their own pecuniary and bureaucratic interest.[68] Predictably, perhaps, CMS never again performed as well as in the period when it benefited from a unique balance between government financial support and enterprise autonomy, suffering instead from the withdrawal of state financial support and an increase in bureaucratic control of its operations.[69]

The same transition was visited upon another of Li Hongzhang's *guandu shangban* enterprises, the Shanghai Cotton Cloth Mill in 1887, and by the same official acting in an enterprise capacity.[70] In that year, Sheng Xuanhuai took over the Shanghai Cotton Cloth Mill and tripled its capital account but, tellingly, by taking more government loans *and by the diversion of the CMS funds he now controlled*.[71] Thus, even by the late 1880s, the government was looking at already promoted enterprises—where the government's role had been advertised as mere "supervision" (or "promotion"), weak in the face of simultaneously offered private ("merchant") management—as subordinate divisions (and not independent legal persons or accounting units), which the government could capitalize directly or allocate capital investment freely between. By the end of the nineteenth century, and after a fire destroyed much of the Shanghai Cotton Cloth Mill's original mill, Sheng converted the enterprise into yet another purely *guandu* (government operated) enterprise, but with funding solely from himself and a group of his associates.[72] He tried to raise public investment for that iteration of the enterprise, which failed entirely as non-state investors were justifiably worried about investing in an industrial enterprise run by the state. So, he took over the enterprise under an assumed name and made it entirely private (but given his official background and roles, "private" in the sense that it was funded and operated by individuals

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67. *Id.* at 75.

68. *See* FEUERWERKER, *supra* note 15, at 137–44 (citing contemporary criticism of Sheng Xuanhuai's simultaneous management of CMS and tending to his official duties); *see also* Lai, *supra* note 33, at 149.

69. Lai, *supra* note 33, at 151.

70. CHAN, *supra* note 33, at 74.

71. *See, e.g.*, *id.* (describing Sheng's takeover of Shanghai Cotton Cloth Mill in 1887, and how he quickly tripled its capital using government loans and the transfer of some CMS funds he controlled).

72. *Id.*

with official backgrounds and roles but acting outside of their government statuses).[73]

Wellington Chan summarized the shared process of merchant (private capital) disillusionment thus:

> Merchant disenchantment with the [*guandu shangban*] type of enterprise stemmed from replacement of merchant-managers by men of bureaucratic background. The merchant investors had not been deterred by their lack of voice in company policies (in fact, one suspects that all of the large shareholders or their friends became directors and managers). But they began to shy away from further investment when they became convinced, rightly or wrongly, that government bureaucrats were in control and making use of their capital for bureaucratic and personal ends. . . . [The] early [iterations of the *guandu shangban* form] fulfilled [Li Hongzhang]'s intention to use merchant capital at the merchant's own risk. From the 1880s, however, as these operations passed into the hands of official-managers and their merchant assistants, and as new ones were founded without responsible merchant-managers, merchant capital too, was conspicuously absent.[74]

This increasingly mixed picture of ownership and operational management, and the relative abandonment of the *guandu shangban* model, can be seen across the late Qing landscape and in the run-up to the demise of that last imperial dynasty. As Elizabeth Köll reports for just the mining sector—an industrial sector the central government might have had a strong interest in for both industrial development and defense reasons—the period between 1895 and 1911 saw thirty-five enterprises *founded* as fully private firms (*shangban*), compared to nine owned by the government alone (*guanban*), two as government-promoted merchant-operated (*guandu shangban*), and ten as government–merchant co-operated (*guanshang heban*).[75] Of course, one of the sharp ironies of this imposed transition from *guandu shangban* to any of *guanshang heban*, orthodox *guanban*, *guanban* run for the private interest of officials and their cronies, or full "privatization" (but really delivery of the enterprise into the hands of specific officials), was that finally the enterprises were unable to attract *domestic* Chinese capital investment—the basic point of the *guandu shangban* establishments in the first place—and thus had to rely on foreign loans, leading to the inevitable foreign takeover of strategic Chinese assets later, a takeover which the *guandu shangban* initiative was supposed to protect against.[76]

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73. *Id.* at 74–75.
74. *Id.* at 75–76.
75. KÖLL, *supra* note 33, at 16.
76. *See* Letter from Li Hongzhang to Zhang Shusheng (Dec. 11, 1972), *in* Lai, *supra* note 33, at 142, and accompanying text. Wellington Chan recites an example of this unanticipated and deeply undesirable consequence with respect to the Kaiping mines. Upon ex-comprador and non-official manager Tang Tingshu's death in 1892, and the Kaiping operation coming under the power of Qing bannerman and official Zhang Yanmo, corruption and fast advancing bureaucratization commenced. Chan then cites to Ellsworth Carlson's work to show that while Tang was in charge, the

The late stage proffer of a legal basis for incorporation and registration, legal personality, and limited liability represented by the Qing government's 1904 *Gongsilü* only accelerated increased involvement of no longer court-tied and thus apparently "private" actors in the financing and operation of important industrial enterprises, as will be seen below in the story of Zhang Jian's Da Sheng.[77] Importantly, however, the availability of incorporation provided a vehicle enabling state officials to first gain governance power over state assets but then leave the public sector, along with the assets entrusted to their care and management.

