10-1-2014

Protecting the State from Itself? Regulatory Interventions in Corporate Governance and the Financing of China's 'State Capitalism'

Nicholas C. Howson
University of Michigan Law School, nhowson@umich.edu

Protecting the State from Itself? Regulatory Interventions in Corporate Governance and the Financing of China's "State Capitalism"

Nicholas Calcina Howson
University of Michigan Law School

ABSTRACT

From the start of China's "corporatization without privatization" process in the late 1980s, a Chinese corporate governance regime apparently shareholder-empowering and determined by enabling legal norms has been altered by mandatory governance mechanisms imposed by a state administrative agency, most often to protect minority shareholders against exploitation by the party state controlling shareholders which are the accepted powers of "state capitalism". This chapter reviews the path of that benign intervention and the structural reasons for it, and then speculates on why this novel identity of the Chinese party state's "fragmented authoritarianism" continues to be tolerated by the same party state, and indeed how it is necessary for the continued financing of China's "state capitalism".

Draft chapter to be published in CHINESE STATE CAPITALISM AND INSTITUTIONAL CHANGE: DOMESTIC AND GLOBAL IMPLICATIONS (Benjamin L. Liebman & Curtis J. Milhaupt eds., Oxford University Press, forthcoming 2015).

Introduction

Many observers assume that the "state capitalism" model for the People's Republic of China ("PRC" or "China") implicates relatively unfettered control of listed subsidiary corporations by the agents of the PRC party-state, whether direct state equity owners, state-affiliated holding companies (or groups), or the *nomenklatura*-origin individuals appointed or elected to the Chinese Communist Party committee, board, supervisory board, or senior management of such firms. This assumption may not be entirely accurate. Instead, China's securities regulator (the China Securities Regulatory Commission ("CSRC")) and other bureaucratic agencies have for many years imposed mandatory governance constraints on a formally shareholder-oriented and "enabling" law-based corporate governance system, and with the express goal of empowering minority shareholders and constraining the power and discretion of the PRC's strongest political economic actors under the "state capitalism" model.[1] This chapter reviews the structural reasons for this sustained intervention, and speculates on how and why one tentacle of the party state – the CSRC – has been permitted to implement this constraining mechanism on the heads of other, far more powerful, tentacles of the same political economic structure, corporatized state-owned enterprises ("SOEs"). I conclude with speculation on how these constraints and enhanced accountability mechanisms contribute in a significant way to the financing, and thus continuing viability, of China's "state capitalism".

[1] *See* Nicholas Calcina 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 (2014) (hereinafter, *Battle Against Party State Power*).

A "Mandatory" Regulatory Intervention into the Province of "Enabling" Law

China's public company regulators have over the past two decades consistently acted to create, re-craft or anticipate the most fundamental aspects of the PRC's formal legal corporate governance system, and institute robust board-related and/or minority shareholder-empowering norms designed to protect against controlling shareholder oppression or malfeasance. The CSRC has historically made these incursions via two distinct methods: (i) the filling-in of substantive corporate law doctrines which still have to be enforced by a state actor, whether the judiciary or a regulator (*e.g.*, corporate fiduciary duties); and (ii) the establishment of "self-enforcing" mechanisms designed to be effective as between the parties to a firm before the state or any external actor needs to be involved in enforcement, if at all (*e.g.*, minority shareholder "class" negative veto rights). These interventions include, *inter alia*:

- Corporate fiduciary duties for orthodox fiduciaries and even controlling shareholders, in both the operational and takeover contexts;
- Super-majority approval/negative veto mechanisms empowering so-called "public shareholders";
- Super-majority approval (and/or controlling shareholder recusal), and super-majority director approval (and/or director recusal) for controlling shareholder related party transactions and self-dealing;
- Independent directors; and
- Broad shareholder "class" negative veto rights (even when shareholder "classes" were prohibited).[2]

I should emphasize that the "self-enforcing" *genus* of regulatory intervention, which can be effective without recourse to enforcement by any external institution, is far more likely to be effective given the structure of China's political economy. For example, if there is concern about the political and economic power of the PRC party state's controlling shareholders, or doubts about the competence, autonomy and independence of the Chinese judiciary, the implantation of substantive corporate fiduciary duties for

[2] *Id*.at 677-84.

orthodox fiduciaries or controlling shareholders into China's company law is not likely to have much effect because articulation and enforcement of these norms may be frustrated by the phenomena animating the reform in the first place. Conversely, a "self-enforcing" mechanism such as the negative veto rights conferred on non-controlling shareholders for approval of related party "external" guarantees forced out of listed companies constitutes a very effective constraint for the identified abuse, especially when compared to reliance on any doctrinal fill-in, a vague and unevenly-applied duty of loyalty standard applied *ex post*. Indeed, the real "bite" and effectiveness of such self-enforcing mechanisms was seen in the run-up to the China National Offshore Oil Company ("CNOOC") bid for Unocal (where the independent directors blocked a Unocal-invited bid) and the bid by Singapore Airlines for a controlling stake in China Eastern Airlines (vetoed by a "class" vote).[3]

The Consequences of "Corporatization without Privatization"

Why has the CSRC been obligated to execute this regulatory intervention? The answer to that question lies in the PRC's two decades-old "corporatization without privatization" program and resultant "state capitalism", the commitment in Chinese corporate law to what is called "shareholder primacy", and the development of China's broader political economy.

"Corporatization" as commenced in the 1980s sought to implement a "modern enterprise system", abolish the traditional SOE as an organizational form[4] by converting SOEs into a legal form of "company" authorized and apparently governed by PRC company law -- (i) a company limited by shares ("CLS"), a joint stock company form for widely-held firms; (ii) a limited liability company ("LLC"), for a smaller and closely-knit group of investors; or (iii) a wholly state-owned sub-form of the LLC ("WSOC"), a company owned by a state agency with no shareholders' meeting and an optional board of

[3] *See* Nicholas C. Howson, *China's Acquisitions Abroad – Global Ambitions, Domestic Effects*, 48 LAW QUADRANGLE NOTES 73 (2006) (regarding the CNOOC directors' vote initially blocking the proposed CNOOC bid) and Barry Naughton, *SASAC and Rising Corporate Power in China*, 24 CHINA LEADERSHIP MONITOR 1 (2007) (regarding the veto rendered by China Eastern's "H" shareholders).

[4] The SOE was not given a *legal* form until 1988 and the promulgation of a "law" governing SOEs, concurrent, ironically, with elimination of the SOE organizational form.

directors --, and create and empower a new class of property rights owners in the PRC, equity shareholders.

