Institutional Investors in China: Corporate Governance and Policy Channeling in the Market Within the State

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Abstract

The extraordinary rise of China's economy has made understanding Chinese corporate governance an issue of global importance. A rich literature has developed analyzing the Chinese Communist Party's (CCP's) role as China's largest controlling shareholder and the impact that this has on Chinese corporate governance. However, the CCP's role as the architect – and direct and indirect controller – of institutional investors in China has been largely overlooked in the comparative corporate law literature.

This Article aims to take the first step in filling this gap in the literature by drawing on Chinese sources and fresh hand-collected empirical, interview, and case study evidence to analyze the meteoric rise of institutional investors in China. It provides a taxonomy of institutional investors in China and reveals how as the market for institutional investors has grown it has become increasingly "atomized" as different types of institutional investors have proliferated. The Article reveals how the CCP has actively and gradually promoted the growth of domestic institutional investors, in terms of types and size, through relaxation of policies and law reforms to improve corporate governance and stabilize the stock market, while limiting the influence of foreign institutional investors. It further analyzes all the Activist Campaigns undertaken by institutional investors in China and maps the network of government bodies, regulations, and tactics that the CCP has developed to directly and indirectly control State-Owned Institutional Investors (SOIIs) and Private-Owned Institutional Investors (POIIs) for the purpose of policy channeling.

This Article concludes by taking a step back and briefly considering what this examination of institutional investors tells us about China's unique form of capitalism and system of corporate governance. It suggests that the rise of institutional investors in China has been strategically developed in a way to reinforce the CCP's ultimate control over the financial system. However, contrary to what some conceptions of "state capitalism" may suggest, the CCP does not micro-manage institutional investors on a day-to-day basis. Rather, institutional investors normally function according to free-market forces and increasingly perform an important corporate governance role – with the CCP using its policy channeling in a targeted way to stabilize the market in times of crisis, execute important legal and market reforms, and to maintain calm in society during critical political events: what this Article coin's the "market within the state" for institutional investors in China.

Keywords: Chinese Corporate Governance, Institutional Investors, Comparative Corporate Governance, Chinese Communist Party, Varieties of Capitalism

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ABSTRACT

The extraordinary rise of China's economy has made understanding Chinese corporate governance an issue of global importance. A rich literature has developed analyzing the Chinese Communist Party's (CCP's) role as China's largest controlling shareholder and the impact that this has on Chinese corporate governance. However, the CCP's role as the architect – and direct and indirect controller – of institutional investors in China has been largely overlooked in the legal literature.

This Article aims to take the first step in filling this gap in the literature by drawing on Chinese sources and fresh hand-collected empirical, interview, and case study evidence to analyze the meteoric rise of institutional investors in China. It provides a taxonomy of institutional investors in China and reveals how as the market for institutional investors has grown it has become increasingly "atomized" as different types of institutional investors have proliferated. The Article reveals how the CCP has actively and gradually promoted the growth of domestic institutional investors, in terms of types and size, through relaxation of policies and law reforms to improve corporate governance and stabilize the stock market, while limiting the influence of foreign institutional investors. It further analyzes all the Activist Campaigns undertaken by institutional investors in China and maps the network of government bodies, regulations, and tactics that the CCP has developed to directly and indirectly control State-Owned Institutional Investors (SOIIs) and Private-Owned Institutional Investors (POIIs) for the purpose of policy channeling.

This Article concludes by taking a step back and briefly considering what this examination of institutional investors tells us about China's unique form of

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capitalism and system of corporate governance. It suggests that the rise of institutional investors in China has been strategically developed in a way to reinforce the CCP's ultimate control over the financial system. However, contrary to what some conceptions of "state capitalism" may suggest, the CCP does not micro-manage institutional investors on a day-to-day basis. Rather, institutional investors normally function according to free-market forces and increasingly perform an important corporate governance role – with the CCP using its policy channeling in a targeted way to stabilize the market in times of crisis, execute important legal and market reforms, and to maintain calm in society during critical political events: what this Article coin's the "market within the state" for institutional investors in China.

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I. INTRODUCTION

Two decades ago, the United Sates had almost twenty times as many Global Fortune 500 Companies as China.[1] Today, the number of Global Fortune 500 Companies in China (124) has surpassed the United States (121).[2] China's listed companies are leaders in many of the world's most important industries, a fact that was unthinkable at the dawn of the new millennium.[3] China now has the world's largest market for initial public offerings[4] and the world's second largest stock market, which has grown five-fold in the past decade.[5]

For corporate law and governance scholars, even more surprising than China's economic miracle, is the central role the Chinese government has played in achieving it. Before China's rise, the idea that a government could play the role of the most important shareholder in a 21st century world-class corporation – let alone in a multitude of listed corporations at the core of the greatest economic miracle of our time – was an anathema.[6] Yet, today, the Chinese government is by far

[1] In 2000, China had 10 Fortune 500 Companies as compared to the USA's 179, see Scott Kennedy, *The Biggest But Not the Strongest: China's Place in the Fortune Global 500*, CTR. FOR STRATEGIC & INT'L STUD. (Aug. 18, 2020), https://www.csis.org/blogs/trustee-china-hand/biggest-not-strongest-chinas-place-fortune-global-500.

[2] Alan Murray & David Meyer, *The Fortune Global 500 is now more Chinese than American*, FORTUNE (Aug. 10, 2020), https://fortune.com/2020/08/10/fortune-global-500-china-rise-ceo-daily/.

[3] Chinese listed companies lead the world in industries such as pharmaceuticals, solar panels and online payment systems, see *A Rising Star: China's pharmaceuticals industry is growing up*, THE ECONOMIST (Sept. 28, 2019), https://www.economist.com/business/2019/09/28/chinas-pharmaceuticals-industry-is-growing-up (Pharmaceuticals); Yukinori Hanada, *China's solar panel markers top global field but challenges loom*, NIKKEI ASIAN REVIEW (July 31, 2019), https://asia.nikkei.com/Business/Business-trends/China-s-solar-panel-makers-top-global-field-but-challenges-loom (Solar panels); Wang Yue, *$7.6 Trillion Online Payments Market Is No Longer Enough For Jack Ma's Ant Financial*, FORBES (Jan. 17, 2020), https://www.forbes.com/sites/ywang/2020/01/17/ant-financial-is-shifting-away-from-chinas-76-trillion-online-payments-market/?sh=37563bda45b5 (Online payment systems).

[4] Laure He, *Shanghai could be the world's biggest IPO market this year. Holding the title will be tough*, CNN BUSINESS (Nov. 1, 2020), https://edition.cnn.com/2020/10/31/investing/china-markets-ipo-intl-hnk/index.html; Evelyn Cheng, *Chinese Companies are leading the global IPO rush amid a 'flight from uncertainty'*, CNBC (Oct. 27, 2020), https://www.cnbc.com/2020/10/27/chinese-companies-are-leading-the-global-ipo-rush-amid-a-flight-from-uncertainty.html; Georgina Lee, *Shanghai overtakes Hong Kong as world's top IPO destination but mega deals waiting in wings will shake up full-year rankings*, SOUTH CHINA MORNING POST (Mar. 31, 2020), https://www.scmp.com/business/banking-finance/article/3077611/shanghai-overtakes-hong-kong-worlds-top-ipo-destination.

[5] The rise of China and fivefold growth of its stock market over the past decade have fueled a growing literature on this market in financial economics. See Jennifer N. Carpenter & Robert F. Whitelaw, *The Development of China's Stock Market and Stakes for the Global Economy*, 9 ANN. REV. FIN. ECON. 233 (2017); See more recently, Hudson Lockett, *China's stock market value hits record high of more than $10tn*, FINANCIAL TIMES (Oct. 14, 2020), https://www.ft.com/content/7e2d1cae-8033-45b1-811c-bc7d4a413e33 (confirming second largest stock market).

[6] Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 GEO. L. J. 439, 446 (2001); Tan Cheng Han et al., *State-Owned Enterprises in Singapore: Historical Insights into a Potential Model for Reform*, 28 COLUM. J. ASIAN. L. 61, 61 (2015); Curtis J. Milhaupt, *The State as Owner – China's Experience*, 36 OXF. REV. ECON. POL'Y 362, 362 (2020), https://academic.oup.com/oxrep/article-abstract/36/2/362/5813051.

the largest controlling shareholder in the Chinese stock market.[7] Indeed, it is the largest controlling shareholder in the world.[8]

The foundation of the corporate governance system that led to the Chinese government's rise as the world's most powerful shareholder is now aptly described as "corporatization without privatization".[9] Starting in the 1990s, a vast array of businesses that were run as units of the government were transformed into companies under the new PRC Company Law.[10] These companies, with boards of directors and shareholders, were then listed on the Chinese stock market. Importantly, however, the government maintained – and still maintains – a controlling equity interest in its listed State-Owned Enterprises (SOEs).[11] This system of equity finance has become known as mixed-ownership, as SOEs shares are split between the government as the (insider) controlling shareholder and (ostensibly, outsider) minority shareholders.[12]

There is a rich literature analyzing the government's role as China's largest controlling shareholder and the unique agency problems that flow from it.[13] This research provides valuable insights into

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[7] Li-Wen Lin & Curtis J. Milhaupt, *We Are the (National) Champions: Understanding the Mechanisms of State Capitalism in China*, 65 STAN. L. REV. 697, 700 (2013); Curtis J. Milhaupt & Wentong Zheng, *Beyond Ownership: State Capitalism and the Chinese Firm*, 103 GEO. L. J. 665, 676 (Mar. 2015).

[8] Lin & Milhaupt, *supra* note 7, at 700; Milhaupt & Zheng, *supra* note 7, at 676 (CCP is the largest controlling shareholder in the world).

[9] Nicholas Howson, *Protecting the State from Itself? Regulatory Interventions in Corporate Governance and the Financing of China's 'State Capitalism'*, *in* REGULATING THE VISIBLE HAND?: THE INSTITUTIONAL IMPLICATIONS OF CHINESE STATE CAPITALISM 49, at 51-52 (Benjamin L. Liebman & Curtis J. Milhaupt eds., 2015).

[10] Howson, *supra* note 9, at 51-52; Jiangyu Wang & Tan Cheng-Han, *Mixed Ownership Reform and Corporate governance in China's State-Owned Enterprises*, 53 VAND. J. TRANSNAT'L L. 1055 (2020).

[11] 'SOEs' in this article include: (1) enterprises in which government agencies own 100% of the shares (wholly state-owned enterprises), and enterprises in which government agencies and the wholly state-owned enterprises directly or indirectly own in aggregate 100% of the shares; (2) enterprises in which government agencies and the enterprises described in paragraph (1), individually or jointly, own in aggregate more than 50% of the shares and in which one of them is the largest shareholder; (3) subsidiaries in which an enterprise described in paragraph (1) and (2) own more than 50% of the shares; and (4) enterprises in which a government agencies or an enterprise described in paragraph (1) and (2) owns less than 50% of the shares, but is the largest shareholder, and is able to exercise effective domination through shareholders' agreements, articles of association, board resolutions or other arrangements. See 企业国有资产交易监督管理办法 [Measures for the Supervision and Administration of the Transactions of State-Owned Assets of Enterprises], promulgated by SASAC and MOF on Jun. 14, 2016, Article 4.

[12] Howson, *supra* note 9, at 51-52; Milhaupt, *supra* note 6; Wang & Tan, *supra* note 10, at 1062-64.

[13] *Id*; Lauren Yu-Hsin Lin, *Institutionalizing Political Influence in Business: Party-Building and Insider Control in Chinese State-Owned Enterprises*, 45 VT. L. REV. 437 (2021); John Zhuang Liu and Angela Huyue Zhang, *Ownership and Political Control: Evidence from Charter Amendments*, 60 INT'L REV. L. & ECON. 105853 (2019); Lauren Yu-Hsin Lin and Yun-chien Chang, *Do State-Owned Enterprises Have Worse Corporate Governance? An Empirical Study of Corporate Practices in China*, EUR. BUS. ORG. L. REV. (forthcoming 2021); Wang & Tan, *supra* note 10;

how the Chinese Communist Party (CCP) has used the government's controlling shareholder power and other idiosyncratic governance mechanisms – such as Party Committees (*dang wei hui*) – to play a central role as a corporate governance insider in listed SOEs and even in many Private-Owned Enterprises (POEs).[14] However, the CCP's role as the architect – and direct and indirect controller – of institutional investors in China has remained underexplored, and is often entirely ignored.[15]

This lack of focus on institutional investors in Chinese corporate governance may have made sense two decades ago. At that time, in listed Chinese companies, institutional investors' shareholdings were miniscule,[16] the CCP had an iron grip on corporate governance through the government's non-tradable controlling block shareholdings,[17] and stringent caps on foreign institutional investor shareholdings rendered them negligible.[18] All of these facts are relics of a bygone era.

The most recent statistics on China's shareholder landscape reveal that institutional investors now hold 18.7% of China's A-Shares market capitalization – almost double the percentage they held in 2014 and over ten times the amount in 2003.[19] Institutional investors now account for almost half of the free float of shares in A-Shares companies, more than a ninefold increase since 2007 – making institutional investors China's most important minority shareholders.[20] At the end of 2019,

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

[14] Wang & Tan, *supra* note 10, at 1094; Lauren Yu-Hsin Lin & Curtis J. Milhaupt, *Party Building or Noisy Signaling? The Contours of Political Conformity in Chinese Corporate Governance*, at 3 (EGCI Law Working Paper No. 493/2020) (SOEs are now expected to expressly give the party's leadership and party committees formal legal status inside the company).

[15] This suggests a lack of awareness of the role of institutional investors in China. See Wang & Tan, *supra* note 10, at 1106 (explains that strategic investors, who themselves have strong links to the party, play the role of supervising the board in China rather than institutional investors); Tamar Groswald Ozery, *Minority Public Shareholders in China's Concentrated Capital Markets–A New Paradigm?*, 30 COLUM. J. ASIAN L. 1, 28-30 (2016) (Several market conditions such as the strict regimentation of institutional services where they only have limited investment choices, the short term investment horizon, and the lack of skillfulness of institutional investors have limited the ability of institutional investors to monitor and meaningfully participate in firms' governance in China); Howson, *supra* note 9, at 53-54 (there is nothing in the law that requires the controlling state actor to take into account the interests of the minority, much less the role of the minority institutional investor to monitor and participate in the firms' governance in China); Milhaupt, *supra* note 6 (when evaluating the corporate governance of a State-owned enterprise vis-à-vis the state, Milhaupt did not consider the possibilities of a minority institutional investor as a check on the company's corporate governance); Edward Rock, *Institutional Investors in Corporate Governance*, *in* THE OXFORD HANDBOOK OF CORPORATE LAW AND GOVERNANCE (Jeffrey N. Gordon & Wolf-Georg Ringe eds., 2018) (when considering the role of institutional investors with regards to corporate governance around the world, Rock made no mention of China; it has completely escaped the debate).

[16] *See infra* Part II.

[17] 上市公司股权分置改革管理办法 [Measures for the Administration of the Share-trading Reform of Listed Companies], promulgated by China Securities Regulatory Commission (CSRC) on Sept. 5, 2005.

[18] *See infra* Part II.

[19] A-Shares are the shares of listed companies incorporated in mainland China that trade in RMBs on the two Chinese stock exchanges, the Shanghai Stock Exchange (SSE) and the Shenzhen Stock Exchange (SZSE). An "A-Shares Company" refers to a company listed on the SSE or the SZSE. *See infra* Part II.

[20] *See infra* Part II.

the assets under management by institutional investors in China reached US$16 trillion – a tenfold increase over the past 10 years, making it the world's most important market for growth in the asset management industry.[21] In 2015, the government made its controlling shareholder stakes in SOEs fully tradable and since then it has significantly decreased the size of its controlling shareholder blocks.[22] In recent years, the caps on foreign institutional investors have been progressively raised and were largely abolished in 2020.[23] This now makes any analysis of Chinese corporate governance that does not consider institutional investors incomplete.

Considering these watershed developments, it is surprising that the legal literature lacks a recent description of who China's institutional investors are, how they are regulated, and what impact they have on Chinese corporate governance.[24] This gap in the literature is especially surprising as the role of institutional investors in corporate governance is a primary focus of several of the world's leading corporate law scholars.[25] This Article aims to take the first step in addressing this conspicuous gap in the literature.

In Part II, we draw on the most accurate and up-to-date Chinese sources to describe the taxonomy of institutional investors in China. The taxonomy reveals that as the percentage of the A-Shares market owned by institutional investors has grown, there has been a proliferation in the different

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[21] World Economic Forum, *China Asset Management at an Inflection Point*, at 5 (July 2020), http://www3.weforum.org/docs/WEF_IR_China_Asset_Management_2020.pdf [hereinafter WEF Report].

[22] Wang & Tan, *supra* note 10, at 1065.

[23] State Administration of Foreign Exchange (SAFE), *PBOC & SAFE Remove QFII / RQFII Investment Quotas and Promote Further Opening-up of China's Financial Market* (May 7, 2020), https://www.safe.gov.cn/en/2020/0507/1677.html. With Chinese A-Shares becoming a part of the MSCI Emerging Markets Index in 2018 (MSCI EMI) and a significant increase in their weightage in the MSCI EMI in 2019, it seems likely that there will be a marked increase in shareholdings by foreign institutional investors (Zhen Wei, *Emerging markets since China A shares' inclusion*, MSCI (Dec. 5, 2020), https://www.msci.com/www/blog-posts/emerging-markets-since-china-a/01662775315). Although recent political tensions with the United States have caused some Chinese companies to be removed from the MSCI EMI due to their alleged connection with the Chinese government, an increase in the amount of foreign institutional investment in China's stock markets still seems likely. In 2020, 2019 and 2018, CSRC approved 71, 20 and 18 foreign institutional investors' application for QFIIs. In 2019, CSRC approved 20 foreign institutional investors as QFIIs respectively, indicating a more relaxed approach towards QFII. Full list of QFII is available at: http://www.csrc.gov.cn/pub/zjhpublic/G00306205/201511/t20151106_286098.htm.

[24] The latest significant article on institutional investor activism in China in the legal literature was 15 years ago, *see* Chao Xi, *Institutional Shareholder Activism in China: Law and Practice*, 17 INT'L CO. & COM. L. REV. 251 (2006). Robin Hui Huang has explained why institutional investors did not perform the role of lead plaintiffs in Chinese-style securities class action, see, Robin Hui Huang, *Private Enforcement of Securities Law in China: A Ten-year Retrospective and Empirical Assessment*, 61 AM. J. COMP. L. 757, 787-89 (2013). Recently, Guo Li and Zhao Yijun have published an article relating to institutional investors, which focused more on the US and EU experience, but less on the description of China's situation, see, Guo Li & Zhao Yijun, *The Regulation of Proxy Advisors: Experiments and Lessons from the US and the EU* (机构投资者投票顾问的法律规制——美国与欧盟的探索及借鉴), 1 J. CORP. L. (比较法研究) 152 (2019).

[25] See for example, Lucian A. Bebchuk et al., *The Agency Problems of Institutional Investors*, 31 J. ECON. PERSP. 89, 92–93 (2017); John C. Coates, IV, *The Future of Corporate Governance Part I: The Problem of Twelve*, 2–5 (Harv. Public Law Working Paper No. 19–07, 2019); Jill Fisch, *The Uncertain Stewardship Potential of Index Funds*, *in* GLOBAL SHAREHOLDER STEWARDSHIP (Dionysia Katelouzou & Dan W. Puchniak eds., forthcoming); Ronald J. Gilson & Jeffery N. Gordon, *The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights*, 113 COLUM. L. REV. 863, 874-76 (2013); Rock, *supra* note 15.

types of institutional investors in China – what we coin the "atomization" of the market for institutional investors. An analysis of the regulations that have driven the growth and atomization of institutional investors demonstrates that for decades, the CCP has actively promoted the growth of institutional investors to improve corporate governance and stabilize the stock market. It also reveals that the CCP has strategically controlled the growth and influence of foreign institutional investors, making China the most domestically dominated major market for institutional investors in the world – in which the big three American institutional investors (i.e., Blackrock, State Street and Vanguard) are inconsequential. This has allowed the CCP to rapidly develop a sizable and effective market for institutional investors, while ensuring that it reinforces the China Model of corporate governance in which the CCP maintains ultimate control.

In Part III, we collect and analyze a growing number of empirical studies in the business school literature that provide three valuable insights into the role played by institutional investors in Chinese corporate governance. First, they provide convincing evidence that different types of institutional investors have different impacts on Chinese corporate governance – confirming the value of the taxonomy of institutional investors analyzed in Part II. Second, several empirical studies find that the impact that institutional investors have on corporate governance is contingent on the extent to which the institutional investor is insulated from the CCP – highlighting the importance of distinguishing between State-Owned Institutional Investors (SOIIs), Private-Owned Institutional Investors (POIIs), and Foreign-Owned Institutional Investors (FOIIs). Third, several empirical studies find that the impact that institutional investors have on corporate governance is contingent on whether the investee company is a SOE or POE – reinforcing the importance of understanding the role of the CCP in China's market for institutional investors.

However, as explained in detail in Part III, as insightful as these empirical studies are, they suffer from some limitations in their currency, data, and analysis. They also fail to explain how institutional investors, who in almost all companies are collectively minority shareholders, produce a statistically significant impact on corporate governance. To overcome some of these blind spots in the empirical studies, we hand-collected and analyzed publicly reported representative cases in which institutional investors, acting as minority shareholders, have been involved in Activist Campaigns in A-Shares Companies. Somewhat surprisingly, our analysis of these cases revealed that SOIIs have undertaken a significant portion of the Activist Campaigns and that POIIs have succeeded in more than half of their Activist Campaigns targeting SOEs.[26] However, over the last decade the number of Activist Campaigns by POIIs, several of which have succeeded in SOEs, are on the rise.[27] Moreover, based on the searches we have conducted, FOIIs have undertaken only

[26] From 1994 to 2021, 30.2% (13 out of 43) of the Activist Campaigns were undertaken by SOIIs, with SOIIs and POIIs collaborating in 11.6% (5 out of 43) of the Activist Campaigns. In the cases in which a POII targeted an SOE, the POII succeeded in 57.1% (4 out of 7) of the Activist Campaigns. See below, Appendix 2.