Köll writes about a second *genus* of Chinese enterprise establishment apparent after 1895, what she calls the "regional enterprise"—an evolution of the government sponsored or state co-operated company in the direction of a privately controlled business, but not to the full extent of a traditional Chinese family-owned business (as originated or maintained). As Köll writes in the introduction to her book-length treatment of Zhang Jian's paradigmatic regional enterprise, the Da Sheng group of businesses:

> Originally designed as motors for industrial development, they were formed by privatization of government enterprises. However, even these incorporated enterprises exhibited many of the managerial characteristics of the family business. . . . Before 1895 regional enterprises were nonexistent; by the time they came to be promoted, the imperial government had already been weakened by war and social disorder. Although [Da Sheng] was founded as a joint government-private venture, government involvement became negligible after the first five years and finally redundant when the company acquired legal status as a shareholding company in 1907. The government never played a role in the management or ownership of the company, but Zhang Jian and his family did, though without ever turning [Da Sheng] into a family business.[78]

It is these regional enterprises that—along with the *guandu shangban* transitioning into *guanshang heban* enterprises described above—have perhaps the most to teach us about the path dependency of China's enterprises, especially when the governing national regime is weak or failing.

Köll's impressive history of the Da Sheng enterprise group and its development from 1895 to its demise in the mid-twentieth century is extraordinarily rich in detail and evocative of the way in which semi-private enterprise developed in China through the end of the

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Kaiping mines operations were funded by merchant investment. Under Tang's successor Zhang, merchant investors would not invest, forcing Kaiping to rely on foreign loans, opening the way for absolute foreign control afterwards. CHAN, *supra* note 33, at 75–76. This is why the Kaiping Mines are still referred to today in China as "British" mines.

77. *See* KÖLL, *supra* note 33, at 124–125 (describing how in 1895 the *Dagongbao* newspaper published announcements of approved and registered companies, satisfying the official company registration required by the Company Law [Gongsilü]).

78. *Id.* at 18.

nineteenth century and the start of the twentieth century.[79] This Article necessarily gives too short shrift to that compelling detail and focuses instead on aspects of the Da Sheng development—and Zhang Jian's personal role in promoting and managing it—which have direct resonance for the PRC's corporatized SOE groups today.

Following is a rendition in summary terms of those elements:

First, the impetus for the promotion of Da Sheng was public and governmental, not private and entrepreneurial. Indeed, the entrepreneurial personality involved (Zhang Jian) only metamorphosed away from his official identity with the development of the enterprise. In fact, the share certificates distributed for the Da Sheng enterprise between 1897 and 1907 were emblazoned with Zhang Jian's name, with no allusion to his enterprise post, but instead a prominent broadcasting of his full official title (of Hanlin Scholar, or "*hanlinyuan xiuzhuan*").[80] As with high Qing official Li Hongzhang's inauguration of the paradigmatic *guandu shangban* establishments, the original driver of the Da Sheng promotion effort was Zhang Zhidong, then governor-general of the Liangjiang Provinces (Jiangsu and Zhejiang) and imperial commissioner of the southern ports and—with the demise of Li Hongzhang—the most powerful official in the Qing court. It was Zhang Zhidong who in late 1895 contacted officials in the Suzhou and Zhenjiang prefectures and the Tongzhou department and asked them to recruit local merchants to establish manufacturing facilities for local goods.[81] Zhang Zhidong's explicit policy aim was to resist "the plans of the foreigners" (Westerners and Japanese) after the Treaty of Shimonoseki permitted them to establish manufacturing businesses in China and outside of the treaty ports.[82] Zhang Jian, then still a Qing official who received this governmental instruction from his bureaucratic superior to search out promoters and start-up capital from the private sector, in turn liaised directly with six promoters active in Guangzhou (Canton), Fujian, Ningbo, Shanghai, Nantong (eventually the site of the origins of the Da Sheng group), and Haimen.[83] Initially, each of these promoters committed to investment (or bundling of investment from associates) in a cotton mill operation that still sitting official Zhang Jian pronounced would be entirely "*shangban*" (merchant-

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79. A great deal of the expositive material following is extracted from Köll's history of Da Sheng.

80. *See* KÖLL, *supra* note 33, at 67, 70 (Noting that this presentational aspect proved changeable, as circumstances required and China saw the demise of imperial rule by scholar officials. For instance, on the 1918 graduation certificate for the Da Sheng-established Nantong Textile School, Zhang Jian is pictured in a Western suit and with a cropped, Western-style, moustache, an image of a Westernized "modernizer" as distinct from the traditional imperial scholar official as possible).

81. *Id.* at 63.

82. *Id.*

83. *Id.* at 63–64.

operated), with the promoters listed on an imperial document as "*jingli dongshi*" (managers or managing directors).[84]

Second, the enterprise was finally established and able to operate in its early years only because it had to backtrack on its proposed "private" or "merchant" identity and rely directly on state (Qing court) capitalization and involvement. This reversal became necessary when the original Guangzhou, Fujian, and Shanghai promoters backed out and definitively changed the future enterprise into a far more local regional effort in terms of both capital raising and operations. More importantly, Zhang Jian as the official and direct godfather of the project found that he could not raise sufficient capital to purchase the machinery needed for manufacturing operations, which under the original plan was to be purchased with the proceeds of the defecting Shanghai-origin cash investment.[85] Thus, Zhang Jian had to appeal to the state for financing support and to obtain the key capital equipment required to commence operations. This appeal came at a very tricky time, and was indicative of how important specific personal official patronage was, because of Zhang Zhidong's resumption of the governor-generalship of the Huguang provinces and his replacement as governor-general of the Liangjiang provinces by an entirely different official, Liu Kunyi. Liu was apparently sympathetic to Zhang Jian's plight but could not in the end arrange financing for the necessary equipment purchase.[86] This resulted in a renewed intervention by the real official-in-interest, Zhang Zhidong, who contributed second-hand English manufacturing equipment originally purchased by the government under Zhang Zhidong's direction for a planned cotton mill in distant Wuchang but since warehoused in Shanghai.[87] Zhang Jian and the Qing state agreed that the contribution of equipment would be booked as state capital investment, comprising fully 50 percent of the capitalization of the future Da Sheng mill, with the remainder of the capital to be contributed by private investors.[88] Thus, even in the planning stages the future enterprise had metamorphosed from being explicitly "*shangban*" to a paradigmatic "*guanshang heban*" enterprise (and something very close to what is seen today in a corporatized SOE with a percentage of public capital markets investment/float, where productive capital has been contributed by the state and is matched with non-state investment now procured through modern capital markets).[89] Over time, this state investment of secondhand foreign