Critically, that process of "corporatization" did not implicate "privatization" of the Chinese economy generally or SOEs individually, or any real withdrawal from the economy of the state or the Communist Party. This is because a controlling equity interest in the SOE/state-owned asset groups converted into a company went to or was maintained by state entities, and party committees remained important actors behind the formal governance structures required by the corporate form.[5] To the present day, the party state remains absolutely committed to retaining control over converted asset groups/enterprises in a very broad range of sectors – not just the usual suspects for state control (*e.g.*, defense, natural resources, key infrastructure, etc.) but also non-national security and non-key infrastructure sectors that promise high returns to central or local state or party insiders when financed with the aid of passive public investors.

Moreover, it appears that the "corporatization without privatization" program was motivated by desires very similar to those which animated late 19th century Qing dynasty attempts to engage in "state (court) capitalism" via establishment of *guandu shangban* ("government supervised/promoted-merchant operated") and later *guanshang heban* ("government merchant co-operated") entities like the China Merchant Steamships Company (*zhaoshangju*), the Jiangnan Arsenal, etc., -- attempts to re-order state-owned asset groupings into a new, "modern" and "western", form that could attract passive capital investment from the domestic and global capital markets, without ceding any real governance power over the subject businesses.[6] At least in this regard, the PRC has been fabulously successful, as "corporatized" SOEs perceived as the mainstays of China's "state capitalism" model – still absolutely controlled by the

5 *See* 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 (Martha Avery, Cai Jinqing & Zhu Min eds., 2009) (hereinafter *Nomenklatura Accountability*) (detailing how party committees operate behind, and over, boards of directors at the PRC's largest international issuers).

6 *See* Wellington K.K. Chan, MERCHANTS, MANDARINS AND MODERN ENTERPRISE IN LATE CH'ING CHINA (1977) and C.K. 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 139 (J.K. Leonard & J.R. Watts eds., 1991).

party state or state holding companies – bring off the largest IPOs in history and presently constitute the world's largest firms by market capitalization.[7]

This design for "corporatization without privatization" coupled with maintenance of central or local state (and behind them, Communist Party) control has impacted both closely-held LLC firm establishments and widely-held CLSs, with a very pronounced effect on the ownership, control, legal and governance structures applicable to the PRC's listed CLS issuers and the disempowerment of those companies' dispersed public minority shareholders: First, the strong prevalence of concentrated ownership in Chinese companies (especially listed firms) means that the key agency problem for PRC corporate governance is not *vertical* (between management insiders and a large body of disaggregated shareholders) but *horizontal* (between controlling shareholders and minority shareholders).[8] Second, the controlling shareholder and its insider appointees are not run-of-the-mill control parties/insiders, but instead are very often an identity of state or party organizations, representatives of central or local government institutions, or party *nomenklatura* appointments, giving them a heady mix of *political* and economic power, especially against disaggregated, non-politically privileged, minority shareholders. Third, the combination of a strong horizontal agency problem, and the nature of who and what the control parties are, means that China's public companies have been run as vehicles to attract passive investment from information-deprived public investors entirely in the interest of those largely unaccountable party state controlling shareholders. The same firms have therefore represented a ready invitation to opportunism, "tunneling", minority shareholder exploitation and oppression, and outright fraud by the controlling shareholders and their appointed insiders -- an invitation taken up with particular gusto at Chinese CLSs with a public float, subject to little monitoring by, or accountability to, a passive, politically disempowered and disaggregated shareholder interest and/or thoroughly compromised judicial

[7] For example, the State Grid Corporation of China (no. 7 on Fortune's 2013 Global 500), Industrial and Commercial Bank of China (no. 29), China Construction Bank (no. 50), the Agricultural Bank of China (no. 64), etc. *See* http://fortune.com/global500/.

[8] The same problem has operated across the Taiwan Straits, in the Republic of China/Taiwan, and continues to elicit similar substantive law and institutional changes. See Christopher J. Guinello, *The Revision of Taiwan's Company Law: The Struggle Toward a Shareholder-oriented Model in One Corner of East Asia*, 28 DEL. J. CORP. L. 92 (2003).

enforcement institutions.[9] Fourth, and as addressed more than a decade ago by Don Clarke, [10] this process of "corporatization without privatization" has led to a very fundamental dilemma in the design and implementation (or not) of Chinese corporate governance and the legal structure supporting it. The state continues to operate enterprises in China and exercise control in furtherance of its goals, which -- good or bad[11] -- must be understood as distinct from the presumed narrower shareholder wealth maximization goal of all other shareholders, *i.e.*, the minority shareholders. (Admittedly, the goals of the state control party and the minority shareholders may converge from time to time, in particular with respect to short-term shareholder gains; however, there is nothing in the corporatization program, or law formal and applied, which requires that the state control party exercise its control in the service of wealth maximization for *all* shareholders in the firm.) Thus, the state through its controlling shareholders in corporatized entities very openly exercises an undiluted form of what (U.S.) Delaware jurisprudence has called the "right to selfish ownership" and exploits the minority shareholders, who have no other way to benefit from their investment in the corporatized firm. As long as Chinese ideology and national industrial policy continue to sanction state shareholders controlling corporate entities where there exist any other shareholders, real protections for such other shareholders present either (i) a constraint on the state's ability to operate in a way that is the very reason the state has maintained control, or (ii) if those constraints are not to operate on state-controlled firms, then the necessity for separate corporate law regimes applicable to state-controlled corporatized firms, on one hand, and all other firms, on the other. There is no immediate prospect of a formal, separate, legal regime for state-controlled firms. Indeed, the

---

[9] *See*: Y. Cheung, L. Jing, T. Lu, R. Rau & A. Stouraitis, *Tunneling and Propping Up: An Analysis of Related Party Transactions by Chinese Listed Companies*, 17 PAC BASIN FIN. J. 372 (2009); H. Berkman, R. Cole & L. Fu, *Expropriation Through Loan Guarantees to Related Parties*, 33 J. BANK. & FIN. 141 (2009); G. Jiang, C. Lee & H. Yue, *Tunneling Through Intercorporate Loans: The China Experience*, 98 J. FIN. ECON. 1 (2010); and Nancy Huyghebaert & Lihong Wang, *Expropriation of Minority Investors in Chinese Listed Firms: The Role of Internal and External Corporate Governance Mechanisms*, 20 CORP. GOV. INT'L REV. 308 (2012).