[27] From 1994 to 2010, 30% (3 out of 10) of the Activist Campaigns were undertaken by POIIs, with SOIIs and POIIs collaborating in 20% (2 out of 10) of the Activist Campaigns; whereas from 2011 to 2021, 60.6% (20 out of 33) of the Activist Campaigns were undertaken by POIIs, with SOIIs and POIIs collaborating in 9.1% (3 out of 33) of the Activist Campaigns and an FOII and a POII collaborating in 1 Activist Campaign. See below, Appendix 2.

two activist campaigns, none of which were in the last decade.[28] Finally, Activist Campaigns overall are clearly on the rise, with three times as many Activist Campaigns in the last decade compared to two decades ago.[29] Taken together, as explained in detail in Part III, this suggests that SOIIs and POIIs are developing into an important corporate governance mechanism to mitigate private benefits of control in China – while the role of FOIIs remains limited. It also suggests that the relationship between the CCP and institutional investors is important and complex.

In Part IV, we aim to make sense out of this complexity by mapping and analyzing the various government bodies, regulations, and tactics that the CCP has developed to control institutional investors formally and informally in China. Based on empirical, case study, and interview evidence, we explain how the CCP can – and has – used various mechanisms to engage in "policy channeling"[30] in SOIIs and POIIs, with foreign institutional investors being largely insulated from policy channeling. Equally important, however, is our evidence that the CCP uses its power to policy channel in a targeted and limited way surrounding significant stock market and political events. On a day-to-day basis, absent these extraordinary events, institutional investors in China appear to be driven mostly by free market-forces. Empirical, interview, and case study evidence suggests that institutional investors often serve an important corporate governance function by acting as a check on corporate controllers in SOEs and POEs. This fits with other research on Chinese corporate governance that demonstrates that the government has created a system to mitigate private benefits of control – even when it means constraining the power of SOEs – while at the same time ensuring the CCP maintains ultimate control.[31]

In Part V, we conclude by taking a step back and briefly considering what this examination of institutional investors tells us about China's unique form of capitalism and system of corporate governance. The evidence in this Article suggests that the rise of institutional investors in China has been done in a way to reinforce the CCP's ultimate control. However, contrary to what some conceptions of "state capitalism" may suggest, the CCP does not micro-manage institutional investors on a day-to-day basis. Rather, institutional investors normally function according to free-market forces and increasingly perform an important corporate governance role – with the CCP using its policy channeling in a targeted way to stabilize the market in times of crisis, execute

[28] The two cases undertaken by FOIIs both occurred in 2012. See below, Appendix 2.

[29] From 1994 to 2010, there were 10 Activist Campaigns; whereas from 2011 to 2021, there were 33 Activist Campaigns. See below, Appendix 2.

[30] The term "policy channeling" was first coined by Milhaupt and Pargendler in their research on related party transactions in SOEs. Curtis Milhaupt & Mariana Pargendler, *Related Party Transactions in State-Owned Enterprises: Tunnelling, Propping, and Policy Channeling*, *in* THE LAW AND FINANCE OF RELATED PARTY TRANSACTIONS 245, 245-46 (Luca Enriques & Tobias Troger eds., 2019). See also, Ronald Gilson & Curtis Milhaupt, *Shifting Influences on Corporate Governance: Capital Market Completeness and Policy Channeling* (ECGI Law Working Paper No. 546/2020, Jan. 2021), https://ssrn.com/abstract=3695309. In this Article, we extend the use of the term "policy channeling" to institutional investors in China. In this context, "policy channeling" refers to the CCP's instrumental use of institutional investors for economic policy or social purposes – as opposed to institutional investors focusing on maximizing the value of the funds they own/manage.

[31] Howson, *supra* note 9, at 52; Wang & Tan, *supra* note 10, at 1094.

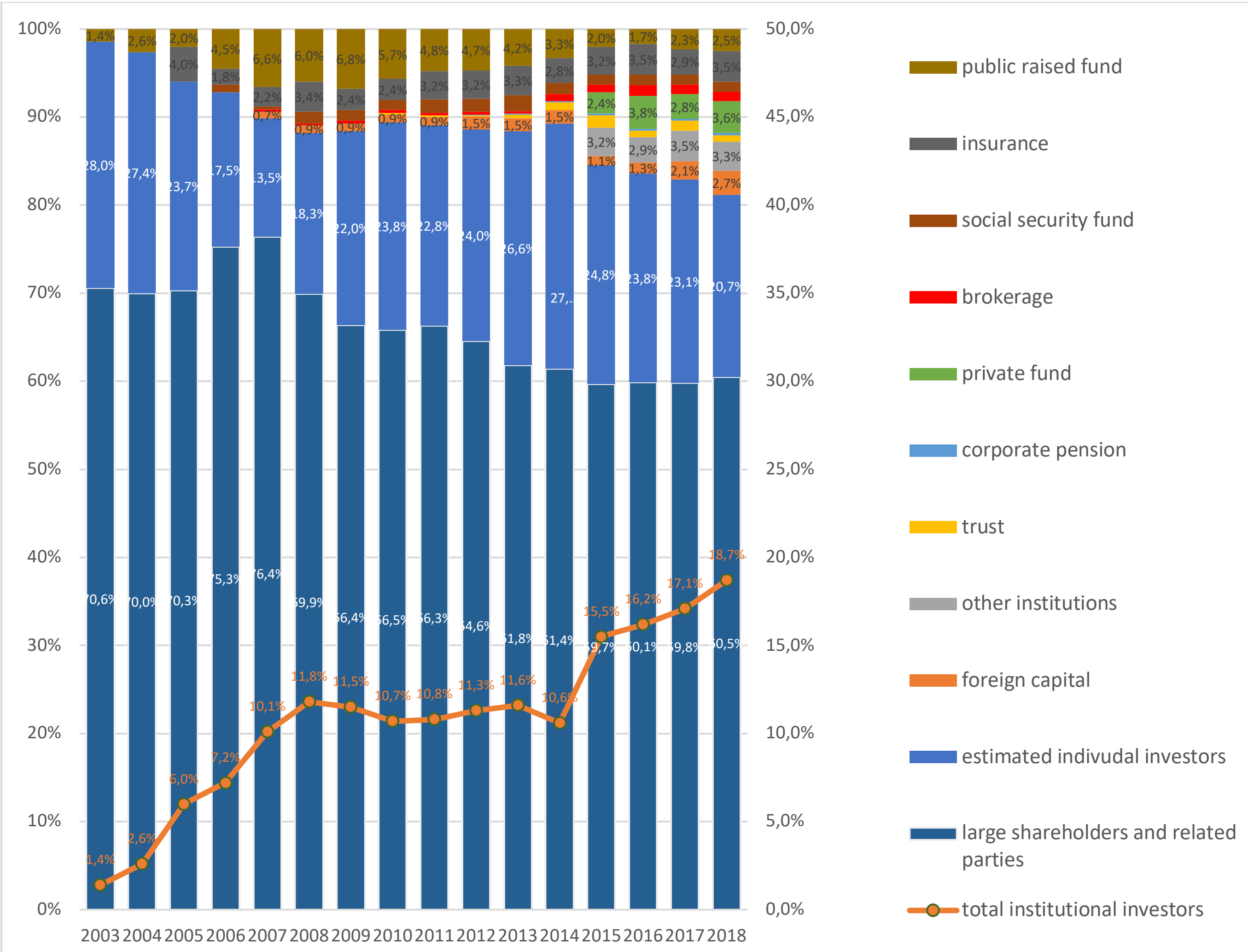
important legal and market reforms, and to maintain calm in society during critical political events. This is what we coin the "market within the state" for institutional investors in China.

II. THE RISE OF INSTITUTIONAL INVESTORS IN CHINA – A REMARKABLE, YET OVERLOOKED, HISTORY

(a) *Institutional Investors in China Can No Longer be Ignored*

The meteoric rise of institutional investors in China is difficult to overstate. As is clear in Chart 1 below, in 2003 the percentage of the A-Shares market owned by institutional investors was a miniscule 1.4%. By 2008, the percentage of institutional investor ownership had increased more than eightfold to 11.8%. As of 2018, institutional investors held 18.7% of the market capitalization of A-Shares.

Chart 1: A-Share Investors Based on Market Capitalization (2003 to 2018)[32]



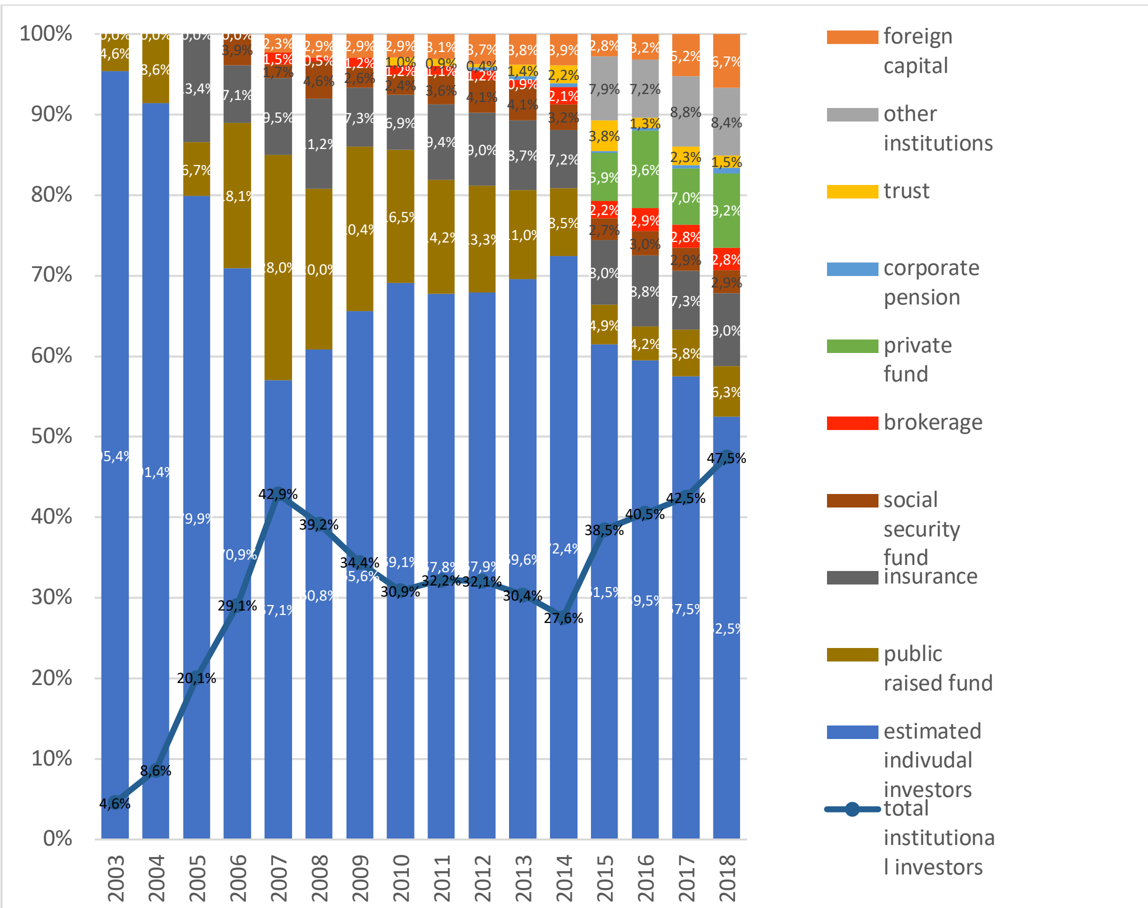
The increase in control that institutional investors have over the free-float in China's A-Shares market has been equally dramatic.[33] As is evident in Chart 2 below, in 2003 institutional investors

[32] The data is taken from 中金公司研究部 [CICC Global Institute], "中金公司：A 股"散户化"已经明显下降" [CICC: the Proportion of Retail Investor in A-Shares Market Has Declined Significantly] (July 2, 2019), https://m.21jingji.com/article/20190702/herald/b39f0f661609f2353cdfafbb8d88b974.html. Other institutions include other professional institutions (其他专业机构) and products (such as asset management plans of futures firms (期货公司资产管理计划), financial companies (财务公司), and wealth management products of commercial banks (商业银行理财产品)); Total institutional investors refer to investors excluding estimated individual investors, large shareholders and related parties.

[33] "Free float market capitalization" is the amount of capital stock (known as free float) that is left after excluding the illiquid shares in the share capital of the listed company and the basically illiquid shares due to strategic holdings or other reasons which multiplied by the share price. It can reflect the stock price changes of the actual shares in circulation in the market. The excluded illiquid shares including: (i) long-term shares held by the company's founders, family members, senior managers; (ii) state-owned shareholders; (iii) shares held by strategic investors; (iv) frozen shares; (v) shares held by restricted employees; and, (vi) cross-held shares of listed companies. The restricted shares

controlled merely 4.6% of the free-float of A-Shares. By 2007, the portion of the free-float controlled by institutional investors had increased more than ninefold to 42.9% and in 2018 reached 47.5% – making institutional investors China's most important minority shareholders. As such, it is now clear that institutional investors are an important part of Chinese corporate governance.

Chart 2: A-Share Institutional Investors as a Percentage of Free-Float Market (2003 to 2018)[34]



The global institutional investor community has come to recognize the importance of institutional investors in China. Recent reports have identified China's asset management market as the world's most important for growth in the industry and have valued it at US$16 trillion.[35] Yet, surprisingly, even though the role of institutional investors in corporate governance has become a core issue

published in the public notice of the listed company and the shares held by the above six types of shareholders and their persons acting in concert over 5% are considered as non-freely circulated capital stock. See 上证 180、上证 50 指数编制细则 (SSE 180 and SSE 50 Index Compilation Rules), promulgated by SSE in June, 2010, http://www.sse.com.cn/market/sseindex/indexlist/indexdetails/indexrules/c/Index_Methodology_CN_000010n16.pdf.

[34] CICC Global Institute, *supra* note 32.

[35] WEF Report, *supra* note 21.

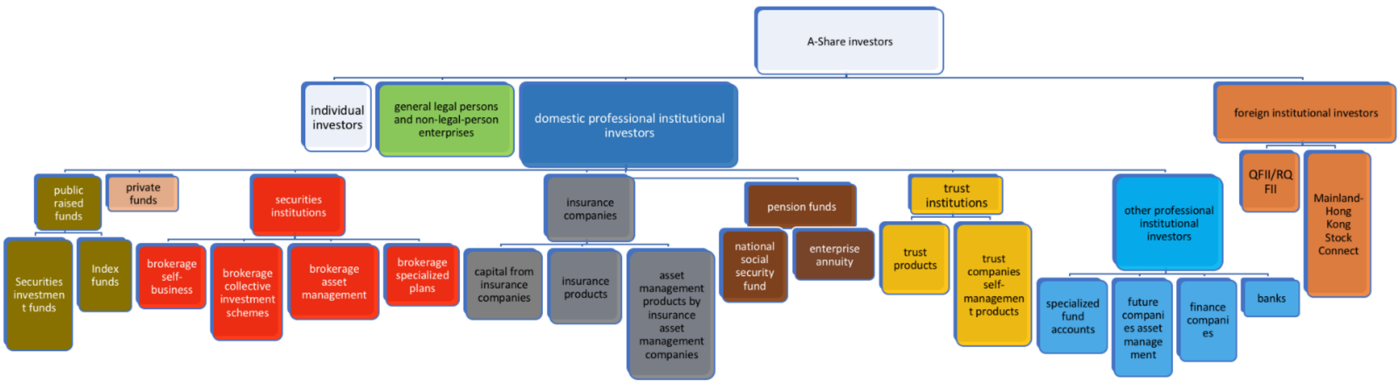
among Anglo-America's leading comparative corporate law scholars, the remarkable rise of Chinese institutional investors has been almost entirely overlooked in the legal literature.[36]

Before analyzing how institutional investors fit into the China Model of corporate governance, it is essential to recognize that institutional investors in China are not monolithic. As illustrated in the taxonomy of institutional investors in Chart 3 below, there are a variety of institutional investors in China. It is important to understand these varieties as each of them is subject to different regulatory regimes. By mapping the regulatory developments for each variety, a clear picture emerges of how the Chinese government has used its regulatory power to facilitate and shape the growth of different types of institutional investors over the last several decades (See, Appendix 1 for a summary of all the relevant regulatory provisions related to institutional investors, listed in chronological order, and categorized based on the type of institutional investor they regulate).

As examined in detail in Part IV, the different varieties of institutional investors have distinct regulatory regimes. As a result, the manner and extent to which each variety is subject to direct and indirect government control also differs among them. However, despite these differences, our detailed analysis below reveals two features that cut across all varieties: (1) over the last several decades the Chinese government has consistently used its regulatory power to facilitate the growth of institutional investors overall; and, (2) the Chinese government has designed a regulatory regime for institutional investors that reinforces the China Model of corporate governance, which aims to improve the efficiency of corporate governance, while ensuring that the CCP maintains ultimate control over the financial system.

[36] Rock, *supra* note 15 (this chapter was part of an extensive global corporate law and governance research project, but there was not a single mention of institutional investors in China. This is consistent with the most of the leading literature on the impact of institutional investors on corporate law and governance, which has tended to focus on the US and UK); *See* generally Bebchuk et al., *supra* note 25, at 92-93; Coates, *supra* note 25; Fisch, *supra* note 25; Gilson & Gordon, *supra* note 25.

Chart 3: Taxonomy of Institutional Investors in China's A-Shares Market[37]



(b) Foreign Institutional Investors: A Small, But Growing, Piece of the Taxonomy

The first important bifurcation in the taxonomy is between domestic institutional investors and foreign institutional investors. Foreign institutional investors refer to investors who enter the A-Shares market through the qualified foreign institutional investors (QFII) regime, the Renminbi qualified foreign institutional investors (RQFII) regime, and Mainland-Hong Kong Stock Connect (*lu gu tong*).

China is unique among most major economies with respect to how small of a percentage of its stock market is owned by foreign institutional investors.[38] As can be seen in Chart 1 above, until 2007 there was no measurable foreign institutional investor ownership registered in the A-Shares market. From 2007 to 2011, the level of foreign institutional ownership in the A-Shares market

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[37] The taxonomy is based on 起底 A 股投资者筹码--A 股投资者结构专题 2020Q2 [Ownership Structure of the A-share Investors], SINA FINANCE (Sept. 9, 2020), https://finance.sina.com.cn/stock/stockzmt/2020-09-09/doc-iivhuipp3290986.shtml. See also, 股票投资者分类标准[The Criteria for Classifying Equity Investors] in 证券期货业统计指标标准指引 [The Guidelines on the Statistical Indicator Standards for the Securities and Futures Industry], promulgated by CSRC on Jan. 1, 2020, http://www.csrc.gov.cn/pub/zjhpublic/zjh/201912/P020191220532662778070.pdf.

[38] Adriana De La Cruz et al., *Owners of the World's Listed Companies*, OECD CAPITAL MARKET SERIES (Oct. 17, 2019), https://www.oecd.org/corporate/Owners-of-the-Worlds-Listed-Companies.htm .

was paltry, remaining at below 1%. Although the percentage of foreign institutional investor ownership has increased since 2016, it registered at only 2.8% of the A-Shares market in 2018. The small percentage of the A-Shares market owned by foreign institutional investors makes China an outlier as foreign institutional investors have come to play a significant (and, in some countries such as the UK, even dominant) role in most of the world's other major stock markets.[39] Relatedly, the US "Big Three" institutional investors (BlackRock, Vanguard, and State Street) – which have attracted considerable academic attention and are the largest institutional investors globally – have heretofore owned a miniscule percentage of shares in the Chinese stock market.[40]

The small percentage of foreign institutional ownership in the Chinese stock market is the result of strict regulatory caps that have historically been placed on foreign institutional investors. In 2002, the Chinese government launched the highly restrictive QFII scheme which for the first time allowed foreign institutional investors to invest in the Chinese securities market.[41] This required foreign investors to apply to the CSRC for its approval to invest. If approved, the foreign investor would receive a limited quota on the approved amount that could be invested from the State Administration of Foreign Exchange (SAFE).

The approved amount under the SAFE investment quota was subject to a one-year lock-in period during which time the investment funds had to remain in China.[42] Under no circumstances could the total combined percentage of shares held by all the QFIIs in a single listed company exceed 20% of its total shares nor could a single foreign investor own more than 10% of shares in a listed company.[43] In addition, to qualify for the QFIIs scheme, fund management companies had to have a minimum of US$10 billion in assets under management in their previous financial year and at least five years of operational experience, while insurance companies were required to have at least 30 years of experience and paid-in capital of at least US$1 billion.[44] The restrictions limited

[39] WEF Report, *supra* note 21.

[40] See 杨佼(Yang Jiao), A 股投资者 30 年变迁：机构话语权提升，散户持股占比降至 30% [The Evolution of A-share Investors in the Past Thirty Years: Voice of Institutional Investors Increased; The Percentage of Retail Investors Decreased to 30%], YICAI (Nov. 30, 2020), https://www.yicai.com/news/100858573.html; Major institutional investors such as Vanguard have relinquished their bid for a fund license, and will instead be relying on their joint venture with Ant Financial. *See Shock and Tears: Behind Vanguard's Retreat From China Market*, BLOOMBERGQUINT (Apr. 30, 2021), https://www.bloombergquint.com/markets/shock-and-tears-behind-vanguard-s-retreat-from-china-s-market.

[41] 合格境外机构投资者境内证券投资管理暂行办法 [Interim Measures for the Administration of Domestic Securities Investment by Qualified Foreign Institutional Investors], promulgated by CSRC and PBOC on Nov. 5, 2002.

[42] Wei Huang & Tao Zhu, *Foreign institutional investors and corporate governance in emerging markets: Evidence of a split-share structure reform in China*, 32 J. CORP. FIN. 312, at n.10 (2015).

[43] See 关于实施《合格境外机构投资者境内证券投资管理办法》有关问题的通知 [Notice on Issues Relating to the Implementation of the Measures for the Administration of Domestic Securities Investment by Qualified Foreign Institutional Investors], promulgated by CSRC on Aug. 24, 2006, http://www.csrc.gov.cn/pub/newsite/flb/flfg/bmgf/jj/hgjw/201012/t20101231_189793.html.