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84. *Id.* at 64.
85. *Id.*
86. *Id.*
87. *Id.* at 64–65.
88. *Id.* at 65.
89. Köll relates the story of a side deal that Zhang Jian tried to bring off when he immediately faced difficulties raising the other 50% of the planned capitalization for the enterprise from non-state sources, and which also has resonance in the modern

equipment was effectively appropriated from the state by the enterprise. How? Until 1908, the last year before Da Sheng's corporatization under law, the court-donated equipment was listed on the enterprise accounts as "official machinery capital" (*guan ji gu chengben*) to indicate that it was the fruits of a capital contribution by the largest investor, the state.[90] After 1908, it was listed simply as "machinery capital" (*ji chengben*) on the books of Da Sheng (even though the accounting category of "state contributed machinery" (*guan ji*) continued to exist), the state was no longer an investor in the corporatized entity or able to collect profit share from Da Sheng for the capital it had contributed and equity it should have received in return, and there is no evidence that Da Sheng or any investor in Da Sheng actually purchased the machinery from the state.[91] In effect then, a non-state enterprise, managed by non-state actors, had appropriated significant assets of the state that had at inception represented 100 percent of the in-kind capitalization of the firm, for *nil* consideration to the state or the contributing/selling party.

Third, Zhang Jian's Da Sheng was intimately involved with political as well as business tasks. Between 1898 and 1903, many of the Nantong area's local cloth businesses were investors in Da Sheng. They were both investors in the productive enterprise and key links between industrial yarn production and cloth weaving in the locality, as well as the historical markets of those local weavers.[92] Those cloth merchant investors included individuals who had previously lobbied the Qing government to reduce a transit tax on commercial goods that had hurt particularly in a slump experienced by such businesses in the late nineteenth century.[93] They had little success on their own, but once they agreed to help finance the initial *guanshang heban* Da Sheng, Zhang Jian—still an official, though now also in charge of a state-invested enterprise—petitioned the court on their behalf to

PRC for the way "state" assets improperly enter the non-state owned economy: in 1897, Zhang Jian approached the former official and later investor *cum* manager extraordinaire of many prominent government sponsored enterprises in the late Qing, Sheng Xuanhuai, for finance help. Zhang Jian's proposal was to "sell" Sheng Xuanhuai half of the machinery contributed to Da Sheng by the government (by Zhang Zhidong specifically) in exchange for cash (250,000 taels). In effect, Zhang was suggesting that Da Sheng sell state assets already contributed to Da Sheng (and already recognized in the state's 50% equity interest in Da Sheng) for cash, which cash would be recognized as cash equity investment in Da Sheng by Sheng Xuanhuai (thus, double counting on the equity account). All of this would allow Zhang Jian to state that he had raised matching "private" investment for Da Sheng, even though he would have effectively disposed of state assets to private interests (with no consideration for the state seller) and radically diminished the productive capital of the planned enterprise. Luckily for all concerned, this particular grab at public assets by Sheng Xuanhuai did not pan out. *See id.*

90. *Id.* at 127.
91. *Id.* at 127.
92. *Id.* at 66.
93. *Id.*

relieve the burden of this tax.[94] Here lies a small demonstration of the mixture between roles and priorities, for both officials intent on financing an enterprise and private investors seeking a public administration benefit. Indeed, as Köll demonstrates in her telling, as state and official patronage—in the person of Zhang Zhidong—was withdrawn, Zhang Jian as promoter of the Da Sheng enterprise relied increasingly on the support of the local business community in Nantong.[95]

Fourth, and again as already seen with respect to the initial *guandu shangban* enterprises, investors in Da Sheng were the beneficiaries not of a participation in *net profits* of the enterprise, but instead of a guaranteed payment (*guanli*)—8 percent in the case of Da Sheng—to be paid by the enterprise to its investors without regard to performance of the firm or even the existence of distributable profits—in effect then a preferred dividend or above-the-line interest payment on a bond.[96] While later the shares of Da Sheng were traded by the Shanghai Stock Merchants Association (starting in 1917) and the shares of Da Sheng No. 1 Cotton Mill and No. 2 Cotton Mill were listed on the Shanghai Stock Exchange (from 1920), and thus investors experienced some amount of equity risk, such investments effectively remained fixed income investments for the private investors who participated in the enterprise group given the guaranteed dividend.

Fifth, the initial cotton mill that Da Sheng was promoted to own and operate—the Da Sheng No. 1 Cotton Mill—was merely the first enterprise in what through the early twentieth century grew to become a group of affiliated enterprises and offices, only some of which were formed as legal subsidiaries, which in the end included flour and oil mills, shipping lines, land reclamation operations, a publishing house, and a distillery.[97] These affiliated operations were established to ensure the provision of raw materials (or the land upon which to create the raw materials) and/or transportation facilities and services solely or chiefly for the Da Sheng-governed cotton mills. These affiliations (many based on ties which had nothing to do with formal ownership), subsidiary relationships, cross-ownership, or even interlocking directorships were maintained even after Da Sheng was

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94. *Id.*

95. *Id.* at 67.

96. *Id.* at 67–68.

