

**CONGLOMERATION UNBOUND:  
THE ORIGINS AND GLOBALLY UNPARALLELED  
STRUCTURES OF MULTI-SECTOR CHINESE CORPORATE  
GROUPS CONTROLLING LARGE FINANCIAL COMPANIES**

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ABSTRACT

Unlike other major financial markets, Mainland China is home to many mixed conglomerates that control a range of large financial and non-financial firms. This Article examines the Leninist origins of these financial-commercial conglomerates (“FCCs”), and how legal and policy changes in the 1980s and 1990s enabled FCC growth during the 2000s. An underexplored topic of research, Mainland China’s FCCs are mostly not subject to group-wide regulation and this Article finds that due to complex ownership structures brought about, in part, by legal ambiguity, potential risks these entities pose to financial markets can be unclear to regulators – in 2019, issues at one FCC-controlled bank ultimately sparked market-wide distress. Using a dataset built by the authors, this Article estimates that by 2017, FCC-controlled companies accounted for thirteen to nineteen percent of Mainland China’s commercial banking assets, over one-

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third of its life insurance policies written, and about thirty percent of assets held by its trust and investment companies (a type of institutional investment vehicle). Given ongoing efforts by the People's Bank of China to implement holding company regulations that may apply to some FCCs, this Article also contrasts the structure and regulation of Chinese FCCs with state-owned and private companies in the EU, Japan, and the United States. In doing so, it examines the extent to which state-owned FCCs in the People's Republic of China ("PRC") are unparalleled in structure, as well as how laws in other jurisdictions either prevent companies organized like the PRC's FCCs from forming or require more restrictive oversight of similarly-structured entities. This Article also finds that unlike financial groups in the EU, Japan, and the United States, many large Chinese FCCs formed using cross-shareholding and pyramid structures. It concludes by summarizing challenges that complex FCC structures in Mainland China may pose to regulators moving forward.

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## I. INTRODUCTION

Mainland China's<sup>1</sup> financial system, arguably the world's second largest,<sup>2</sup> is uniquely characterized by the prevalence of massive "mixed conglomerates" that control multiple large financial and non-financial businesses.<sup>3</sup> This Article classifies these business organizations as a type of financial-commercial conglomerate ("FCC")—a multi-layered corporate group, usually led by a non-financial<sup>4</sup> entity, that: (1) operates sizable non-financial business lines; and (2) controls two or more types of financial institutions that

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<sup>1</sup> For the purposes of this Article, the term "Mainland China" refers to areas of the PRC where the People's Bank of China, the China Banking and Insurance Regulatory Commission, and the China Securities Regulatory Commission have direct jurisdiction to regulate and supervise financial institutions.

<sup>2</sup> At the end of 2016, the PRC's banking system became the world's largest, surpassing the Eurozone's in size by assets. Gabriel Wildau, *China Overtakes Eurozone as World's Biggest Bank System*, FIN. TIMES (Mar. 5, 2017), <https://www.ft.com/content/14f929de-ffc5-11e6-96f8-3700c5664d30> [<https://perma.cc/V8VZ-KA6D>]. At year-end of 2017, Mainland China's banking assets (\$38.8 trillion) doubled those of the United States (\$16.2 trillion). See Alfred Liu & Benjamin Robertson, *China's \$35 Trillion Problem: Managing Financial Assets Is Hard*, BLOOMBERG (Oct. 25, 2018), <https://www.bloomberg.com/news/articles/2018-10-26/china-warns-of-financial-asset-mismanagement-after-initial-tally> [<https://perma.cc/X9MJ-MYJM>] (citing regulator data). Mainland China accounts for the third highest share (\$9.6 trillion) of 2017 assets belonging to "financial institutions that are not central banks, banks, insurance corporations, pension funds, public financial institutions, or financial auxiliaries," behind the Eurozone (\$32.2 trillion) and the U.S. (\$27.1 trillion). FIN. STABILITY BD., GLOBAL SHADOW BANKING MONITORING REPORT 2017, at 2, 15-17 (2018), <https://www.fsb.org/wp-content/uploads/P050318-1.pdf> [<https://perma.cc/9YHX-QE9H>] (defining "other financial intermediaries" and providing data). Mainland China is also the world's third largest insurance market (\$575 billion of life and nonlife premiums in 2018), behind the United States' and Europe's advanced economies. See DANIEL STAIB, MAHESH H. PUTTAIAH, & OLGA TSCHAKASSIN, WORLD INSURANCE: THE GREAT PIVOT EAST CONTINUES 9 (2019), [https://www.swissre.com/dam/jcr:b8010432-3697-4a97-ad8b-6cb6c0aece33/sig\\_ma3\\_2019\\_en.pdf](https://www.swissre.com/dam/jcr:b8010432-3697-4a97-ad8b-6cb6c0aece33/sig_ma3_2019_en.pdf) [<https://perma.cc/6ZGP-38GM>]. Japan's is the fourth largest. See *id.*

<sup>3</sup> Global banking regulators define "mixed conglomerates" as "groups which are predominantly industrially or commercially oriented but contain at least one regulated financial entity." TRIPARTITE GRP. BANK, SEC. & INS. REGULS., THE SUPERVISION OF FINANCIAL CONGLOMERATES 8 (1995), <https://www.bis.org/publ/bcbs20.pdf> [<https://perma.cc/C7AE-N9PW>].