[44] Huang & Zhu, *supra* note 42, at 315.

QFIIs to major international investment banks who, due to the strict quotas and restrictions, individually and collectively could only own a small percentage of shares in Chinese listed companies.

Since 2002, as set out in detail in Appendix 1, the investment restrictions and lock-in period for QFIIs have progressively been relaxed to facilitate the inflow of more foreign institutional investments. Importantly, as part of this initiative, in 2005, the Ministry of Commerce, the CSRC, the State Administration of Taxation, the State Administration for Industry and Commerce, and the State Administration of Foreign Exchange jointly issued a new measure to allow strategic investments in A-Shares listed companies by foreign investors. The measures took effect in 2006, and as is clear in Chart 1 above, foreign institutional investors began to invest in the A-Shares market in 2007.[45]

In 2012, the limitations on the total combined percentage of shares held by all the QFIIs, RQFIIs, and Mainland-Hong Kong Stock Connect investors[46] in a single listed company was increased to 30%.[47] In 2018, SAFE issued new provisions[48] that abolished the lock-in period and the CSRC announced that it would further relax the qualification requirements on foreign investors. In 2019, SAFE announced its decision to abolish the investment quota system under the QFII scheme and, in 2020, SAFE and People's Bank of China (PBOC) issued a new regulation to simplify the administrative requirements on domestic investments by foreign institutional investors.[49] These policies should make it more convenient for foreign investors to invest in A-Shares in the future –

[45] 外国投资者对上市公司战略投资管理办法 [Administrative Measures for Foreign Investors' Strategic Investments in Listed Companies], promulgated by the Ministry of Commerce, the CSRC, the State Administration of Taxation, the State Administration for Industry and Commerce, and the SAFE on Dec. 31, 2005

[46] "Mainland-Hong Kong Stock Connect investors" refers to individual investors and institutional investors who trade shares in SSE and SZSE with Hong Kong Securities Clearing Co., Ltd. as the nominee shareholder. See, 上海证券交易所沪港通试点办法 [SSE-Hong Kong Stock Connect Pilot Scheme], promulgated by SSE on Sep. 27, 2014; 内地与香港股票市场交易互联互通机制若干规定 [Certain provisions of the interoperability mechanism for trading in the Mainland and Hong Kong stock markets], promulgated by CSRC on Sep. 30, 2016; 内地与香港股票市场交易互联互通机制登记、存管、结算业务实施细则 [Implementation Rules for the Registration, Depository and Settlement Services of the Mainland-Hong Kong Stock Market Trading Interoperability Mechanism], promulgated by China Securities Depository and Clearing Co., Ltd. on Sep. 30, 2016, Article 6

[47] 关于实施〈合格境外机构投资者境内证券投资管理办法〉有关问题的规定 [Provisions on Issues concerning the Implementation of the Administrative Measures for Securities Investment Made in China by Qualified Foreign Institutional Investors], promulgated by the CSRC in July 27, 2012, Article 9(2).

[48] 合格境外机构投资者境内证券投资外汇管理规定 [Provisions on the Foreign Exchange Administration of Domestic Securities Investment by Qualified Foreign Institutional Investors], promulgated by SAFE on June 10, 2018.

[49] See, 国家外汇管理局：取消合格境外投资者（QFII/RQFII）投资额度限制 扩大金融市场对外开放 [State Administration of Foreign Exchange (SAFE): Abolish the limit of investment quota for qualified foreign investors (QFII/RQFII) to expand the opening of financial market], promulgated by SAFE on Sep. 10, 2019, http://www.safe.gov.cn/safe/2019/0910/14040.html; 境外机构投资者境内证券期货投资资金管理规定 [Regulations on Funds of Securities and Futures Investment by Foreign Institutional Investors], promulgated by PBOC and SAFE on May 7, 2020, http://www.gov.cn/zhengce/zhengceku/2020-05/07/content_5509577.htm.

but the 30% cap on foreign investor ownership in a single A-Shares company will still limit their ability to influence corporate governance.[50]

Although the *average* percentage of ownership by foreign institutional investors in the A-Shares market has remained small (below 3%), it is noteworthy that recently they have collectively acquired significant minority holdings in some high profile listed companies.[51] For example, as of 30 April 2020, QFII, RQFII, and Shenzhen Connect investors held 1.872 billion shares of Midea group, accounting for 26.74% of its shares.[52] With Chinese listed companies' inclusion in the MSCI EMI and the aforementioned regulatory caps recently abolished, it seems possible that foreign institutional investors will acquire significant *minority* stakes in more high-profile A-Shares companies in the future.

There are two important observations that arise from our examination of the regulatory developments in the foreign component of the taxonomy of institutional investors in China. First, the remarkable rise of institutional investors in China has been driven predominantly by Chinese – not foreign – institutional investors. It appears that the lack of foreign investment has been the direct result of the Chinese government's strict regulatory caps and restrictions. Empirical evidence supports this conclusion as foreign institutional investment has increased in lockstep each time the quotas and restrictions have been eased.[53] As such, the Chinese government, through its regulatory design, has given itself a strong hand to shape and effectively control the vast majority of the market for institutional investors as they are overwhelmingly domestic – a stark contrast to most other major jurisdictions that have struggled to effectively regulate foreign institutional investors which have composed a sizable portion of their markets.[54] It has also allowed Chinese institutional investors to develop and capture market share with limited competition from foreign institutional investors.

Second, the small ownership stakes of foreign institutional investors have limited their ability to influence Chinese corporate governance – especially as most listed companies in China are dominated by powerful domestic controlling-block shareholders. As examined in detail in Part III below, there is some empirical evidence suggesting that foreign institutional investors have on

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[50] See, 关于实施〈合格境外机构投资者境内证券投资管理办法〉有关问题的规定 [Provisions on Issues Relating to the Implementation of the Measures for the Administration of Domestic Securities and Futures Investments by QFIIs and RQFIIs], promulgated by CSRC on Sep. 25, 2020, Article 7(2).

[51] 证监会：超百家上市公司第一大股东是外资战略投资者 [CSRC: The largest shareholder of over 100 listed companies is a foreign strategic investor], SOHU (Oct. 12, 2020), https://www.sohu.com/a/424142681_561670; Gao Chang, 外资加速流入 A 股 3 公司持股逼近上限被预警 [Accelerating the Inflow of Foreign Capital into A-Shares, 3 Companies are Approaching the Upper Limit of Shareholders], XINHUA NEWS (May 27, 2020), http://www.xinhuanet.com/fortune/2020-05/27/c_1126037849.htm.

[52] *Id*.

[53] Ningyue Liu et al., *The investment behavior of Qualified Foreign Institutional Investors in China*, 54 J. MULTI. FIN. MGMT. 100614 (2020).

[54] *See* Brian R. Cheffins, *The Stewardship Code's Achilles' Heel*, 73 MOD. L. REV. 1004 (2010).

occasion "punched above their weight"[55] in their ability to impact corporate governance in listed companies in China, despite their small minority shareholdings. However, as explained in Part IV, even if foreign institutional investors increase their holdings and continue to sporadically punch above their weight, this will merely continue to assist with mitigating the extraction of wealth reducing private benefits of control in A-Shares companies, but not fundamentally change the China Model of corporate governance – in which the CCP has ultimate control over SOIIs and POIIs, who dominate the market for institutional investors in China.

(c) Domestic Institutional Investors: The Core of the Taxonomy

The roots of domestic institutional investors in China can be traced back to 1991 when the first batch of *Securities Investment Funds* (SIFs, commonly referred to as mutual funds) – Wuhan Securities Investment Fund and Nanshan Venture Capital Fund – were established. In its first few years, the security investment fund industry was fledgling and remained loosely regulated. This started to change in 1997 when the Securities Commission of the State Council (currently dissolved) issued the "Interim Measures on the Management of Securities Investment Funds" (SIF Interim Measures), which established the first provisional framework for the industry. Within a few years, a handful of asset management companies were established, and several close-ended funds were launched. In addition, 75 close-ended funds, which were launched prior to the introduction of the SIF Interim Measures, continued to function. [56]

At the dawn of the new millennium, the Chinese government made it a strategic initiative to develop SIFs as a mechanism to stabilize the market and improve Chinese corporate governance. In 1999, the CSRC began the process of liquidating and amalgamating the 75 close-ended funds launched prior to the introduction of the SIF Interim Measures. In 2000, the President of the CSRC and the Vice-Chairman of the Standing Committee of the National People's Congress both made the development of SIFs a priority to facilitate the development of institutional investors.[57] Their views were echoed in a CSRC policy paper published in 2000, which promoted the development of SIFs as a mechanism to stabilize the stock market and monitor the controllers of listed companies.[58]

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[55] Huang & Zhu, *supra* note 42, at 312–326.

[56] In March 1998, Jin Tai Fund and Kai Yuan Fund became the first two regulated funds permitted under these Measures. Between 1998 to 1999, the "Old Ten" SIFs were established, comprising 10 companies including China Southern Asset Management, Guotai Asset Management, China Asset Management.

[57] Open-end mutual fund should be the main institutional investors. See 周小川指出：尽早使基金成为主要机构投资者 [Zhou Xiaochuan Points Out: Make the Fund a Major Institutional Investor as Soon as Possible], SHANGHAI SECURITIES DAILY (Oct. 25, 2000), http://finance.sina.com.cn/2000-10-25/18600.html.

[58] 开放式证券投资基金试点办法[Open-ended Securities Investment Fund Pilot Scheme], promulgated by CSRC on Oct. 8, 2000..

In 2001, China's first open-ended SIF was launched, and open-ended funds quickly came to dominate the industry.[59] In 2002, China designated institutional investors as an important feature of its corporate governance system by affirming in its inaugural Corporate Governance Code that "institutional investors shall play a role in the appointment of company directors, the compensation and supervision of management and major decision-making processes."[60] On 28 October 2003, the "PRC Securities Investment Fund Law" was promulgated, marking a major milestone as it was the first national law regulating SIFs.[61]

As illustrated in Chart 1 and Chart 2 above, until 2005, SIFs were essentially the only type of institutional investor in the market. As the stock market strengthened in 2006 and boomed in 2007, the popularity, profitability, and size of SIFs increased significantly – and they came to account for 6.6% of capitalization and 28% of the free-float of the A-Shares market.[62] Since 2003, hedge funds and index funds have been gradually launched, but open-ended mutual funds continue to dominate the market.[63] In April 2018, the Guiding Opinions on Regulating the Asset Management Business of Financial Institutions[64] placed the regulation of SIFs under the unified supervision of the PBOC, the China Banking and Insurance Regulatory Commission (CBIRC), and the CSRC.[65] As of 2019, China had a total of 6084 public offering funds with a total value of 14.66 trillion Yuan – representing over a tenfold increase in the number of funds a decade earlier, and, in 2020,

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[59] By the end of 2002, the number of open-ended SIFs had increased to 17 and it went on to gradually replace closed-ended funds.

[60] CSRC, CODE OF CORPORATE GOVERNANCE FOR LISTED COMPANIES IN CHINA (2002), Art. 11. See Appendix 1.

[61] 中华人民共和国证券投资基金法[PRC SECURITIES INVESTMENT FUND LAW], promulgated by Standing Committee of the National People's Congress on Oct. 28, 2003.

[62] Before 2005, the subscription of these public offering funds relied on a policy of apportionment, where banks often required employees to subscribe to funds proportional to their top-down allocations. After 2006, the stock market begun to strengthen and securities fund investment became a successful way of making money. As a result, investors begun to treat these funds differently and more investors begun to subscribe to the fund on a pro rata basis. With the continued unilateral rise in the stock market in 2007, the size of the public offering fund industry proliferated, peaking at 3.2 trillion Yuan. 刘雪菲(Liu Xuefei), 2018 年中国公募基金行业发展战略研究：逐鹿大资管，寻基金的危与机(2018 Nián zhōngguó gōngmù jījīn hángyè fāzhǎn zhànlüè yánjiū: Zhúlù dà zī guǎn, xún jījīn de wēi yǔ jī) [Research on the Development Strategy of China's Public Equity Fund Industry in 2018: Competing for Big Asset Management, Looking for Crisis and Opportunities], SOHU (July 10, 2018), https://www.sohu.com/a/240329974_313170.

[63] The first Chinese index fund was set up in January 2003, *see* 指数基金如何选? [How to Select Index Fund], ECONOMIC DAILY (Nov. 22, 2019), https://finance.sina.com.cn/roll/2019-11-22/doc-iihnzahi2509827.shtml?source=cj&dv=; The first Chinese hedge fund was launched in September 2010, *see* 国内首只对冲基金产品面世 易方达基金拔头筹[First Domestic Hedge Fund was Launched], RENMIN DAILY (Sept. 2, 2010), https://finance.qq.com/a/20100902/001842.htm.

[64] 关于规范金融机构资产管理业务的指导意见[Guiding Opinions of the People's Bank of China, the China Banking and Insurance Regulatory Commission, the China Securities Regulatory Commission, and the State Administration of Foreign Exchange on Regulating the Asset Management Business of Financial Institutions], promulgated by PBOC, CBIRC, CSRC and SAFE on Apr. 27, 2018.

[65] *See* Liu, *supra* note 62.

there were 143 fund management companies in China.[66] Despite this rapid growth over the past decade in absolute terms, the percentage of market capitalization and free-float of the A-Shares market controlled by SIFs has declined (see above, Chart 1 and Chart 2) and now stands at 2.5% and 6.3% respectively. This is due to the entry of other types of institutional investors into the market and the even more explosive growth in the capitalization of the A-Shares market as a whole, which we will now describe.

The second major type of domestic institutional investor to enter the Chinese A-Shares market was *insurance companies*.[67] In 1980, China's domestic insurance business resumed and the management of insurance funds progressed substantially after the open-door and economic reform policies.[68] In 2004, the China Insurance Regulatory Commission (CIRC) gave the greenlight to insurance companies to directly invest in the stock market.[69] Initially, insurance companies and their asset management subsidiaries could only invest up to 5% of their total assets into the A-Shares market.[70] Despite this restriction, as shown in Chart 1 and Chart 2 above, in 2005, insurance companies quickly came to hold 4% of the market capitalization and 13.4% of the free-float of the A-Shares market. In 2009, the revised insurance law expanded the scope of investments permitted for insurance companies, which allowed them to indirectly invest in the stock market through SIFs.[71] In 2014, the CIRC raised the limit of the proportion of the assets that insurance companies can invest in equities to 30%.[72]

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[66] Asset Management Association of China, 公募基金行业数据 [*Public Fund Industry Data*], http://www.amac.org.cn/researchstatistics/datastatistics/mutualfundindustrydata/.

[67] The three types of funds that insurance companies have include: (1) the "funds owned by an insurance company" (保险公司自有资金), which refers to the funds accumulated through insurance premiums paid by the insured or the policyholder as well as the funds provided by its investors during its establishment; (2) "insurance products" (保险产品), which refer to the financial instruments, products and services provided by insurance companies to their customers in the insurance market; and, (3) "insurance asset management products" (保险资管产品) which are financial products that are not for public distribution. The insurance company issuing asset management products may sell them by themselves or entrust the products to other institutions to sell them with a commission. Institutions allowed to sell such products on behalf of the insurance company are financial institutions or institutions recognised by the CBRC, such as banks, insurance companies, securities brokerages, trusts, etc.

[68] 杨倩雯 (Yang Wenqian), 中国保险 70 年：从保险大国走向保险强国 [70 Years of Insurance in China: From a Big Insurance Country to a Strong Insurance Country] YICAI (Aug. 15, 2019), https://www.yicai.com/news/100297014.html.

[69] *See* Xu Binglan, *Insurance firms get greenlight on stocks*, CHINA DAILY (Oct. 25, 2004), http://www.chinadaily.com.cn/english/doc/2004-10/25/content_385567.htm.

[70] 保险机构投资者股票投资管理暂行办法[Interim Measures for the Administration of Stock Investments of Insurance Institutional Investors], promulgated by CIRC and CSRC on Oct. 24, 2004.

[71] National People's Congress (NPC), INFORMATION ON THE REVISION OF INSURANCE LAW (Mar. 2, 2009), http://www.npc.gov.cn/zgrdw/huiyi/lfzt/bxf/2009-03/02/content_1480632.htm.

[72] 中国保险监督管理委员会关于加强和改进保险资金运用比例监管的通知 [Notice of the China Insurance Regulatory Commission on Strengthening and Improving the Proportional Regulation of the Utilization of Insurance Funds], promulgated by CIRC on Jan. 23, 2014, Article 2.

The CCP has actively encouraged insurance companies to increase their investment in the A-Shares market. In 2018, as shown in Chart 1 and Chart 2 above, 3.5% of the capitalization and 9.0% of the free-float of the A-Shares market are owned by insurance companies. In 2019, the premiums collected by the Chinese insurance industry totaled RMB4.26 trillion, ranking third in the world in terms of their total size, after the United States and Japan.[73] As less than 20% of insurance funds are currently invested in equities – and the cap is 30% – there is scope for future growth in the size of the investment by insurance companies in the A-Shares market.[74]

The third major type of domestic institutional investor to enter the Chinese A-Share market were *pension funds*. The public pension fund market is bifurcated between government pension funds – which are called *social security funds* (SSFs) – and corporate pension funds – which are called *enterprise annuities*. SSFs exist at the local and national levels, the largest of which is the National Social Security Fund (NSSF).

Established in 2000, the NSSF's operations are governed by the Ministry of Finance (MOF) and the Ministry of Labor and Social Security (MOLSS, currently dissolved); while the CSRC and PBOC supervise the activities of the NSSF's investment managers and are the custodians of its funds. From 2001 to 2016, several laws have been promulgated to increase the rate of return of NSSF funds.[75] One of the major initiatives has been to facilitate the NSSF in investing a portion of its funds in the A-Shares market. Initially, the NSSF invested directly in the A-Shares market. However, since 2003, the NSSF has outsourced a portion of its investments to private fund managers,[76] resulting in it being both a direct and indirect investor in the A-Shares market.[77] The portion of the NSSF's total funds that can be invested directly and indirectly in A-Shares is currently capped at 40%.

As illustrated in Chart 1 and Chart 2 above, in 2006, SSFs accounted for 0.9% of capitalization and 3.9% of the free-float of the A-Shares market. Although the size of the NSSF has grown

[73] 2020 年全国各地区原保险保费收入情况表[Original Insurance Premium Income in Various Regions of the Country in 2020], promulgated by CBIRC on Jan. 28, 2021, https://www.cbirc.gov.cn/cn/view/pages/ItemDetail.html?docId=963083&itemId=954&generaltype=0.

[74] *See* 2020 年保险业经营情况表[Insurance Operation Status in 2020], promulgated by CBIRC on Jan. 28, 2021, https://www.cbirc.gov.cn/cn/view/pages/ItemDetail.html?docId=887993&itemId=954&generaltype=0.

[75] Since 2001, various regulations were issued to facilitate the development of SSF, including: 全国社会保障基金投资管理暂行办法 [Interim Provisions on the Administration of Investment by the National Social Security Fund], promulgated by MOF and MOLSS on Dec. 13, 2001; 全国社会保障基金境外投资管理暂行规定 [Interim Provisions on the Administration of Overseas Investment by the National Social Security Fund], promulgated by MOF, MOLSS and PBOC on Mar. 14, 2006; 全国社会保障基金条例[Regulation on the National Social Security Fund], promulgated by the State Council on May. 1, 2016.

[76] 经济观察网, "2003 年 社保基金正式进入股市 [National Social Security Fund (NSSF) entered into an agreement with 6 fund management companies in 2003 and entrusted them to make investments in the A-share market], SINA (Apr. 9, 2018), http://finance.sina.com.cn/stock/marketresearch/2018-04-09/doc-ifyteqtq6470236.shtml.

[77] Zhou Jingya, 间接参与"股指期货融资融券[NSSF Indirectly Invested in Index Funds], CBN DAILY NEWS (Mar. 30, 2010), https://finance.qq.com/a/20100330/000302.htm.

substantially over the past decade – the total capitalization of the A-Shares market has increased concomitantly. As a result, over the last decade, SSFs have consistently accounted for approximately 1% to 2% of the total capitalization and 2% to 4% of the free-float of the A-Shares market.

In 2011, the revised Measures for the Management of Enterprise Annuity Funds was promulgated, which limited the amount that corporate pension funds could invest in equities to 30% of their financial net worth. As shown in Chart 1 and Chart 2 above, corporate pension funds started investing in the A-Shares market in 2012. Presently, corporate pension funds remain a small portion of the A-Shares market, accounting for less than 0.5% of its capitalization and free float – but they have been increasing gradually in importance since 2007 and their total cumulative value likely reached 300 billion yuan by the end of 2020.[78]

The fourth major type of domestic institutional investor to enter the Chinese A-Shares market were Chinese *securities institutions.* Securities institutions (*zheng quan ji gou/quan shang*) are the Chinese version of international investment banks. They invest their own capital and the capital of their clients in a variety of investments, including the A-Shares market. [79] In 2007 and 2014, the government enacted several policies which provided greater access to, and accelerated trading in, the A-Shares market. These reforms appear to have sparked the establishment of securities institutions as significant institutional investors in 2007 and propelled their growth after 2014. As shown in Chart 1 and Chart 2 above, securities institutions first accounted for an extremely small percentage of the A-Shares market in 2007; but since 2016 have consistently accounted for approximately 1% of the total capitalization and 3% of the free-float of the market.

The fifth major type of domestic institutional investor to enter the Chinese A-Share market were *trust companies*. Prior to 2012, the CSRC had strict restrictions on the ability of trust companies to hold A-Shares. In August 2012, a notice was issued to officially abolish the restrictions on trust companies investing their funds on the stock exchange.[80] As of 2018, trust companies accounted for 0.7% of the total capitalization and 1.5% of the free-float of the A-Shares market.

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[78] Deng Xiongying, 3 万亿年内可破！年金规模进入爆发增长期，权益投资占比有望上升 [Corporate Pension Fund Growth burst], SECURITIES DAILY (Oct. 5, 2020), https://news.stcn.com/sd/202010/t20201005_2407640.html.

