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**Regulation and Corporate Governance of China's top 100 listed
companies: Whither the Rule of Law?**

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1. Introduction:

China has experienced dramatic developments in the growth of a rule-based approach to its securities market and the operation of corporate law since the early 1990s. These efforts sought to keep pace with the speed at which the market economy has grown in China over this time. However, the development of a sophisticated system of corporate law and corporate governance has tended to lag well behind rapid market developments, even in regard to the most advanced sector of China's major stock exchange listed companies. This paper seeks to assess the nature of current patterns of law and regulation of this sector by reference to data derived from China's top 100 listed companies. This paper will explore this theme by reference to findings from fieldwork undertaken by the authors in China over the last two years.¹

China's efforts to re-establish a market-oriented economy began to assume momentum in the early 1990s; this saw the formal establishment of Stock Exchanges in 1990 and 1991 in Shanghai and Shenzhen, respectively.² This was followed by the creation of the China Securities Regulatory Commission (CSRC) in 1992, although it was not until 2002 that the Commission was finally given sole responsibility for the management of stock exchanges and a range of policy making and regulatory powers in this area.³

The development of China's "socialist market economy" received a considerable stimulus as a result of the 1992 tour of southern China by PRC paramount leader Deng Xiaoping; this led to pressure from state owned enterprises to corporatize and to become shareholding companies.⁴ As Ruan Ming noted in 1994 in his biography of Deng Xiaoping, "the economic forces released during China's ten-year reform [effort since the early 1990s] made it impossible to push the country's economy back into the bird cage of the old planned economy."⁵ As Ruan noted in regard to Deng's approach to reform, "...Deng has always lingered at the crossroads of an open economy and a closed political system..."⁶ His was a pragmatic and cautious approach to reform as

¹ Professor Neil Andrews also played a leading role in the conduct of this fieldwork in China.

² S Green, *The Development of China's Stock Market, 1984-2002, Equity politics and market institutions*, London, RoutledgeCurzon, 2004 at pp 62-65. Also see: CE Walter and FJT Howie, *'To Get Rich is Glorious' China's Stock Markets in the '80s and '90s*, Houndmills, Hampshire, Palgrave, 2001; and S Green, *China's Stockmarket : A Guide to its Progress, Players and Prospects*, London, The Economist and Profile Books Ltd, 2003; CE Walter and FJT Howie, *Privatizing China: The Stock Markets and their Role in Corporate Reform*, Singapore, John Wiley & Sons, 2003.

³ Green (2004), *supra* at p 137. For some further historical background on the CSRC see its web site at: http://www.csrc.gov.cn/en/homepage/about_en.jsp

⁴ In regard to the development of corporate forms in China see further, J Fu, "The Enterprise Concept in Chinese Law and its Application in PRC Company Law", (1998) 8 *Australian Jnl of Corporate Law* 266-299.

⁵ R Ming, *Deng Xiaoping: Chronicle of an Empire*, Boulder, Westview, 1994 at p 243.

⁶ *Ibid* at p 244.

was illustrated in 1992 when he discussed the possible risks associated with stock market reform and observed:

“As for securities and the stock market, are they finally good or bad? Are they dangerous? Are they things that only capitalism has or can socialism also make use of them? To decide whether they can be used, we must experiment first. If we think they work, if after a year or two we think they are good, then we can expand them. If problems arise, we can close them down, immediately and completely. And even if we close them down, we can do so quickly or slowly, or we could even leave a little tail.”⁷

Deng Xiaoping suggested that stock markets were not necessarily capitalist institutions, but were capable of being used by a “socialist market economy”. Deng’s capacity to communicate a new vision for China was encapsulated in a number of subsequently oft repeated observations made by Deng; these included: (i) “It doesn’t matter if a cat is black or white, as long as it catches mice;” (ii) “Poverty is not socialism. To be rich is glorious;” (iii) “When you open the window the flies come in” and (iv) “We will cross the river by feeling the stones under our feet, one by one.” These kinds of expressions were “deliberately elastic” in nature, adding to their effectiveness.⁸ In pointing to the momentum created by expressions such as this, Gordon Redding has noted that:

“What Deng and his successors created was a state in which pragmatism would rule and policy would change in pursuit of prosperity; in which the attitudes which accompany ownership would take over from the assumption of dogma in which the family would be restored, but still a state where the role of government, and the Party, would be to maintain order – a sacred duty not abandoned, despite the ferment of experimentation swirling around it.”⁹

Chinese officials would continue to resist describing their system as a “capitalist” one, and would instead describe it as one which has utilised the corporate form and share ownership. In any event, as Jianfu Chen observes, the use of the term “socialist market economy” from 1992 “introduced a practical licence to use capitalism in the economic sphere and to introduce capitalist mechanisms and measures (including legal measures) that will facilitate economic development.”¹⁰

Interestingly, as Peter Nolan has argued, in contrast to other centrally planned economies, China’s economic development may have been influenced less by economic theories than by strong internal political forces, such as the dominance of the state in ensuring political stability whilst encouraging economic reform. In addition, the influence of Hong Kong and Taiwanese models may have been

⁷ Quoted by S Green in *The Development of China’s Stock Market, 1984-2002*, supra at pp 138-139.

⁸ RC Keith and Zhiqiu Lin, *Law and Justice in China’s New Marketplace*, London, Palgrave, 2001 at p 239.

⁹ G Redding, “Feeling the stones on the river bed: Prospects and implications for China’s entry into the world of global competition”, *Ivey Business Journal*, May/June 2005 at pp 1-2.

¹⁰ JF Chen, “Policy as Law and Law as Policy – The Role of Law in China’s Development Strategy”, (pp 251-270) in *Law and Development in East and Southeast Asia* (ed by C Antons), London, RoutledgeCurzon, 2003 at p 257.

important in guiding change¹¹; Taiwan demonstrated that planning was important in a period of economic transformation, whilst Hong Kong demonstrated that a vibrant market economy could develop without dramatic political liberalisation.¹²

By 2005, there were over 800 companies listed on the Shanghai Stock Exchange and another 500 companies were listed in Shenzhen. In addition about 140 mainland companies were listed on the Hong Kong Stock Exchange and over 30 Chinese companies were listed in London, New York or on the NASDAQ exchange in the United States. Whilst the PRC Mainland stock markets have become somewhat sluggish in recent years, the Chinese economy has been reporting average growth rates of about 8% per annum over two decades.¹³ However, despite all these dramatic economic developments, the supporting institutions of a stock market failed to keep up with the pace of change.¹⁴ Law and the legal system stand out as some of these laggards.

2. Fashioning a New Legal System in China

In response to the rapid economic development that has occurred in China since the early 1990s, a new legal system had to be fashioned; this was to in keeping with the professed commitment to the rule of law that China's leaders had been making since the commencement the current reform movement in 1979, after the decade long tragedy of the Cultural Revolution which had so politicised the role of law in China.¹⁵ Since this time the decision was made to use legislation rather than policy as the basic source of rules in China.¹⁶

The emergence of the rule of law as a priority of the Chinese State may be seen to begin in this period from the later 1970s, although the implementation of this ideal has been mixed, despite the fact that in 1999 the Chinese Constitution was amended to provide for the establishment of "a socialist rule-of-law state".¹⁷ This also required that government should act in accordance with the law. Thus, the following new paragraph was added to Article 5 of the PRC Constitution on 15 March 1999:

¹¹ Experience in these two jurisdictions was certainly more attractive than the instability that had occurred with the economic changes that had been commenced in the former Soviet Union and in the former communist countries of Eastern Europe.

¹² P Nolan, "Introduction : The Chinese Puzzle", pp 1-20 in *China's Economic Reforms: The Costs and Benefits of Incrementalism*, (ed by Q Fan and P Nolan), London, St Martin's Press, 1994 at pp 12-17.

¹³ E Prasad and T Rumbaugh, "Overview", in *China's Growth and Integration into the World Economy: Prospects and Challenges*, (ed by E Prasad), Washington DC, International Monetary Fund, 2004, at p 1. Also see generally, LJ Brahm, *China's Century: The Awakening of the Next Economic Powerhouse*, Singapore, John Wiley & Sons, 2001; J Story, *China : the race to market*, London, Prentice Hall 2003; and D Guthrie, *Dragon in a Three-Piece Suit: The Emergence of Capitalism in China*, Princeton, Princeton University Press, 1999.

¹⁴ Green (2004) supra at p 138

¹⁵ S. Lubman, "Introduction: The Future of Chinese Law" pp 1-21 in *China's Legal Reforms*, (ed by S Lubman), Oxford, Oxford University Press 1996 at p. 2

¹⁶ SB Lubman, *Bird in a Cage: Legal Reform in China After Mao*, Stanford, Stanford University Press, 1999 at p 7 and p 138 ff.

¹⁷ R Peerenboom, *China's Long March toward Rule of Law*, Cambridge, Cambridge University Press, 2002 at p 1.

“The People’s Republic of China governs the country according to law and makes it a socialist country ruled by law.”

The provision of greater protection to private property rights may also serve to enhance the development of the rule of law in China. In this regard, the passage of a further constitutional amendment in March 2004 which strengthened private property rights is an important signal regarding adherence to the idea of the rule of law in China. Thus, Article 13 of the PRC Constitution now states that:

“The legal private property of citizens is inviolable. The State protects the private property and inheritance rights of citizens in accordance with law. The State may in the public interest expropriate the private property of citizens and provide compensation in accordance with law.”¹⁸

Legal reform in China may not have been an essential precondition to economic reform as evidenced by the fact that these reforms actually occurred after economic reforms had gained momentum. Pragmatism has tended to dominate over strict adherence to law. Nevertheless, two leading Chinese government researchers, Xin Chun Ying and Fan Gang, confidently observed in 2000 that:

“The importance and the need for the rule of law has been more and more recognized during the process of economic reform and development...The trend of legal and economic development seems irreversible: more laws and strong law enforcement will be needed to legalize the relations under [the] market system...‘The era of rule of man’ or ‘rule of a good leader’ is going to be over as its foundations [are] being dissolved. 1995 was..[a]..milestone because after 20 years [of] debate in [the] political and legal field, the ‘rule of law’ became an accepted basic principle of the Government.”¹⁹

Drawing on the work of Lon Fuller²⁰ and Clifford Geertz²¹, Randall Peerenboom accepts that China is well advanced in being able to demonstrate that it has at least a “thin” theory of the rule of law, which “stresses the formal or instrumental aspects of the rule of law”. Such a “thin” system of laws would have laws and legal institutions that are “general, public, prospective, clear, consistent, capable of being followed, stable, and enforced.”²² However, Peerenboom warns that China’s system still looks more like a system of rule by law than a system of the rule of law. As he explained in 2002:

“Whereas the core of the rule of law is the ability of law and legal system to impose meaningful restraints on the state and individual members of the ruling elite, rule by law refers to an instrumental conception of law in which law is merely a tool to be used as the state sees fit.