[10] *See* Donald C. Clarke, *Corporate Governance in China: An Overview*, 14 CHINA ECON. REV. 494, 494-5 (2003) (hereinafter, *Corporate Governance in China*).

[11] The "goals" for which the state exercises its control rights can range from the assumed private interests of officials and cadres asked to represent "all of the people" of the state (much discussed in public governance literature) to various wider political or social imperatives (cross-subsidization of failing firms, full employment, etc.) which seem more benign, but still potentially operate to the detriment of external, minority, investors in a specific firm.

1994 PRC Company Law, the 2006 PRC Company Law, and the "modern enterprise system" and "corporatization" policies were all proclaimed as major steps in the opposite direction, elimination of any distinction between state firms and non-state controlled companies. Instead, the history of *non*-implementation/adjudication of China's company law with respect to public capital markets-financed and corporatized SOE issuers [12] – a neat expression of the dilemma which Mary Gallagher refers to as "authoritarian legality"[13] -- indicates resistance to the idea of any constraint on, or accountability for, the party state's ability to operate subsidiary firms in the way in which it desires, again the reason for which it maintained control in the first place.

[12] *See*, for example, Nicholas C. Howson, *Corporate Law in the Shanghai Courts, 1992-2008: Judicial Autonomy in a Contemporary Authoritarian State*, 5 E. ASIA L.REV. 303, 400-16 (2010) (hereinafter, *Corporate Law in the Shanghai Courts*), and 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 (Daniel Puchniak, Harald Baum & Michael Ewing-Chow eds., 2012) 243, 254-56, 267-69 & 275-78 (2012) (hereinafter, *Derivative Actions in the PRC*) (both noting the complete absence of widely-held or listed company governance-related shareholder company law-related suits (other than securities law claims alleging fraudulent or misleading disclosure pursuant to a very limited allowance made under pressure by the PRC Supreme People's Court) in the Chinese courts, and the partially-related hostility of the People's Courts to any cases involving a large number of parties, resulting in large parts of the PRC Company Law left unimplemented).

[13] *See* MARY GALLAGHER, AUTHORITARIAN LEGALITY: LAW, WORKERS, AND THE STATE ___ (forthcoming 2015) ("… institutionalization brings the allure of constraints and rules on others while continued state-led control over deployment of these institutions provides opportunity for discretion and flexibility… This is one of the privileges (and dilemmas) of single-party regimes. It makes the rules; it doesn't necessarily bind itself to those rules.").

Shareholder Primacy and "Enabling" Corporate Law in China -- Enabling Exploitation of Minority Shareholders by the Party State

Since 1994, China's corporate law has expressed fealty to a robust version of what scholars call a "shareholder primacy" model. Moreover, for the last decade China's company law has been made increasingly "enabling", as epitomized by the wholesale changes seen in the 2006 Company Law. Continued shareholder primacy and the increasingly "enabling" orientation of the corporate law and governance system, when coupled with the "corporatization without privatization" program, has resulted in something widely acknowledged as pernicious in China and abroad -- the open and continued exploitation of minority shareholders in Chinese firms. It is that phenomenon which has made necessary the CSRC-imposed mandatory provisions noted here.

"Shareholder primacy" refers to a model of corporate law and governance that bestows significant formal governance power on firm shareholders, as the firm's ultimate "owners", rather than the agents of those owners, the firm's directors and officers. In theory, shareholder primacy can appear well-justified because shareholders are the true owners or stakeholders in the firm residual. Moreover, in a corporate ecology characterized by widely-held firms and extensive separation of ownership and managment, where there is concern about those agents acting in their own interest and not that of all the owners (*i.e.*, the firm), any mechanism that can rein in those agents and make them accountable to the firm's owners seems advisable. Indicia of shareholder primacy include the power to elect members of the firm's centralized management body, the board of directors, oust incumbent directors mid-stream with or without cause, and vote on significant firm decisions, etc. From this view, China's modern corporate law system represents a strong version of the shareholder primacy model, for example requiring that the general shareholders' meeting approve dividend distributions.

"Enabling" corporate laws are general corporation codes which provide something like a standard form contract structured around default provisions, with very few mandatory or immutable rules working on firm participants' internal rights and obligations or the firm's external activities. In most developed capitalist jurisdictions, corporate governance at specific firms is now determined by a mixed application of some default provisions left unchanged by the participants, specific arrangements crafted *ex ante* by contracting-out of other default rules, and extremely broad common law doctrines interpreted and enforced *ex post* by a usually circumspect (and business judgment rule-constrained) judiciary as prodded by private shareholder plaintiffs (and in the U.S. their attorneys working with the benefit of contingency fee arrangements and liberal cost-sharing/class action rules). Basic theories of the corporation have developed in parallel, from the 18th and 19th century idea that firms were a creation of the state pursuant to a specific legislative act, to the 20th century "contractarian" conception of the company as a creation of private contract. For many analysts, it is the enabling, standard form contract- and default rule-providing – and *non*-mandatory – character of corporate law that both defines and recommends it. Indeed, in the Anglo-American legal system capitalist economies there is a bedrock confidence that capital accumulates (*i.e.*, it is invested by private parties), and will be efficiently allocated to useful projects, through an infinite variety of complex and individualized arrangements regarding entity governance and investor rights, which arrangements are in turn determined by different levels of information-availability, the value brought to the table by specific investors, and many other factors. Said another way, there is a strong belief in the developed world, capitalist, nations that any attempt to significantly pattern or constrain those arrangements (and beyond what the public interest or basic accountability absolutely requires) will impede realization of the best, privately-negotiated, arrangements, and thus fatally dampen capital formation.[14]

In 1993-4 the Chinese Communist Party-led government began its experiment with company law-making decidedly in the "mandatory" and not the "enabling" mode.[15] Indeed, that orientation was but a

---

[14] *See*, for example, Frank H. Easterbrook, *The Race for the Bottom in Corporate Governance*, 95 VA. L. REV. 685, 688 (2009) ("Corporate law came to be enabling rather than directory in the United States because that serves investors' interests, not because it serves managers' interest. States that adopt inefficient regulation propel capital out of their jurisdictions.")