[79] As shown in the taxonomy of institutional investors in China's A-shares market in Chart 3 above, there are four types of securities institutions in China: (1) "brokerage proprietary securities" (券商自营), which refers specifically to securities companies investing in their own name, with their own funds or with other funds, buying and selling securities products for themselves; (2) "brokerage collective wealth management firms" (券商集合理财), which is also known as the "collective asset management business", and refers to a financial product issued by a securities company that pools the assets of its clients and is managed by professional investors (brokerage firms); (3) "directed asset management securities firms" (券商定向资管), which mainly refers to the activities of securities firms accepting single client entrustment, signing contracts with clients, and managing client entrusted assets through clients' accounts according to the manner, conditions, requirements and restrictions agreed in the contracts; and, (4) "dedicated asset management by securities companies" which mainly refers to asset securitization financing (券商专项计划).

[80] 中国证券登记结算有限责任公司关于信托产品开户与结算有关问题的通知[Notice of the China Securities Depository and Clearing Corporation Limited on Issues Concerning the Account Opening and Settlement for Trust

The sixth major type of domestic institutional investor to enter the Chinese A-Share market were *private investment funds*. These are private funds, which normally receive their capital from high-net-worth individuals and are managed by investment professionals who launch such funds. Private investment funds have existed since the early 2000s. However, historically, due to legal restrictions on the establishment of private investment funds, they could only invest in the stock market indirectly by opening accounts in the name of corporations, partnerships, or purchasing products from trust companies. This restriction resulted in private investment funds incurring high operational costs. In 2014, the Securities Investment Fund Law was amended to explicitly recognize private investment funds and permit them to open trading accounts to invest directly in the A-Shares market.[81] As can be seen in Chart 1 and Chart 2 above, this change in the law created a significant new category of institutional investor, which by 2018 accounted for 3.6% of the total capitalization and 9.2% of the free-float of the A-Shares market.

There are four conclusions that can be drawn from the domestic side of the China institutional investor taxonomy. First, the government has consistently promoted the growth of institutional investors in the A-Shares market. Since the 1990s, the government has had an explicit policy to expand the size and scope of domestic institutional investors. It has achieved this by making the growth of institutional investors an explicit policy of the CCP and, in turn, by consistently promulgating laws relaxing investment restrictions to encourage an increasingly wide scope of financial institutions and investment managers to invest their capital in the A-Shares market. This has made domestic institutional investors the primary driver of the growth of institutional investors in China and resulted in China having the world's most important growth market for assets under management.

Second, as China's market for institutional investors has grown it has become increasingly atomized. As illuminated above, before 2005, SIFs were the only significant institutional investor in the A-Shares Market and until 2010 they accounted for more than 50% of the market. However, today, there are at least six major categories of institutional investors – none of which hold more than 4% of the total capitalization of the A-Shares market. This atomization of institutional investors requires a more nuanced understanding of what drives each of the varieties and provides a caution about speaking generally about "institutional investors" in China – which may have been more justified in the early 2000s when SIFs dominated the market.

Third, as discussed in more detail in Part IV below, the different varieties of domestic institutional investors have different levels of independence from the government. For example, most trust

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Products], promulgated by China Securities Depository & Clearing Co., Ltd. (CSDC) on Aug. 31, 2004. http://www.chinaclear.cn/old_files/1346407535100.pdf

[81] CSDC, *Zhou Ming: Private Investment Funds Now Admitted for Account Opening and Trading* (Apr. 1, 2014), http://www.chinaclear.cn/english/sdc/201404/017e5994a0f34ba680b4ced5dd8f7a18.shtml.

companies[82] and securities companies[83] are SOIIs and, therefore, the CCP can more directly control their engagement and voting policies as institutional investors – which may allow the CCP to utilize them more directly for policy channeling. While some of the largest insurance companies are SOEs, there has been a proliferation of private insurance companies who act as POIIs in China. As such, as explained in Part IV, these POIIs are more independent from the CCP, but the CCP may still use its indirect control over them for policy channeling. Also, the empirical research and our hand-collected evidence from Activist Campaigns in Part III demonstrates the need to recognize the varieties of institutional investors in China – especially the distinction between SOIIs, POIIs, and FOIIs – as this appears to affect their impact on corporate governance.

Fourth, even if all institutional investors were to speak with one voice (which is clearly not the case), collectively institutional investors will still be minority shareholders in almost every Chinese listed company. This is significant as it distinguishes China from the UK and US, where institutional shareholders collectively control a majority of shares in most listed companies – which gives them the legal right to collectively "steward" them.[84] However, in China, similar to in most non-UK-US jurisdictions, the ability of institutional investors to collectively steward listed companies normally does not exist – which makes understanding the role institutional investors can play as minority shareholders, in the context of companies with a dominant controlling block shareholder, critically important. As our hand collected evidence from Activist Campaigns by institutional investors who are minority shareholders in Part III demonstrates, increasingly institutional investors are engaging in shareholder activism to spur corporate governance change. As expected, these campaigns tend to be in A-Shares companies with more dispersed shareholders. However, somewhat surprisingly, SOIIs have led the majority of these Activist Campaigns, and, in some cases, have succeeded in these campaigns against SOEs. It is to this that we now turn.

III. FILLING THE GAP IN THE LEGAL LITERATURE ON INSTITUTIONAL INVESTORS IN CHINA: EMPIRICAL RESEARCH AND ACTIVIST CAMPAIGNS

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[82] *See* 2021年最新68家信托公司注册资本及股东背景[Registered Capital and Shareholder Background of 68 Trust Companies in 2021], SINA FINANCE (Feb. 22, 2021), https://finance.sina.cn/fund/sm/2021-02-22/detail-ikftpnny9049345.d.html?from=wap.

[83] 8 out of the top 10 securities companies are actually controlled by the government, including Huatai Securities Co., Ltd. (the actual controller is SASAC of Jiangsu Province), Guotai Junan Securities Co., Ltd. (the actual controller is SASAC of Shanghai City), China Merchants Securities Co., Ltd. (the actual controller is State Council), Shenwan Hongyuan Group Co., Ltd. (the actual controller is State Council), Haitong Securities Co., Ltd. (the actual controller is SASAC of Shanghai City), China Galaxy Securities Co., Ltd. (the actual controller is State Council), CICC (the actual controller is State Council), and China Securities Co., Ltd. (the actual controller is SASAC of Beijing City). See, 证券公司 2020 年经营业绩指标排名情况[Ranking of Securities Companies by 2020 Operating Performance Indicators], promulgated by Securities Association of China (SAC) on Jun. 18, 2021, https://www.sac.net.cn/hysj/zqgsyjpm/202106/P020210621502887608210.pdf; The information of actual controller is taken from "Qichacha" (an enterprise information enquiry system): https://www.qcc.com/ (accessed July 15, 2021).

[84] Dan W. Puchniak, *The False Hope of Stewardship in the Context of Controlling Shareholders: Making Sense Out of the Global Transplant of a Legal Misfit*, AM. J. COMP. L. (forthcoming 2021).

(a) Illuminating the Gap in the Legal Literature

As demonstrated in Part II, there has been a meteoric rise in the size, ownership stake, and free-float of shares that institutional investors have in the A-Shares market. However, as noted above, the rise of institutional investors in China has been almost entirely overlooked in the legal literature.[85] This is somewhat surprising as the role of institutional investors in corporate governance – particularly in the United States and United Kingdom – has become a major focal point for many of the most prominent corporate law scholars.[86]

We suspect that this gap in the legal literature may have arisen for three reasons. First, comparative corporate law scholars have primarily focused on the Chinese government as China's most powerful controlling shareholder through its ownership of non-financial SOEs – which may have caused the rise in the shareholder power of institutional investors to be overlooked.[87] Second, the atomization of China's institutional investors highlighted in Part II may have made the collective rise of institutional investors in China less conspicuous and makes analyzing their impact on corporate governance more complex. Third, the rise of institutional investors in China is uniquely domestically driven, with the big three American institutional investors – which have been the focus of considerable academic attention – playing an inconsequential role in its development.[88]

However, despite the dearth in legal scholarship, over the past decade, there have been a number of empirical studies in the business school literature that provide interesting insights into the role played by institutional investors in Chinese corporate governance. As these studies use different datasets, cover different time periods, and focus on different issues, as would be expected, there is some variation (and even incongruency) in their findings. Also, as many of the empirical studies focus on data which extends back over a decade, the focus has tended to be on SIFs – which makes sense because, as shown in Part II, SIFs were the only significant institutional investor in the A-Shares market until 2005 and until 2010 they accounted for more than 50% of the market.[89]

Keeping these limitations in mind, we analyze this interesting body of empirical studies below. In addition, we attempt to address some of the shortcomings in the empirical studies by analyzing our hand collected summary of the publicly reported representative Activist Campaigns that institutional investors have undertaken in China (see Appendix 2). Ultimately, the empirical

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[85] Xi, *supra* note 24.

[86] Bebchuk et al., *supra* note 25, at 92-93; Coates, *supra* note 25, at 2-5; Fisch, *supra* note 25; Gilson & Gordon, *supra* note 25, at 865, 874–876.

[87] Lin & Milhaupt, *supra* note 7; Wang, *supra* note 13; Howson, *supra* note 9, at 51-52; Milhaupt, *supra* note 6, at 362; Wang & Tan, *supra* note 10, at 1094.

[88] Jan Fichtner & Eelke M. Heemskerk, *The New Permanent Universal Owners: Index Funds, Patient Capital, and the Distinction between Feeble and Forceful Stewardship*, 49(4) ECON. & SOC'Y (2020); Lucian Bebchuk & Scott Hirst, *The Specter of the Giant Three*, 99 B.U. L. REV. 721 (2019); Lucian Bebchuk & Scott Hirst, *Index Funds and the Future of Corporate Governance: Theory, Evidence, and Policy*, 119 COLUM. L. REV. 2029 (2019).

[89] See *supra* Part II.

studies and Activist Campaigns demonstrate that the taxonomy of institutional investors analyzed in Part II matters, as different types of institutional investors appear to play different roles in Chinese corporate governance. Also, the empirical studies and Activist Campaigns suggest that the influence that the government has over SOIIs – and, in some instances, POIIs – may have a significant effect on their impact on corporate governance. Relatedly, there is some evidence that the impact that institutional investors have on the corporate governance of their investee companies may be contingent on whether the investee company is an SOE or POE. Importantly, and somewhat surprisingly, our analysis also reveals that SOIIs have undertaken a majority of the Activist Campaigns and that SOEs have been the target of a number of successful Activist Campaigns.

Taken together, these results highlight the important impact that the CCP's ability to influence SOIIs, and in some cases POIIs, has on the function they play in Chinese corporate governance – and how the insulation of FOIIs from the CCP's influence matters. The mechanisms and tactics that the CCP uses to wield its influence, and the policy channeling reasons for wielding its influence, are the focus of Part IV. For now, we turn to analyzing the interesting body of empirical studies for a more granular view of the impact of institutional investors in Chinese corporate governance.

(b) An Analysis of the Existing Empirical Research

Keeping in mind the limitations on the empirical studies highlighted above, there are at least three meaningful general observations that can be drawn from this body of empirical research. First, most of the empirical studies find that the impact that institutional investors have on the corporate governance of A-Shares companies is contingent on the *type of institutional investor* – with statistically significant differences in several studies being found between domestic institutional investors and foreign institutional investors,[90] and between SIFs and other types of institutional investors.[91] Second, several empirical studies find a statistically significant difference in the impact that certain institutional investors have on corporate governance based on the extent to which the institutional investor is *insulated from government pressure* – due to their size,

[90] Yongjia Rebecca Lin & Xiaoqing Maggie Fu, *Does institutional ownership influence firm performance? Evidence from China*, 49 INT'L. REV. ECON. FIN. 17 (2017) (results show that foreign and large institutional shareholders have the greatest positive effects on firm performance); Huang & Zhu, *supra* note 42 at 324 (results suggest that foreign institutional investors are less prone to political pressure from the controlling state shareholders and are more likely to perform an unbiased monitoring role); Reena Aggarwal, May Hu & Jingjing Yang, *Fraud, Market Reaction, and the Role of Institutional Investors in Chinese Listed Firm*, 41 J. PORT. MGMT. 92, 107 (2015) (results show the opposite, that domestic mutual funds are the only type of institutional investor who will play any role in monitoring).

[91] Several articles generally suggest that SIFs, more so than other institutional investors, are the best at corporate governance monitoring as compared to other institutional investors: Michael Firth et al., *Institutional stock ownership and firms' cash dividend policies: Evidence from China*, 65 J. BANKING & FIN., 91, 105 (2016); Jing Chi et al., *Institutional stock ownership and firm innovation: Evidence from China*, 50 J. MULTINATL. FIN. MGMT. 44, 55 (2019); Amon Chizema et. al, *Mutual funds, tunneling and firm performance: evidence from China*, 55 REV. QUANT. FIN. 355, 382-83 (2020).

independence from direct government ownership, or foreign status.[92] Third, several empirical studies find that the impact that institutional investors have on the corporate governance of A-Shares companies is contingent on the *type of company* in which institutional investors own shares – with statistically significant differences in several studies being found between SOEs and POEs.[93]

Collectively, these observations confirm that the taxonomy of institutional investors analyzed in Part II is important as there is significant empirical evidence demonstrating that the impact of institutional investors on corporate governance in China's A-Shares companies differs based on the type of institutional investor. The empirical evidence confirming the importance of the extent to which institutional investors are insulated from government pressure suggests that there is also a need to understand the channels through which the government influences institutional investors and the extent to which different types of institutional investors are influenced by these policy channels – which is the focus of Part IV below. The empirical evidence that the impact of institutional investors on corporate governance differs depending on whether the investee company is a SOE or POE requires further analysis – which is also provided in Part IV below.

A review of these empirical studies also suggests some more specific normative implications of the rise of institutional investors on Chinese corporate governance. Several studies suggest that SIFs – particularly domestic SIFs when compared with other types of institutional investors – improve the corporate governance of A-Shares companies. Yuan, Xiao, and Zou (2008), published a pioneering study that found statistically significant empirical evidence that ownership by domestic SIFs had a positive impact on the performance of A-Shares companies[94] – which has been repeatedly cited in support of the Chinese government's consistent effort over the past two decades to promote SIFs as a valuable corporate governance mechanism.[95] In a later article, Aggarwal, Hu, and Yang (2015), found that domestic SIFs are the only type of institutional investor to play a positive monitoring role in Chinese corporate governance – based on a positive correlation between higher domestic SIF ownership and lower fraud.[96] They also suggest that foreign institutional investors are ineffective monitors due to their small ownership stakes and other domestic institutional investors (i.e., insurance companies, pension funds, and trusts) are compromised by their business relationships with the investee companies they are supposed to monitor.[97]

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[92] Lin & Fu, *supra* note 90, at 18.
[93] *Id*.
[94] Rongli Yuan et al., *Mutual funds' ownership and firm performance: Evidence from China*, 32 J. BANKING & FIN. 1552, 1563 (2008).
[95] Lin & Fu, *supra* note 90, at 18.
[96] Aggarwal et al., *supra* note 90, at 107.
[97] *Id*.

In a similar vein, Firth et al. (2016) conclude that SIFs improve corporate governance monitoring based on evidence of a positive correlation between SIF ownership and higher cash dividends – which is absent with respect to other institutional investors such as banks, insurance companies, and securities companies.[98] Chi, Liao, and Yang (2019) similarly find that SIFs significantly increases firm innovation, but this effect is not found for other types of institutional investors, such as insurance companies, pension funds, or QFIIs.[99] Chizema et al. (2019) also find that an increase in SIF ownership improves firm performance in A-Shares companies by effectively mitigating the tunneling behavior of controlling shareholders.[100]

Collectively, these empirical studies suggest that SIFs – particularly domestic SIFs in comparison to other types of institutional investors – improve the corporate governance in A-Shares companies. However, for three reasons, this conclusion may not be as definitive as it appears. First, all these studies suffer from the risk of endogeneity as it makes sense that SIFs would invest in companies with better corporate governance, raising the specter of reverse causality. Second, none of these studies provide a detailed explanation of how SIFs, with their minority shareholdings, produce a statistically significant impact on corporate governance. Third, many of these studies are based on at least some pre-2010 data, which precedes the atomization of institutional investors and was a time when SIFs dominated the institutional investors market – which raises the possibility that other types of institutional investors may now have a greater impact given their increased shareholdings. However, even considering these complicating factors, this body of empirical evidence suggests that there is reason to believe that domestic SIFs appear to improve Chinese corporate governance by acting as a monitor of corporate controllers.

In this context, it is noteworthy that one of the most cited empirical studies on the impact of institutional investors in the A-Shares market provides strong empirical evidence that in certain circumstances the government can – and will – also exert political pressure on SIFs to achieve its political and economic objectives. Historically, the A-Shares market was divided into tradable and non-tradable shares. In 2005, to remedy the incentive and corporate governance problems created by this unique feature of the A-Shares market, the Chinese government initiated the "split share structure reform" to convert non-tradable shares into tradable shares.[101] To compensate non-tradable shareholders for the dilution in their stock values that would result from the reform, the government established a requirement that in each company an amount of compensation had to be proposed by the non-tradable shareholders to the tradable shareholders, and that the proposal had to be approved by two-thirds of the tradable shareholders for the reform to be finalized.[102] If the proposal was not approved, a three-month waiting period was required before another proposal could be put forward – which would delay the reform process and, if it occurred in too many

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[98] Firth et al., *supra* note 91, at 105 (Without examining the distinction between foreign and domestic SIFs).

[99] Chi et al., *supra* note 91, at 55.

[100] Chizema et al., *supra* note 91, at 382-83.

[101] Huang & Zhu, s*upra* note 42, at 313.

[102] *Id.*

companies, would be seen as a blackmark on the government officials responsible for the reform.[103] As an earlier attempt at reforming China's unique split share structure in 2001 had failed, the CSRC was determined for this new reform scheme to proceed smoothly and it set the end of 2006 as the deadline for all A-Shares companies to complete the reform.[104]

Firth, Lin, and Zou (2010) examined the impact of state shareholders and SIFs on the amount of the compensation received by tradable shareholders in the split share reform of A-Shares companies. They found that there was a positive statistically significant relationship between state ownership and the compensation received by tradable shareholders.[105] Considering the earlier failed attempt to reform the split share structure, they reasoned that the government bureaucrats overseeing the non-tradable shares in SOEs had strong incentives to offer higher compensation to tradable shareholders as this would ensure the reform proceeded as quickly as possible by setting a positive example for other A-Shares companies to follow.[106] It would also advance the government's goal of listing more SOEs as it would avoid shareholder conflict and create favorable investor sentiment.[107] For the bureaucrats proposing the compensation packages on behalf of the non-tradable shares, completing the reform quickly would provide them with political credit for executing the reform successfully, which would move them up the political hierarchy.[108] Thus, the empirical evidence that bureaucrats in SOEs offered statistically significant higher compensation to tradable shareholders makes perfect sense – it allowed bureaucrats to capture political benefits of control by executing an efficient reform, while not suffering any direct consequences of providing higher compensation which came from the government. Conversely, in POEs, where private investors owned non-tradable shares, they would directly suffer the cost of providing higher compensation to tradable shareholders and would not receive any political benefits for an efficient reform – which explains why in POEs there was statistically significant lower compensation provided to tradable shareholders.

Interestingly, Firth, Lin, and Zou also found a statistically significant negative relationship between SIF ownership of tradable shares and the amount of compensation provided to tradable shareholders – which is contrary to the evidence from the other empirical studies reviewed above that SIFs improve corporate governance and protect (minority) shareholders' interests.[109] They also found that SIF "ownership weakens the positive link between state ownership and

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[103] *Id.*

[104] Robin Hui Huang, *The New Takeover Regulation in China: Evolution and Enhancement*, 42 INT'L LAW. 153, 156-157 (2008).

[105] Michael Firth et al., *Friend or Foe? The Role of State and Mutual Fund Ownership in the Split Share Structure Reform in China*, 45 J. FIN. & QUANT. ANAL. 685, 697 (2010).

[106] *Id*. at 690.

[107] *Id.* at 689.

[108] *Id.* at 689-690.

[109] *Id.* at 697.

compensation, suggesting that [SIFs] help state-owned firms get the reform done more quickly and at a relatively lower cost".[110]

Importantly, Firth, Lin, and Zou identified and explained a unique policy channel that was used in the context of this reform to put pressure on domestic SIFs to work with the government to ensure a quick and noncontentious reform. Specifically, for the purpose of the split share reform, the CRSC removed the authority from fund managers who normally decide how to vote shares under their management based on market forces and reallocated the decision over voting rights to the Investment Decision Committee (IDC) of the fund management companies.[111] As explained in more detail in Part IV, this reallocation of voting rights was critically important as the CSRC has a veto power over the appointment and removal of the members of the IDCs of fund management companies,[112] who are often former government officials and CCP members. Also, to speed up the reform process "the CSRC put direct pressure on mutual funds to vote in the interest of expediting the reform… [by holding] regular meetings with all fund management firms and [using] these occasions to stress the need for reaching a speedy and noncontentious conclusion to the share structure reform proposals".[113]

Firth, Lin, and Zou also found a statistically significant negative relationship between ownership of voting shares by other institutional investors (e.g., insurance companies, securities companies, and investment trusts) and compensation.[114] They concluded that this empirical finding may be due to the relationship these other institutional investors have with the management of the investee companies – which would provide an incentive for these other institutional investors to support the compensation proposed by the management that was backed by non-tradable shareholders.[115] Importantly, they also posit that these other institutional investors "are owned by the state [and] may also be under pressure from the CSRC to agree to the compensation terms" – suggesting that these other institutional investors were also coopted by government pressure to ensure that the split share reform was quick and noncontentious.[116]

In another follow-up study on the split share reform, Huang and Zhu (2015) confirmed the statistically significant positive relationship between state ownership and higher compensation.[117]

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[110] *Id.* at 703.