¹⁸ This amendment was inserted in the Constitution at the Second Session of the Tenth National People’s Congress on 14 March 2004.

¹⁹ CY Xin and G Fan, *The Role of Law and Legal Institutions in China’s Economic Development: 1978-1995*, Beijing, Law Press, 2000 at pp 84-85. See further, CAG Jones, “Capitalism, Globalization, and Rule of Law: An Alternative Trajectory of Legal Change in China, (1994) 3 *Social and Legal Studies* 195-221.

²⁰ LL Fuller, *The Morality of Law*, Revised Edition, New Haven, Yale University Press, 1969.

²¹ C Geertz, *The Interpretation of Cultures : Selected Essays*, New York, Basic Books, 1974;

²² Peerenboom, *supra* at p 3 and p 6.

Despite remarkable progress, the reach of the law is still clearly limited. The [Communist] Party's actual role in governing the country is at odds with or not reflected in the Constitution or other legal documents. In some cases, Party policies continue to trump laws. The *nomenclatura* system whereby the Party is able to appoint or at least veto the appointment of key members of the people's congresses and courts undermines the legitimacy, independence, and authority of the legislature and judiciary."²³

As we will see when we come to discuss corporate governance within the largely state controlled top 100 PRC listed companies, the Communist Party also continues to play a critical role in making senior appointments and decisions within most of these corporations. As the fieldwork for this study has found, it is often the case that the Secretary of the Party Committee within such listed companies also holds a senior position on the board, such as that of Chairman or General Manager.²⁴ Contemporaneously, in regard to the private company sector, and in recognition of the contribution that private entrepreneurs had made to China's modernization efforts, in July 2000, President Jiang Zemin overturned the old ban on such entrepreneurs being admitted as members of the Party.²⁵

This change followed from Jiang's "Three Represents" slogan that sought to adapt the Party's ideology to changed circumstances and to capture the principal new forces in China's economy; thus the Party was seen as not only representing workers and peasants, but, in line with more recent developments, it was also seen as representing the broad range of people contributing to economic and cultural development in China.²⁶ Whilst cooptation of private entrepreneurs into the Party may serve to prevent them from forming opposition political parties to represent them, their inclusion into the CCP conflicted with the Party's traditional Leninist principles.²⁷ It has however been suggested that the Party had no choice other than to bolster its links with this emerging new business elite.²⁸ This was yet another pragmatic response by China's political leaders to rapidly changing economic and social conditions.

In any event, whilst the new economic system in China has replaced the "bird cage" of the old planned economy²⁹, it has been suggested by some that such a "bird cage" still exists in regard to law and legal reform in China.³⁰ Reviewing the reforms of

²³ Ibid at p 8.

²⁴ This can also be seen from many annual reports issued by listed companies.

²⁵ BJ Dickson, *Red Capitalists in China: The Party, Private Entrepreneurs, and Prospects for Political Change*, Cambridge, Cambridge University Press, 2003 at pp 161-162. By 2003, over 100,000 private owners or capitalists had joined the Communist Party since the change in policy in 2000: Xiaobo Hu, "The State and the Private Sector in a New Property Rights System", pp 69-89 in *China after Jiang* (ed by Gang Lin and Xiaobo Hu), Woodrow Wilson Center Press, Washington DC, 2003 at p 83.

²⁶ See further, Jiang Zemin, *On the "Three Represents"*, Beijing, Foreign Language Press, 2001. Also see generally, B Gilley, *Tiger on the Brink: Jiang Zemin and China's New Elite*, Berkeley, University of California Press, 1998.

²⁷ Dickson, *supra* at p 166.

²⁸ Xiaobo Hu, "The State and the Private Sector in a New Property Rights System", pp 69-89 in *China after Jiang* (ed by Gang Lin and Xiaobo Hu), Woodrow Wilson Center Press, Washington DC, 2003 at p 85. Hu also notes (at pp 83-84) that some have questioned whether the "three represents" may have a narrower constituency than Jiang intended in that it may "represent only the rich, the powerful, and the fortunate – those bureaucrats and managers 'in the right place at the right time...'"

²⁹ As Ruan Ming *supra* had described it (at p 243).

³⁰ SB Lubman, *supra*; Also see Peerenboom *supra*.

recent decades, Stanley Lubman noted in 1999 that by that time: “Law has gained more importance than it has ever possessed in Chinese history,” but he warned that “..given the novelty of the legal institutions created or revived since the late 1970s, it is no wonder that their development has been limited, hesitant, and uncertain.”³¹ Path dependency theorists would also no doubt point to the historically limited role of law and the dominance of the State both during the Communist era as well as during earlier periods of Chinese history.³²

Reviewing earlier studies of the Chinese legal system, Peerenboom observes in regard to the pre-Communist Imperial legal systems that “...although the Imperial system was quite well-developed in many respects, it could not be characterized in terms of rule of law if by that one means a system in which law imposed meaningful limits on the rulers...Nevertheless, law was indisputably a tool to serve the interests of the state.”³³ During the Mao era, law was seen as a system that should serve political ends and “at no time during the Mao period was the law meant to impose meaningful restraints on the CCP. Law was indisputably a tool to serve the interests of the Party-state.”³⁴ None of this is really controversial; for example, the Chief Justice of the Supreme People’s Court and former Minister of Justice of the PRC, Xiao Yang, has also observed that:

“Enacting law is the premise of legal system construction and the enforcement of law is the crux of legal system construction. Only by turning the stipulations of law into the practice of law and ensuring the unimpeded implementation of law, can legal system construction obtain final success. In China, as a ruling party, the Communist Party’s attitude towards law will directly affect the enforcement of law. In order to redress such past phenomena as existed within the Party – such as negating the law, making light of the legal system, using the Party to replace governance, using power to override the law and not complying with the law – we must demonstrate our determination to carry out legal system construction and guarantee strict enforcement of the law.”³⁵

The problem of the implementation of China’s increasing body of economic laws is clearly one of growing importance.³⁶ In addition to the problems noted by Xiao

³¹ SB Lubman, supra at p 2.

³² Jing Junjian, for example, points out that a very similar set of basic principles guided Chinese civil law for almost twelve centuries, from the Codes of the Tang dynasty (618-907), through the Ming (1368-1644) and Qing (1644 -1911) dynastic Codes: “Legislation Related to the Civil Economy in the Qing Dynasty” (pp 42-84) in *Civil Law in Qing and Republican China*, (Ed by K Bernhardt and PCC Huang), Stanford, Stanford University Press, 1994; Also see, PCC Huang, *Civil Justice in China: Representation and Practice in the Qing*, Stanford, Stanford University Press, 1996; PCC Huang, *Code, Custom and Legal practice in China : The Qing and the Republic Compared* , Stanford, Stanford University Press, 2001.

³³ Peerenboom, supra at p 41.

³⁴ Ibid at pp 45-46. Also see generally, PB Potter, *From Leninist Discipline to Socialist Legalism Peng Zhen on Law and Political Authority in the PRC*, Stanford, Stanford University Press, 2003.

³⁵ Xiao Yang, “A New Chapter in Constructing China’s Legal System” (pp 219-233) in *China’s Century: The Awakening of the Next Economic Powerhouse*, (ed by LJ Brahm), Singapore, John Wiley & Sons (Asia) Pte Ltd, 2001 at pp 223-4.

³⁶ See generally the collection of essays on this topic, Jianfu Chen, Yuwen Li and JM Otto (Eds), *Implementation of Law in the People’s Republic of China*, The Hague, Kluwer Law International, 2002.

Yang, Randall Peerenboom concludes his overview of China's legal developments by noting that:

“On the whole, however, China's traditions do not provide a very friendly environment for rule of law to grow in. Ironically, the main contribution of the Mao era may have been to highlight the urgent need for a more law-based order. The disastrous Cultural Revolution made it clear to all that China needed to rebuild its legal system to limit government arbitrariness and provide the predictability and certainty required to attract foreign investors and grow the economy.”³⁷

Politics is seen by many as being at the heart of the problem regarding the effectiveness of law and legal institutions in contemporary China because of the Communist Party's “determination to retain political control....[L]aw and the courts are still expected to be secondary to Party policy.”³⁸ Law has been seen as a means of governing China, provided that this occurs under the leadership of the Party.³⁹ Chief Justice Xiao Yang also points out that “[o]ne of the important items of concern is to urge party members to observe the Constitution and law.”⁴⁰ In so far as the rule of law is concerned, an instrumentalist approach to the use of law dominated during the Maoist period and subsequently, under the leadership of Deng Xiaoping, law was used to establish order and stability after the chaos of the Cultural Revolution and to foster economic development.⁴¹

In a transitional period, this is not necessarily bad as it preserves a degree of social stability that may otherwise be lacking in the absence of a “thick” civil society and legal culture that may provide the basis for authority and corporate governance in the corporate sector. It is for this reason that the articulation of “thin” models of law and governance in China may at times seem somewhat shrill as this may hamper the movement from an instrumentalist conception of law to a more broadly based version of the rule of law which guarantees human rights and democracy.⁴² In the meantime, as Lubman argued that it is still the case that law is only permitted to play “a secondary role in the governance of China.”⁴³

³⁷ Peerenboom, *supra* at p 49. Also see Lubman *supra* at pp 71-101 and JF Chen, *From Administrative Authorisation to Private Law: A Comparative Perspective of the Developing Civil Law in the People's Republic of China*, Dordrecht, Martinus Nijhoff Publishers, 1995.

³⁸ Lubman *supra* at p 2.

³⁹ JF Chen, *supra* (2003) at 260.

⁴⁰ Xiao Yang *supra* at p 229

⁴¹ *Ibid* at p 255.