[15] *See* Corporate Governance in China, *supra* note 10, at 496, 500 ("…and the [1994] Company Law is thus clearly more concerned with regulating and suppressing than with fostering and nurturing."… "The policy choice in the current [1994] Company Law is clear; the rules are almost uniformly mandatory.")

continuation of China's earliest, from the late Qing to1949, identities of corporate law specifically,[16] and law (as "rule *by* law") generally.[17] All of that in turn is consistent with the Chinese state's (and before that, the imperial Chinese court's) desire to control or monitor very closely potentially independent capital accumulation and business activity, and benefit from it. [18] At the same time, China's first post-1949 corporate law held high the banner of shareholder primacy, putting significant formal power into the hands of shareholders over directors, officers or supervisors. Without any doubt, this was deemed permissible to PRC policy makers and legislators, and the promoters of what became "state capitalism", because of the distinctive capital structure of corporatized SOEs described above -- featuring a large, party state-tied, controlling shareholder given full power to dominate the subsidiary firm directly as a shareholder or via a board of directors elected entirely by it also acting as a shareholder.

Only with the passage of the 2006 PRC Company Law did the PRC move away from a business regulation philosophy and in a new direction: towards an enabling statute which allows for increased contracting-out of default rules *ex ante* alongside continuing self-enforcing mechanisms, and which creates very significant work for the judiciary applying standards *ex post*. In fact, this development in the direction of a formally enabling corporate law system and away from a directive, business regulation, orientation, has been celebrated widely in the PRC among academics and People's Court officials alike. For example, a 2007 commentary by the Shanghai Higher People's Court (regarding a 2003 case where the Shanghai No. 1 Intermediate People's Court had to choose between *statutory* rights of first refusal due

16 *See* William C. Kirby, *China Unincorporated: Company law and Business Enterprise in Twentieth-Century China*, 54 J. ASIAN STUD. 43 (1995).

17 *See* Liang Zhiping, *Explicating "Law": A Comparative Perspective of Chinese and Western legal Culture*, 3 COLUM. J. CHINESE L. 55, 61, 89 (1989) .

18 *See* Chan, *supra* note 6; Kirby, *supra* note 16, at 44 ("The history of this first modern Chinese law [company law] is to some degree a barometer of the state's assumptions towards the economy over the course of the twentieth century…. [T]he Chinese state would be the prime beneficiary of the adoption of the corporate form of business activity. But the first assumption of the [early twentieth century] Qing reformers, that the modern corporation on a Western model would be the essential vehicle for *private* Chinese economic development, would prove quite mistaken."); and Madeleine Zelin, *The Firm in Early Modern China*, 71 J. ECON. BEHAVIOR & ORG. 623 (2009).

to existing shareholders and the rights of a good faith purchaser under a fraudulently-approved securities purchase *contract*) appears to channel Frank Easterbrook[19] directly:

> First and foremost, the thing we must clarify is this: the jurisprudential logic underlying the giving of priority to the [right of first refusal] over the purchase rights of the transferee is absolutely not because the former right is in statute and the latter is merely a contractual right. This is because statutory rights are not always superior to contractual rights – in fact, it is just the opposite. Approaching it systematically and *adhering to the orientation which protects private ordering, regulation of the market requires that application of the law fully respect the freedom to contract to encourage successful transactions*…. There is significant meaning in this.[20]

Yet, even as China's corporate law and the rhetoric surrounding it moved in one direction, the mandatory norms imposed by the CSRC and other agencies before 2006, and the absorption of many of those originally regulatory and shareholder-primacy countering mandates into the 2006 PRC Company Law,[21] have pushed the applied law of corporate governance in precisely the opposite direction.[22]

---

19 *Supra* note 14.

20 Commentary regarding the case reported as "A Investment Company v. Wang and Other Shareholders", (Shanghai No. 1 Intermediate People's Court, on appeal 2003), in 2005 NIAN SHANGHAI FAYUAN ANLI JINGXUAN [2005 SELECTION OF SHANGHAI COURT CASES] 106-109 (Shanghai Higher People's Court ed. 2007); with the quoted portion of the commentary *id.* at 111 (emphasis added).

21 *See*, for example, 2006 PRC Company Law, arts. 20 (fiduciary duties for controlling shareholders and an oppression remedy), 106 (cumulative voting, formally enabling but made mandatory by CSRC regulation and approval practice), 16 & 122 (cap on external guarantees, recusal of controlling shareholders on shareholder votes for such guarantees, and a supermajority vote for any such guaranty greater in value than 30% of corporate assets, or a majority of non-control shareholders; supermajority shareholder vote on disposition of significant assets), 123 (independent directors), 125 (recusal of conflicted directors), and 127 (allowance for different classes of shares and preferred shares), and 148 (fiduciary duties for orthodox corporate fiduciaries).

22 Interestingly, my own research has shown how the Chinese People's Courts – contrary to some expectations and certainly the doctrinal rhetoric quoted from the A. Investment Company v. Wang case commentary above -- have mimicked this trajectory, adjudicating some enabling provisions of the 1994 and 2006 PRC Company Laws as mandatory. *See* Corporate Law in the Shanghai Courts, *supra* note 12, at 382-3 ("'Conservative' Adjudication – iii. Enabling to Mandatory").

Regulatory Intervention – Structural Exploitation, Legislative Competence and Independence, and the Judiciary

The pernicious implications of the "corporatization without privatization" program, coupled with an ever more controlling shareholder-empowering and enabling corporate law, make the reasons for the CSRC's counter-strike obvious. Given lopsided capital structures and thoroughly dominated directorates and shareholders' meetings, not to mention the unconstrained political and economic power of state controlling shareholders (and their appointed insiders) and a radical information asymmetry between such controlling shareholders and diffuse public investors, an "enabling" company law design built on strong notions of shareholder primacy has been a broad invitation for dominant shareholders to oppress and exploit far weaker actors in the firm, especially where minority shareholders have very little power to bargain for information or effective protections, or obtain any price discount to compensate for their disadvantageous position. Therefore, mandatory provisions – from whatever source -- designed to protect the basic informational and governance rights of minority capital providers against such control parties were required.