97. By 1910, and even after Da Sheng had procured limited liability company status in 1907, the group comprised seventeen different affiliated operations, including: the original Da Sheng No. 1 Cotton Mill and one branch mill on Chongming Island (established 1907); the Guansheng Oil Mill (1901); the Tonghai Land Reclamation Company (1901); the Hanmolin Publishing House (1902); the Dalong Soap Factory (1902); the Zisheng Iron Workshop (1905); and the Fuxin Flour Mill (1909). In 1921, another branch mill was established in Haimen County.

corporatized as a limited liability company under China's first company regulation, the Qing dynasty's 1904 *gongsilü*.

Indeed, the corporatization of one part of the Da Sheng complex of enterprises under "law," and the relationship of the resulting "legal" property and ownership relationships to actual managerial control—in particular, the way in which critical financial and managerial control of the entire group was exercised by a Shanghai "office" external to the formal legal network of enterprises—has close resonance to the way in which corporatized SOE groups are run in the modern PRC.[98]

Köll reports that the Da Sheng No. 1 Cotton Mill's status *qua* a *guansheng heban* enterprise was never formally annulled. The share certificates for the enterprise issued between 1897 and 1903 all advertised the operation's *guansheng heban* nature with the legend that the Da Sheng mills "were established in Tongzhou with approval granted by [imperial] edict in response to a memorial from the Imperial Commissioner of the Southern Ports . . . , per contract established in perpetuity to be jointly managed (*dingli hetong yongyuan heban*) by officials and gentry."[99] By March of 1905, an announcement appeared in the *Da Gong Bao* newspaper indicating that the Da Sheng No. 1 Cotton Mill had been approved and registered as a company (*gongsi*) with the Qing Commerce Ministry (*shang bu*) per the 1904 companies regulation.[100] Two years later, in 1907, the report of the first shareholders' meeting of the Da Sheng No. 1 Cotton Mill states that it is specifically a company limited by shares (*gufen youxian gongsi*) under the 1904 Qing statute.[101] However, after 1907 the company's share certificates never refer to its status as a company limited by shares, and only four years after the demise of the Qing dynasty in 1911 (from 1915) stop alluding to government involvement in what was once a *guanshang heban* enterprise.[102] Da Sheng's Chongming Island No. 2 Branch Mill, which had many of the same investors as the No. 1 Cotton Mill, was registered as a company (*gongsi*) with the Qing Commerce Ministry in 1905 but not specifically a company with limited liability and with no indication of a subsidiary relationship to the Da Sheng No. 1 Cotton Mill company limited by shares (which appears correct, because the registered company limited by shares apparently did not own any equity in the Chongming Island No. 2 Mill).[103] As the group grew in the early twentieth century, the Da Sheng No. 1 Cotton Mill as incorporated became both a holding company (holding direct equity

98. *See infra* text on pps. 996–1000.
99. KÖLL, *supra* note 33, at 124–125 (Figure 5.1, showing the 1897 certificate).
100. *Id.* at 124.
101. *Id.*
102. *Id.* at 125.
103. *Id.* at 125–126.

stakes (10 percent, 32 percent, 15 percent, and 17 percent) in, and maintaining interlocking directorships regarding, four true subsidiaries, and the hub of "affiliations" (for thirteen other operationally and legally separate enterprises).[104] The affiliations grew out of common management or shareholders, investment by the Da Sheng No. 1 Cotton Mill acting as an investment/holding company, financing of the affiliates in the form of "deposits" (*cun*) by the Da Sheng parent, and exclusive contractual relationships between the affiliates and the main cotton mill business. The "deposit" transactions—whereby Da Sheng financed the affiliates without making equity investment in other such enterprises (or, more importantly perhaps, creating a dividend obligation) but instead by making a donation of capital much harder to retrieve—were clearly a way for Zhang Jian to deprive the investors in Da Sheng No. 1 Cotton Mill from any governance power over the affiliates receiving the "deposit" funding, as power remained in the hands of Zhang Jian and his close associates. Here are early indications of the very fuzzy borders between clearly affiliated and co-governed enterprises (the same kinds of operations, with many of the same investors, governed by the same system of human agents), but not strictly related or even affiliated in any legal or property rights sense.

In another strong echo of the modern PRC circumstance, the corporatization of Da Sheng under law and the simultaneous creation of a class of "shareholder-owners" did little to empower those investors, at least insofar as management of Da Sheng or any of the affiliated enterprises was concerned. Zhang Jian was not elected by those shareholders to the position of managing director (*zongli*) of the enterprise and instead just continued as the manager of the enterprise through the transition from *guanshang heban* to company limited by shares.[105] When faced with criticism at the first shareholders' meeting in 1907—because of rich salaries and bonuses given to other managers (including family) and even funding of welfare and educational projects expressive of the personal virtue of Zhang Jian—Zhang Jian was able to ignore the shareholder concerns and instead critique the shareholders for seeking involvement in substantive decision making in enterprise affairs.[106] Indeed, the shareholders of the corporatized entity were never able to stop Zhang Jian from engaging in these transactions, which as they complained for years were both related party transactions (in a situation where

104. *See id.* at 136–37 (laying out the organization of the Dasheng business complex as a whole, and the function of the No. 1 Cotton Mill in that complex).

105. *Id.* at 126–127.

106. Precisely the reason the patriarch of the Nanyang Brothers Tobacco enterprise resisted seeking finance of the family business (necessary to compete with British American Tobacco) via incorporation and a minority equity public float because it would lead to the introduction of "disloyal", short-term oriented, and non-family-tied investors. COCHRAN 1980, *supra* note 33, at 96–102.

Zhang Jian and his family probably held shares under so-called business names) or aspects of corporate "waste."[107] This first interaction then between newly minted Da Sheng "shareholders" and continuing managing director, part government official, part promoter, reveals the state of corporate governance in the Chinese tradition of the early twentieth century, a picture deeply familiar for those who study modern PRC corporatized SOE groups and their listed companies.