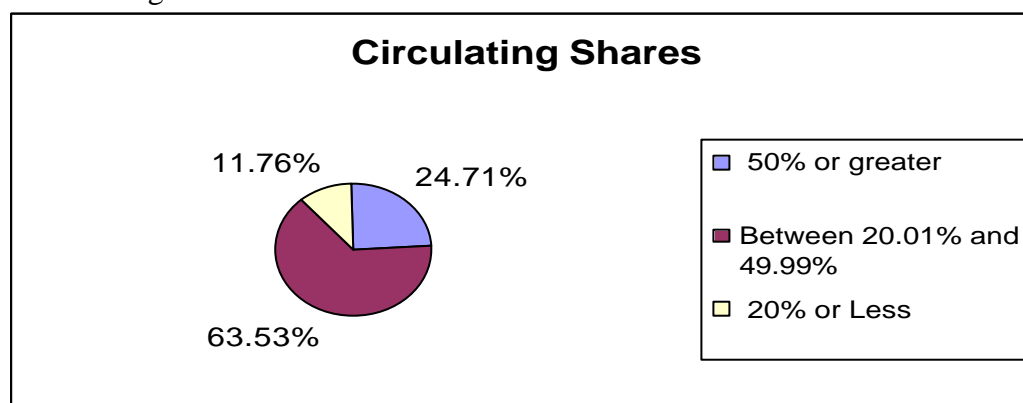
⁴² See further, the essays republished in Chinese and English in Beijing in 2005 by Law Press: J Thesing and W Jung (eds), *The Rule of Law*, Beijing, Law Press, 2005.

⁴³ Lubman, *supra* at p 4.

3. The Rise of the Corporate Sector

The reform efforts of the 1970s saw the transformation of the old state owned enterprise sector, the listing of shareholder companies on China's stock exchanges and the widespread adoption of the corporate form for private business activity in China.⁴⁴ Corporatization, rather than privatization, was adopted as the strategy for the reform of the state owned enterprise sector. The establishment of companies limited by shares was not seen as threatening; as the State Committee for the Reform of the Economic Systems noted in 1989, "The purpose of the share system is the share system [itself] and not to issue shares to the public."⁴⁵ However, the need to raise new capital meant that some shares need to be able to be sold. Nevertheless, as one survey found in 2002, of the 1175 listed companies at that time, 1051 (or 89.4%) had controlling shareholders and 813 of these (or 77.4%) were state-owned controlling shareholders.⁴⁶ Of course, the number of other types of corporate entities in China is much larger.⁴⁷ Figure A shows that only about a quarter of China's listed companies had 50% or more circulating shares; almost two thirds of these listed companies had more than 20% and less than 50% of their capital in the form of circulating shares.

Figure A: Circulating Shares in Companies Listed on the Shanghai and Shenzhen Stock Exchanges in 2003



The success of the corporatization experiment of the 1990s has led to an increase in the amount of state assets that have been transferred into the hands of companies limited by shares; although such state owned shares were generally not tradeable on stock markets, there was nevertheless official recognition of the importance of share

⁴⁴ See generally, ES Steinfeld, *Forging Reform in China: The Fate of State-Owned Industry*, Cambridge, Cambridge University Press, 1999; Gao Shangquan and Chi Fulin, *Reforming China's State-Owned Enterprises*, Beijing, Foreign Language Press, 1997.

⁴⁵ Quoted by Walter and Howie, *Supra* at pp 9-10.

⁴⁶ As noted by Chen Jiagui, "Understanding the significance and complexity of corporate governance", (pp 178-181) in *Corporate Governance Reform: The International Experience and China's Practice*, (ed by Lu Tong), Beijing, China Development Publishing House, 2004 at p 180.

⁴⁷ In 1995 there were 1.37 million companies in China, of which 179,901 were regulated by the Company Law: per CY Xin and G Fan, *The Role of Law and Legal Institutions in China's Economic Development: 1978-1995*, Beijing, Law Press, 2000 at p 114. This figure has clearly increased significantly since that time given the rapidly growing size of China's private sector; see further: R Garnaut and L Song (eds), *China's Third Economic Transformation: The Rise of the Private Economy*, London, RoutledgeCurzon, 2004.

trading in the remaining minority-owned shares, as well as a recognition of the need to try to protect the interests of minority shareholders.

The rise of the private company sector has also been a significant development which has further contributed to “a hollowing out” of the state sector in a country where for three decades before the 1980s state planning “...had effectively eliminated the private sector of the economy.”⁴⁸ However, this does not mean that there has been any real disintegration in State power as a result of the wide-ranging reforms that have occurred over the last two decades.⁴⁹

In regard to the corporate sector, the State has been slow to move to dispose of its controlling shareholdings in major top 100 listed companies, despite recognising that some movement in this regard is necessary.⁵⁰ Furthermore, corrupt practices by Party members⁵¹ and the widespread nature of related party transactions within Chinese listed companies have not inspired public or investor confidence. Professor Tong Lu, Director of the China Center for Corporate Governance at the China Academic of Social Sciences, has noted that:

“Most listed companies in China were reformed state-owned enterprises in which holding shareholders control the shareholders general meeting and the board of directors is an outstanding problem, with the board serving basically as the agency of major shareholders...This governance structure enables holding shareholders to cause large numbers of connected deals to take place between a listed company and themselves by manipulating the shareholders general meeting and the board, at the expense of the interests of the company and medium-sized and small shareholders.”⁵²

This reflects a much wider problem of corrupt practices in China. For example, in 2001, Huang Weiding, a senior official of China’s Red Flag Publishing House, a central government agency, has painted a bleak picture of the extent and possible consequences of widespread Party corruption when he noted that :

“[T]he number of high-level cadres involved in corruption cases has also been on the rise. In the 1980s, most cases of corruption occurred at the local or grass roots level. After the 1980s, the number of violations of both economic law and discipline by leading cadres increased dramatically...Rampant corruption causes great harm to the economy as state-owned enterprises are constantly being nibbled away at, with State assets being swallowed in their entirety. Politically, corruption makes an extremely ugly impression upon the population. If corruption cannot be

⁴⁸ Walter and Howie, *Supra* at p196.

⁴⁹ BJ Dickson and CM Chao, “Introduction - Remaking the Chinese State” (pp 1-16) in CM Chao and BJ Dickson (Eds), *Remaking the Chinese State - Strategies, Society, and Strategy*, London, Routledge, 2001 at p 2; However, for a more radical view see: GG Chang, *The Coming Collapse of China*, London, Random House, 2001 pp 214-222.

⁵⁰ See for example, S Wyatt, “Privatisation more hype than reality”, *The Australian Financial Review* 7 June 2005 at p 13.

⁵¹ See generally, Xiaobo Lu, *Cadres and Corruption; The Organizational Involution of the Chinese Communist Party*, Stanford, Stanford University Press, 2000.

⁵² T Lu, “Corporate Governance in China”, paper available at : <http://222.iewp.org.cn/cccg/en/publications.htm>

stopped in the long term, this will shake the confidence and trust of the people in both the Party and government, causing dissension and discord.”⁵³

This pattern of conduct may well have serious problems for the development of rule-oriented behaviour (and the rule of law) in China. As Huang Weiding insightfully also noted :

“The market economy system is incomplete and remains imperfect, providing gaps within which corruption activities may occur. The lack of a complete market economy becomes particularly obvious in that there is a market in the first stage but no market regulations. Market rules and regulations may be required for economic development, but due to the gradual process of market economic reform, all kinds of systems, policies and measures cannot possibly be completed at one time. So these gaps can be fully utilized by those who wish to use their power for payment.”⁵⁴

With the growth of both the largely state-owned listed company sector and the rapidly growing private company sector in China, the modernization of law and the development of other regulations and standards that reflect international commercial practice has become more urgent. This problem has become evident in the ongoing discussions regarding the adoption of corporate governance principles in China’s major companies.

Corporate governance ideas are reflected in the package of rules and practices that are to be found in most market oriented countries.⁵⁵ The corporate governance movement is perhaps best reflected internationally in the OECD’s Principles of Corporate Governance⁵⁶, which have themselves been copied in China by the China Securities Regulatory Commission. The idea of corporate governance gained official currency in China in the late 1990s and as such it is still poorly understood in the wider corporate sector.⁵⁷ Although 2002 was designated by the CSRC as the year of corporate governance, the improvement of corporate governance practices has however now become a major priority of the Chinese government and its regulatory bodies. Nevertheless, China has been engaged in a frank annual policy dialogue with

⁵³ Huang Weiding, “Fighting Corruption Amidst Economic Reform”, (pp 39-55) in *China’s Century: The Awakening of the Next Economic Powerhouse*, (ed by LJ Brahm), Singapore, John Wiley & Sons (Asia) Pte Ltd, 2001 at pp 39-41.

⁵⁴ Ibid at pp 43-44.

⁵⁵ See generally, JH Farrar, *Corporate Governance – Theories, Principles and Practice, Second Edition*, Melbourne, Oxford University Press, 2005; and RAG Monks and N Minnow, *Corporate Governance, Second Edition*, Oxford, Blackwell, 2001.

⁵⁶ Organisation for Economic Cooperation and Development, *OECD Principles of Corporate Governance*, Paris, OECD, 2004.

⁵⁷ Zhou Xiaochuan, (Governor of the People’s Bank of China) has noted that whilst evidence of the use of the concept of corporate governance can be found as early as Third Plenary Session of the Fourteenth National Congress of the CPC held in 1993, he notes that “it was not until 1999 when the concept was formally cited in the major documents published by the Fourth Plenary Session of the Fifteenth National Congress of the CPC”: Zhou Xiaochuan, “Improve Corporate Governance and Develop Capital Market”, speech delivered at the *Euromoney* “China Forum: Capital Market and Corporate Governance”, December 1, 2004, Beijing.

the OECD regarding corporate governance issues; these meetings have been held in Shanghai in 2004 and in Beijing in 2005.⁵⁸

Corporate governance rules are to be found in legislation, judicial decisions, regulations and best practice standards issued by stock exchanges and various industry groups. To some degree, the emergence of corporate governance talk in China is laying the foundations for a corporate culture that may be seen as necessary for a “thick” understanding of the operation of law in a market based society. Assessing whether China’s major publicly listed corporations are able to “walk the talk” in regard to their corporate governance practices, is vital to understanding corporate law in action in China. In this regard, China is still at a relatively early stage of its development, as is recognised by observers both domestically and internationally.

For example, in a Standard and Poor’s country study of corporate governance in China, the authors pointed to some “fundamental weaknesses in China’s corporate governance infrastructure”, most importantly the effects of the concentration of government ownership and influence in corporatized former SOEs. This is a view that is acknowledged even by those in China’s central bureaucracy controlling these companies.⁵⁹ It Standards and Poor’s have also suggested that the “effective implementation and enforcement “of China’s corporate governance codes, listing rules and regulations “may prove elusive for years to come.”⁶⁰

Similarly, the Shanghai Stock Exchange (SSX) has also identified some serious challenges facing the development of corporate governance in China. The SSX has however, also been prepared to offer some important recommendations for reform, such as the “downsizing” of the scale of state assets and the “strategic withdrawal” of government from the public company sector.⁶¹ And the gradual floating of presently un-tradeable state shares.