Observers might respond that the remedy to this baked-in exploitation of minority property rights holders should have been available from either the legislator or the court system. Certainly there was an effort to create or make more effective legal remedies for minority shareholders against politically powerful firm insiders and controlling shareholders via wholesale reformation in 2005-6 of the defective 1994 PRC Company, with the concretization of CSRC regulatory mandates[23] and the addition of substantive claims (*e.g.*, duty of care, controlling shareholders' fiduciary duties, piercing of the corporate veil, etc.) and procedural innovations (*e.g.*, a derivative action, the ability of shareholders to call special shareholders' meetings, etc.) However, China's developing legal system and the institutional *status quo ante* made clear that substantive legal change would not be enough, because of at least three additional factors: First, there have been and remain serious issues pertaining to the technical competence of PRC legislators at the National People's Congress, especially with respect to complex areas like corporate law

[23] *See*, *supra* note 21.

and securities regulation. Moreover, it is apparent that China's national law-making institutions may lack objectivity, at least insofar as their legislative product conflicts with the interests of the party state's SOE systems.[24] Second, while the situation is better than some observers surmise, there must be continuing doubts about the competence, autonomy and political independence of PRC judicial institutions called upon to implement, *ex post*, corporate law standards, accountability, or remedies.[25] Said another way, even if state-of-the-art substantive provisions and procedural mechanisms are introduced into PRC company law – as they assuredly were in November 2005 with promulgation of the final 2006 PRC Company Law -- there is a continuing concern as to whether the PRC People's Courts will be competent and powerful enough to utilize, adjudicate, and enforce such law with respect to any kind of PRC corporation, LLC, CLS or WSOC, much less accept or be permitted to accept disputes concerning the same.[26] Third, is one result of the basic dilemma in China's corporate governance project described above and a hallmark of Mary Gallagher's "authoritarian legality", the almost complete *non-*

---

[24] *See*, for example, Xi Chao, *Piercing the Corporate Veil in China – How Did We Get There?*, 5 J. BUS. L. 413, 423-7 (2011) (describing the role of State-owned Assets Supervision and Administration Commission ("SASAC") in sabotaging the CSRC's more permissive statutory veil-piercing standard originally set forth in the Company Law Amendment's Consultation Draft, due to SASAC concern that the more liberal doctrine would also be applied to unlisted corporatized SOEs).

[25] *See*, for example, Corporate Law in the Shanghai Courts, *supra* note __ (corporate law adjudication in the Shanghai Higher People's Court system between 1992 and 2008); Wang Jun, *Gongsi Jingyinzhe Zhongshi He Qinmian Yiwu Susong Yanjiu – Yi 14 Sheng, Zhixiashi De 137 Jian Panjueshu Wei Yangben* [Analysis of Litigation Regarding Company Management's Duties of Loyalty and Care – Using 137 Judgment Opinions from 14 Provinces and Directly Administered Municipalities], 5 BEIFANG FAXUE [NORTHERN JURISPRUDENCE] 24 (2011) (corporate fiduciary litigation nationwide); Derivative Actions in the PRC, *supra* note __ (the corporate derivative action); and Hui Huang, *Piercing the Corporate Veil in China: Where is it Now and Where is It Headed?*, 60 AM. J. COMP. L. 743 (2012) (corporate veil piercing).

[26] I should note in passing that the PRC judicial *bureaucracy – i.e.*, not courts issuing opinions on adjudicated cases -- has played some role in implanting substantive corporate law doctrine and procedural innovations into China's corporate law and governance system. Before 2005, this was done via the creation by individual (Provincial/Directly-Administered Municipality) Higher Level People's Court systems of "opinions" on issues presented in litigation concerning the woefully deficient 1994 PRC Company Law. Notable Higher People's Court opinions on corporate law came from Jiangsu (2003), Shanghai (2003), and Beijing (2004). Importantly, none of these local court system opinions attempted to institute self-enforcing governance mechanisms like supermajority negative veto rights, etc. in the style the CSRC has for public companies. After the effectiveness of the 2006 PRC Company Law, the Supreme People's Court has released three judicial "regulations" concerning the company statute, and has embarked on a "Guiding Cases" project, none of which, however, remake corporate governance norms in the same fashion as the CSRC regulation described here. To date, only one of such Guiding Cases has involved corporate governance matters, "Guiding Case No. 10" (Li Jianjun v. Shanghai Jiapower Environmental Protection Science & Technology Co., Ltd. (Final Version, Nov. 9, 2012)) *available at* http://cgc.law.stanford.edu/wp-content/uploads/2013/04/CGCP-Chinese-Guiding-Case-10.pdf (shareholder challenge to a board resolution).

implementation of China's company law for minority shareholder plaintiffs in public capital markets-financed corporatized issuers, arising from the system's denial of any constraint on the state's ability to operate public-invested investee firms in the way in which it desires, the reason for which it maintained control in the first place.

The CSRC – A Conflicted Actor

From an institutional standpoint then, the above-described factors worked together to leave the CSRC as one of the only state institutions in China capable of: (i) expert drafting of substantive provisions, in particular of the "self-enforcing" type; (ii) technical resistance against controlling state shareholders (and the political economic systems backing them); and (iii) substitution for another state institution, an inexpert, overly bureaucratic, or politically-cowed judiciary, at least with respect to PRC companies explicitly under the CSRC's jurisdiction: firms issuing publicly-traded securities.[27]

Importantly, I do not mean to assert in this chapter that the CSRC is entirely, or even mostly, a "good actor" under the Chinese party state's model of state capitalism, or that it uniformly acts to constrain the power of PRC SOE party state controlling shareholder groups. Chen Ruoying's eloquent lament in this book regarding the low quality human capital trap created by "state capitalism" -- including specifically the CSRC with respect to regulatory elaboration related to IPO approvals[28] --, developing empirical work in the PRC showing how the CSRC evidences considerable bias in favor of central government-owned listed SOEs,[29] abundant anecdotal evidence regarding corrupt and opaque listing approvals, seemingly automatic waivers granted to major party state shareholders from the mandatory offer rule under the CSRC's own Listed Company Acquisition Rules and the like, and my own work on illegal and *ultra vires* enforcement by the CSRC against insider trading,[30] all make identification of the

[27] Note that from January 1, 2013, the CSRC asserted expanded jurisdiction beyond domestically or overseas exchange-listed companies to include CLSs with more than 200 shareholders, and CLSs which have issued securities "to the general public" or "in a public manner", an elaboration of regulatory power very likely to gain a statutory basis in the revised PRC Securities Law. *See* Battle Against Party State Power, *supra* note __, at 713.

[28] *See* Chen Ruoying, *State Monopoly and Human Capital Development*, *in* CHINESE STATE CAPITALISM AND INSTITUTIONAL CHANGE: DOMESTIC AND GLOBAL IMPLICATIONS (Benjamin L. Liebman and Curtis J. Milhaupt eds.., 2015) .

[29] *See*, for example, China University of Politics and Law's Zhou Tianshu's: *Is the CSRC Protecting a "Level Playing Field" in China's Capital Markets: Public Enforcement, Fragmented Authoritarianism and Corporatism*, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2505568.