[111] *Id*. at 693. See also, 刘瑛 [Liu Ying], 股改投票权上收 基金经理翻云覆雨难, [It is difficult for fund managers to participate in split share reform as the voting right is reallocated], CHINA BUSINESS NEWS (Aug. 31, 2005), http://futures.money.hexun.com/1303024.shtml.

[112] SECURITIES INVESTMENT FUND LAW OF THE PEOPLE'S REPUBLIC OF CHINA, STANDING COMMITTEE OF THE ELEVENTH NATIONAL PEOPLE'S CONGRESS OF THE PEOPLE'S REPUBLIC OF CHINA, adopted on Oct. 28, 2003 and revised on Dec. 28, 2012.

[113] Firth et al., *supra* note 105, at 692.

[114] *Id.* at 697.

[115] *Id.*

[116] *Id.* at 698.

[117] Huang & Zhu, *supra* note 42, at 314.

They also confirmed that this positive relationship decreased with the level of SIF ownership – suggesting that "the controlling state shareholders may exert political influence on [SIF] managers and offer a lower compensation ratio for companies with [SIF] ownership".[118] Huang and Zhu then extended on Firth, Lin, and Zou's research by examining the relationship between compensation and QFIIs. They found a statistically significant positive relationship between the level of QFII ownership and compensation, "suggesting that QFIIs are less prone to political pressure".[119] Based on several statistically significant empirical findings, they concluded that "foreign institutional investors are less prone to political pressure than their local peers and are more likely to perform arm's length monitoring".[120] In Part IV, we identify and explain the specific regulatory architecture which makes it clear why this is the case.

There are five important observations that can be derived from the empirical evidence from the split share reform. First, it demonstrates how the CCP's influence over institutional investors can be used for policy channeling – which reaffirms the importance of understanding how the policy channels for institutional investors work as they can turn the role of institutional investors on its head. Second, it demonstrates how different types of institutional investors are impacted differently by policy channeling (in this case, the difference between domestic and foreign institutional investors) and how understanding the extent to which the CCP can influence different types of institutional investors is critically important. Third, it demonstrates how the CCP may quickly rearrange the regulatory environment – in this case by reallocating the decision over voting rights from fund managers to the IDC – to enhance its ability to use certain types of institutional investors for policy channeling in particular situations. Fourth, it demonstrates how even when the CCP wants to policy channel free market forces remain important – in this case the CCP could have decided the level of compensation by fiat, but instead it chose to subject the compensation to market forces and then to use policy channeling to shape the outcome.[121] Fifth, the ability for foreign institutional investors to have a significant impact was unique in this case. As the compensation offered by non-tradable shareholders had to be approved by two-thirds of tradable shareholders this increased the voice of foreign institutional investors which, as highlighted in Part II, normally only own a small minority of shares in A-Shares companies. Also, on average, only 35% of tradable shareholders chose to exercise their votes in the split share reform proposals – suggesting that a (foreign) tradable shareholder with as little as 3.5% of the total shares may have

[118] *Id.*
[119] *Id.* at 319-320.
[120] *Id.* at 314.
[121] It should be noted that before the split share structure reform in 2005, the State Council issued a government-imposed reform plan in 2001 to sell the non-tradable shares at the market price to make them tradable. However, this reform was followed by a plunge in the share price. To stabilize the A-shares Market, the CSRC announced the suspension of the reform. In 2005, after the unsuccessful experience of government-imposed reform, the CSRC chose the split share structure reform where the tradable shareholders could receive compensation subject to market forces. See Huang, *supra* note 104.

been able to veto the proposal, making the split shareholder reform atypical in terms of the ability of small minority foreign institutional investors to have formal veto power.[122]

However, even outside of the context of the split share reform, there is a body of empirical research which suggests that foreign institutional investors may have a positive impact on the corporate governance of A-Shares companies – with the most consistent evidence of this effect in POEs (and sometimes contrary evidence in SOEs). Hai, Min, and Barth (2018), found a statistically significant positive relationship between QFII ownership and various measures of good corporate governance, which suggests QFII's reduce agency costs.[123] However, this effect disappeared in SOEs, which they attributed to the negative effects of political pressure in SOEs on the ability of QFIIs to improve corporate governance.[124] Liu, Bredin, and Cao (2020), found a statistically significant positive relationship between the presence of QFIIs and better operating performance in A-Share companies, with this positive effect less pronounced in SOEs.[125] Li found a statistically significant negative relationship between QFII holdings and wealth tunneling, but this effect was less pronounced in SOEs.[126] Lin and Fu (2017) found statistically significant empirical evidence demonstrating that institutional investor ownership positively affects the performance of A-Shares Companies – with pressure-insensitive, foreign, and large institutional shareholders having greater positive effects on firm performance than pressure-sensitive, domestic, and small institutional shareholders.[127] Liu et al. (2018), found statistically significant strong empirical evidence that QFII and SIF ownership significantly improve corporate transparency and governance.[128]

Taken together, this empirical evidence seems to suggest that foreign institutional investors have a positive impact on corporate governance in A-Shares companies – especially in POEs. It also suggests that understanding the role played by the state is critically important for understanding the impact of institutional shareholders in China – as the positive corporate governance impact of foreign institutional investors seems to be negatively impacted when the state is the controlling shareholder in SOEs. However, as shown in Part II and acknowledged in several of these studies,[129] foreign institutional investors *collectively*, on average, have only accounted for between approximately 1% to 3% of A-Shares market capitalization over the past two decades, which makes the consistent empirical evidence of their positive impact on corporate governance

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[122] Firth et al., *supra* note 105, at 690.
[123] Jiang Hai et al., *On Foreign Shareholders and Agency Costs: New Evidence from China*, 54 EMERG. MKT. FIN. & TRADE 2815, 2831 (2018).
[124] *Id.* at 2821.
[125] Liu et al., *supra* note 53, at 14.
[126] Zhengyu Li, *The Impact of Qualified Foreign Institutional Investors on Controlling Shareholder's Tunneling: Evidence of Listed Companies in China*, 7 AM. J. INDUS. & BUS. MGMT. 522, 534 (2017).
[127] Lin & Fu, *supra* note 90, at 54 (i.e., institutional investors lacking a business relationship with the investee company).
[128] Ningyue Liu et al., *Institutional ownership and corporate transparency in China*, 24 FIN. RES. LETTERS 328, 332 (2018).
[129] Liu et al., *supra* note 53, at 14; Lin & Fu, *supra* note 90, at 17.

somewhat puzzling. Also, similar to our observation regarding the empirical evidence that domestic SIFs have a positive impact on corporate governance, the fact that foreign institutional investors are likely to invest in companies that have better corporate governance, raises the possibility that these studies are confounded by reverse causality.

The opacity of exactly how foreign institutional investors may exercise their minority power to have a statistically significant impact on corporate governance highlights an issue that cuts across all types of institutional investors in the A-Shares market. As explained in Part II, although there has been a meteoric rise in the overall percentage of institutional investors in the A-Shares market from 1.4% in 2003 to 18.7% in 2018[130]collectively they still, on average, make up a minority of shareholders in A-Shares companies – and most A-Shares companies have a dominant controlling shareholder. This raises the question of exactly how institutional investors have exercised their power to impact corporate governance in A-Shares companies.

To shed some light on this question, we now consider our individual hand-collected case studies that provide a window into exactly how institutional investors have had an impact on the corporate governance of A-Shares companies.

(c) Activist Campaigns: How Institutional Investors as Minority Shareholders Impact Corporate Governance in China

To gain a better understanding of how institutional investors may be having an impact on the corporate governance in A-Shares companies, we undertook an extensive search using Chinese and English language sources to attempt to locate all the reported representative instances in which institutional investors have taken steps to intervene in the corporate governance of A-Shares companies (Activist Campaigns).[131] Based on our detailed review of all of the reported representative Activist Campaigns that we could locate, a summary of which is in Appendix 2 below, they reveal six important insights about how institutional investors in China have had an impact on corporate governance.

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[130] *See supra* Part II.

[131] To attempt to locate all reported instances in which institutional investors have taken steps to intervene in the corporate governance of A-Shares companies, we took the following steps: for Activist Campaigns that occurred from 1994 to 2015, we extracted the information about Activist Campaigns from a research report prepared by the Shanghai Stock Exchange, which is considered to be the most accurate record of Activist Campaigns for this period: Xinchun Wu, 大力推进机构投资者参与上市公司治理 [Vigorously Promoting Institutional Investors' Participation in the Governance of Listed Companies], SHANGHAI STOCK EXCHANGE CAPITAL MARKET RESEARCH INSTITUTE (2015), http://www.sse.com.cn/aboutus/research/research/c/3986593.pdf. In June 2021, for Activist Campaigns that occurred from 2016 to 2021, we searched in Chinese and English on the internet for activist campaigns involving institutional investors. We used several search engines and library databases for our searches which used a variety of key words including: "activist shareholder campaigns" ("激进股东活动"), "shareholder activism" ("股东激进主义"), "institutional investor activism" ("机构投资者激进主义"), "institutional shareholder activism" ("机构股东激进主义") , "institutional shareholder lawsuits" ("机构股东诉讼"), "institutional shareholder veto" ("机构股东否决"), and "institutional shareholder proposals" ("机构股东提议").

First, institutional investors have not used Activist Campaigns to intervene in the corporate governance of A-Shares companies very often. As shown in Appendix 2, from 1994 to 2021, there were only 43 Activist Campaigns, which on average amounts to 1.54 campaigns per year. By comparison, from 2018 to 2020, there were 116 activist campaigns per year in the United States.[132] This stark difference between Chinese and American corporate governance is unsurprising considering that most A-Shares companies have a dominant controlling shareholder and institutional investors normally are small minority shareholders – the opposite to the United States where institutional shareholders hold 80% of shares in listed companies and the vast majority of listed companies lack a dominant controlling shareholder.[133] The ability of institutional investors to engage in shareholder activism is significantly curtailed when they are a small minority shareholder in a company with a dominant controlling shareholder.[134] As such, it is unsurprising that our review of the 43 Activist Campaigns revealed that they targeted A-Share companies which were corporate governance outliers: 76.7% of companies did *not* have a dominant controlling shareholder and 62.8% of institutional investors involved in the campaigns owned more than 5% of the company's shares.[135] Although, at the earlier stage of the development of the A-Shares market, most of the listed companies were SOEs,[136] dispersedly held A-Shares companies without a dominant controlling shareholder are becoming more common. This suggests that there may be more activist campaigns by institutional shareholders in A-Shares companies in the future. This may explain why, as shown in Appendix 2, there were more than three times as many Activist Campaigns from 2011 to 2021 than there were from 2000 to 2010 – as A-Shares companies have become more dispersed over the past decade.

Second, Activist Campaigns by foreign owned institutional investors (FOIIs) are extremely rare. Based on Appendix 2, only 2 out of the 43 Activist Campaigns involved FOIIs and in 1 out of the 2 Activist Campaigns involving FOIIs, the FOII joined with a POII to undertake the campaign. Based on the search we conducted to create Appendix 2, we could not find even a single Activist Campaign involving an FOII after 2012. This is unsurprising considering that, as highlighted in Part II, foreign institutional investors did not hold any meaningful percentage of A-Shares companies until 2007 and since then they have held only between 1% to 3% of the shareholder capitalization of A-Shares companies. In addition, although the regulations limiting foreign institutional investors have been gradually relaxed, there is still a 30% cap on the percentage of

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[132]Lazard*, 2018 Review of Shareholder Activism*, at 3 (2018), https://www.lazard.com/media/450805/lazards-2018-review-of-shareholder-activism.pdf; Lazard, 2019 *Review of Shareholder Activism*, at 3 (2019), https://www.lazard.com/media/451141/lazards-2019-review-of-shareholder-activism-vf.pdf; Lazard, *2020 Review of Shareholder Activism*, at 6 (2020), https://www.lazard.com/perspective/lazards-annual-review-of-shareholder-activism-2020/.

[133]De La Cruz et al., *supra* note 38, at 12; Puchniak, *supra* note 84.

[134] Yu-Hsin Lin, *When Activists Meet Controlling Shareholders in the Shadow of the Law: A Case Study of Hong Kong*, 14 ASIAN J. COMP. L. 1, at 7-8 (2019).

[135] The 'dominant' controlling shareholder' here refers to shareholders who control the investee's shares of over 50%. The data is taken from disclosures of investee companies. See http://eid.csrc.gov.cn/.

[136] Robin Hui Huang, *Shareholder Derivative Litigation in China: Empirical Findings and Comparative Analysis,* 27 BANKING & FIN. L. REV. 619, 649 (2012).

shares that foreign institutional investors can own in an A-Shares company – which prevent foreign institutional investors from being able to execute, or even to threaten to execute, a change of control in A-Shares companies.[137] It is interesting that out of the two Activist Campaigns involving foreign institutional investors, one targeted an SOE and the other targeted a POE, and both were successful. In the case targeting an SOE, the foreign institutional investors partnered with private domestic institutional investors to elect their directorial candidate over another candidate who was supported by a government shareholder which was the actual controller of the SOE. As explained in more detail in Part IV, this illustrates how foreign institutional investors in some circumstances may be able to have a positive impact on corporate governance as they are more insulated from the mechanisms that the CCP uses to carry out policy channeling in SOIIs and POIIs.

Third, 13 out of the 43 Activist Campaigns listed in Appendix 2 were undertaken by SOIIs, while 23 were undertaken by POIIs – with POIIs and SOIIs collaborating in 5 Activist Campaigns and a POII and FOII collaborating in 1 Activist Campaign.[138] It is noteworthy that prior to 2010, half of the Activist Campaigns were undertaken by SOIIs, which are owned by the government and ultimately controlled by the CCP directly or indirectly; whereas since 2010, over half of the Activist Campaigns were undertaken by POIIs.[139] This suggests an increasing reliance on the private market for institutional investors, in which the CCP only exercises indirect control. As discussed in Part IV, to varying extents, the CCP through a matrix of policy channels may also control institutional investors which it does not directly own.

Taken together, this challenges the idea that the rise of institutional investors in China may threaten the CCPs ultimate control. However, as we explain in Part IV, merely because the CCP directly or indirectly controls SOEs does not mean that free-market forces are irrelevant. On the contrary, in normal times free-market forces govern the behavior of SOIIs and POIIs, like institutional investors in other financial markets. However, in extraordinary times (e.g., when there is market instability, or the government wants to undertake a major reform) both SOIIs directly and POIIs indirectly may serve as agents to execute government policy. This reliance on market forces in regular times and use of policy channeling for extraordinary purposes is a phenomenon which we explain as the institutional shareholder "market within the state" in the Conclusion.

Fourth, SOEs were the target in 11 out of 43 Activist Campaigns, and there were 7 cases in which a POII targeted an SOE. It is noteworthy that in 4 of these cases the POII succeeded in its campaign. This illustrates how the government has allowed POIIs to serve as a check on SOEs – which further highlights the complexity and sophistication of China's market within the state. As explained in Part IV, although the government has promoted the emergence of POIIs to serve as a useful check

[137] *See supra* Part II.

[138] There was 1 Activist Campaign that was undertaken by an FOII. See below, Appendix 2.

[139] From 1994 to 2010, 50% (5 out of 10) of the Activist Campaigns were undertaken by SOIIs, with SOIIs and POIIs collaborating in 20% (2 out of 10) of the Activist Campaigns; whereas from 2011 to 2021, 60.6% (20 out of 33) of the Activist Campaigns were undertaken by POIIs, with SOIIs and POIIs collaborating in 9.1% (3 out of 33) of the Activist Campaigns and an FOII and a POII collaborating in 1 Activist Campaign. See below, Appendix 2.

on SOEs, it has also developed policy channels that ensure that the CCP maintains ultimate (indirect) control over POIIs. In addition, POEs were the target in 32 out of 43 Activist Campaigns, with 14 of them involving SOIIs, which demonstrates that this may be another policy channel in which the state can influence or police POEs. It is interesting that only 6 of these campaigns succeeded – again illustrating how SOIIs are bound by the laws and market-forces. Merely because the state is the direct owner of SOIIs does not axiomatically result in a successful Activist Campaign.

Fifth, the evolution of the types of institutional investors that have executed Activist Campaigns confirms our observation in Part II that the market for institutional investors in A-Shares companies has become increasingly atomized. As illuminated in Part II, prior to 2010, SIFs dominated the market. As such, it is unsurprising that, prior to 2011, 8 out of 10 Activist Campaigns were executed by SIFs. However, from 2011 to 2021, 20 out of 33 Activist Campaigns were undertaken by other types of institutional investors such as trust companies, securities companies, insurance companies and other professional institutions – illustrating how other types of institutional investors have started to participate in the corporate governance of investee companies. This reinforces the importance of the taxonomy of institutional investors described in Part II and highlights why understanding the different types of regulatory regimes impacting different types of institutional investors is important – which is the focus of Part IV.

Sixth, 58.1% (25 out of 43) Activist Campaigns listed in Appendix 2 were successful, with successful campaigns normally resulting in institutional investors having an impact on corporate governance by preventing the company from engaging in a transaction that would harm minority shareholders or providing minority shareholders with a voice on the board. To succeed, small minority institutional investors have had to convince other investors to support their proposals – reinforcing the observation that such campaigns normally only have a chance to succeed in dispersed companies without a dominant controlling shareholder. The only successful hostile takeover bid by an institutional investor was executed in 2017 by Zhemin Tianhong Investment Partnership (L.P.) in its successful $2.7 billion hostile takeover bid for Zhenxing Biopharmaceutical and Chemical Co., Ltd.[140] Arguably the key to Zhemin Tianhong Investment Partnership (L.P.)'s success was that Zhenxing Biopharmaceutical was an outlier among A-Shares companies in terms of having an extremely dispersed shareholding structure – illustrating how dispersed shareholding is a key factor in the success of Activist Campaigns in A-Shares companies.

Finally, we would be remiss to not acknowledge what these case studies cannot tell us. Institutional investors often meet and communicate with investee companies informally – which may have an impact on corporate governance. Although most of this communication is normally unobservable, Cheng et al. examined the impact of "site visits" (i.e., when investors visit corporate headquarters

[140] Zhenxing Biopharmaceutical and Chemical Co., Ltd. has changed its name to Pacific Shuanglin Bio-pharmacy Co., Ltd., *See*, 付健青[Fu Jian Zi]，解码 A 股首例成功市场化敌意收购案[Decoding the First Successful Market-Oriented Hostile Acquisition of A-Shares], JNJ (June 29, 2018), https://m.jrj.com.cn/madapter/stock/2018/06/29033024743240.shtml.

or manufacturing facilities to meet with managers in A-Shares companies).[141] These "site visits" are required to be disclosed in the annual reports of A-Shares companies. They found a significant positive market reaction to corporate site visits and that the market reaction was stronger for visits conducted by SIF managers.[142] This suggests that some of the empirical evidence described above, which finds that SIFs have a positive impact on corporate governance, may result from informal activities and may not be reflected in Activist Campaigns. We are unaware of any similar research that has focused on foreign institutional investors, but this also raises the possibility that the empirical evidence which suggests that they have a positive impact on the corporate governance of A-Shares companies may be related to their informal activities. More research will have to be done to confirm whether this is the case.

In sum, the relative infrequency of Activist Campaigns illustrates how A-Shares companies are still dominated by controlling shareholders – with institutional shareholders remaining a small minority. However, the rise in the number of Activist Campaigns over the last decade appears to confirm the rising shareholder power of institutional investors highlighted in Part II. The increasing variety in the types of institutional investors executing Activist Campaigns also confirms the atomization of institutional investors and the value of the taxonomy of institutional investors in Part II. Perhaps, most interesting, is the extent to which SOIIs have executed campaigns against SOEs and POIIs have succeeded in campaigns against SOEs. This illustrates the complexity and sophistication of China's unique system of corporate governance, in which the CCP maintains ultimate control, while promoting checks and balances within the government and a "free market within the state". It is to this that we now turn.

IV: THE DUAL ROLES OF INSTITUTIONAL INVESTORS IN CHINA: CORPORATE GOVERNANCE AND POLICY CHANNELING

(a) Illuminating the CCPs Targeted Use of Policy Channeling in an Otherwise Free-Market

The empirical research and Activist Campaigns in Part III suggest that there is a complex relationship between the CCP and the role that institutional investors play in Chinese corporate governance. This Part aims to make sense out of this complexity by mapping the formal and informal mechanisms that the CCP utilizes to engage in policy channeling. We demonstrate that the CCP can – and has – used various mechanisms to engage in policy channeling in SOIIs and POIIs. Interestingly, for SOIIs and POIIs there are two distinct paths – composed of various government bodies, regulations, and tactics – for engaging in policy channeling; with FOIIs being largely insulated from both paths.

Equally as important is our evidence that the CCP uses its power to policy channel in a targeted and limited way surrounding significant stock market and political events. On a day-to-day basis, absent these extraordinary events, institutional investors in China appear to be driven by free market-forces. Empirical, interview, and case study evidence suggests that institutional investors often serve an important corporate governance function by acting as a check on corporate

[141] Qiang Cheng et al., *Do Corporate Site Visits Impact Stock Prices?*, 36 CONTEMP. ACCT. RES. 359, 364 (2019).
[142] *Id.* at 381.

controllers in SOEs and POEs. This fits with other research on Chinese corporate governance that demonstrates that the government has created a system to mitigate private benefits of control – even when it means constraining the power of SOEs – while at the same time ensuring the CCP maintains ultimate control.[143]

Ultimately, it appears that institutional investors play an important function within the unique China Model of corporate governance. The CCP does not micro-manage institutional investors in a way that some conceptions of "state capitalism" may suggest.[144] Rather, institutional investors normally function according to free-market forces and perform an important corporate governance role – with the CCP using its various mechanisms for policy channeling to execute important policies, which may benefit the market and society, while also possibly blunting the effectiveness of efficient corporate governance. This system is what we explain in the Conclusion as "the market within the state" for institutional investors in China.