In its important 2003 survey of corporate governance in China, the Shanghai Stock Exchange identified the following ten basic features of Chinese corporate governance:

⁵⁸ For further details, see Policy Dialogue on Corporate Governance, Shanghai China 25-26 February 2004, http://www.oecd.org/document/32/0,2340,en_2649_34813_31173536_1_1_1_1,00.html and the Second Policy Dialogue on Corporate Governance, Beijing 19 May 2005 at http://www.oecd.org/document/45/0,2340,en_2649_34813_34965229_1_1_1_1,00.html.

⁵⁹ For example, Shao Ling, Deputy Director of the State Council’s State-Owned Assets Supervision and Administration Commission noted in 2004 that “...where equity is relatively concentrated and the Chinese State is the controlling shareholder at most listed companies, the behaviour of the State as controlling shareholder is crucial to improving the system of corporate governance. For this reason we are endeavouring to restrict irregular behaviour by the State as controlling shareholder...”, Shao Ling, “Policy Dialogue on Corporate Governance in China”, Shanghai, 25-26 February 2004.

⁶⁰ K Tai and CR Wong, “Corporate Governance in China”, see further at: <http://icf.som.yale.edu/research/china/newpage/cnfeature/mainland/corporate%20gove> (visited at 7 April 2005). This Standard & Poor’s report can also be found at : http://www.acga-asia.org/loadfile.cfm?SITE_FILE.ID=187. Reference should also be made to the World Bank study of Chinese corporate governance: S Tenev and C Zhang, *Corporate Governance and Enterprise Reform in China: Building the Institutions of Modern Markets*, Washington DC, World bank and the International Finance Corporation, 2002.

⁶¹ Shanghai Stock Exchange, “Corporate Governance Report 2003: Executive Summary,” mimeo, Shanghai, at p 41-43

- (i) There is a conflict of interest when the government is both the referee and player in regard to Chinese listed companies;
- (ii) Although China's legal infrastructure is constantly improving, many aspects of the Company Law and the Securities Law are outdated (such as the inadequate protection of medium and small shareholders);
- (iii) It is clear that large shareholders have violated the interests of other shareholders, eg by providing guarantees to shareholders;
- (iv) The SSX recognises that the independence of the board's is crucial to a company's corporate governance and notes that the independence of boards is improving;
- (v) New incentive mechanisms are important and as such new measures of this kind are being tested to improve the performance of managers;
- (vi) There has been remarkable progress in the development of the mergers and acquisitions market in China;
- (vii) The significance of institutional investors is growing rapidly, so that these "investors are gradually becoming the pillar of the securities market..."
- (viii) Greater attention is being given to the role of creditors in corporate governance;
- (ix) Similarly, self-regulatory organisations and intermediaries (such as accountants) are playing an increasingly important role; and
- (x) The effectiveness of information disclosure in China is improving, especially in regard to the screening and approval system for IPOs.⁶²

However, the Shanghai Stock Exchange's (SSX) 2003 corporate governance survey also frankly identified eight basic problems facing corporate governance in China's listed companies.⁶³ These well known problems are worth listing here:

- (i) Chinese listed companies were found by the SSX to have an "improper shareholding structure" with an "overwhelmingly large percentage of non-tradeable shares, which represent about 2/3 of all the listed companies' combined equity." Moreover, only 0.5% of the remaining shares are held by institutional shareholders.
- (ii) The role of government in regard to corporate governance has often been "misplaced". The SSX reported that "[i]n making economic decisions, the state still has not broken out of the traditional path of administrative control." The decisions of the state "directly affect business decisions [of listed companies] and burden these enterprises with public functions."
- (iii) The SSX found that China's "legal and regulatory framework is far from mature, although there is a noticeable improvement in the legal and regulatory environment for corporate governance." The Exchange also reported that the market lacked "clear, concrete and implementable laws for victims of securities market violation, such as insider trading, market manipulation..." It was also found that there was a lack of "clear channels for civil action and protection for investors", such as class actions.
- (iv) The SSX found that there is excessive insider control in corporate affairs and too heavy a reliance was placed by companies on the "key man model", where this person "easily controls and manipulates the company's

⁶² Ibid at pp 3-19.

⁶³ Ibid at pp 19-40.

- general shareholder's meeting, board meeting and the supervisory board..."
- (v) The SSX also pointed to immaturities in the external governance structure, due mainly to the underdevelopment of current market mechanisms, such as the M&A market for corporate control; whilst institutional investors still play a relatively insignificant role, the stock market is dominated by individual investors who do not follow the "buy and long-term holding strategy." Minority public shareholders find it difficult to gain control of the company due to the problem of the majority non-tradeable shares.
 - (vi) According to the SSX, the quality of information disclosure by listed companies is not reliable, as "the form of disclosure is far more important than the substance."
 - (vii) The SSX also found a lack of due diligence in fiduciary duties that require directors and managers to act in the best interests of shareholders.
 - (viii) Finally, the SSX noted that there is a lack of adequate supervision of companies by the financial press and the public to "mitigate the asymmetry in information on the securities market."

Many of these issues were also raised by interviewees during the course of our field-work for this study.

4. Lagging Behind the Market: China's Modest Economic Law Reforms

Legal reform has continued to lag behind the pace of economic developments in China. In building up the framework of a "thin" model of the rule of law, the 1980s saw the passage of a number of key laws that were to serve as an important basis for the development of a more market oriented economy; these included the Economic Contract Law⁶⁴ (1981), the General Principles of Civil Law⁶⁵ (1986), and the Enterprise Bankruptcy Law (for Trial Implementation) (1986). However, although a comprehensive new Contract Law was enacted in 1999 (replacing three earlier contract laws), we have yet to see the passage of the much-discussed Civil Code or the long-awaited new Bankruptcy Law.

It was not until 1993 that a new Company Law was passed after a decade of debate.⁶⁶ The new PRC Securities Law was passed in 1998 together with some other basic new laws to facilitate transactions in a market economy.⁶⁷ These various economic laws

⁶⁴ This Law came into effect on 1 July 1982 and was revised in September 1993.

⁶⁵ This Law became effective on 1 January 1987. Chen has noted that the General Principles of Civil Law is "the only, albeit simplistic, piece of legislation that provides some general principles which create and define the structure of civil law as well as establishing basic abstract civil law institutions..." : Jianfu Chen, *Chinese Law: Towards an Understanding of Chinese Law, Its Nature and Development*, The Hague, Kluwer Law, 1999 at p 222. As Albert Chen added in 2004. "The GPCL is still the most basic enactment on civil law, pending the enactment of a comprehensive civil code", AHY Chen, *An Introduction to the Legal System of the People's Republic of China, Third Edition*, Hong Kong, LexisNexis, 2004 at p 241.

⁶⁶ See further, R Tomasic and J Fu, "Company Law in China", (pp 135-181) in *Company Law in East Asia*, (ed by R Tomasic), Aldershot, Dartmouth Publishing, 1999; and GG Wang and R Tomasic, *China's Company Law: An Annotation*, Singapore, Butterworths, 1994.

⁶⁷ These included the Guarantee Law (1995), the Law of Trusts (2001), the Law of Partnership Enterprises (1997), the Insurance Law (1995), the Law of Negotiable Instruments (1995) and the Law

relied very heavily upon the transplanted ideas from foreign legal systems and the desire to bring Chinese economic laws into harmony with international practice, provided of course that they accord with fundamental principles that give the Party great influence over the content of such laws.⁶⁸ The Company Law was also heavily influenced by the need to secure the position of the state as owner of major corporatized entities. As DC Clarke has graphically noted:

“[T]he need to provide for the special circumstances of state sector enterprises ends up hijacking the entire Company Law so that instead of state sector enterprises being made more efficient by being forced to follow the rules for private sector enterprises (the original ambition), potential private sector enterprises are hamstrung by having to follow rules that make sense only in a heavily state-invested company.”⁶⁹

Both the Company Law and the Securities Law were in many respects almost immediately out of date after their passage and it was left to the Supreme People’s Court to issue interpretations of these statutes and to regulatory bodies, such as the China Securities Regulatory Commission to promulgate regulations, guidelines, interpretations and other rules to allow the corporate sector to function more effectively. Despite the frequently expressed desire of senior Chinese officials to encourage further foreign investment in China⁷⁰, investment in Chinese companies was limited under Article 138 of the 1998 Securities Law. This required that a potential investor had to be a Chinese citizen before they could open a securities trading account with a securities company in China, allowing them to trade in Chinese securities.

This prohibition led to unusual distinctions being made between different classes of tradeable shares⁷¹ as well as the introduction of the Qualified Foreign Institutional Investors (QFII) scheme to circumvent this statutory restriction.⁷² More comprehensive reform of the 1993 Company Law is being discussed, as is the likely

on Commercial Banks (1995). For a more detailed discussion of these laws see: G Yu, and M Gu, *Laws Affecting Business Transactions in the PRC*, The Hague, Kluwer Law International, 2001.

⁶⁸ Jianfu Chen, “Market Economy and the Internationalisation of Civil and Commercial Laws in the People’s Republic of China”, (pp 69-94) in *Law, Capitalism and Power in Asia: the rule of law and legal institutions*, (ed by K Jayasuriya), London, Routledge, 1999 at pp 84-85.

⁶⁹ DC Clarke, “Corporate governance in China: An overview”, (2003) 14 *China Economic Review* 494-507 at p 495.

⁷⁰ See for example, Chen Siwei, *Studies on Economic Reforms and Development in China*, Oxford, Oxford University Press, 2001. Also see generally, CM Vaughn, “Venture Capital in China: Developing a regulatory Framework”, (2002-2003) 16 *Columbia Journal of Asian Law* 227-252.

⁷¹ The distinction is made between “A” shares that are only open to investment by Chinese citizens (paying in RMB), and “B” shares that are open to foreign citizens (paying in US\$ in Shanghai and HK\$ in Shenzhen). In 1999, a total of 923 Chinese listed companies issued “A” shares, whilst 108 listed companies issued “B” shares that were created to be invested in only by foreigners (with 26 companies issuing “B” shares only); a further 46 companies had overseas “H” shares (for Chinese companies listed in Hong Kong); these figures are cited in : <http://www.oecd.org/dataoecd/6/60/1931117.pdf>. However, foreigners have not shown much interest in “B” class shares, preferring to buy “H” shares in Hong Kong; furthermore, it seems that over 66% of those who buy “B” shares are really Chinese nationals; see further, Walter and Howie, *supra* at p 46 and p 165.