[30] *See* Nicholas Calcina Howson, *Enforcement Without Foundation? – Insider Trading and China's Administrative Law Crisis*, 60 AM. J. COMP. L. 955 (Fall 2012) (critiquing the CSRC as acting illegally with respect to the enforcement of insider trading prohibitions, a critique acknowledged as valid with issuance of a responsive joint explanation by the PRC Supreme People's Court and the PRC Supreme People's Procuratorate ("SPP") drawing such illegal enforcement back within the bounds of legality, at least in criminal prosecutions by the SPP.)

CSRC and its human agents as the saviors of the PRC capital markets, or immune from agency capture, highly implausible.

Instead, I would note that the CSRC can be a “bad actor” in its day to day gatekeeper, approval and enforcement roles, while still being the “good actor” source of longer-term, highly sophisticated (and thus relatively opaque) pre-enforcement or legal constraints on the power of state capitalism’s control groups analyzed in this chapter.

"How" Have the CSRC and Other Agencies Been Permitted to Push Back, and What Does It Mean for China's "State Capitalism" Model?

In the preceding sections of this chapter I have reviewed some of the reasons *why* the CSRC and other agencies have intervened to constrain or hold more accountable party state-rooted controlling shareholders in the paradigmatic firm operating under "state capitalism".

If I was to speculate further on a separate *why* question -- the reasons for the dichotomy of action by the CSRC alluded to immediately above (*i.e.*, "bad" corrupt, captured, agency with increasingly degraded human capital doling out listing approvals and mandatory offer waivers to favored party state control groups vs. creator and enforcer of sophisticated pre-enforcement constraints blocking the same groups) -- there is little doubt regarding the significance of input from foreign capital markets regulators and academics (often delivered via foreign-educated officials or academics active inside the PRC), and the basic competitiveness of the increasingly integrated international capital markets requiring such mechanisms to allow Chinese issuers to attract capital.

The far more intriguing question is *how* the CSRC has been permitted to erect and enforce effective constraints on the power of China's party state-tied controlling shareholders. While the PRC party state is not the homogeneity many popular accounts perceive, it does seem startling that there is any allowance for an agency that is embedded in the same party state (with no economic and little independent political power) to conceive and implement mechanisms which limit the power of, or seek to hold accountable, politically far better-endowed actors – SOEs and their controlling shareholders and the sprawling systems of political economic power they spring from.

In starting to answer these questions, I should note up front that there are several areas I do not speculate upon in this chapter. First, here I do not address the more traditional political scientist's inquiry: the sources of the CSRC's concrete power over more than two decades. Thus, for example, I do not seek to answer the following questions: What rank does the CSRC have in the state bureaucracy (and its party organ in the parallel party system)? What, or whose, patronage network does the CSRC lie in? What individual or groups of leaders have empowered the CSRC at different times in its development?

What resources are the CSRC able to attract, and conversely what resources does it control? Is the CSRC able to resist agency capture, and how? While the development of the CSRC as an institution of the PRC party state is a rich area for continued research, the answers to these questions will vary greatly over time, given the power (and power bases) of different individuals (*e.g.*, compare Zhou Xiaochuan and Shang Fulin), and the development of the PRC capital markets and their engagement with global capital markets, and that variance may in turn obscure larger structural features which explain what the CSRC is doing. Instead, I address the CSRC's normative power in trying to explain the phenomenon identified in this chapter and its relationship with "state capitalism" as practiced in the PRC.

Second, although what I describe in this chapter may appear to be a very specific and technical aspect of the established PRC "fragmented authoritarianism" narrative,[31] I think it is different. The traditional "fragmented authoritarianism" account focuses on how vertical (from center to locality) *governmental* and *bureaucratic* systems battle across *horizontal* lines (within a given geographic area), and uniformly with respect to *governmental policy or approvals*. This chapter addresses something distinct, and a phenomenon directly tied to the rise of "state capitalism": an admittedly *horizontal* contest between a central government agency creating *pre-enforcement* mechanisms and *ex post*-applied doctrines which systemically constrain the economic and directorial power of a supremely powerful, *non-governmental, non-regulatory*, constituency – SOE groups and the controlling shareholders they produce. It goes without saying that this new kind of "fragmentation" of the purportedly authoritarian party state is the inevitable result of the "state capitalism" model, where units endowed with both political and economic power are ranged against other units with merely political-governmental/administrative power.

[31] *See* Kenneth Lieberthal & Michel Oksenberg, POLICY MAKING IN CHINA: LEADERS, STRUCTURES AND PROCESSES 3-34 (1988); Kenneth Lieberthal, *Introduction: The "Fragmented Authoritarianism" Model and Its Limitations*, *in* BUREAUCRACY, POLITICS AND DECISION MAKING IN POST-MAO CHINA 1-32 (Kenneth Lieberthal & David M. Lampton eds., 1992); and Kenneth Lieberthal, GOVERNING CHINA – FROM REVOLUTION THROUGH REFORM 186-88 (2004). Political Scientist Andrew C. Mertha has also written more recently on this aspect of PRC governance. *See*: Andrew C. Mertha, *"Fragmented Authoritarianism 2.0": Political Pluralization of the Chinese Policy Process*, 200 THE CHINA QUARTERLY 1 (December 2009); and Andrew C. Mertha, *Policy Enforcement Markets – How Bureaucratic Redundancy Contributes to Effective Intellectual Property Implementation in China*, 38 COMPARATIVE POLITICS 295 (April 2006). However, all of these studies focus on horizontal competition (or, in Professor Mertha's case, redundancy in enforcement) between vertically-arranged *governmental and bureaucratic* actors, and usually with respect to specific policy decisions or approvals.

My speculations on the *how* question focus on the CSRC's normative power against corporatized SOEs, their control groups, and the systems which support them, and finally the extent to which the expression of that normative power is necessary for the flourishing of "state capitalism" in contemporary China. In the following paragraphs, I speculate on what may be at work, and from four different standpoints: (i) what it is about the CSRC, as a new kind of government unit in China, that empowers it to act in this fashion; (ii) what might cause powerful controlling shareholder groups to allow the CSRC this provocative space for maneuver; (iii) the ways in which the human agents who are appointed by the party state to run corporatized SOEs might welcome such constraints; and (iv) reasons why the "state capitalism" model might require both the expression and enforcement of the constraints identified here to finance itself in a sustained manner.