(b) Illuminating, Classifying, and Mapping the CCP's Mechanisms for Policy Channeling

The split share reform research provides convincing empirical evidence that the CCP can – and has – used its regulatory power to transform domestic institutional investors into a mechanism for policy channeling.[145] The CCP's use of institutional investors to achieve its political goals comports with the more recent creation of a "National Team" of government-controlled SOIIs which were tapped to stabilize the A-Shares market after its collapse in 2015.[146] Although, as explained in Part II, the CCP has a long history of using its regulatory power to promote institutional investors as a market stabilizing mechanism, the enormous scale of investment and strategic coordination of a select group of SOIIs in 2015 crystallized the idea of the National Team as an important feature of the A-Shares market – which investors now count on to intervene in times of market volatility.[147]

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[143] Howson, *supra* note 9, at 52; Wang & Tan, *supra* note 10, at 1094.

[144] Telephone interview, 30 May 2021, Investment Manager CICC (Shenzhen); Telephone interview, May 30, 2021, Legal Counsel, DBS Securities (China); Telephone interview, May 30, 2021, Senior Manager, CMS (Shanghai); Telephone interview, May 30, 2021, Legal Counsel, DBS Securities (China); Telephone interview, May 30, 2021, Partner, Global Law Office (Beijing); Telephone interview, May 31, 2021, Legal Officer, SAFE; Andrew Szamosszegi & Cole Kyle, *An analysis of state-owned enterprises and state capitalism in China*, US-CHINA ECONOMIC AND SECURITY REVIEW COMMISSION, at 52 (Oct. 26, 2011).

[145] Firth et al., *supra* note 105, at 697; Huang & Zhu, *supra* note 42, at 314; *See supra* Part III.

[146] Moxy Ying, *When Stocks Crash, China Turns to Its 'National Team'*, WASHINGTON POST (Mar. 9, 2021), https://www.washingtonpost.com/business/when-stocks-crash-china-turns-to-its-national-team/2021/03/09/d13c540a-80df-11eb-be22-32d331d87530_story.html; Hudson Lockett & Sun Yu, *How the Invisible hand of the state works in Chinese stocks*, FINANCIAL TIMES (Feb. 4, 2020), https://www.ft.com/content/0d41cb6e-4717-11ea-aeb3-955839e06441; Evelyn Cheng, *Goldman: Government-directed traders bought up billions in Chinese stocks last quarter*, CNBC (Sept. 11, 2018), https://www.cnbc.com/2018/09/11/goldman-government-directed-traders-bought-nearly-17-billion-in-local-stocks-last-quarter.html; Shen Hong & Stella Yifan Xie, *That Calm Chinese Stock Market? It's Engineered by the State*, WALL STREET JOURNAL (May 31, 2018), https://www.wsj.com/articles/that-calm-chinese-stock-market-its-engineered-by-the-government-1527775089?mod=e2tw.

[147] *Id.*; Narayanan Somasundaram, *Chinese government-back funds snap up stocks to halt plunge*, NIKKEI ASIAN REV. (Mar. 9, 2021).

There is also empirical and anecdotal evidence that beyond being a mechanism to facilitate regulatory reforms and stabilize the A-Shares market, the CCP uses its ownership and control over SOIIs to achieve more overt political objectives. There is evidence that prior to major CCP political events and meetings, the government uses its control over SOIIs to ensure a general level of social stability by keeping the markets calm.[148] The extent to which market stability is crucial for social stability in China is evident from the fact that, with over 100 million Chinese citizens invested in the A-Shares market, shareholders form an even larger constituency than CCP members.[149]

There is also empirical and anecdotal evidence that the CCP uses its formal and informal power to pressure POIIs – a tactic that has become known as "window guidance" – to reinforce its policy channeling through institutional investors.[150] In addition to the empirical evidence demonstrating the control over POIIs to facilitate the split share reform, anecdotal evidence suggests that window guidance is used to alter the behavior of POIIs to bolster the CCPs ability to utilize domestic institutional investors to achieve social stability surrounding major political events.[151]

Perhaps unsurprisingly, the empirical evidence in Part III suggests that the CCPs ability to use FOIIs as a conduit for policy channeling is considerably more limited, if not non-existent. This is supported by the empirical evidence regarding the split share reform which suggests that QFIIs acted in the interest of their beneficiaries and their investee companies' tradable shareholders in negotiating the compensation in the reform – as opposed to jettisoning their interests to make the CCP's market reform a success.[152] There appears to be no evidence that QFIIs have participated in any market stabilization efforts, including the campaign carried out by the National Team following the 2015 market collapse. The independence of QFIIs from the CCP may also help explain why several empirical studies examined in Part III found that QFIIs played a positive monitoring role in A-Shares companies, despite their modest shareholdings – which, as explained

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[148] Shen & Xie, *supra* note 146.

[149] Charlotte Yang, *Caixin Explains: How a Stock Market Crash Created China's 'National Team'*, CAIXIN (Oct. 19, 2018), https://www.caixinglobal.com/2018-10-19/caixin-explains-how-a-stock-market-crash-created-chinas-national-team-101337087.html.

[150] Telephone interview, May 30, 2021, Partner, Global Law Office (Beijing); Telephone interview, May 30, 2021, Investment manager, CMS (Shanghai); Telephone interview, May 30, 2021, Legal Counsel, DBS Securities (China); Telephone interview, May 30, 2021, Investment manager, CICC (Shenzhen). See also Lockett & Yu, *supra* note 146; Cheng Pangyue, *Drivers of Institutional Investors' Shareholder Behaviour in China's Listed Companies: A Socio-legal Research of Incentives and Challenges in the New Era*, at 25 (on file with authors); See section 3(1) of SUPERVISION AND ADMINISTRATION MEASURES FOR DIRECTORS, SUPERVISORS, SENIOR MANAGEMENT AND PRACTITIONERS OF SECURITIES AND FUND MANAGEMENT ORGANIZATIONS (CONSULTATION PAPER) (Nov. 20, 2020) (the appointment of directors, supervisors, senior management and branch heads by securities and fund operators should be filed with the relevant dispatching agencies of CSRC in accordance with the law). Tomoyuki Fukumoto et al., *Effectiveness of Window Guidance and Financial Environment – In Light of Japan's Experience of Financial Liberalization and a Bubble Economy*, BANK OF JAPAN REV. (Aug. 2010), https://www.boj.or.jp/en/research/wps_rev/rev_2010/data/rev10e04.pdf.

[151] Shen & Xie, *supra* note 146.

[152] Huang & Zhu, *supra* note 42, at 319.

in Part II, have historically been limited by strict regulatory caps that have only recently been relaxed.

Taking a step back, based on the ability of the CCP to utilize institutional investors for the purpose of policy channeling, institutional investors in China can be classified into three broad categories, as depicted in Diagram 1 below. The first category, *State-Controlled Institutional Investors*, is composed of China's SOIIs. The CCP exercises two-tiers of control over SOIIs through both its shareholding network and the appointment of the "First in Command" (*yi ba shou*) of SOIIs.[153]

First, as the controlling shareholder or actual controller who holds over 50% of the shares of SOIIs directly or indirectly, the government agencies are able to exercise legal control over SOIIs as their majority shareholders.[154] As illustrated in Diagram 1 below, the institutional architecture that has progressively been developed during the SOE reform process has created a complex network of different government agencies (e.g., the State Council, State-owned Assets Supervision and Administration Commission of the State Council (SASAC), and the Ministry of Finance and State Administration of Foreign Exchange (SAFE)) holding shares in SOIIs on behalf of the state.[155] However, it should be noted that more recently, the government policy has been to consolidate the state-owned shares of SOIIs into MOF in order to simplify the shareholding network between government agencies and SOIIs and to strengthen the government's control over state-owned shares.[156]

As the major shareholder of SOIIs, the MOF is able to exercise its shareholder rights under the PRC Company Law (e.g., participating in appointment and dismissal of senior managers[157] and

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[153] The chairman of the board, general manager, and party committee secretary are often referred to collectively using the political term the "First in Command" (yi ba shou) of the SOIIs.

[154] The data is taken from "Qichacha" (an enterprise information enquiry system): https://www.qcc.com/> last accessed on Jun. 13, 2021.

[155] See 中华人民共和国企业国有资产法 [The Law of the People's Republic of China on the State-Owned Assets of Enterprises], promulgated by the Standing Committee of the National People's Congress on Oct. 28, 2008, Article 4 and 11. The State Council and the local people's governments perform respectively the investor's functions for state-invested enterprises and enjoy the investor's rights and interests on behalf of the state. The central SASAC, local SASAC or other government agencies can perform the investor's functions and enjoy the investor's rights and interests of the state on the authorization of the State Council and the local people's governments. For example, as depicted in Diagram 1 below, the State Council directly controls CITIC Group and China Everbright Group; SASAC indirectly controls Zhonghai Trust Co., Ltd., China Huadian Finance Co., Ltd. and China State Shipbuilding Finance Co., Ltd.; Additionally, the State Council indirectly controls SOIIs such as Guotai Fund Management Co., Ltd., BOC Wealth Management Co., Ltd. and CCB Wealth Management Co., Ltd. through Central Huijin Investment Co., Ltd., which is the second-tier subsidiary of the State Council.

[156] See 中共中央、国务院关于完善国有金融资本管理的指导意见, [Guiding Opinions of the CPC Central Committee and the State Council on Improving the Management of State Financial Capital], June 30, 2018; 国有金融资本出资人职责暂行规定, [The Interim Provisions on the Duties of State-owned Financial Capital Contributors], promulgated by the General Office of the State Council on Nov. 7, 2019; 国有金融资本管理条例征求意见稿 [Regulations on the Management of State-owned Financial Capital (Draft for Comments)], promulgated by MOF on May 11, 2020.

[157] "Senior managers" includes directors and supervisors.

revising of the articles of association and other decision-making processes)[158] to control the corporate governance of SOIIs. Notably, this does not mean that MOF exercises any external regulatory power over these SOIIs – which is critically important as all the domestic institutional investors including SOIIs and POIIs are effectively regulated by the three financial regulatory agencies (i.e., PBOC, CBIRC and CSRC, the three agencies are also known as 'one bank and two commissions', *yi hang liang hui*). Specifically, banks, insurance companies and other institutional investors such as financial asset management companies, trust companies and financing companies are subject to the regulation of CBIRC; whereas securities companies and SIF firms are regulated by CSRC.[159] In addition, according to the Interim Measures for the Supervision and Administration of Financial Holding Companies, which was issued recently on September 11, 2020, the financial holding companies are subject to the regulation of the PBOC.[160]

Second, for SOIIs which are listed in the Directory of Central Financial Enterprises, the CCP is able to exercise its control through the appointment of their First in Command.[161] According to the Interim Regulations on the Management of the Leading Personnel of Central Financial Enterprises, which was issued by the General Office of the CCP in 2011, the appointment of the senior managers of central financial enterprises shall be administered by the CCP (which relies on the principle referred to in Chinese as "*dang guan gan bu*" (which in English can roughly be translated as "the Party administers the management of cadres").[162] In addition, for the senior managers in SOIIs who are government officials and who are CCP members, they are bound by the Law of the People's Republic of China on Administrative Discipline for Public Officials and related CCP

[158] See 中华人民共和国公司法 [Company Law of the People's Republic of China (2018 Amendment)], adopted at the Sixth Session of the Standing Committee of the 13th National People's Congress on Oct. 26, 2018, Article 37.

[159] *See* 保险公司管理规定, [Provisions on the Administration of Insurance Companies], promulgated by CIRC on Oct. 19, 2015; 中华人民共和国银行业监督管理法, [Banking Supervision Law of the People's Republic of China], adopted at the 24th meeting of the Standing Committee of the 10th National People's Congress of the People's Republic of China on Oct. 31, 2006; 第十三届全国人民代表大会第一次会议关于国务院机构改革方案的决定 [Decision of the First Session of the Thirteenth National People's Congress on the State Council Institutional Reform Proposal], adopted at the First Session of the Thirteenth National People's Congress on Mar. 17, 2018; 证券公司监督管理条例, [Regulations on the Supervision and Administration of Securities Companies], promulgated by State Council on July 29, 2014; 证券投资基金管理公司管理办法, [The Measures for the Administration of Securities Investment Fund Management Companies], promulgated by CSRC on Nov. 1, 2012.

[160] 'Financial holding company' refers to limited liability companies or companies limited by shares that are formed according to the law, that control two or more different types of financial institutions, and that only conduct equity investment management and do not directly carry out commercial business activities.

[161] *See*, 中央金融企业名录[Directory of Central Financial Enterprises], promulgated by Finance Department of MOF on Feb. 20, 2021, http://bgt.mof.gov.cn/zhuantilanmu/rdwyh/czyw/202102/t20210219_3658752.htm

[162] *See*, 中管金融企业领导人员管理暂行规定 [Interim Regulations on the Management of Leading Personnel of Central Financial Enterprises], promulgated by General Office of the CCP on Nov. 16, 2011, Article 3:

> The management of the leading personnel of financial enterprises shall adhere to the principle of the Party administers the management of cadres; adhere to the criteria of both virtue and talent and with virtue as the first priority; adhere to democracy, openness, competition and meritocracy; adhere to the unity of rights and responsibilities, incentives and constraints; adhere to the combination of the acceptance of investors, the market and employees; adhere to the law and procedural compliance.

regulations.[163] These mechanisms ensure that the CCP maintains control over the governance of SOIIs and illustrates how the CCP can effectively exact its control over SOIIs for the purpose of policy channeling.

It is noteworthy that although all the members of the National Team are State-Controlled Institutional Investors, there are many SOIIs in this category that are not part of the National Team.[164] This makes sense as the National Team merely refers to the SOIIs that were tapped to stabilize the markets in 2015 and is a loose category that appears to evolve based on market circumstances.[165] In this sense, the National Team is an illustration of how the CCP can quickly and effectively utilize SOIIs for policy channeling and is not a fixed category of institutional investors unto itself.

The second category is *State-Influenced Institutional Investors*, which includes domestic POIIs in China. As all State-Influenced Institutional Investors are privately owned, unlike in State-Controlled Institutional Investors, the CCP does not have the ability to directly control POIIs through the exercise of its shareholders' rights and, in turn, by directly appointing senior managers of SOIIs. Also, the senior managers of POIIs are generally recruited from the private sector and receive market-based salaries – unlike the public regulated salaries of the government officials who compose most of the First in Command in SOIIs.[166]

However, despite the initial free-market appearance of POIIs, they are categorized as State-Influenced Institutional Investors because of the formal and informal mechanisms that the CCP may use to influence POIIs to engage in policy channeling. In terms of formal power, although the senior managers in POIIs are not directly appointed by the CCP, they are required to be approved by relevant regulatory government agencies (i.e., PBOC, CBIRC or CSRC) before their appointment. As mentioned above, domestic institutional investors are regulated by PBOC, CBIRC or CSRC depending on the financial industry that they are a part of. Historically, part of

[163] Cheng, *supra* note 150, at 25; It must be noted that strictly speaking, senior managers of SOIIs do not have formal administrative levels or ranks. See 中共中央关于国有企业改革和发展若干重大问题的决定 [Decision on Several Major Issues Concerning the Reform and Development of State-owned Enterprises], promulgated by General Office of the CCP on Sept. 22, 1999. However, as many of those "First in Command" are appointed and removed by the Organization Department of the CCP, they have an administrative level or rank. It must be noted that not all senior managers of SOIIs are government officials and, therefore, not all of them have to follow the Law of the People's Republic of China on Administrative Discipline for Public Officials, issued by the Standing Committee of the National People's Congress on June 20, 2020. Only those who were government officials before they joined SOIIs will be subjected to this law.

[164] Ying, *supra* note 146; *See* Diagram 1 below.

[165] Ying, *supra* note 146; Cheng, *supra* note 146; Yang, *supra* note 149.

[166] Cheng, *supra* note 150, at 22. Telephone interview with legal counsel, Ms. C, DBS (Securities), Mar. 30, 2021 (on file with author).

the regulatory power of these three government agencies is derived through their power to approve the appointment of senior managers of POIIs.[167]

Taking SIF firms as an example, normally, every SIF has an Investment Decision Committee (IDC) which is responsible for making high level business and policy decisions in the SIF.[168] The IDC is composed of the SIF firm's senior managers,[169] which give them an air of independence as they are private sector employees.[170] Historically, the CSRC had a veto power over the appointment and removal of all IDC members which it could exercise due to the fact that the appointment of all executives of securities companies had to be reported to the SEC for filing.[171] Notably, following the new Securities Law, which came into force on March 1, 2020, several laws and regulations were issued to revise the ex-ante approval requirement of the appointment of POIIs' senior managers to only ex post filing.[172] However, it is too early to tell whether this will make a difference in the CSRCs actual influence over POIIs. In terms of informal mechanisms, research based on anonymous interviews with senior employees in POIIs suggests that the CSRC uses window guidance to effectively control the selection of senior managers (who are also the IDC members),[173] and IDCs are often composed of CCP members.[174] The CSRCs window

[167] *See*, 银行业金融机构董事（理事）和高级管理人员任职资格管理办法, [The Measures for the Administration of the Office-holding Qualifications of the Directors and Senior Managers of Banking Financial Institutions], promulgated by CBRC on Dec. 18, 2013; 保险公司董事、监事和高级管理人员任职资格管理规定, [Provisions on the Administration of the Office Qualifications for the Directors, Supervisors and Senior Executives of Insurance Companies], promulgated on Jan. 23, 2014; 证券公司董事、监事和高级管理人员任职资格监管办法, [Measures for the Supervision and Administration of the Professional Qualifications of Directors, Supervisors and Senior Managers of Securities Companies], promulgated by CIRC on Oct. 19, 2012; 证券投资基金管理公司高级管理人员任职管理办法, [The Measures for the Administration of Post-holding of Senior Officers of Securities Investment Fund Management Companies], promulgated on Oct. 1, 2004.

[168] Cheng, *supra* note 150, at 26; Telephone interview with fund manager, Mr. Y, GF Securities, Mar. 18, 2021 (on file with author).

[169] Which generally consists of the principals of management (including the chairman, general manager, chief financial officer. Telephone interview with fund manager, Mr. Y, GF Securities, Mar.18, 2021 (on file with author). Telephone interview with legal counsel, CICC, Mar.30, 2021 (on file with author).

[170] Yu Jin & Hou Wei Xiang, *Investment Decision-Making Committee Characteristics and Investment Performance and Ability* (投资决策委员会特征与投资业绩，投资能力－甚于公墓基金的研究), 6 REV. INV. STUD. (投资研究) 116 (2017).

[171] CSRC, 证 券 公 司 类 报 备 指 引 [Securities Company Filing Guidelines] (Sept. 14, 2015), http://www.csrc.gov.cn/zjhpublicofheb/bszn/201509/t20150914_283941.htm.

[172] *See*, 中华人民共和国证券法, [The Securities Law of the PRC], Mar. 1, 2020; 证券基金经营机构董事、监事、高级管理人员及从业人员监督管理办法（征求意见稿）, [The Measures for the Supervision and Administration of Directors, Supervisors, Senior Managers and Practitioners of Securities and Fund Management Institutions (Draft for Comments)], issued by CSRC on Nov. 20, 2020; 金融控股公司董事、监事、高级管理人员任职备案管理暂行规定, [The Interim Provisions on the Administration of Recordation for the Office-Holding of Directors, Supervisors, and Senior Executives of Financial Holding Companies], promulgated by PBOC on May 1, 2021.

[173] Cheng, *supra* note 150, at 24-25.

[174] Firth et al., *supra* note 105, at 693.

guidance, combined with its formal veto power, suggests that IDCs provide a conduit for the CCP to pressure POIIs to engage in policy channeling.[175]

However, it must be noted that generally speaking, the IDC would not interfere in the day-to-day investment activities in the SIF, as it normally delegates its authority over investment decisions to the SIF's fund managers.[176] Research based on anonymous interviews with senior managers in SIFs suggests that under normal circumstances the IDC does not intervene in decisions of fund managers with respect to what stock they choose to purchase nor in how fund managers choose to engage in the corporate governance of investee companies.[177] The CCP's ability to directly control the day-to-day investment activities in SIFs is limited as fund managers are not within the list of senior managers whose appointments are subject to the approval of the CSRC. However, as highlighted in Part III, for the purpose of the split share reform the relevant voting decision in investee companies was reallocated from fund managers to the IDC. This illustrates how the CCP can – and has – used its regulatory power and indirect control over IDCs to engage in policy channeling. In addition, senior fund managers in SIFs are licensed by the Securities Association of China (SAC) – which is a non-profit organization under the supervision and guidance of the CSRC.[178] This provides another possible avenue for the CCP to exact pressure on POIIs for the purpose of policy channeling, even when the IDC does not interfere in the decisions of fund managers.

The third category is *Foreign-Owned Institutional Investors* (FOIIs), which includes all QFIIs and the other foreign institutional investors described in Part II. As mentioned above, there is no evidence that the CCP uses FOIIs as a mechanism for policy channeling. The senior managers of FOIIs are not required to seek the approval of the CSRC.[179] Moreover, the person in charge of the QFII's Chinese investments does not have to meet the licensing requirements of the SAC – the only requirement is for them to meet the qualifications for investment professionals in their

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[175] Mo Shensheng, *Financial restructuring and economic development in China from the perspective of institutional arrangement* (Zhejiang University, PhD dissertation) (2014).

[176] Cheng, *supra* note 150, at 26; See s10, Guiding Opinions on the Fair-Trading Rules of Securities Investment Fund Management Companies (2011 Rev).

[177] Cheng, *supra* note 150, at 26. Telephone interview with fund manager, Mr. Z, China International Capital Corporation Limited, May 26, 2020; Telephone interview with legal counsel Ms. X, China International Capital Corporation Limited, Mar. 3, 2021; Telephone interview with fund manager, Mr. Y, GF Securities Mar. 18, 2021 (on file with author); Telephone interview legal counsel, Ms. C of DBS Securities (China), Telephone interview with senior manager, Ms. J, CMS (Shanghai).

[177] Cheng, *supra* note 150, at 24.

[178] Cheng, *supra* note 150, at 26.