⁷² See further, Decree of the China Securities Regulatory Commission and the People’s Bank of China, No 12, The “Provisional Measures on Administration of Domestic Securities Investments of Qualified Foreign Institutional Investors (QFII)”, which came into effect on 1 December 2002.

passage by China of a new corporate Bankruptcy Law. However, neither law is likely to be consistent with international best practice; the Company Law being far more rigid or mandatory in character than is common in other modern company laws⁷³, whilst the proposed new bankruptcy law is likely to fall short of being a comprehensive rescue oriented law which seeks to minimize the role of the state in dealing with issues of corporate insolvency.⁷⁴

Apart from legislation, there have been other relevant legal developments worth noting here. One of the most important non-statutory documents is the *Code of Corporate Governance for Listed Companies in China* jointly issued on 7 January 2002 by the CSRC and State Economic and Trade Commission (SETC).⁷⁵ Also, in the absence of more detailed provisions in the corporate and securities legislation that the CSRC has had oversight of, the Commission has promulgated important rules in regard to the implementation of information disclosure (1993); requirements for public offerings of stocks (1993); regulations governing the shareholders' general meeting of listed companies (1996); guidelines for introducing independent directors onto the boards of listed companies (2001); guidelines for on-line voting for shareholders meetings of listed companies (2004); and provisions to strengthen the protection of the rights and interests of public shareholders (2004).

One of the most important recent efforts to use rules to change market conduct has been the issue by the CSRC on 29 April 2005 of a Notice regarding “..Relevant Issues of Pilot Reform of Equity Divisions of Listed Companies.” This Notice sought to deal with one of the most important problems facing corporate governance in major listed companies by putting in place a pilot program under which shareholders of public companies could agree to split blocks of state-owned shares in the company and to arrange for some of these to be sold more widely on the stock market.⁷⁶ This program is to be supervised and administered by the CSRC with four firms being identified as ones in which this program could commence. However, it is likely that it will be some time before this pilot program begins to have any significant effect on the dominance of the state as shareholder in most of China's major listed companies; it is also unlikely that strategically important companies will be allowed to make such equity splits.⁷⁷

In this context, the Listing Rules issued by the Shanghai and Shenzhen Stock Exchanges should also be noted. They at least set a minimum standard for listed companies to comply with. Finally, recent policy statements by other agencies aimed at dealing with some significant problems affecting the corporate governance

⁷³ DC Clarke, *supra* at p 500.

⁷⁴ See generally, RW Harmer, “Insolvency Law Reforms in the Asian and Pacific Region” (2000) Vol 1 *Law and Policy Reform at the Asian Development Bank* pp 8-86.

⁷⁵ For the text of this Code see further at :

<http://www.csrc.gov.cn/CSRCSite/eng/edeplt/rule/frz102042901.htm>

⁷⁶ *Notice of China Securities Regulatory Commission on Relevant Issues of Pilot Reform of Equity Division of Listed Companies*, Promulgated by the CSRC on 29 April 2005; and *Opinions of the China Securities Regulatory Commission and the State-owned Assets Supervision and Administration Commission of the State Council on Well Performing of Pilot Reform of Equity Division*, Promulgated by the CSRC and the State-owned Assets Supervision and Administration Commission (SASAC) on 30 May 2005.

⁷⁷ See further, S Wyatt, “Privatisation more hype than reality”, *The Australian Financial Review*, 7 June 2005 at p 1.

practices of listed companies should be noted; these include the recent announcement by the State-owned Assets Supervision and Administration Commission (SASAC) that senior positions in 22 of China's large State-owned Enterprises would be allowed to be filled from outside the normal Communist Party controlled appointments system. SASAC supervises around 190 major Chinese SOEs. However, this is unlikely to apply to the most senior positions in listed companies such as those of chairman or general manager and this is unlikely to undermine the dominance of the Party in major listed companies with large state owned blocks of shares.⁷⁸ In the absence of more comprehensive reforms, such pragmatic and *ad hoc* measures have provided only limited assistance to investors and companies.

It is clear, as Chen has also noted, that the lack of a clear direction in the process of economic reform has meant that law making in China has been somewhat *ad hoc* and piecemeal in nature, producing a large array of individual pieces of legislation, administrative regulations, orders and decisions, often issued by different agencies with their own policy focus.⁷⁹ Whilst these legal changes may be important contributions to fashioning a "thin" theory of the rule of law, we need to look at the law in action in the Chinese legal system to better understand the effectiveness of these rules. As we have seen, there is widespread recognition of the importance of the implementation of legal rules in China.⁸⁰

The quality of corporate governance and the rule of law will not be secured merely by fashioning elegant legislative and other market rules; a whole range of other institutions and social mechanisms is required. These include a vigorous financial press⁸¹, robust and independent legal and accounting professions, independent stock exchanges and independent stock-broking and banking sectors, and effective mechanisms for securing legal remedies (such as compensation for losses suffered by shareholders through improper conduct of corporate controllers). The limited capacity of the courts in China to interpret or strike down laws is well known.⁸² Furthermore, the courts have been unprepared to encourage civil actions seeking compensation from listed companies or their officers; such legal proceedings were invariably brought by shareholders who had lost money as a result of such action as the falsification of financial statements.⁸³

It is possible for government agencies to bring criminal or administrative actions against companies and their officers who have been engaged in such conduct as market manipulation. It has been reported that between 1999 and 2001, 220 listed companies were investigated for actions of this kind and 92 were fined a total of RMB 1.42bn or US \$17 million; however, investors have had much less success when they

⁷⁸ Sun Min, "SOEs cast net wider to find new bosses," *China Daily*, 1 June 2004.

⁷⁹ JF Chen (2003) *supra* at p 256.

⁸⁰ Chief Justice Xiao Yang, *supra* at p 224.

⁸¹ DC Clarke, *supra*, at p 504, has noted that the "financial information industry...is significantly crippled by the state's continuing insistence on control over all information. Control over information is a cornerstone of the Chinese Communist Party's system of political control and is unlikely to disappear much before the Party itself."

⁸² Peerenboom, *supra* at pp 316-318.

⁸³ On a related issue, see further, Jianfu Chen, "Mission Impossible: Judicial Efforts to Enforce Civil Judgments and Rulings in China", (pp 85-111) in Jianfu Chen et al (Eds), *Implementation of Law in the People's Republic of China*, *supra*; DC Clarke, "Power and Politics in the Chinese Court System: The Enforcement of Civil Judgments" (1996) 10 *Columbia Journal of Asian Law* 93.

have sought compensation through the courts by way of civil actions, despite the existence of legal provisions which seem to allow for such actions.⁸⁴ Under Article 63 of the PRC Securities Law a liability to compensate investors who suffer losses as a result of “any falsehoods, misleading statements or major omissions” is imposed on the issuer of securities or the company responsible; this liability extends to any director, supervisor or manager of the company or the issuer of securities.

This is supplemented by Article 207 of the Securities Law which provides that where the property of persons who have breached a provision of the Securities Law is insufficient to pay both damages and the fine, the person involved will bear civil liability for the damage suffered (this is similar to Article 228 of the Company Law). In addition, where a number of persons (such as shareholders or investors) have been injured by the same action, the People’s Court is empowered by Articles 53, 54 and 55 of the Civil Procedure Law to permit a representative action to be brought against the offender. Also, Article 63 of the Company Law provides for compensation proceedings being taken, stating that: “Directors, supervisors and the manager shall be liable for compensation, if they violate the laws, administrative rules and regulation or the articles of association in performance of their duties and thus cause damage to the company.”

These various statutory provisions provide a legal basis for compensation to be sought from the listed company or its directors, but the courts have rarely allowed such actions to succeed; this may be attributed to the desire to protect state assets held by listed companies from having to make payments to large numbers of defrauded investors or shareholders, as well as to the desire of the state to protect the stability of the stock market itself. It may also be the case that local courts have had pressure put on them by local government to protect locally based companies and their directors.⁸⁵ Such local pressures also impact on the effectiveness of the local offices of the CSRC based in provincial cities. It should also be noted that in the past the courts have not had much experience in regard to civil actions involving securities law violations.⁸⁶ The resort to the courts in cases such as those of market manipulation or the provision of misleading information has been made more difficult for investors and shareholders by the actions of the Supreme People’s Court (SPC).

In September 2001, the SPC issued circular No 406 which required that local courts should refrain from accepting civil compensation cases for securities law breaches on the grounds that lower courts did not have the appropriate skills to handle such complicated cases.⁸⁷ Furthermore, in December 2002 the SPC issued another notice

⁸⁴ Figures quoted by Naomi Li, “Civil litigation against China’s listed firms: Much ado about nothing?” Asia Programme Working Paper, No 13, London, The Royal Institute of International Affairs, February 2004 at p 3.

⁸⁵ In regard to the serious problem of local protectionism, see further, SB Lubman, *Bird in a Cage*, supra at pp 266-269. Lubman notes (at 268) that “‘local protectionism’ is an ominous reason for nonenforcement of judgments because it testifies so strongly to the weakness of the central government and the fragmentation of the legal system.”

⁸⁶ See further, S Green, *The Development of China’s Stock Market, 1984-2002*, supra at pp 197-199.

⁸⁷ Cited by Baohai Hu (Director of the Department of Legal Affairs, CSRC), “On Civil Compensation in Securities Law Violations – in the perspective of the company law and the securities law”, Centre for International Private Enterprise, see: <http://www.cipe.org/china/civil.htm> (visited on 31 May 2005). Based on CSRC experiences, Dr Hu listed the following reasons for local People’s Courts failing to accept civil compensation cases of this kind:

in which it required that before a lower court could hear a civil action for a breach of the Securities Law, either the CSRC must first have imposed an administrative sanction against the alleged wrongdoer, or a criminal sentence must have been imposed upon the wrongdoer; it is also necessary to show a causal link between the losses suffered and the false statement that may have been made.⁸⁸ About 1,000 such civil compensation cases have reportedly been filed in China's local courts, with some having been settled out of court, but few if any being successfully heard; many were dismissed on the grounds that the plaintiffs had already sold their shares. At best the company and not its directors, may be fined where the CSRC has taken action for breaches of the securities law.⁸⁹ This ultimately has the effect of further damaging the interests of shareholders who have invested in these companies. As one commentator observed in regard to private securities litigation in China, "[t]here are no rights without remedies...A wholesale reform of the current system, which is fundamentally flawed, should be elevated to a burning priority."⁹⁰

Due to these kinds of problems, senior officials of the CSRC have suggested that specialised securities courts should be set up to deal with such compensation cases. This is seen as ensuring greater stability in the market.⁹¹ None of this is very comforting for those seeking to use the legal system to obtain compensation from a company or its directors in the event of a securities law or company law breach that has caused loss to them.