The CSRC as New Kind of PRC Party State Agency

The CSRC was the first agency and subsequently ministry-level body in the PRC's history with jurisdiction over an area that is not a specific *industrial sector*, but a *market activity* in an increasingly market economy. Thus, just as, for example, the Ministry of Textile Industry once governed the PRC's entire textile industry and its productive SOEs, the CSRC can be seen – and more importantly, sees itself -- as China's "Ministry of Capital Markets", a regulator certainly, but also a government department charged with maintaining the operation, integrity and attractiveness of China's domestic capital markets. This sense of ownership of the capital markets, and bureaucratic investment in the success of the sector/activity it governs, contributes to the CSRC's concrete moves to resist the power of even politically well-endowed SOEs and their supporting systems (coupled with affirmative regulation of the issuers, funds, brokers, underwriters and accountants it is charged with oversight of). In addition, and notwithstanding the strengthening of its regional offices, the CSRC is very much an organ of the national, central, government, and therefore an organ of the party state which is not tied to or reliant upon any given industrial or manufacturing sector, or any geographic region. While most large SOE systems have their origin in some kind of central authority (usually a former ministry metamorphosed into a group holding company), their admittedly robust political and economic interest eventually becomes narrowed into a specific sector (*e.g.*, telecoms, power generation, downstream oil and gas and petrochemicals, etc.) and a part of that specific sector (as part of a duopoly or tri-opoly, etc.), and then often into a region.[32] Here, think of how CNOOC, China National Petroleum Corporation ("CNPC") and Sinopec have their origins at the national level, but have since been directed into specific sectors (upstream exploration, development and production (onshore vs. offshore) vs. downstream oil and gas and petrochemicals) and in specific geographical areas in China. The same might be observed for the corporatized offspring of the former PRC Ministry of Post and Telecommunications, China Telecom, China Mobile and the later mobile phone era but centrally-promoted new entrant China Unicom. Thus, while observers may understand the corporatized SOE systems of China's "state capitalism" as all-powerful, and rooted in the "center", the breadth of their power is actually narrower than that of a purely central, sectorally all-encompassing or non-specific, organ like the CSRC.

Party State Controlling Shareholders

From the standpoint of the PRC party state's political economic behemoths, corporatized SOE systems and their control groups, the CSRC pushback described in this chapter may be perceived as harmlessly expressive, understood *ex ante* by such powerful forces to be without effect or risk of real enforcement, or to take an idiom from 19th century Brazil, "*para inglês ver*" ("for English eyes")?[33] This view might explain the long-standing allowance for the CSRC's mandatory constraint mechanisms, especially if they are understood as intended merely to be expressive for either foreign investors or a domestic capital markets audience, or for the foreign audience coupled with symbolic enforcement for them only, in each case as comfort for public investors given the open exploitation of minority shareholders under the "corporatization without privatization" program. If this were true, the control groups which occupy the heights of China's "state capitalism" might be quite content to allow such

[32] *See*, generally, Li-Wen Lin & Curtis J. Milhaupt, *We are the (National) Champions: Understanding the Mechanisms of State Capitalism in China*, 65 STAN. L.REV. 697, 704-33 (2013).

[33] Under pressure from the anti-slave trade British Parliament, in 1831 Brazil promulgated a law declaring free all slaves trafficked to Brazilian ports. As was intended, the law went largely unenforced, as slaves continued to arrive at Brazilian ports and be sold, and so the law was "for English eyes" or "for appearances only", known ahead of time as a norm that would not be enforced and for external consumption only.

mechanisms, secure in the knowledge that they will not generally be enforced or provide any real obstacles to their power and discretion with respect to dominated subsidiaries. In my view, this explanation does not possess real force, however, precisely because many of the CSRC-initiated mechanisms have nothing to do with overseas listing issuers (and thus no effect on "English [now American] eyes") and work purely with respect to domestically-listed issuers. Moreover, while the "for English eyes" answer might fit for some of the doctrinal gap-filling that the CSRC has pursued over the years – *e.g.*, fiduciary duties for, and anti-oppression remedies against, controlling shareholders which are never subject to adjudication because they involve large plaintiff groups – it does not account for the self-enforcing *genus* of constraints, such as supermajority shareholder or board votes after recusal of related parties, which are respected and implemented at China's largest firms, and where there is ample evidence of concrete application of the mandatory constraints described in this chapter. And, of course, there is no guaranty that even some of the non-"self-enforcing" constraints introduced into the governance mix for China's "state capitalism" powers might not increasingly gain traction over time. A perhaps more nuanced version of this view is that these mechanisms – the self-enforcing type in particular – are understood immediately by the SOE control groups as being more than merely expressive, and known to be subject to implementation in fact, but that the prospect of implementation spurred by private claimants is nonetheless largely discounted by the most powerful controlling shareholders of corporatized SOEs because of familiar collective action, information deficit and passivity problems for the great mass of public (minority) shareholders.

Party Nomenklatura Appointees to State Controlled Firms

It is now well-established that many of the human agents of party state control at the largest corporatized SOEs are party officials embedded in the Chinese Communist Party's personnel appointments or *nomenklatura* system who seek advancement in reform-era China through both governmental and enterprise appointments, and rotate easily through both spheres. Thus, the nominal CEOs (but more importantly ranking party officials) at direct competitors China Mobile and China Unicom may switch jobs, the CEO of Sinopec may leave that corporate position to take up the post of governor of a major coastal province, or the head of one of the major state-owned commercial banks may become the Governor of the PRC's central bank, or indeed the Chairman of the CSRC. When such appointment rotations result in members of the *nomenklatura* being charged with direction of a large corporatized SOE that is a key instrument of the PRC's "state capitalism", it may be critical for that individual's further advancement that the SOE assets or the firm they are tasked with operating are successful in business terms, but also do not attract public opprobrium, shareholder dissension, or negative press attention, domestically or abroad.[34] It is therefore not absurd to think that these individuals might counter-intuitively welcome constraints on their power (and indirectly the power of the party state which brought them to the firm) to protect themselves against having to direct, for example, inefficient or unprofitable related party transactions, or at least allow them the safety of prior super-majority, interested party-recused, approvals.[35] Flat constraints may allow them to avoid risky, possibly pressurized decisions entirely; adherence to mandatory procedures for super-majority approvals and the like may provide for some measure of *ex post* protection for transactions that go sour.