Likewise, the fact of corporatization and the conferring of limited liability on the Da Sheng No. 1 Cotton Mill did very little to change the *status quo ante* of the enterprise's internal governance, other than the start of annual general shareholders' meetings in 1907. Thus, internal management of the enterprise remained static, with the various department heads still directly appointed by the "managing director" (Zhang Jian) rather than the new "board of directors" (*dongshiju*).[108] Moreover, even though the 1904 Qing company law regulation required the appointment of two "auditors" to review the accounts of the newly corporatized entity, the Da Sheng auditors were actually Da Sheng board members, and thus also directly under the power of Zhang Jian as the managing director, and therefore generally functioned to justify the decisions they had signed off on *qua* directors.[109] As Köll summarizes the changes *not* wrought by incorporation:

> On the whole, incorporation, which we tend to associate with "modern" business enterprise in the Western sense, did not seem to lead to significant improvements in shareholder protections or curbs on the power of the managing director [Zhang Jian]. To judge from the complaints at the 1907 meeting and their complete futility, shareholders were still at a disadvantage despite the potential for openness and accountability through incorporation. The balance of power did not change in the company. The fact that from 1919 on shareholder meetings frequently took place in Zhang Jian's private villa in Nantong City symbolically confirmed his steady, strong personal hold over [Da Sheng] and his power vis-à-vis its shareholders.[110]

Sixth, and perhaps most evocative of modern-day PRC enterprise structures, financial and managerial control of the entire Da Sheng group of enterprises (corporatized and not, listed and not) was exercised by a Shanghai "office" external to the formal legal and reporting network of companies, group departments, and productive operations, and ruled absolutely by Zhang Jian and his personal team (including, but not limited to, family members), few of whom had formal management or equity positions in the Da Sheng complex of

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107. *See* KÖLL, *supra* note 33, at 127 (detailing Zhang Jian's unpopular business practices and the shareholder response to them).
108. *Id.* at 129.
109. *Id.*
110. *Id.* at 129–30.

subsidiaries and affiliated enterprises.[111] That office was the Da Sheng consortium's "Shanghai Central Accounts Office" (*hu zongzhangfang*), authorized in financial reporting terms by the company's 1897 articles of association, but already by 1910 the absolute center of decision-making and what would today be called intra-company finance for the entire Da Sheng group.[112]

Above I have described how Da Sheng both (i) invested in group subsidiaries and (ii) contributed cash capital to "affiliated" group enterprises without making equity investment but instead by "depositing" funds (*cun*) with the affiliates. Eventually, the external investors in Da Sheng complained about this method of intra-group financing and so at the first post-incorporation shareholders' meeting of 1907 suggested the establishment of a true holding company, the Tonghai Industrial Limited Liability Company; the idea being that an entity fully capitalized by Da Sheng would be under the indirect governance power of the Da Sheng investors.[113] As shareholder Zheng Xiaoxu argued at that shareholders' meeting, "the volume of transactions between the subsidiary companies and Da Sheng . . . has become too large. [It is necessary] to draw a clear line by taking all the debts of the various companies as the share capital of the Tonghai Industrial Limited Liability Company."[114] In the event, the new holding company was duly authorized but in fact made into a free standing account of the Da Sheng No. 1 Cotton Mill entity, whereby "deposit" debt to the affiliated enterprises was written off or converted into Da Sheng No. 1 Cotton Mill's equity in the debtor enterprise held by the holding company.[115] This attempt at reform of intra-group transactions and financial flows spurred by the Da Sheng shareholders, and its almost immediate frustration, reveals the true function of the Shanghai Central Accounts Office (under the personal supervision of Zhang Jian, not the Da Sheng firm or its managers): it was a vehicle for management and financial control of the entire group of enterprises and an institution that allowed Zhang Jian and his fellow insiders to almost completely work around the incorporated Da Sheng No. 1 Cotton Mill that had procured capital from external investors.[116] For in fact, the affiliated enterprises and subsidiaries of Da Sheng reported not to the No. 1 Cotton Mill incorporated entity, much less the Tonghai Industrial Limited Liability Company established to assuage concerned shareholders, but instead to the Shanghai Central Accounts Office, an institution not referred to in the company's articles or any statute or regulation but which

111. *See id.* at 131 (outlining the internal organization of the Da Sheng business group, and recounting excerpts from Zhang Jian's diaries).
112. *Id.* at 135–36.
113. *Id.* at 139.
114. *Id.* at 139–40.
115. *See id.* at 140–41.
116. *Id.* at 141.

consistently acted as the true holding company or finance holding company for the entire Da Sheng group.[117]

As Köll demonstrates in precise detail, the Shanghai Central Accounts Office acted as investment company, and paymaster and broker, for the Da Sheng subsidiaries and affiliated companies. With the head of the Shanghai Office dealing directly with the managing director of Da Sheng (Zhang Jian), this "office" did everything a group headquarters/holding company might do and more: it invested in (via "deposits") and received interest on deposits directed at the affiliates; managed and drafted the accounts of the affiliates; represented the Da Sheng group of enterprises in Shanghai (and engaged in group product transportation and sales, the negotiation of loans, and sale of equity interests (including the delivery of share certificates), for such entities); ordered machinery for affiliated enterprises; made payments to external institutions *on behalf of* Da Sheng and/or group affiliates; balanced out intra-enterprise accounts moving net amounts to the affiliates; and decided how various group financial transactions should be entered and on which affiliate's books, etc.[118] Critically, this mere "office" effected all of these group transactions not from the platform of an independently established holding entity or via cross-directorships that—in law or via property rights connections—controlled the subsidiaries or affiliates, but through an entirely extra-legal institution that operated outside of shareholder governance or management and without regard to separate legal personality, distinct aggregations of investors, or the notion of separate accounts. Perhaps just as important, the Shanghai Central Accounts Office was at the same time Zhang Jian's personal office running his private and family accounts, with receipts and expenditures easily commingled with Da Sheng accounts and transactions.[119] This is not to say that Zhang Jian was in the modern sense "corrupt," or that he impermissibly used the Da Sheng complex of enterprises as a piggy bank from which he consistently misappropriated value. Instead, the Shanghai Central Accounts Office reveals the existence of (i) a well-understood institution in Chinese commercial organization that effectively looks through the constraints of separate legal personality, accountability to investors in specific entities, and independent entity accounts; and (ii) the mechanism by which personal (insider) control of a family of enterprises, many financed with the capital of strangers, is implemented and maintained, an aspect of control which does not distinguish between private power and managerial control over publicly financed assets. After noting the roots of this kind of