[179] See, 合格境外机构投资者和人民币合格境外机构投资者境内证券期货投资管理办法, [The Administrative Measures for Securities and Futures Investment Made in China by Qualified Foreign Institutional Investors and RMB Qualified Foreign Institutional Investors], promulgated by CSRC, PBOC and SAFE on Nov. 1, 2020, Article 6:

> Whoever applies for the qualification as a qualified foreign investor shall meet the following conditions: …
> (2) The principal person in charge of its investment in China satisfies the relevant requirements for practicing qualifications prescribed by the foreign country or region where the applicant is located (if any)…

respective home jurisdictions.[180] As such, with respect to FOIIs the CCP lacks the direct channels of authority it has over SOIIs and the indirect channels for window guidance it has over POIIs – leaving FOIIs considerably more insulated from the primary mechanisms that the CCP uses to engage in policy channeling, which may provide one reason for the empirical evidence in Part III that they improve corporate governance in their investee companies.

However, based on the evidence concerning FOIIs in Part II, it could be argued that by strategically capping the total amount of investment by FOIIs and their ability to purchase a controlling shareholder stake in A-Shares companies, the CCP has ensured that FOIIs will not be major players in the A-Shares market. Despite the recent relaxation of these restrictions, there is no evidence that the irrelevance of FOIIs in policy channeling will change in the foreseeable future. This comports with the observation made in Part III that Activist Campaigns by FOIIs are extremely rare.

(c) Day-to-Day Corporate Governance Function of Institutional Investors in China

Equally as important as recognizing the CCP's ability to use institutional investors as a powerful mechanism for policy channeling, is the observation that the CCP appears to use this power only in a selective and targeted manner. In the case of POIIs, as highlighted above, empirical and anecdotal evidence suggests that the CCP's use of policy channeling is reserved to facilitate major reforms, to stabilize the market in times of crisis, or to ensure social stability surrounding major political events.[181] Based on interviews conducted by one of us in 2020 and 2021, senior employees in POIIs uniformly were of the view that in "normal times" POIIs worked as asset owners and/or asset managers to maximize the returns for their ultimate beneficiaries – and not for policy channeling.[182] This finding is confirmed by another research project which concluded, based on anonymous interviews of executives in POIIs, that on a day-to-day basis they were driven by free-market forces – and not policy channeling.[183]

We recognize that the answers provided by the employees who were interviewed in POIIs may be self-serving. However, with respect to POIIs, particularly SIFs, this comports with the empirical studies described in Part III demonstrating the positive impact that SIFs tend to have on the

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[180] Cheng, *supra* note 150, at 26; See Service Guide for Administrative Licensing Matters: Qualified Foreign Investor Qualification Approval, CSRC (Sept. 25, 2020).

[181] Shen & Xie, *supra* note 146.

[182] Telephone interview with fund manager, Mr. Z, China International Capital Corporation Limited, May 26, 2020; Telephone interview with legal counsel Ms. C, DBS Securities, Mar. 31, 2021; Telephone interview with senior manager, Ms. J, CMS, Mar. 30 2021; Telephone interview with fund manager, Mr. Y, GF Securities Mar. 18, 2021 (on file with author).

[183] Cheng, *supra* note 150, at 24. Telephone interview with fund manager, Mr. Li, CICC, May 26, 2020; Telephone interview with legal counsel Ms. C, DBS Securities, Mar. 31 2021; Telephone interview with senior manager, Ms. J, CMS, Mar. 30 2021; Telephone interview with fund manager, Mr. Y, GF Securities Mar. 18, 2021; Telephone interview with partner, Ms. K, Global Law Office Mar. 30, 2021 (on file with author).

performance of A-Shares companies[184] – with the notable exception of the split share reform which was an extraordinary situation where an important CCP policy objective was involved.[185] It is also supported by the evidence in Part III of the increasing number of Activist Campaigns by POIIs and, most importantly, that half of the Activist Campaigns carried out against SOEs have been successful.[186] Although the number of Activist Campaigns has been relatively small, this illustrates that outside of major events and reforms the CCP has sometimes allowed POIIs to play an active market-based role as institutional investors – even when it involves challenging the corporate governance of SOEs. This demonstrates that although the CCP can transform POIIs into State-Influenced Institutional Investors it appears to exercise its power in a targeted manner to achieve specific and important policy objectives – with POIIs normally being driven by free-market forces.

In terms of SOIIs, the evidence from Activist Campaigns in Part III also suggests that in normal times SOIIs are driven by free-market forces to improve the corporate governance of their investee companies. This is suggested by the fact that a majority of Activist Campaigns undertaken in the A-Shares market were conducted by SOIIs.[187] Interestingly, a significant number of these campaigns targeted SOEs – suggesting that the CCP realizes the corporate governance and economic benefits of having SOIIs serve as a check on the controlling shareholder power of SOEs, which is congruent with the CCP's long standing policy to support the development of institutional investors as a mechanism to improve corporate governance and stabilize the stock market.[188] The Activist Campaigns by SOIIs against POEs also demonstrate that the CCP uses SOIIs as a mechanism to serve as a check on controlling shareholder power more generally.

This comports with the government's creation of the China Securities Investor Services Centre – a non-profit organization which owns 100 shares in all A-Shares companies for the purpose of facilitating lawsuits to protect minority shareholders' rights.[189] As of April 2020, the ISC had facilitated 25 cases by appointing attorneys for the claimant minority shareholders and had successfully filed a lawsuit in its own name to invalidate a corporate resolution in an investee company.[190] The ISC also acts as a mediator to help resolve corporate governance disputes between institutional investors and investee companies free of charge.[191] This is congruent with

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[184] Chizema et al., *supra* note 91, at 382-83; Chi et al., *supra* note 91, at 55; Lin & Fu, *supra* note 90, at 18; Firth et al., *supra* note 91, at 105; Aggarwal et al., *supra* note 90, at 107; Yuan et al., *supra* note 94, at 1563.

[185] Firth et al., *supra* note 105, at 697; Huang & Zhu, *supra* note 42, at 314.

[186] See Appendix 2.

[187] *Id.*

[188] *Id.*

[189] Robin Hui Huang, *Rethinking the Relationship Between Public Regulation and Private Litigation: Evidence from Securities Class Action in China*, 19 THEORETICAL INQUIRIES L. 333, 359 (2018); Cheng, *supra* note 150, at 20.

[190] Cheng, *supra* note 150, at 24; China Securities Investor Services Center, Rights Protection Service, http://www.isc.com.cn/html/wqfw/.

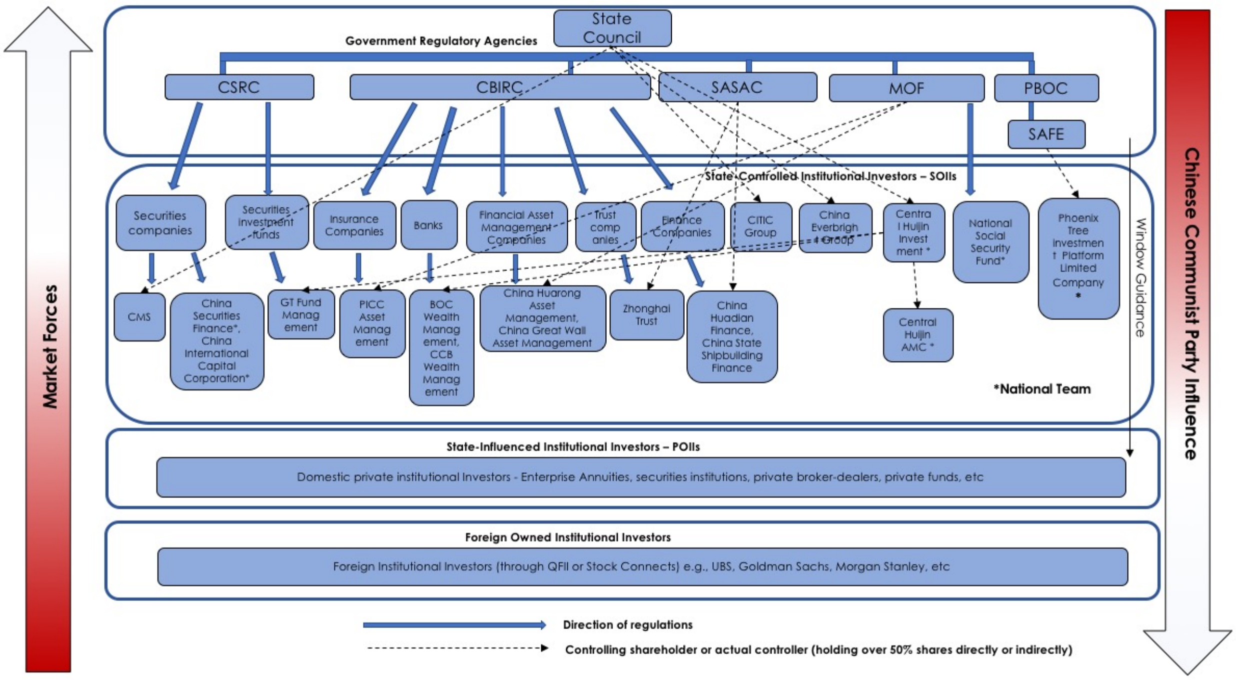
[191] Cheng, *supra* note 150, at 24; Notice by the Supreme People's Court and the China Securities Regulatory Commission of Issuing Opinions on Comprehensively Advancing Establishment of Diversified Resolution Mechanism of Securities and Futures Disputes No. 305, SPC, CSRC (Nov. 13, 2018).

the amendments made to the 2020 Corporate Governance Code which encourage institutional investors to be actively engaged in the corporate governance of their investee companies.[192] As highlighted in Part II, this is unsurprising based on the long history of the CCP promoting the development of institutional investors as a mechanism to stabilize the market and improve corporate governance. It also provides strong evidence that on a day-to-day basis – outside of extraordinary political and market events – the CCP not only allows, but encourages, institutional investors to be actively engaged shareholders driven primarily by free-market forces.

Finally, to be clear, we are not suggesting that the system is perfectly bifurcated between SOIIs/POIIs always serving as an effective mechanism for policy channeling in extraordinary times and always being an efficient corporate governance mechanism on a day-to-day basis. Empirical studies in Part III suggest that in some instances SOIIs may be less effective than POIIs and/or FOIIs in monitoring investee companies.[193] In other instances, empirical evidence suggests that SOEs may be more insulated against corporate governance pressure from institutional investors than POEs.[194] This suggests that sometimes, on a day-to-day basis, the lack of independence from the government may blunt the effectiveness of SOIIs and shield SOEs from effective monitoring by institutional investors. This may be more likely to occur when the circumstances in a given case elevate a corporate governance issue into an issue of political importance to the CCP. However, based on the totality of the empirical, case study, and interview evidence, it is our view that this stylized picture of the CCPs formal and informal targeted use of policy channeling (or lack thereof), as depicted in Diagram 1, largely approximates what plays out in practice.

[192] *See supra* Part II (Principle 11 of the Chinese Corporate Governance Code).
[193] *See supra* Part III.
[194] *See supra* Part III.

Diagram 1: Network of Influence over Institutional Investors in China[195]



V: INSTITUTIONAL INVESTORS IN CHINA: THE MARKET WITHIN THE STATE

Institutional investors have clearly become an important feature of Chinese corporate governance that can no longer be ignored. This Article takes the first step, in what will likely require an academic marathon, to gain an accurate understanding of the role that institutional investors play in China's unique model of corporate governance. From a broader perspective, there are three general observations that can be drawn from the rise of institutional investors in China.

First, the rise of institutional investors does not portend the rise of an Anglo-American system of corporate governance or Western-style capitalism. At first blush, the rise in institutional investors may suggest that China is converging on the Anglo-American model of corporate governance, with institutional investors at its core. However, if the percentage of the A-Shares market controlled by institutional investors continues to rise, what will arise will be uniquely Chinese. The primary reason for this, as has been shown, is that the CCP will maintain its ultimate control over most institutional investors – a unique feature of the China Model without an equivalent in Anglo-American corporate governance.

Second, the complexity of China's regulation of institutional investors and its government-centered system of corporate governance requires further analysis. This Article identifies the varieties of institutional investors in China and maps out the various government bodies,

[195] Institutional investors in Diagram 1 include general legal persons and non-legal-person enterprises, domestic professional institutional investors and foreign institutional investors, *see supra* Chart 3.

regulations, and tactics that provide the CCP with the ability to use SOIIs and POIIs as mechanisms for policy channeling. It also demonstrates that institutional investors, on a day-to-day basis, increasingly appear to work as an effective mechanism to improve corporate governance. However, a more detailed understanding of the functioning of each of the varieties of institutional investors – which may be more suitable for a book than an article – would add greater insight into China's increasingly atomized market for institutional investors. Also, the role played by institutional investors in China's autochthonous government-controlled system of corporate governance – with the unique internal checks and balances suggested by SOIIs successfully engaging in Activist Campaigns against SOEs – is a promising avenue for future research.

Third, the complexity of China's regulation of institutional investors and the unique model of corporate governance it has created, do not paint a picture of the CCP micro-managing corporate governance in the way that some notions of "state capitalism" may suggest.[196] Rather, it appears that, on a day-to-day basis, the Chinese government purposefully allows the free market to govern the relationship between institutional investors and companies even when it has ultimate control over both. However, when there is a need to push through a major reform, stabilize the market, or maintain calm in society for important political reasons, institutional investors are used as an effective mechanism for the CCP to engage in policy channeling. This suggests that the free market is the *de facto* norm and that the CCP uses its power to intervene in a targeted manner. Rather than suggesting that China is governed by "state capitalism", where SOEs have the dominant position in major industries,[197] our analysis of institutional investors seems to suggest that China is better described as a system defined by "the market within the state", where the free market and the state coexist, and the free market functions within the boundaries set by the state.[198]

[196] Telephone interview, May 30, 2021, Partner, Global Law Office (Beijing); Telephone interview, May 30, 2021, Investment manager, CMS (Shanghai); Telephone interview, May 30, 2021, Legal Counsel, DBS Securities (China); Telephone interview, May 30, 2021, Investment manager, CICC (Shenzhen). Wang Feng, 中国特色社会主义市场经济的界说——基于对“新国家资本主义”的批判[The Definition of Socialist Market Economy with Chinese Characteristics - Based on the Critique of "Neo-State Capitalism"], 28 管理学刊 [J. MGMT.] 17 (2015).

[197] *The Rise of State Capitalism: The Emerging World's New Model*, THE ECONOMIST (Jan. 21, 2012), https://www.economist.com/leaders/2012/01/21/the-rise-of-state-capitalism.

[198] Yongnian Zheng & Yanjie Huang, MARKET IN STATE: THE POLITICAL ECONOMY OF DOMINATION IN CHINA, 31-32 (2018).

APPENDICES

APPENDIX 1: LEGAL DEVELOPMENTS AND THE GOVERNMENT'S ROLE IN DEVELOPING INSTITUTIONAL INVESTORS IN CHINA 1978-2020[199]

Dates	Law/Policy	Implications and Significance
ALL INSTITUTIONAL INVESTORS		
2002	The China Securities Regulatory Commission and State Economic and Trade Commission promulgated the "Code of Corporate Governance for Listed Companies in China".	China designated institutional investors as an important feature of its corporate governance system by affirming in its inaugural Corporate Governance Code that "institutional investors shall play a role in the appointment of company directors, the compensation and supervision of management and major decision-making processes.
2018	Revised Code of Corporate Governance	Chapter 7 concerning institutional investors and other related institutions has been added into the Revised Code. Article 78 encourages institutional investors such as the managers of social security funds, enterprise annuities, insurance funds, public funds, and other investment entities under the supervisory and regulatory remits of national financial regulatory authorities, to engage in corporate governance reasonably by exercising their shareholder rights such as voting rights, inquiry rights and advisory rights in accordance with laws. Article 79 states that institutional investors may play an active role in corporate governance by participating in decision-making on major issues, recommending candidates for directors and supervisors, and supervising the performance of directors and supervisors in accordance with laws and regulations and the company's articles of association. Article 82 highlights that minority investors protection agencies should play an active role in the governance of listed companies and protect the legitimate rights and interests of minority investors through "holding shares for exercising rights" and other channels.
DOMESTIC INSTITUTIONAL INVESTORS		
Securities Investment Funds		

199 This table seeks to highlight the most important legal developments in relation to the development of institutional investors in China.

Dates	Law/Policy	Implications and Significance
1985-1990	China's domestic financial institutions cooperated with overseas financial institutions, launching an "China investment fund".	With the injection of overseas funds into the Chinese investment fund, it stimulated the development of the domestic investment fund industry. [200]
14 Nov. 1997	The State Council promulgated the "Interim Measures on the Management of Securities Investment Funds" (证券投资基金管理暂行办法)	Regulators started to regulate Securities Investment Funds in China. Jin Tai Fund and Kai Yuan Fund became the first two regulated funds permitted under the Measures. The "Old Ten" fund management companies were established between 1998-1999, comprising of 10 companies including the China Southern Fund Management, Guotai Fund Management, China Fund Management. At the beginning of March 1999, the CSRC begun the process of standardizing and liquidating the 75 funds that were established prior to the Measures in order to bring them in line with the Measures. By the end of September 2003, these 75 funds were consolidated into 29.
Sept. 2001	China's first open-ended securities investment fund, Hua-an Innovation Investment Fund, came into existence. This marked the start of a new era, where public offering funds begun to adopt an open-ended fund model.	By the end of 2002, the number of open-ended securities investment funds had increased to 17 and it went on to gradually replaced closed-ended funds as opened-ended funds had more advantages. This period was also the norming stage for the industry.
28 Oct. 2003	The "PRC Securities Investment Fund Law" (证券投资基金法) was promulgated and implemented.	This law accelerated the developments of securities investment funds. By the end of 2003, there were 3 money market funds in China. However, as of 2005, fund management companies still had little influence in the capital market because the size of the industry remained relatively small and the strategy it adopted, value investing, has yet to be widely accepted. [201]

[200] Liu, *supra* note 62.
[201] *Id*.

Dates	Law/Policy	Implications and Significance
27 Apr. 2018	The Guiding Opinions on Regulating the Asset Management Business of Financial Institutions (No. 106 [2018] of the People's Bank of China) (关于规范金融机构资产管理业务的指导意见) was promulgated by PBOC, CBIRC, CSRC and SAFE.	The opinion standardized the regulation of securities investment funds under the unified supervision of the People's Bank of China, the China Banking and Insurance Regulatory Commission and the CSRC. The Guidelines unified regulation standards for all asset management products issued by an asset management business such as financial services provided by a banking, trust, securities, fund, futures, insurance asset management institution, financial asset investment company. The Guidelines regulate the risks present in various aspects of the asset management business, such as product nesting, capital pool operations, non-standard asset investment, rigid repayment and the disorderly business operation of non-financial institutions.
6 Jan. 2020	Guiding Opinions of the China Banking and Insurance Regulatory Commission on Promoting the High-quality Development of Banking and Insurance Industries (中国银保监会关于推进银行业和保险业高质量发展的指导意见) were issued.	Foreign funded banks are encouraged to collaborate with their parent banks in the featured business including the wealth management business. Foreign financial institutions are encouraged to make equity investment(s) in the wealth management subsidiaries of commercial banks. Foreign asset management institutions are allowed to set up foreign-controlled joint venture wealth management companies with subsidiaries of domestic funded banks or insurance companies.
National Social Security Fund (NSSF)		
Aug. 2000	The NSSF was established	
2011	China's basic pension fund officially begun to enter the market.[202]	With the approval of the State Council, the NCSSF was entrusted with the investment operations of the basic pension funds of Guangdong and Shandong province in 2012 and 2015 respectively, each valued at 100 billion yuan, and has achieved high rates of return.[203]

[202] Capital Markets Institute of SSE, 长期资金发展现状及入市问题研究 [Study on the Development of Long-Term Funds and their Entry into the Market], 上证研报 [SSE Research Reports], at 5 (2019), http://www.sse.com.cn/aboutus/research/report/c/4800716.pdf.

[203] *Id.*

Dates	Law/Policy	Implications and Significance
23 Aug. 2015	The State Council promulgated the "Measures for the Administration of Investment in Basic Pension Insurance Funds" (基本养老保险基金投资管理办法)	The measures broadened the scope of investment for the funds, stipulating that the proportion of investment in stocks, stock funds, hybrid funds and stock pension products should not be higher than 30% of the net asset value of the funds, and allowing the funds to participate in the trading of stock index futures and treasury bond futures for the purpose of value preservation.
1 May 2016	The NSSF is required to comply with the 'Regulation on the National Social Security Fund' ("Regulation"), which came into force on 1 May 2016.	The Regulation consist of clear rules for the asset management of the NSSF, regarding the financing, management and use of the fund. On top of the Regulation, the NSSF is also required to comply with the PRC Social Insurance Law, the Interim Provisions on the Administration of Investment by the National Social Security Fund ("Interim Provisions"), the Interim Provisions on the Administration of Overseas Investment by the National Social Security Fund, and any other relevant documents approved by the State Council, the Ministry of Finance and the Ministry of Human Resources and Social Security in its operation and investment of the SSF.
Nov. 2016	The State announced the four custodians of the pension funds, namely, the Industrial and Commercial Bank of China, the Bank of China, the Bank of Communications and the China Merchants Bank.	
Insurance Fund		
1 Oct. 2009	The revised Insurance Law of the People's Republic of China came into force.	The revised Insurance Law significantly expanded the scope of investments permitted for insurance companies in China.
30 July 2010	The CIRC promulgated the "Temporary Measures for the Administration of the Utilization of Insurance Funds" (保险资金运用管理暂行办法)	Provided guidance for using insurance funds.
5 Sept. 2010	The CIRC issued "Interim Measures for Equity Investment with Insurance Funds" (保险资金投资股权暂行办法).	Insurance funds were allowed to make equity investments.