The Financing of "State Capitalism"

Finally, and perhaps most importantly, the governance constraints visited on the control parties of China's "state capitalism" addressed in this chapter may be welcomed or at least tolerated by corporatized SOE systems and the controlling shareholders they have spawned as the (small) price of continued access to financing in the domestic and global capital markets. Said another way, formal constraints on controlling shareholder governance power within a specific listed firm may be the price that has to be paid for the appearance of functioning, apparently level-playing field, and investment-attracting, capital markets, something even the heights of China's "state capitalist" ecology desperately needs to continue serving its corporate finance needs. It may be difficult to prove this idea to the satisfaction of the law and finance fraternity, as it is exceedingly unlikely that the CSRC-origin mandatory constraints on state

[34] *See* Nomenklatura Accountability, *supra* note 5.

[35] I am grateful to my former University of Michigan colleague Professor Zhao Minyuan for this insight.

controlling shareholder power will be removed or weakened,[36] and thus there will be no chance for an event study that tracks the pricing of PRC issuers before and after such change. We do know, however, that many of the CSRC-implemented mandatory rules – like the December 2004 "Regulations Regarding Strengthening Protection of the Rights and Interests of Public Shareholders" which defined public equity shareholders other than controlling shareholders (holding listed or unlisted stock) as a kind of class and conferred upon that class negative veto rights regarding a broad range of important decisions[37] – were issued by the CSRC in direct response to rumblings in the domestic investor population and increasingly autonomous PRC financial press. And while this notion may seem unlikely in the Chinese, or any, context, it is precisely the dynamic at work in India more than a decade ago, where in 2001 the Indian securities regulator implemented the Sarbanes-Oxley ("SOX")-like (but pre-SOX) "Clause 49" reforms (added to stock exchange listing requirements) based upon the recommendations of the 1999 Kumarmangalam Birla Committee, which recommendations in turn were based upon a voluntary 1998 Corporate Governance Code devised by none other than the Confederation of Indian Industry ("CII"). The CII is an organization made up of, and representing the interests of, India's largest public firms.[38] Finally, this proposed rationale for acceptance of significant constraints on state controlling shareholders aligns perfectly with what I assert is the original policy rationale for the "corporatization without privatization" process itself – the re-ordering of SOE asset groupings into a new legal form that could attract passive capital investment from the domestic and global capital markets.

[36] Quite the opposite in fact – the author has reviewed a draft, revised, PRC Securities Law distributed inside China, and its provisions incorporate all of the CSRC-origin mandatory rules described here, and provides for new and more robust constraints (and mandatory disclosure).

[37] See Battle Against Party State Power, *supra* note 1, at 680-1.

[38] *See* Bernard S. Black & Vikramaditya Khanna, *Can Corporate Governance Reforms Increase Firm Value? Event Study Evidence from India*, 4 J. EMPIRICAL LEGAL STUD. 749, 759 (2007) ("Corporate governance reform efforts in India were largely triggered by CII's promulgation of its Corporate Governance Code in 1998. CII then followed up by lobbying SEBI to implement mandatory reforms – presumably consistent with the CII Code…. Much like the Business Roundtable in the United States, major Indian firms were the interest group most likely to oppose governance reform. Instead, however, CII *initiated* the reform effort.")

Conclusion

In this chapter I have reviewed two distinct, and often opposing, projects of the PRC party state with respect to "corporatized" SOE groups -- the undisputed engines of China's domestic and global economic activity under "state capitalism". On the one hand, we can understand the Chinese party state as a multi-faceted and over-bearing economic actor spawning a parade of politically well-endowed controlling shareholders uniquely positioned to dominate subsidiary corporations established as passive vehicles to receive public capital markets financing, and in their own interest. On the other hand, the same PRC party state has also established a partially publicly-interested securities markets regulator with the undisputed power to regulate the internal corporate governance arrangements for such dominated subsidiary corporations, which regulator has established sophisticated mechanisms of resistance against the control parties of "state capitalism" with gusto.

From a legal systems perspective, this understanding of two opposing prongs of the PRC party state should help us to comprehend better the CSRC's serial mandatory-type regulatory incursions into the province of mostly enabling legal corporate governance norms. For, in the PRC's "corporatization without privatization" program in the embrace of a shareholder primacy model of corporate law, we are confronted with a notional and mostly rhetorical "retreat" from the economy of the party state "under law" (the enabling-oriented Company Law specifically), a retreat which in fact cloaks the reassertion or maintenance of concentrated power (the state metamorphosed into a politically privileged controlling shareholder), all in a context of "authoritarian legality" where the control parties can ensure that formally-conferred "legal" protections for the exploited minority are not utilized (*i.e.*, the absence of listed company corporate governance cases in the Chinese courts, and blocks against multi-party actions of any kind).

The only effective remedy for this baked-in deprivation of limited governance participation and minority owner oppression embodied in the structurally-determined exploitation of minority shareholders, and the inability of the system to apply and enforce whatever "legal" protections are on offer, is state intervention of another sort: the injection by a competing party state institution into enabling corporate law of immutable substantive doctrines and mandatory corporate governance mechanisms – and best "self-enforcing" mechanisms so that the party state rule maker cannot escape being bound by their own rules -- designed to protect those who will suffer such deprivations, and constrain the awesome powers vested in the continuing control parties. That is precisely the path pursued by the CSRC and other bureaucratic actors over the last several decades.

From the distinct perspective of understanding how the PRC party state operates in the context of "state capitalism", we may query how a bureaucratic agency like the CSRC has been permitted this counter-strike against the focal point of party state political economic power. In this regard, we must remind ourselves of a central idea behind the twenty-year-old PRC "corporatization" program, itself a direct echo of China's 19th century imperial fetish for the corporate form – repackaging SOEs and SOE asset groupings into a legal entity that can attract large scale public investment with only minor disruption of incumbent governance arrangements. That major underlying policy driver for the "corporatization" program from inception aligns well with one explanation for how the CSRC and other bureaucracies have been permitted to impose constraints on the power and discretion of dominant state-tied controlling shareholders of China's listed companies. Those constraints imposed by administrative regulation, in theory and as applied, only make corporatized SOEs more competitive as they seek financing from domestic and global capital markets, and thereby help ensure continued access by the very same vehicles of China's "state capitalism" to abundant, relatively passive, capital, with the desired minimal disruption of incumbent governance arrangements. Said another way, these effective governance constraints and accountability mechanisms imposed on PRC party state controlling shareholders in listed firms may be one of the most critical long term elements enhancing the party state's ability to finance "state capitalism" on the domestic and global capital markets. More than merely protecting the state from itself, these mechanisms are necessary for the Chinese party state's continued ability to finance its involvement in the capital intensive sectors of the PRC and global economies.