A Brief Note on Methodology: Researching China's top 100 companies

In recent years a body of empirically based research into Chinese business life has begun to emerge.⁹² So, with funding from the Australian Research Council, and in collaboration with Professor Neil Andrews, the authors of this paper have sought to look closely at the development of corporate governance in the top 100 Chinese listed

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- (i) the legal system concerning civil compensation cases is not sound enough and it is difficult for investors to sue;
 - (ii) judicial practice is inadequate and it is difficult to hear securities civil compensation cases;
 - (iii) there is obstruction in freezing company or other property prior to the commencement of civil actions;
 - (iv) it is difficult to implement securities civil compensation cases;
 - (v) because many of those seeking damages are scattered small investors, they do not have the energy and financial strength to bring such civil actions;
 - (vi) such investors may damage the market position of a company by taking too radical action against it, detrimentally affecting the already poor financial position of the company.

⁸⁸ See further, Article 6, *Some Provisions of Supreme People's Court on Trying Cases Involving False Statements Related to Securities Market*, approved by the Supreme People's Court's Judicial Committee on 26 December 2002, with effect from 1st February 2003.

⁸⁹ S Green, *supra* at p 199.

⁹⁰ Wenhai Cai, "Private Securities Litigation in China: Of Prominence and Problems", (1999) 13 *Columbia Journal of Asian Law* 135-151 at 151.

⁹¹ Baohai Hu (Director of the Department of Legal Affairs, CSRC), *supra* at pp 5-6.

⁹² For other interview-based studies see: D Guthrie, *Dragon in a Three-Piece Suit: The Emergence of Capitalism in China*, Princeton, Princeton University Press, 1999; KS Tsai, *Back Alley Banking: Private Entrepreneurs in China*, Ithaca, Cornell University Press, 2002; DN Sull and Yong Wang, *Made in China: What Western Managers can learn from Trailblazing Chinese Entrepreneurs*, Boston, Harvard Business School Press, 2005; and P Nolan, *China and the Global Economy*, Houndsmills, Hampshire, Palgrave, 2001.

companies. Drawing upon the listing of the top 100 companies that has been published annually by *Fortune* magazine since January 2002 (see composite of this list in Appendix A), interviews were conducted across China with senior office-holders from these top 100 companies, as well as with independent directors, auditors and legal advisers, stock exchange officials and corporate regulators who have had experience working with these companies.

Over 100 face-to-face interviews with these persons were conducted using a lengthy interview schedule. Each interview took between one and two hours to complete and was usually held in the offices of the company, adviser or regulatory body. Usually at least two interviewers were present at each interview. This greatly helped to maintain control of the interview process. Despite the difficulties that have sometimes been referred to in regard to undertaking empirical research in China, this research encountered a high degree of co-operation from those interviewed, with most potential interviewees being relatively comfortable with the process, once they had agreed to be interviewed. Those interviewed included persons such as the secretary to the listed company board and its independent directors. These were clearly prepared to make their time available to help with what was widely perceived to be a study of an important topic in contemporary China.

Most of those interviewed treated the research very seriously, but some were prepared to be more open than others. The access that was obtained in this study in itself is a notable development given the relatively closed nature of Chinese bureaucracies and the difficulties sometimes experienced by foreign researchers seeking to do fieldwork in China. Some assistance in furthering this research was obtained from the utilization of various internal networks within government and universities to gain support for this project. In addition, a conference was held in Beijing in April 2004 and helped us to publicise some of the corporate governance issues that we were concerned with in our fieldwork. This conference was reported favourably in the English language *China Daily* newspaper.⁹³

Whilst interviews were generally conducted in English, we conducted interviews in Chinese where it was necessary to do so. These interviews were subsequently transcribed and supplemented by other sources of information on contemporary corporate governance in China. As illustrated in Table 1, project interviews were held in eight cities across China: Beijing, Chongqing, Guangdong, Jinan, Nanjing, Qingdao, Shanghai and Shenzhen. This provided data from a good cross - section of the listed companies in China's top 100 companies.

⁹³ Xu Binglan, "Improving corporate governance", *China Daily*, 31 May 2004 at p 11. Some papers from this government funded conference were published in (2004) 17(1) *Australian Journal of Corporate Law* 1-156. Also see R Tomasic et al (Eds) *Corporate Governance – Challenges for China*, Beijing, Law Press, (forthcoming, July 2005).

City	Listed Companies	Professionals, Academics and Independent Directors	Regulators	Subtotal
Beijing	17	12	3	32
Shanghai	19	8	5	32
Hong Kong	7	7	6	20
Shenzhen	7		3	10
Qingdao	4			4
Jinan	3			3
Chongqing	2			2
Nanjing	2			2
Guangzhou	2		1	3
Subtotal	63	27	18	108

5. The Role of the Stock Exchanges: between the CSRC and companies

In many countries, stock exchanges have played a leading role in regard to the improvement of corporate governance practices of listed companies. In the fieldwork reported here, interviewees were asked whether they thought that the Chinese stock exchanges were effective as monitors of corporate governance practices of listed companies.⁹⁴ On the whole, whilst the role of stock exchanges was seen as being an important one, there was a strong perception that mainland exchanges have had limited success as regulators, although their impact in regard to the improvement in the quality of information disclosure by listed companies was frequently singled out for praise.

A number of interviewees noted that the two main roles of China's exchanges were to provide a market for trading corporate securities and to monitor disclosures made by companies. However, as one Shanghai based informant noted of the stock exchanges, "[t]hey play their most important role in monitoring the truthfulness, accuracy and timeliness of information disclosure." It is also the case that they have sought to play a leadership role in regard to corporate governance, but many pointed to their lack of real power to act, and a lack of sufficient resources to do more than to react to matters brought to their attention.

Although China's two mainland exchanges were often described as being the "front line" monitors of listed companies, they were seen to operate in the shadows of the China Securities Regulatory Commission. It was often noted that the stock exchanges were ultimately controlled by the CSRC, which appointed the senior staff of these exchanges. It was often emphasised that the CSRC was the sole regulator with power to make rules for the market and that the stock exchanges were seen as being "a

⁹⁴ Question 29 asked "In your experience, is the Stock Exchange an effective monitor of corporate governance practices?"

subsidiary of the CSRC.” This is because corporate governance rules are generally issued by the CSRC and may be implemented through the stock exchanges. However, the educational role played by the stock exchanges is significant. As one stock exchange official noted:

“Although we are a promoter of corporate governance in China, we do not have enough resources to enforce it. Our main role is to promote a corporate governance culture and bring together experts from different ministries. We press for reform rather than directly monitoring the practice [of corporate governance].”

Whilst there are many impressive people working in China’s stock exchanges, because of the resource constraints faced by these exchanges, they were widely seen as reactive institutions that merely responded to perceived inadequacies in information disclosure by companies. One stock exchange official remarked that due to the poor quality of accounting standards and other legal infrastructure, China’s exchanges “cannot know the real situation of the company.” Not surprisingly, one corporate officer observed, “stock exchanges do not have the resources to locate problems and to resolve them.” Thus, whilst the role of stock exchanges is an important one in seeking to fashion a corporate governance culture in China, their success as regulatory bodies is not perceived to have been great, despite the well-developed disclosure regime that China has put in place.

Stock exchange listing rules have had a mixed reception within the corporate sector in China.⁹⁵ These were seen as setting minimum standards and, as a result, companies would not generally see these as being a major burden; as one Guangzhou regulator reported in this regard, “minimal compliance is their usual practice, unless there is some positive information which may drive up their share price.” One reason why listing rules had limited effect in China is that they are often not internalised within a company, but (as one Beijing based accountant noted) they are seen as a requirement imposed from outside the company. Chinese listing rules are also seen to be much simpler than those of foreign exchanges, such as those found in New York. However, even with these simpler rules, Chinese directors have often not seen these rules as a great threat; as one company official in Jinan remarked:

“At an early stage of listing companies do well [in complying with listing rules]. But, after a while they relax their compliance with the Listing Rules. This is because some directors do not treat these rules very seriously; also, the old management structure does not allow 100% compliance with these regulations.”

When asked how the regulatory role of Chinese stock exchanges might be improved,⁹⁶ a number of suggestions were put forward, such as by making better use of the media to scrutinize the conduct of companies, by the introduction of stricter rules to deal with market misconduct and by improving the market experience of stock exchange staff. It was noted by one interviewee that the regulatory tools available to stock exchanges were limited and that at present exchanges “can only

⁹⁵ Question 31 asked “Have the Stock Exchange Listing Rules affected practices of PRC Listed Companies?”

⁹⁶ Question 30 asked “How might this regulatory role be improved, if at all?”

publicly criticize companies and rely on the good faith of directors of listed companies.” Consequently, an independent director lamented that in the current situation “.it is all about punishment and raising the costs and risks for misconduct; [whilst] there are a few famous cases, but mostly people get away with it; virtually no one is held to account.”

The lack of independence of China’s stock exchanges was often referred to as a key problem. The power of the Chinese government was often seen to be a limitation on the power of exchanges; as one legal expert told us, “as long as the listed companies are state controlled, the Stock Exchange officials will be outranked.” Put differently, one mining executive observed that, alone, a stock exchange “does not have legal effect on companies; it needs government support [to be effective].” Similarly, an experienced Chinese accountant working in an international accounting firm observed that improvement in the regulatory role of stock exchanges would only come about if there was “less government interference [and] more industry and professional involvement” in exchanges.

Another factor, which may facilitate improvement in the regulatory role of exchanges, is to seek to energise other actors, such as shareholders, the media and companies themselves. The weak position of minority shareholders is such that they tend to have a short-term view of their involvement in the company and, as such, they lack the incentive to take a more activist approach to corporate governance. One legal expert went so far as to say that there was no point in seeking to improve stock exchange regulations unless a wider group of investors themselves took an active interest in corporate governance. Furthermore, it was noted that it was critical that “the company itself needs to take responsibility” for improving corporate governance; this was in part a reflection of the corporate culture within these companies.

Finally, it should be remembered that stock exchanges have financial incentives to seek to increase the number of companies listing on their exchanges, so that they benefit from such listings and the consequent trading in their shares. However, the competition that has existed between different mainland exchanges was seen as a factor that may have lowered standards. For example, one Qingdao company executive noted that the Shanghai and Shenzhen stock exchanges were competitors and that some companies also looked to list abroad. A Shanghai based legal practitioner observed that “when there was fierce competition between the two mainland exchanges this led them to lower their listing requirements; but now there is less competition and an effort is being made to improve listing standards.”

This problem may be alleviated somewhat by proposed changes in the roles of the two exchanges, such as by the Shanghai Stock Exchange taking over the main board from Shenzhen and the Shenzhen Stock Exchange focussing on setting up a Growth Enterprise Market.⁹⁷ However, not much movement has as yet occurred to adequately differentiate the two exchanges. The loss of some of China’s best companies to foreign exchanges may have led to a further lowering of standards on China’s mainland exchanges. It is therefore clear that the improvement in the regulatory

⁹⁷ See further, S Green, *China’s Stockmarket : A Guide to its Progress, Players and Prospects*, London, The Economist and Profile Books Ltd, 2003 at pp 24-26.

effectiveness of China's stock exchanges will depend on a number of inter-related factors and that such improvement will take some time to occur.