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117. *See id.* (positing that Zhang Jian did not want to regulate and publicize the activities of the Shanghai Office, which was the true head of the Da Sheng business complex).

118. *Id.* at 141–43.

119. *Id.* at 144.

central office or account hub in traditional Chinese family businesses, and even other post-Republican explicitly corporate structures, Köll summarizes:

> As this institution [the traditional accounts office in Chinese family businesses] was adapted to an industrial joint-stock enterprise with limited liability, one would expect conflicts of interest between the shareholders and the managing director (who was also the founder). However, in Zhang Jian's case, his personal authority and control were not curtailed by but embedded in the Shanghai office as an institutionalized tool of control. In fact, the internal organization of the Shanghai office and its placement outside the formal structure of the [Da Sheng] complex allowed Zhang Jian to exert full vertical authority, to use a modern management expression.[120]

Seventh and finally, Zhang Jian as the official *cum* private promoter of the Da Sheng complex relied heavily on a network of individuals, which included but was not limited to family members (notably his brother Zhang Cha) and non-family associates with business, political, or personal ties.[121] People with a superficial understanding of Chinese business organization might assume that such networks would have to be based in family ties. Zhang Jian's promotion and management of the Da Sheng consortium makes clear, however, that such Chinese networks are not exclusively family based, but instead are rooted in a network of individuals with common work experiences, geographical backgrounds, or involvement in a specific sector of industry of commerce. This kind of network might be seen as the analog to modern day PRC enterprise groups, which can be dominated by networks rarely based in familial relationships and not truly disturbed by Communist Party appointments, but instead affiliated with a given "system" (*xitong*)—for the PRC's present day corporatized SOE groups, the ministry group from which the enterprise group sprung.[122]

A final word about what the historical literature calls "family enterprise" in pre-CCP-ruled China: Family businesses of course have a very long tradition in China, and those long-standing family firms gave rise to a large number of important enterprises. Specifically, the nineteenth and early twentieth centuries saw apparently "modern" enterprises grow out of family businesses, which increasingly engaged with the law and legality after promulgation of the *Gongsilü* in 1904 and successor statutes and regulations. Between 1904 and 1908, 272 companies registered with the Qing government, more than 50 percent of them as what would be recognized as joint stock companies with limited liability.[123] Indeed, after the fall of the Qing dynasty in 1911, and into the uncharted waters of the Provisional

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120. *Id.* at 146.
121. *Id.* at 69.
122. *See* LIEBERTHAL, *supra* note 32.
123. KÖLL, *supra* note 33, at 17.

Republic, the Beiyang Government of Yuan Shikai, and the warlord contest that followed, family businesses continued to register as joint stock companies with whatever Beijing-based regime claimed the title of national government.[124] Importantly, although registered as companies under then-applicable corporate law, many of the apparently incorporated family businesses were governed in contravention of law and entirely pursuant to norms applicable to family partnerships with no separation of ownership and management (at least with respect to family owners) and scant regard for, even hostility towards, stranger investors.[125] In that sense—formal corporatization under law with incumbent control powers undisturbed—such incorporated family businesses show a similarity to the PRC's corporatized SOEs. In addition, and as described above with respect to Zhang Jian's Shanghai Central Accounts Office for his Da Sheng group of entities, these incorporated family businesses also used the office of "financial controller" to allocate finance capital within the corporate group and its controlling shareholders—with the same lack of respect for legal person or independent accounting unit boundaries seen in today's PRC finance company transactions and the same diversions of value implemented by official patrons of the *guandu shangban* and *guanshang heban* enterprises.

IV. COMMONALITIES AND DISTINCTIONS

The unavoidably superficial and perhaps overly-specific recitation above should allow observers of the modern PRC's corporatized SOEs to see distinct commonalities between China's largest companies and corporate groups today and their firm ancestors from the late 1800s and early to mid-1900s. Above all, each generation of firm institution evidences acceptance of the strong Legalist assumption that state control of the key instruments of the productive economy was and is necessary in order to bring wealth and power to the Chinese nation. This assumption strongly refutes a long time counter-assumption (foreign and Chinese)—a touch "Orientalist" or at least mildly exoticizing—which speaks to the hostility of the Confucian tradition to merchant (private, commercial) activity *per se*. Reflecting on history, there is an almost unshakeable view that the Chinese state, of whatever species, must control industrial development and the instruments that can bring about such development.

Second, it seems clear that one of the key policy drivers supporting large-scale and state-controlled Chinese enterprises is the

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124. *Id.* at 41.
125. *See* COCHRAN 80, *supra* note 33.

desire to create entities that can resist the political and economic incursions in China made by foreign firms or simply aggregations of capital managed by non-Chinese interests. Even though it seems slightly ironic in a world where PRC enterprises "march outside" (*zou chuqu*) seeking control of assets and businesses abroad, the project of firm development that commenced in the nineteenth century must be seen as in part defensive, and in the modern era, effective.