Dates	Law/Policy	Implications and Significance
19 Feb. 2014	The Notice of the China Insurance Regulatory Commission on Strengthening and Improving the Proportional Regulation of the Utilization of Insurance Funds (关于加强和改进保险资金运用比例监管的通知) was issued by CIRC.	The notice raised the limit of the proportion of the assets of insurance funds invested in equity assets from 25% to 30%. This amendment allowed insurance funds to invest more in the securities market to maximise their profits. By the end of 2019, the outstanding balance of insurance funds had reached RMB18.5 trillion, 13.15% of which was invested in stocks and funds.[204]
27 Jan. 2018	The Measures for the Administration of the Utilization of Insurance Funds (保险资金运用管理办法) was issued by CIRC.	These measures expanded the scope of investments by insurance fund, including investments into securitization products, setting up private funds by insurance asset management firms, investments into venture capital sector.
FOREIGN INSTITUTIONAL INVESTORS		
5 November 2002	The Interim Measures on the Administration of Domestic Securities Investment by Qualified Foreign Institutional Investors (合格境外机构投资者境内证券投资管理暂行办法) were promulgated by CSRC and PBOC.	Foreign investors must comply with this measure in order to make investments in China's securities market.
4 May 2011	Guidelines on the Participation of Qualified Foreign Institutional Investors in Stock Index Futures Trading (合格境外机构投资者参与股指期货交易指引) were issued by the CSRC.	QFIIs participating in stock index futures trading may only conduct hedging transactions pursuant to the relevant provisions of the China Financial Futures Exchange (CFFE). In addition, both the value of stock index futures contracts held by a QFII at the end of any trading day and the trading amount of stock index futures (except closing positions) of it during any trading day shall not exceed its investment quotas thus preventing short-selling.

[204] CBIRC, *supra* note 74.

Dates	Law/Policy	Implications and Significance
10 June 2018	The Provisions on the Foreign Exchange Administration of Domestic Securities Investment by Qualified Foreign Institutional Investors (合格境外机构投资者境内证券投资外汇管理规定) were issued by the SAFE.	The state shall conduct quota management of QFIIs' domestic securities investment and the investment quota of a single QFII shall be subject to the recordation and approval administration by the SAFE. QFIIs may, after obtaining the qualification license from the CSRC, obtain in the form of recordation an investment quota of not more than a certain proportion (hereinafter referred to as the "basic quota") of its asset size or the size of securities assets managed by it (hereinafter referred to as the "asset size"). Any application for an investment quota beyond the basic quota must be subject to approval by the SAFE. The investment quota of a foreign sovereign fund, central bank, monetary authority or other institution shall not be subject to the restriction of the proportion of asset size, and such institution may obtain corresponding investment quota based on its needs for investment in the domestic securities market. The standards for the basic quota of a QFII are as follows: (1) If the assets of (or assets managed by) a QFII or the group to which it is affiliated are mainly outside China, the formula for calculating the basic quota is: USD 100 million + average asset size in the last three years * 0.2% - obtained quota for RMB qualified foreign institutional investors (in US dollar, hereinafter referred to as the "RQFII quota"); (2) If the assets of (or assets managed by) a QFII or the group to which it is affiliated are mainly within China, the formula for calculating the basic quota is: five billion yuan or its equivalent + asset size in the last year * 80% - obtained RQFII quota (in US dollar); (3) The basic quota shall not exceed USD five billion (including institutions such as foreign sovereign funds, central banks and monetary authorities); (4) The basic quota shall not be less than USD 20 million.
10 Sept. 2019	The SAFE announced its decision to abolish the investment quota system under the QFII and RQFII Schemes pursuant to the approval of the State Council. Moreover, the restrictions on the pilot countries and regions under the RQFII Scheme were removed.	This decision marked a major step taken by the SAFE to deepen the reform and opening-up of the Chinese financial market.

Dates	Law/Policy	Implications and Significance
7 May 2020	The PBOC and the SAFE issued the Regulations on Funds of Securities and Futures Investment by Foreign Institutional Investors.	The Regulations have clarified and simplified the management requirements for QFIIs' investments in securities and futures in China, thus facilitating the further participation of foreign investors in China's financial market. The key points of the Regulations include: (1) Restrictions on investment quota of the QFII and RQFII have been scrapped and replaced by registration-based rules for QFIIs to register their cross-border funds transfer and currency exchange with the SAFE; (2) Integrated management will be implemented for both Renminbi and foreign currencies and QFIIs are given the freedom to choose which currency and when they remit money into the country; (3) The procedures for QFIIs' outward remittance have been significantly simplified as Tax Commitment Letters signed by QFIIs will replace previously required documents including the special audit reports on investment returns and tax clearance or tax filing certificates issued by Chinese certified public accountants; (4) The limit on the number of custodians is lifted, allowing a single QFII to entrust multiple domestic custodians and appoint one of them as the main custodian; (5) Foreign exchange risk and investment risk management mechanism for QFIIs' domestic securities investment will be further enhanced.

APPENDIX 2: REPRESENTATIVE ACTIVISM CASES BY INSTITUTIONAL INVESTORS IN CHINA (1994-PRESENT)[205]

No.	Year	Target Company	Type of the Target Company as of the Day of the Activism	Goal	Institutional Investor	Activism Strategies	Type of Activists as of the Day of the Activism	Result (whether the goal has been achieved)
1	1994	China Vanke Co., Ltd. 万科企业股份有限公司	POE	Claimed that some minority shareholders had teamed up to propose a restructuring of the company	Jun'an Securities (now Guotai Jun'an Securities, 国泰君安证券股份有限公司) and others	Teaming up with other institutional investors Informal influence: held a press conference to ask for a governance change through restructuring	SOII, Securities company, Founded by 5 SOEs in 1992, but the proportion of state-owned shares was unknown.	Failed
2	2002	ZTE Corporation 中兴通讯股份有限公司	POE	Objection to the issuance of additional H shares	Dacheng Fund Management 大成基金管理有限公司 and others	Exercise of voting rights Object shareholder proposal to prevent the decrease in share price	SOII, SIF firm, State Council, MOF, SASAC and other government agencies indirectly held over 50% of the shares	Succeeded (H shares were issued in 2004, after a two year delay)
3	2003	China Merchants Bank 招商银行股份有限公司	POE (but the state held over 30% of the shares)	Objection to the issuance of convertible bonds	China Asset Management Co., Ltd. 华夏基金管理有限公司 and others	Teaming up with other institutional investors Object shareholder proposal to prevent the decrease in share price	SOII, SIF firm, SASAC of the Government of Beijing City, the Government of Beijing City and SASAC of the Government of Chongqing City held over 50% of the shares	Failed

[205] Institutional investors in Appendix 2 include general legal persons and non-legal-person enterprises, domestic professional institutional investors and foreign institutional investors, *see supra* Chart 3.

4	2004	China Vanke Co., Ltd. 万科企业股份有限公司	POE (but an SOE held over 10% of the shares, and was the largest shareholder of Vanke)	Amendment of the articles of association	China Asset Management Co., Ltd. 华夏基金管理有限公司 Boshi Fund Management Co., Ltd. 博时基金管理有限公司 and others	Teaming up with other institutional investors	SOII, SIF firm, SASAC of the Government of Beijing City, the Government of Beijing City and SASAC of the Government of Chongqing City held over 50% of the shares (China Asset Management) POII, SIF firm (Boshi)	Succeeded
5		Chongqing Department Store Co., Ltd. 重庆百货大楼股份有限公司	SOE (the actual controller disclosed in financial report was SASAC of the Government of Chongqing City)	Objection to the issuance of additional shares	Fortune Sg Fund Management Co., Ltd. 华宝基金管理有限公司	Exercise of voting rights	SOII, SIF firm, SASAC indirectly held 49.98% of the shares.	Succeeded
6	2007	Guangxia (Yinchuan) Industry Co., Ltd. (now Ningxia Western Venture Industrial Co., Ltd. 宁夏西部创业实业股份有限公司)	POE	Sued for the civil tort of misrepresentation	Dacheng Fund Management 大成基金管理有限公司	Litigation	SOII, SIF firm, State Council, MOF, SASAC and other government agencies indirectly held over 50% of the shares	Failed
7	2008	Ping An Insurance 中国平安保险（集	POE	Objection to the refinancing proposal	Dacheng Fund Management 大成基金管理有限公司	Exercise of voting rights	SOII, SIF firm, State Council, MOF, SASAC and other government	Failed

		团）股份有限公司			Lion Fund Management 诺安基金管理有限公司		agencies indirectly held over 50% of the shares (Dacheng) POII, SIF firm (Lion Fund)	
8		China Eastern Airlines 中国东方航空股份有限公司	SOE (the actual controller disclosed in financial report was SASAC)	Veto an acquisition of shares by Singapore Airlines	Rongtong Fund Management 融通基金管理有限公司 and Boshi Fund Management Co., Ltd. 博时基金管理有限公司	Exercise of voting rights	POII, SIF firm, (Rongtong) and POII, SIF firm, But State Council indirectly held 26% of the shares (Boshi)	Succeeded
9		Ningxia Building Materials Group Co.,Ltd. 宁夏建材集团股份有限公司	POE	Request for participation in management	Shanghai Baoyin Investment Consulting Co., Ltd. 上海宝银投资咨询有限公司	Informal influenceublicly made requests to the board.	POII, Other professional institutions	Failed
10	2010	Henan Shuanghui Investment & Development Co., Ltd. 河南双汇投资发展股份有限公司	POE	Veto a waiver of the right of first refusal	Harvest Fund Management 嘉实基金管理有限公司 Boshi Fund Management Co., Ltd. 博时基金管理有限公司 and others	Exercise of voting rights	POII, SIF firm, But MOF indirectly held 8% of the shares (Harvest Fund) POII, SIF firm, (Boshi)	Succeeded
11	2011	Xiamen Xiangyu Co.,Ltd. 厦门象屿股份有限公司	SOE(the actual controller disclosed in financial report of 2007 was	Sued for the civil tort of misrepresentation	Huarun Shenguotou Trust Co., Ltd. 华润深国投信托有限公司,	Litigation	SOII, Trust company, SASAC indirectly held over 50% of the shares (Huarun)	Succeeded

			a wholly state-owned enterprise)		Hongshan Fund Management 深圳市红山投资管理有限公司		POII, Private equity firm, (Hongshan)	
12		Anhui Quanchai Engine Co., Ltd. 安徽全柴动力股份有限公司	SOE (the actual controller disclosed in financial report was the Government of Quanjiao County)	Urge the company as well as Jiangsu Rongsheng Heavy Industries Co., Ltd. To perform their respective contractual obligations	Aegon-Industrial Fund Management 兴证全球基金管理有限公司, Orient Securities 东方证券股份有限公司	Teaming up with other institutional investors	POII, SIF firm, But the Financial Department of Fujian Province indirectly held 10.3% of the shares (Aegon-Industrial Fund) POII, Securities company, But the biggest shareholder was wholly state-owned. (Orient Securities)	Failed
13		Dashang Co., Ltd. 大商股份有限公司	POE	Propose the giving of cash incentive to the company's management	Franklin Templeton Sealand Fund Management Co., Ltd. 国海富兰克林基金管理有限公司, Penghua Fund Management 鹏华基金管理有限公司 and others	Teaming up with other institutional investors	POII, SIF firm, But the Government of Guangxi Zhuang Autonomous Region indirectly held 14.7% of the shares (Franklin) POII, SIF firm, But SASAC of the government of Shenzhen province indirectly held 22% of the shares (Penghua Fund)	Failed
14	2012	Chongqing Brewery Co., Ltd	POE	Recommend the removal of the	Dacheng Fund Management 大成基金管理有限公司	Shareholder proposal Governance change	SOII, SIF firm	Failed

		重庆啤酒股份有限公司		chairman			
15		Gree Electric Appliances Inc. 珠海格力电器股份有限公司	SOE (the actual controller disclosed in financial report was SASAC of Government of Zhuhai City)	Selection and recommendation of candidates for the board of director	Penghua Fund Management 鹏华基金管理有限公司 Yale University Endowment	Teaming up with other institutional investors	POII, SIF firm, (Penghua) FOII, Other professional institution (Yale)	Succeeded
16		Beingmate Baby & Child Food Co., Ltd. 贝因美股份有限公司	POE	Recommend the sale of its infants related businesses	J.V.R International	Shareholder proposal	FOII, SIF firm	Succeeded
17		Zhejiang Huahai Pharmaceutical Co., Ltd. 浙江华海药业股份有限公司	POE	Veto the proposal for the dismissal of the general manager	E Fund Management 易方达基金管理有限公司 Lion Fund Management 诺安基金管理有限公司 and others	Exercise of voting rights Prevent governance change	POII, SIF firm, But the government of Guangdong province indirectly held 37.7% of the shares (E Fund); POII, SIF firm (Lion Fund)	Succeeded
18	2013	Shanghai Jahwa United Co., Ltd. 上海家化联合股份有限公司	POE	Selection and recommendation of candidates for the board of director	E Fund Management 易方达基金管理有限公司 China Universal Asset Management	Teaming up with other institutional investors	POII, SIF firm, (E Fund) POII, SIF firm, But SASAC of the government of Shanghai City indirectly held	Succeeded

					汇添富基金管理股份有限公司 China Merchants Fund Management Co., Ltd. 华商基金管理有限公司		11.2% of the shares (Huashang Fund) POII, SIF firm, But SASAC of government of Gansu Province indirectly held 12% of the shares (China Universal Asset)	
19		Dashang Co., Ltd. 大商股份有限公司	POE	Veto the proposal for a major asset restructure	Fullgoal Fund 富国基金管理有限公司	Exercise of voting rights	POII, SIF firm	Succeeded
20		China Merchants Bank 招商银行股份有限公司	POE (but the state held over 30% of the shares)	Nomination of candidates for the position of non-executive director	Anbang Insurance Group 安邦保险集团股份有限公司	Shareholder proposal Governance change	SOII, Insurance company, MOF indirectly held 98% of the shares	Failed
21	2014	Taiji Computer Corporation Limited 太极计算机股份有限公司	SOE (the actual controller disclosed in financial report was a wholly state-owned enterprise)	Veto the proposal regarding the activities constituting daily transactions	Baoying Fund Management 宝盈基金管理有限公司	Exercise of voting rights	SOII, SIF firm SASAC indirectly held 57% of the shares	Succeeded
22		China Minsheng Bank 中国民生银行股份有限公司	POE	Nomination of candidates for the board of directors	Anbang Insurance Group 安邦保险集团股份有限公司	Shareholder proposal Governance change	SOII, Insurance company, MOF indirectly held 98% of the shares	Succeeded

23		GuiZhou QianYuan Power Co., Ltd. 贵州黔源电力股份有限公司	SOE (the actual controller disclosed in financial report was SASAC)	Issue of bonus shares	Shanghai Zexi Investment Management 上海泽熙投资管理有限公司	Shareholder proposal	POII, SIF firm	Failed
24		Ningbo United Group Co., Ltd. 宁波联合集团股份有限公司	POE	Issue of bonus shares	Shanghai Zexi Investment Management 上海泽熙投资管理有限公司	Shareholder proposal	POII, SIF firm	Failed
25		Ningbo Zhongbai Co., Ltd. 宁波中百股份有限公司	POE	Re-election of the board of directors	Xizang Zexi Investment Management 西藏泽添投资发展有限公司	Shareholder proposal Governance change	POII, SIF firm	Succeeded
26		Huadong Medicine Co., Ltd. 华东医药股份有限公司	POE	Veto the proposal of exempting the company's controlling shareholder's asset injection commitment	Penghua Fund Management 鹏华基金管理有限公司 and others	Exercise of voting rights	POII, SIF firm, But SASAC of the government of Shenzhen province indirectly held 22% of the shares.	Succeeded
27		Shanghai Aiko Solar Energy Co., Ltd. 上海爱旭新能源股份有限公司	POE	Selection and recommendation of candidates for the board of directors and supervisors and	Beijing Zhengmou Management Consulting Co., Ltd. 北京正谋管理咨询有限责任公司	Open call for voting rights Governance change	POII, Other professional institution	Failed

				auction off some of the company's assets				
28		AN HUI WENERGY COMPANY LIMITED 安徽省皖能股份有限公司	SOE (the actual controller disclosed in financial report wasSASAC of Government of Anhui Province)	Proposed to revise the company's 2013 annual profit distribution plan	HONGTA HOTLAND AMC 红塔红土基金管理有限公司 and others	Shareholder proposal	POII, SIF firm, But the State Council indirectly held 30.9% of the shares	Failed
29		Tongwei Co., Ltd 通威股份有限公司	POE	Establish buyout fund in cooperation with the investee company	Heaven-Sent Capital Management Group Co., Ltd 硅谷天堂产业集团股份有限公司		POII, Private equity firm	Succeeded
30	2016	FAW Jiefang Group Co., Ltd 一汽解放集团股份有限公司	SOE (the actual controller disclosed in financial report was SASAC)	Veto the proposal for extending the term of commitment	Venus Investment Management Co., Ltd.深圳市明曜投资管理有限公司	Open call for voting rights to vote	POII, SIF firm	Succeeded
31		Yinchuan Xinhua Commercial (group) Co.,ltd. 银川新华百货商业集团股份有限公司	POE	Proposal to convert the company's capital reserve into share capital	Shanghai Bao Yin Chuang Ying Investment Management Co., Ltd 上海宝银创赢投资管理有限公司 and Shanghai Zhao Win Equity Investment Fund	Shareholder proposal	POII, SIF firm (Bao Yin Chuang Ying) Other professional institution (Zhao Win)	Failed

					Management Co., Ltd. 上海兆赢资产管理有限公司			
32		Gree Electric Appliances Inc. 珠海格力电器股份有限公司	SOE (the actual controller disclosed in financial report was SASAC of Government of Zhuhai City)	Veto the proposal for acquiring Zhuhai Yinlong Electric Appliance Co., Ltd.	China Securities Finance Co., Ltd. 中国证券金融股份有限公司	Exercise of voting rights	SOII, Securities company, SZSE, SSE and CSRC held 81.3% of the shares in total	Succeeded
33	2017	Zhenxing Biopharmaceutical & Chemical Co., Ltd. (now Pacific Shuanglin Bio-pharmacy Co., LTD 派斯双林生物制药股份有限公司)	POE	Hostile takevoer	Zhemin Tianhong Investment Partnership (L.P.) 杭州浙民投天弘投资合伙企业（有限合伙）	General offer to shareholders	POII, General legal persons and non-legal-person enterprises	Succeeded
34		Sinovel Wind Group Co.,Ltd. 华锐风电科技（集团）股份有限公司	POE	Sued for the civil tort of misrepresentation	Beijing Yongxing Honsheng Investment Co., Ltd. 北京永兴鸿升投资有限公司	Litigation	POII, General legal persons and non-legal-person enterprises	Succeeded
35		Shanghai Hile Bio-Technology Co., Ltd. 上海海利生物技术股份有限公司	POE	Sued to void the resolution of shareholders meeting	China Securities Investor Services Center 中证中小投资者服务中心有限责任公司	Litigation	SOII, Non-profit financial institution, (under the direct administration of CSRC)	Succeeded

36	2019	Shenzhen Sunrise New Energy Co.,Ltd. 深圳市兆新能源股份有限公司	POE	Proposed to dismiss the chairman of the board	Shenzhen Huitong Zhengyuan Private Equity Investment Fund Partnership Enterprise L.P. 深圳市汇通正源股权投资基金合伙企业（有限合伙）	Shareholder proposal Governance change	POII, Private equity fund	Failed
37		Elec-Tech International Co.,Ltd. 安徽德豪润达电气股份有限公司	POE	Proposed to dismiss several directors	China Life Insurance Security Fund Management 国寿安保基金管理有限公司 CCB Principal Asset Management 建信基金管理有限责任公司 Beixin Ruifeng Fund Management 北信瑞丰基金管理有限公司	Teaming up with other institutional investors Shareholder proposal	SOII, Subsidiary of state-owned insurance company, the State Council indirectly held 69% of the shares (China Life Insurance Security Fund Management) POII, Subsidiary of state-owned commercial bank, But the State Council indirectly held 37% of the shares (CCB Principal Asset Management) POII, Subsidiary of state-owned trust company, But the Government of Beijing City indirectly held 20% of the shares	Failed

							(Beixin Ruifeng Fund Management)	
38		Jiangsu Protruly Vision Technology Group Co., Ltd. 江苏保千里视像科技集团股份有限公司	POE	Sued for the civil tort of misrepresentation	CRRC Jinzheng Investment Co., Ltd. 中车金证投资有限公司	Litigation	SOII, General legal persons and non-legal-person enterprises SASAC held 100% of the shares	Succeeded
39	2020	Dalian Sunasia Tourism Holding Co.,Ltd. 大连圣亚旅游控股股份有限公司	SOE (the actual controller disclosed in financial report was Dalian Xinghai Bay Development and Construction Management Centre)	Proposed to dismiss the former chairman and vice chairman of the company	Pan jing equity investment fund management (Shanghai) co., LTD 磐京股权投资基金管理（上海）有限公司	Shareholder proposal Governance change	POII, Private equity firm	Succeeded
40	2021	Innovation Medical Management Co.,Ltd. 创新医疗管理股份有限公司	POE	Proposed to dismiss certain members of the board	Hangzhou Lanchuang Investment Partnership 杭州岚创投资合伙企业（有限合伙）, Zhejiang Fu Zhe Capital Management 浙江富浙资本管理有限公司	Teaming up with other institutional investors Shareholder proposal	POII, General legal persons and non-legal-person enterprises (Hangzhou Lanchuang), SOII, General legal persons and non-legal-person enterprises SASAC of the government of Zhejiang province indirectly held 100% of the shares (Fu Zhe Capital)	Failed

41		Beijing Jingxi Culture& Tourism Co., Ltd. 北京京西文化旅游股份有限公司	POE	Veto the proposal for appointing an accounting firm	Fuld Life Insurance Co., Ltd. 富德生命人寿保险股份有限公司	Exercise of voting rights	POII, Insurance company	Succeeded
42		Shandong Xinchao Energy Corporation Limited. 山东新潮能源股份有限公司	POE	Proposed to dismiss the board of director	Shenzhen Jinzhichangsheng Investment Co., Ltd.深圳市金志昌盛投资有限公司 and others	Teaming up with other institutional investors Shareholder proposal	POII, General legal persons and non-legal-person enterprises	Failed
43		Zhengzhou Sino-Crystal Diamond Co., Ltd. 郑州华晶金刚石股份有限公司	POE	Veto six proposals in the general meeting	Henan Lianchuan Investment Co., Ltd. 河南农投金控股份有限公司	Exercise of voting rights	SOII, General legal persons and non-legal-person enterprises The department of Finance of Henan Province indirectly held 79.8% of the shares	Succeeded

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