6. The Role of the CSRC: between law and politics

In contrast to the role of the Stock Exchanges, the main guardian of corporate governance in China is the China Securities Regulatory Commission; this is reflected in the Code of Corporate Governance that was jointly issued by the CSRC in 2002. This Code has more formal authority than similar codes in other countries due to the administrative pressure that the Commission may be able to impose on listed companies that fail to comply with them. However, this applies mainly to the mandatory provisions of the Code, with companies at least seeking to meet the minimum standards that the Code requires. As one experienced Chinese legal adviser noted, "I don't think that many listed companies pay much attention to that [i.e. the Code]. Of course, if there is a compulsory requirement, they just follow."

It is clear that, even though the Code is not a law of the National People's Congress, directors and senior officers of listed companies sometimes take it seriously. The Code has had an effect on the structure of the Board by requiring that companies have independent directors and various special committees; it has also strengthened the quality of corporate disclosure by these companies. One senior regulator thought that the Code had had a variable impact; he observed that "Some people take more notice of it; some see it as a matter of concern, but when economic pressure becomes paramount, they try to ignore it."

The CSRC has been active in seeking to raise the consciousness of directors in regard to corporate governance, such as through training programs for such directors and officers. But as one experienced Chinese former regulator observed, "[t]here has not been an environment to apply it." He added that the Code "...has been learnt but not necessarily internalised." A Hong Kong-based regulator noted that much of the Code is prescriptive, and wondered about its effectiveness, noting, "whether it has a deep effect, I am sceptical about that." Nevertheless, there was a widespread view that the Code had had the effect of filling a gap left by the Company Law, which was silent about some important matters, such as the appointment of independent directors. It was felt by many of those interviewed that the Code had a broad impact in advancing the ideas of corporate governance in China, but that its actual day to day impact varied and was harder to establish. One Shenzhen-based officer of a top 100 company offered the following fairly characteristic opinion of the Code:

"It is only another regulation, another western transplant once again. A lot of other legal systems need to be developed [in China]. For example, the PRC Company Law is outdated and needs to be rewritten. The Code of Corporate Governance is only a regulation and not a law. Law will only be developed later. The Code does however have some effect but no punitive effect."

One of the oft mentioned problems facing the CSRC is that sometimes a company chairman may have a higher rank than the CSRC official and as a result it may be difficult for the CSRC to deal with the company effectively, especially where there is

some room for negotiation. As one Guangdong company official remarked, “as a monitoring institution, the CSRC is only a quasi-government department and not that powerful in the eyes of listed companies.” This is because senior managers of companies are usually cadres appointed and removed only by the organisational department of the Central or local Party Committee of the Communist Party. However, where such an officer is engaged in fraud or corruption, they may be less certain of gaining such protection. Despite these concerns, the CSRC remains the main vehicle for the improvement of corporate governance practices in China.

It is sometimes said that corporate regulatory commissions are too rigid or inflexible, given the needs of the market. We were interested to see if there was also a perception in China that this was the case with the CSRC. What was surprising was the widely held rejection of the view that the CSRC was too legalistic in its approach to corporate regulation⁹⁸. A number of reasons were offered in support of the proposition that the Commission was not too legalistic in its approach. Firstly, it was frequently said that it is normal in China to expect a somewhat paternalistic approach to regulation. As an experienced company secretary in a top 100 company colourfully observed:

“[This regulatory style is in accordance with Chinese culture. Chinese parents always worry about their children and want to know what they are doing. This style can prevent serious problems.]”

One former regulator added somewhat philosophically, that “this is always the problem; on the one hand there is too much legislation and on the other hand there is not enough. This goes down to the governing philosophies of our government; this is a 2000 year old problem.” A stock exchange official added that the practical advice that “Law is very important in China as companies will only comply with compulsory legal requirements.” He added that this legalistic approach was “a useful way to promote corporate governance.” A Hong Kong based Chinese company official also added that “in China, if you do not have legal requirements, companies will do whatever they want.” Similarly, an experienced lawyer in a Hong Kong based international law firm expressed the view that “..in the context of China, I don’t think it is too legalistic. In China if you are to be taken seriously, you have to promulgate a comprehensive set of regulations as a starting point.” It was probably for this reason that a Chinese partner in an international accounting firm told us in answer to this question that, “China is still a rule-based culture.”

Another strand of opinion noted that a legalistic approach to corporate regulation was called for at this point in the development of China’s economy, some arguing that there “is actually a need for more regulations” and another remarked that when compared with some foreign regulators, “the CSRC has not issued enough rules.” A good explanation of this general position was provided by a leading law professor in Beijing who observed that:

“The CSRC has issued so many rules and guidelines as the current provisions in the Company Law are too simple and lacking in detail.

⁹⁸ Question 33 asked : “We note that the CSRC has issued many rules and guidelines for companies. Do you think that China has an excessively legalistic approach to corporate governance ?

Corporate governance is still in an early stage of development in China, so that the CSRC has had no choice but to do so.”

A colourful maternalistic expression of this developmental explanation for legalism was put by a commercial lawyer who noted that:

In the present stage of development of the Chinese capital market, CSRC rules are very important. In the future, we should expect improvement of the market itself; a mature market should have a small monitor. The CSRC is like a young mother looking after its first baby – not experienced.”

Another former senior regulator also used the developmental law explanation of the CSRC’s legalism when he said that:

[The CSRC] has had to choose some kind of road for it to take. If it issued soft principles like the OECD Code, there would not be enough guidance; There need to be a bright line, rule-based, rather than a principle-based approach. It is legalistic. In a developing market this is the easiest thing to do, but ultimately, like the US and UK, they will have to get into a principled approach.”

Another view was that this legalism was more symbolic than real as “a lot of rules are paid lip service,” according to a Hong Kong based regulator. A mainland stock exchange official also noted that “not many [of these] rules are truly enforced.” He explained that “[t]his is due to the connections that companies often have with local government, which protects them when violations occur.”

Many pointed to deficiencies in the existing rules used by the CSRC. Thus, one Beijing-based company secretary thought that “the rules released by the CSRC are not enough...[Moreover]..CSRC regulations are out of date as well as insufficient.” In addition, it was said by one company official that because many of the CSRC’s rules were merely copied from foreign markets, “it is hard to implement these rules as the situation is so complicated.” Others pointed to the impractical nature of some of these CSRC rules, some of which were seen as not being sufficiently market sensitive. For example, it was noted by one Guangzhou-based company officer that the CSRC’s market disclosure rules were more stringent than those found in many other markets. A Chongqing based company officer also pointed out that whilst the independent director rules were well intended, they did not do much to protect the interests of minority shareholders.

There were a small minority who thought that there had been legalism in the CSRC’s approach to regulation, but the overwhelming view was that there the number of rules promulgated by the CSRC was not excessive; if anything, there was a strong view that there were not sufficient such rules and regulations at this stage of China’s market development.

Finally, we were interested in the degree to which the Commission used its discretion to exempt compliance with such regulatory rules, given that discretion is often seen as

an essential tool of regulatory agencies.⁹⁹ In many countries it is common for companies and their professional advisers to approach corporate regulatory commissions to ask it to use its discretionary powers to exempt the company from a technical provision of the corporate or securities law, or to modify a technical provision of the law, so as to allow the company to complete a commercial transaction. Of course, such requests do not involve seeking approval for any market misconduct or moral hazard, and are usually presented on the basis that such an approval would be commercially sensible to make. Decisions to exempt a company from a provision would be made public in many developed markets. Interviewees in this study were asked to assess the flexibility of the CSRC in regard to its rules and regulations.¹⁰⁰

It seems that there is a strong opinion on the part of those interviewed that the CSRC is generally quite strict in applying its rules and regulations. A Beijing based academic lawyer thought that “it seems that the CSRC is usually very strict.” Similarly, a senior legal practitioner with close experience of the operation of the CSRC observed that:

“They haven’t been prepared to be flexible as the people who apply rules are not very experienced; they do not have experience of the market. Rules are as legalistic as possible as they are scared to death about applying discretion as they will be thought to be corrupt.”

A senior company officer noted in this regard that “you are just told what the rules are; the CSRC is reluctant to solve problems or to give an explanation for a rule.” In part this may also be linked to the CSRC’s lack of commercial experience.

However, the position became less clear when a legal rule was ambiguous or unclear in its meaning, in which event there was a perception that there was some room for flexibility on the part of the CSRC. As a senior CSRC official in a southern provincial city explained: “We do have flexibility, but it is not used frequently as it can be used in some areas only, such as where there is ambiguity in the rules.” Furthermore, where the law was silent about a matter, it was difficult to expect the CSRC to take action; as one legal and security adviser working within a large Shanghai company noted:

“There are still a lot of things that cannot be decided simply by resorting to rules and regulations; it is hard for the rules and regulations to cover all the issues that may arise. A key problem is the lack of a law imposing sanctions; all current punishments are administrative in nature and are not legal punishments like imprisonment or the payment of compensation. No one will be imprisoned for cheating small investors or for making false information disclosure.”

⁹⁹ See generally, K Hawkins (Ed), *The Uses of Discretion*, Oxford, Oxford University Press, 1992; and MR Kadish and SH Kadish, *Discretion to Disobey: A Study of Lawful Departures from FLegal Rules*, Stanford, Stanford University press, 1973.

¹⁰⁰ Question 34 asked: “How flexible do you see the CSRC being in the application of its rules and regulations ?”

A well-known Chinese solution to regulatory flexibility in the areas of corporate and securities regulation is to simply not enforce some rules in some areas. One legal critic thought that although the CSRC was “very active in creating rules, it does not have the incentive to enforce these rules.” Another observer thought that the CSRC enforced laws selectively, so as “to avoid a market crash.” A former CSRC official also noted that although the CSRC have the rules, “they do not enforce the rules.”

One factor that was frequently mentioned in the context of regulatory flexibility on the part of the CSRC was the influence of political factors. For example, one stock exchange official thought that although the CSRC “rules are not really flexible, not many are truly enforced due to the connection that companies often have with local government which protects them when violations occur.” A Beijing based corporate lawyer also noted that:

“it is a problem for the CSRC when the person at the top of a company has the status of a senior minister. This problem not only exists in listed companies. It exists in most companies, eg when a senior company person is to be punished by the CSRC, the Commission will usually encounter influence from the national or local government. If the relevant government does not agree with the decision, the CSRC will have to reconsider it.”