Third, the same mix of policy imperatives over more than one hundred years led to the same kind of firm institution in the 1880s as now seen in the late 2010s: the state was (and is) intent on maintaining state control and creating entities that can check foreign capital and competitors, while also raising enough capital to fund the appropriate scale of operations but without disturbing the state's incumbent control position. Where the state cannot or will not pony up that capital, the easy answer is public capital markets financing which introduces significant funds to the state-dominated firm alongside the assurance of passive or entirely dominated "stranger" investors. Thus was born both the initial *guandu shangban* entity described above, and the (still) state-dominated corporatized SOE issuer collecting capital on the world's capital markets with a decidedly minority float (and the public capital markets-accessing company predecessor, the Chinese-foreign joint venture which from the late 1970s matched foreign capital (and know-how) alongside mostly insolvent state-owned assets).[126]

Fourth, in both eras state law seems to have little traction on or relevance for what is the quintessential "legal" form, the modern corporation with legal personality, limited liability for shareholders, centralized management and alienation of shareholders, and accountability of managers to owners, all conferred *by law*. As noted above, China's first firms were created without benefit of any statute, regulation, or even imperial edict, but instead came as a policy innovation conceived and implemented by a powerful government official. Even when something like law did appear in 1904, these corporate entities either acted outside of such mundane constraints or imposed work-arounds which thoroughly gutted any law-based architecture, rules, or standards, and any possibility of voicing minority shareholder rights or enforcing governance constraints. Similarly, even though the PRC's first post-Revolution Company Law appeared in 1994, and was well and expertly re-written in 2006, it still has embedded in it an entire section (i.e., the part regarding the WSOC sub-species of LLC) and many provisions with an extreme "shareholder orientation" (pernicious, where corporatized entities are dominated by a Party State controlling shareholder), which only make sense for the establishment of corporatized SOEs with no, or

126. *See* YASHENG HUANG, SELLING CHINA: FOREIGN DIRECT INVESTMENT DURING THE REFORM ERA 340–42 (2003).

radically disempowered, minority shareholders. As many commentators have remarked, the PRC Company Law was never imposed upon corporatizing SOEs, instead the corporatization without privatization program has worked in the opposite direction to almost fully cannibalize China's "modern enterprise" system aspirations and the law that shapes and enforces it.[127] In the modern case then, the seeds of a thoroughgoing disrespect of company law, shareholder protections, and managerial accountability reside in the PRC Company Law itself.

Fifth, firms in both eras are established and able to operate only with the contribution of public, or non-privately owned, assets into the apparently autonomous corporate vehicle, and in an environment with quasi-monopoly protections provided to the enterprise by the state promoter, regulated pricing (in the form of discounted inputs or guaranteed margins embedded in revenues), and something like a fixed income return to non-state investors. Thus, such companies are anything but entrepreneurial or (for initial investors) risk-bearing, but instead represent the opportunity to purchase a fixed return via participation in a state-protected monopoly or franchise.

Sixth, Chinese firm establishments across more than a century share a perpetual contest over who precisely will govern these massive aggregations of capital, a contest between state (court, or Party) functionaries on one side, and private sector entrepreneurs (merchants and merchant participation in the Qing), on the other. Through Chinese history, the respective power balance has been extremely fluid, and as noted above, made more complex given the opportunistic migration of "official"-side personnel to the "merchant" side (very often along with control of what were state assets). This contest is unavoidable, because assets and governance power must be tied to individuals or networks of individuals and cannot be the instruments of the paradigmatic "absent principal," the imperial court or "all the people" (or "the state" or the Party behind the Party State). Nonetheless, this struggle over governance of firms and their productive assets has very serious implications for the efficiency gains that can be wrought from them, and the transfer of public assets into what looks like a private, and what economists assume is a more efficient, sector. Moreover, it has significant implications for the extent to which generally applicable state legal norms or regulation can be enforced or effective against corporate actors who represent the same state that promoted the enterprise.

Seventh, this look back in history reveals clearly the roots of the particular PRC institution that is the corporatized SOE group

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127. Clarke & Howson, *supra* note 11, at 245–47; Clarke, *Corporate Governance in China: An Overview*, *supra* note 11, at 494–95; Howson, *Corporate Law in the Shanghai People's Courts*, *supra* note 11, at 321–27; Howson, "*Quack Corporate Governance*", *supra* note 11, at 689–94.

"finance holding company." As noted above with respect to Zhang Jian's Shanghai Central Accounts Office, as was a common feature of family business consortia in China and the Chinese diaspora, and as functioned through the person of the sponsoring official in the earliest days of the *guandu shangban* firms (e.g., Li Hongzhang, Zhang Zhidong, Sheng Xuanhuai, etc.), the history of Chinese firms shows the presence of an institution (or a person) which directly managed group governance and financing, *without any regard for legal boundaries, property rights, or governance structures.* One need not be offended by such obvious disregard for these formal relationships; instead, one can simply recognize that, for good or ill, PRC enterprise groups, even with companies listed on the world's most mature markets and subject to the most modern corporate law and securities regulation, still exert managerial and financial control over their group entities through such institutions, and still in disregard of formally proclaimed boundaries or governance relationships. This insight is useful in understanding the function of finance holding companies not only in the PRC, but also the superior Communist Party system that sits behind all formal (legal) enterprise institutions, like the board of directors, the officers corps, etc.[128]