An experienced foreign business consultant working in Shanghai thought that flexibility arose from the fact that frequently “the regulations are not applied or enforced.” He added that: “it is still hard sometimes for the CSRC to pressure a senior company official; if the CCP says no, then it does not matter what the CSRC says. For example, if the Party may lose face, that trumps. This happens all the time.”

A company executive who remarked that the CSRC “should be strict as it was a government agency” expressed another slant on this political problem. However, he pointed out that because “the majority of listed companies are state-owned companies, there is a dialogue.” He added that because the head of a company like Sinopec is a Minister, “it is hard for the CSRC to enforce rules against Sinopec.” This political problem is especially acute when a “state secret” is involved. For example, a political decision to purchase aircraft from a foreign supplier may be reported to the CSRC, but this may not be disclosed to the market under disclosure rules because of such political concerns. A different kind of political explanation for the limited or selective application of rules by the CSRC was put by a Hong Kong-based corporate governance authority who explained philosophically:

“The CSRC is legalistic in the sense that it produces a large number of rules and regulations. Their core competence is making rules, rather than enforcing rules. They try to enforce, but have difficulty. Enforcement budgets are always limited. What do governments do when they set up a regulator? It is a bargaining process between the government and business communities. The CSRC probably has to be benign in enforcement and they are flexible in enforcement as there is no incentive to enforce mainly due to the existence of lots of private benefits (i.e. corruption). My impression is that in China corruption has a massive impact.”

8. Conclusions

This paper has only begun to tap the rich vein of data that has become available from an empirical study of corporate governance in China's top 100 listed companies. These companies are major state-controlled entities that are passing through a period of major change in China at a time that China's markets have been booming. Nevertheless, these companies are well aware of the importance of the corporate governance debates going on around them, although these debates do not always play themselves out as one might expect from the rhetoric of corporate governance that is to be found in China and more widely.

In part this is due to the size of the problem of change and the social and political obligations that have been accumulated by these companies. The desire to protect these large companies and position them for the next stage of global expansion by Chinese companies has meant that the state has had much greater influence over them than might otherwise be considered appropriate.

Laws and legal institutions have had difficulty keeping up with the changes that have been taking place in China's corporate sector and China's regulatory institutions are still at an early stage of development. Both the China Securities Regulatory Commission and China's two mainland stock exchanges are labouring under heavy burdens as they seek to perform their tasks with limited resources, limited legislative authority and within set national economic objectives. In many respects, they are reactive rather than proactive institutions and their principal roles are educative in nature as they seek to fashion China's emerging corporate governance culture.

Unfortunately, China's court system is ill-equipped to support these regulatory bodies or the other stakeholders who have interests in China's major listed companies. A paternalistic approach to the protection of these companies has meant that there has been a lack of appropriate legal remedies that might be expected to be available to investors and shareholders in a commercial marketplace. This will no doubt begin to change, but the pace of legal change has been far slower than the pace of change in the wider society and the market. Law reform and the implementation of laws have not been in the vanguard of China's economic reforms, despite recent official recognition of the importance of a law-based approach to society and the economy.

The rule of law is often seen as vital to the development of financial markets, but this ideal has been slow to take hold in regard to the application of Chinese corporate and securities laws. The securities market and corporate governance are still dominated by the rule by man rather than the rule of law. This was especially so in the context of the Asian financial upheavals at the late 1990s and improved corporate governance is not helped by the continuing lack of a buoyant securities market in China. Minority shareholders are especially disadvantaged in this regard and the legal remedies available to them remain poorly developed. In this context they have relatively little interest in corporate governance issues or in enforcing their legal rights. It is unlikely that their position will change quickly. However, as always, law and economy are changing very rapidly in China, but many things remain the same due to continuing underlying patterns of thought and paths of development.

Appendix A:**Top 100 Chinese Listed Companies (2001 –2004) #**

Organisations	Rank 2004	Rank 2003	Rank 2002	Rank 2001
China Petroleum & Chemical	1	1	1	1
PetroChina	2	2	2	2
China Mobile (Hong Kong)	3	3	3	3
China Telecom	4	4	-	-
China Life Insurance Company Limited	5	-	-	-
China Unicom	6	5	4	6
PICC Property and Casualty Company Limited	7	-	-	-
Minmetals Townlord Technology	8	8	11	16
Baoshan Iron & Steel	9	6	5	4
CNOOC	10	9	8	-
China Resources Enterprise	11	7	7	9
Sinopec Shanghai Petrochemical	12	11	9	8
Sinopec Zhenhai Refining & Chemical	13	12	10	7
TCL Corporation	14	-	-	-
CITIC Pacific	15	10	12	10
Legend Group	16	13	6	5
Huaneng Power International Holdings	17	15	15	14
Aluminum Corp. of China	18	17	14	-
Sinopec Yangzi Petrochemical	19	18	17	11
Jilin Chemical Industrial	20	24	19	13
Bank of China Hong Kong Holding	21	14	-	-
Sinotrans Limited	22	-	-	-
China Southern Airlines	23	16	13	12
Shanxi Taigang Stainless Steel	24	32	42	56
UTStarcom	25	44	67	-
TCL International Holdings	26	21	22	21
Shenzhen Zhongxing Telecom	27	28	26	62
Maanshan Iron & Steel	28	29	23	27
Beijing Shougang	29	23	18	15
AviChina Industry & Techonology Company Limited	30	-	-	-
COFCO International	31	26	47	-
Angang New Steel	32	31	25	19
Chongqing Changan Automobile	33	33	36	38
Digital China Holdings	34	20	27	-
Tangshan Iron & Steel	35	36	31	35
Sichuan Chanhong Electric	36	22	24	18
China Eastern Airlines	37	19	16	17
Beiqi Futian Vehicle	38	55	79	90
China International Marine Containers Group	39	37	43	25
Guangdong Midea Holding	40	30	21	26

Organisations	Rank 2004	Rank 2003	Rank 2002	Rank 2001
China Merchant Bank	41	25	-	-
Konka Group	42	47	44	23
Hunan Valin Steel Tube & Wire	43	34	29	45
Handan Iron & Steel	44	51	37	46
China Minsheng Banking	45	59	68	-
Shanghai Pudong Development Bank	46	43	38	48
China Aviation Oil (Singapore)	47	45	71	-
Qingdao Haier Holdings	48	27	20	57
Shanghai Friendship Group	49	54	58	-
Sinopec Beijing Yanhua Petrochemical	50	35	55	28
Bengang Steel Plates	51	81	64	34
BOE Technology Group	52	87	-	-
Great Wall Technology	53	40	57	42
Jinzhou Petrochemical	54	39	28	22
Sinochem International	55	50	48	50
Shanghai Construction	56	38	32	29
Laiwu Steel	57	74	70	61
Ningbo Bird	58	72	-	-
Inner Mongolia Baotou Steel Unicom	59	70	59	-
Sinopec Yizheng Chemical Fibre	60	49	33	24
Torch Investment Co., Ltd.	61	-	-	-
Brilliance China Automotive Holdings	62	57	53	44
Gree Electric Appliances of Zhuhai	63	62	46	43
Beijing Datang Power Generation	64	48	49	49
Shanghai Pharmaceutical	65	58	65	59
FAW Car	66	91	97	95
Qilu Petrochemical	67	60	40	33
Anyang Iron & Steel	68	67	56	-
Panzhuhua New Steel & Vanadium	69	53	35	31
Xiamen C&D	70	56	54	54
Yanzhou Coal Mining	71	46	50	58
Beijing Enterprises Holdings	72	63	45	51
Huaxia Bank Co., Ltd.	73	-	-	-
Sinopec Kantons Holdings	74	68	52	20
China Overseas Land & Investment	75	71	41	39
Huadian Power International Corporation Limited	76	52	39	37
Shenzhen Kaifa Technology	77	73	85	73
Tsingtao Brewery	78	65	63	85
Hangzhou Iron & Steel	79	82	77	70
Henan Shuanghui Investment & Development	80	90	-	-
SGIS Songhan	81	-	84	89
Nanjing Textiles Imp & Exp Corp., Ltd.	82	-	-	-
Guangzhou Phamaceutical	83	75	62	67
Harbin Phamaceutical Group	84	69	61	41
Shanghai Automotive	85	89	92	-

Organisations	Rank 2004	Rank 2003	Rank 2002	Rank 2001
Shanghai Material Trading Center	86	98	-	-
Nanjing Iron & Steel	87	92	82	88
Amoisonic Electronics	88	97	-	-
Wuhan Steel Processing	89	66	51	36
Tsinghua Tongfang	90	80	69	91
Lianyungang Ideal Group	91	95	-	-
Guangzhou Iron & Steel Co., Ltd.	92	-	-	-
Weiqiao Textile Company Limited	93	-	-	-
China Vanke	94	94	74	71
Yibin Wuliangye	95	76	72	69
Inner Mongolia Yili Industry Group Co., Ltd.	96	-	-	-
Guangdong Kelon Electrical Holdings	97	86	73	72
Guangdong Electric Power Development	98	78	60	65
Shijiazhuang Refining-Chemical	99	88	66	47
Shenzhen Development Bank	100	79	76	-
TCL Communications Equipment	-	41	-	-
Eastern Communications	-	42	30	30
Guangdong Investment	-	61	34	53
Dongfeng Automobile	-	64	75	86
Hisense Electric	-	77	88	64
People's Food Holdings	-	83	78	-
Hainan Airlines	-	84	-	-
Shanghai Bright Dairy & Food	-	85	-	-
SVA Electron	-	93	80	55
Shanghai Founder Yanzhong Sci. & Tech.Group	-	96	93	-
Shanghai Electric	-	99	90	77
Shandong Chenming Paper Holdings	-	100	-	-
China Railway Erju	-	-	81	-
Shanghai Tunnel Engineering	-	-	83	-
Guangzhou Development Industry Holdings	-	-	86	83
China Shiping Development	-	-	87	93
Shanghai Shenhua Industrial	-	-	89	-
Chongqing Iron & Steel	-	-	91	75
Ningbo United Group	-	-	94	-

Organisations	Rank 2004	Rank 2003	Rank 2002	Rank 2001
China Resources Land	-	-	95	-
Guangzhou Investment	-	-	96	80
Gansu Jiugang Group Hongxing Iron & Steel	-	-	98	97
Shanghai Industrial Holdings	-	-	99	96
Qingling Motors	-	-	100	63

In some years a company's ranking is not stated as the company was not included in the top 100 Chinese listed companies in that year.

Source: This table has been compiled using the listings of the top 100 PRC Listed Companies published in *Fortune* magazine since January 2002.