Finally, this historical consideration of Chinese firm development from the mid-1800s on demonstrates a pattern that is also discernible today. These aggregations of state assets (or access to a state franchise or monopoly) are initially financed by external investors invited in with the promise of significant enterprise autonomy and shareholder wealth maximization. Admittedly, those promises might be subordinate to what in the Qing was a "guaranteed return" and the chance to make money in the embrace of a state-enforced monopoly, yet they appeared to be important promises, at least from the standpoint of central government policy makers anxious to attract such investment. (Just as later in Chinese history, under both the Qing court and later the Communist Party of China, guarantees residing in formal "law" seemed important.) Notwithstanding those initial promises, however, both in the late Qing and in the contemporary PRC, the trajectory whereby the state has reasserted its governance power over such assets after initial promotion and financing is extremely common. In history, this has occurred both with the financial success of the enterprise, or the occurrence of a broader political or military crisis. The only real deviation from this pattern has occurred when former state

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128. *See* Nicholas Calcina Howson, *China's Restructured Commercial Banks:* Nomenklatura *Accountability Serving Corporate Governance Reform?*, *in* CHINA'S EMERGING FINANCIAL MARKETS: CHALLENGES AND GLOBAL IMPACT 123, 129–131 (Zhu Min et al. eds., John Wiley & Sons (Asia) Pte. Ltd. 2009) (describing the continued, and determinative, role of Party organizations and cadres behind formal corporate and legal structures).

functionaries leave their official role and misappropriate what were state assets (albeit financed by external investors) to assert governance over them—and the returns—as non-state actors (e.g., Sheng Xuanhuai and Zhang Jian in the late Qing, PLA officers in the 1990s, the insiders connected to Pingan and Anbang in the 2010s, etc.).

Of course, it goes without saying that China, and the world, in the late 1800s and the 2010s are very different, and some of those differences frustrate the effort to see a useful identity between the state-promoted firms of long ago and today's corporatized SOE behemoths. China's degree and style of engagement with the outside world is radically different, although in this context, only better in that the PRC and its corporate issuers are able to access a much deeper global market for capital (compare Shanghai's Fuzhou Road Teahouse Exchange from the 1880s and the New York Stock Exchange presently). Likewise, the pressures that China faces, and the occasional "shocks" it must navigate, are of a different order (contrast the defeat of the Qing empire by the upstart Japanese in 1895 and the humiliation of the Treaty of Shimonoseki, on one side, and the lesser shocks presented to the PRC by the WTO accession in 2000, the Global Financial Crisis in 2008, and the Chinese stock exchange "crashes" of 2015-16). The situation in the late nineteenth century was dire for China and constituted an existential threat to its sovereign power and the very fact of imperial government (duly overthrown in 1911). Nonetheless, both eras present the same development and nation strengthening imperatives, which shaped and shape similar responses at least insofar as enterprise establishment was and is concerned. Finally, by way of example, the development of a domestic legal and regulatory system in China, and engagement by China with external legal and regulatory systems, are now of a completely different order than what they were at the end of the 1800s. That being true, it only highlights the strong persistence or path dependency of certain institutions, arrangements and practices related to enterprise formation, financing, and governance stretching back more than a century, and notwithstanding real advances in what the PRC calls "legal construction."

V. CONCLUSION

This Article has attempted to draw a line between specific institutions that arose or were promoted by the Qing court in the latter part of the 1880s and contemporary China's corporatized SOE enterprise groups and their domestically and internationally listed subsidiaries.

The aim of this Article has been to show that the PRC's program of "corporatization without privatization"—whereby traditional SOEs

or specific groups of SOE assets were transformed into companies limited by shares under the PRC Company Law and financed through the public capital markets (domestic and foreign), but continue to be managed by non-professional CCP *nomenklatura* appointments and feature transparent exploitation of non-state capital investors by controlling (state) shareholders empowered under a "shareholder-oriented" corporate law—is not something that rose from a blank slate in the mid-1990s.

Instead, these modern era PRC institutions have their roots in very similar enterprise establishments conceived in the mid-1880s and continuing right through to the start of the Anti-Japanese War, wherein the state promoted large-scale enterprise in protected or monopoly sectors deemed necessary to build China's "wealth and power" with the promise of a guaranteed return and non-state management to attract non-state capital investment.

In the modern case, this program has succeeded beyond the wildest dreams of any PRC policy maker, allowing the nation to finance the creation and maintenance of the world's largest (by market capitalization and revenues) enterprises critical to China's industrial development policy and ability to compete globally, without any promise of autonomous management much less ousting of state functionaries from their direct management role.

Indeed, if the comparison holds, it only means that the future trajectory of PRC firm development will see ever-increasing assertion of state control over such enterprises as the financing mechanism has worked and continues to work well, and there is no cost associated with, or real resistance—political, economic, or legal—to, state controlling shareholder domination even when identified. There are only two ways in which this trajectory in the direction of increasing state-controlling shareholder domination may be altered. First, if state origin insiders continue to misappropriate state assets initially placed under their governance power and convert them and the associated value flows to private or non-state property (their own), then there may be enough domestic political resistance—elite and popular—to re-think the process and its institutional expressions. (The PRC is seeing some of this resistance in the course of the still very popular Anti-Corruption Campaign being implemented by Xi Jinping and Wang Qishan.) Second, there is the chance, but only a slim chance, that foreign capital participation in these enterprises (and eventually perhaps domestic investor participation), and the expectations of such investors regarding formal legal constraints and enforcement, may push back against minority shareholder oppression or firm-injuring self-dealing by the control shareholders and/or their agents, or force equity price discounts unacceptably large for the securities issuers involved. This possibility is slim because the investor population that now participates in the modern PRC's version of the late Qing's *guandu shangban* or *guanshang heban*

enterprise is much more diffuse and distant, and never had the expectations dear to the late nineteenth century "merchant" investor/operators of any management influence in the first place. Ironically then, a twentieth century Communist Party-led government navigating modern capital and information markets, and facing the existence of a substantive domestic legal system, has achieved for its enterprises and national development strategy what a nineteenth century imperial regime—even without the burden of international investment expectations or developed legal and regulatory systems—could not for its enterprises or national development program.