<sup>4</sup> For purposes of this Article, "non-financial" describes activities, businesses, and entities that are commercial or industrial in nature, and thus do not primarily relate to business activities involving financial intermediation, such as banking, insurance, investing, or trading financial products.

conduct a substantial level of financial intermediation.<sup>5</sup> These groups can be state-owned (“SFCCs”) or privately-owned (“PFCCs”), although some PFCCs may have state-owned noncontrolling shareholders. Mainland China’s FCCs operate major non-financial businesses in a range of sectors including construction, e-commerce, energy, healthcare, mining, and transportation.<sup>6</sup> They also control multi-billion-dollar banks, large funds, and major payment systems.<sup>7</sup>

The existence of large corporate groups made up of sizable commercial, financial, and industrial businesses is not necessarily

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<sup>5</sup> For purposes of this Article, “substantial level of financial intermediation” generally means that an FCC’s total 2017 financial assets exceeded over \$10 billion U.S. dollars (“USD”) or that the FCC began facilitating over \$1 trillion USD annual payments in volume. This Article’s definition of FCC is based on the People’s Bank of China’s (中国人民银行, “PBOC”) definition of “de-facto financial holding companies” (“de-facto FHCs”), which it classifies as “non-financial companies [that] have acquired majority shareholding in two or more types of financial institutions.” PEOPLE’S BANK OF CHINA, CHINA FINANCIAL STABILITY REPORT 2018, at 168 (2018), <http://www.pbc.gov.cn/english/130736/3729741/index.html> [<https://perma.cc/J5AP-F2UM>]. To align with the PBOC’s analysis, this Article considers the following types of financial institutions when identifying FCCs: banks, funds, securities companies, insurers, futures companies, trust and investment companies (“TICs”), and internal financial companies. See *infra* note 272 and accompanying text (listing types of financial institutions owned by “de-facto financial holding companies”); *infra* notes 66-6967 and accompanying text (explaining internal financial companies); *infra* note 215 and accompanying text (explaining modern-day TICs). Consistent with the PBOC’s approach, for the purposes of identifying FCCs, this Article also treats the following as a “type of financial institution” if it is controlled by one of three e-commerce/internet conglomerates classified by the PBOC as a “de-facto FHC” (Suning Commerce Group, Tencent, and Alibaba): 1) a company with a national third-party payments license that processes over \$1 trillion USD in payments volume; and 2) a company that, through one or more non-bank lending businesses, conducts a high level of financial intermediation. See PEOPLE’S BANK OF CHINA, *supra* note 5, at 168-69. Given this Article’s focus on non-financial and financial businesses existing within one corporate group, its FCC definition does not include investment institutions that control several financial firms, which do meet the PBOC’s definition of “de-facto FHCs.” See *id.* at 169 (classifying state-owned asset managers that control various financial institutions as one type of “de-facto FHCs”). When identifying FCCs, this Article considers arrangements constituting an FCC’s control over a financial company besides direct ownership of a majority of shares in the company. See *infra* notes 217-230 and accompanying text. For a list of conglomerates that meet this Article’s definition of an FCC, see Appendix A. All FCCs analyzed in this Article are led by non-financial entities except for two insurance companies—Anbang Insurance Group Co., Ltd. and Ping An Insurance (Group) Company of China, Ltd.—that by mid-2017 also controlled large non-financial business lines, and are thus treated as FCCs. See *infra* notes 157, 169 and accompanying text. Throughout this Article, the term “FCC” generally refers to entities based in Mainland China.

<sup>6</sup> See *infra* Appendix A.

<sup>7</sup> See *infra* notes 197-215 and accompanying text.

problematic.<sup>8</sup> Yet as the People's Bank of China ("PBOC") warned in its 2018 Financial Stability Report, the rapid growth of inadequately regulated FCCs over the last few years may pose a threat to the Chinese economy.<sup>9</sup> As this Article explains, the complex structures of Mainland China's FCCs can impede private and public sector risk monitoring by obfuscating financial relationships within FCCs and between these groups and other entities. This in turn may reduce the likelihood that Mainland China's FCCs have sufficient resources to withstand negative idiosyncratic events or broader economic shocks. Notably, the prevalence of FCCs in Mainland China distinguishes it from the world's three other largest financial markets—the European Union ("EU"), Japan, and the United States—where similarly structured groups are rare or non-existent due to different regulatory frameworks and policy approaches.<sup>10</sup>

The PBOC is actively pursuing regulatory responses to the comparatively significant role that FCCs play across the PRC's financial system relative to other jurisdictions including the EU, Japan, and the United States.<sup>11</sup> One particularly important issue flagged in the PBOC's Financial Stability Report and explored in this Article is the prevalence of intra-group transactions between

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<sup>8</sup> See FIN. STABILITY BD., *BIG TECH IN FINANCE: MARKET DEVELOPMENTS AND POTENTIAL FINANCIAL STABILITY IMPLICATIONS* 23 (2019), <https://www.fsb.org/wp-content/uploads/P091219-1.pdf> [<https://perma.cc/2H9U-Q7WT>] (finding that by allowing technology companies to offer financial services, Chinese firms were able to drastically expand financial inclusion); Keith A. Noreika, Acting Comptroller of the Currency, Remarks at the Clearing House Annual Conference 10 (Nov. 8, 2017), <https://www.occ.gov/news-issuances/speeches/2017/pub-speech-2017-134.pdf> [<https://perma.cc/UFX5-X5K3>] (observing that "mixing banking and commerce can generate efficiencies that deliver more value to customers and can improve bank and commercial company performance with little additional risk").

<sup>9</sup> PEOPLE'S BANK OF CHINA, *supra* note 5, at 164 (observing that "[w]ithout adequate regulation and supervision," the rapid growth of non-financial corporate groups that control financial entities and engage in high levels of intra-group transactions "may pose threats to [the PRC's] economic and social stability").

<sup>10</sup> See *infra* notes 288-406 and accompanying text.

<sup>11</sup> See PEOPLE'S BANK OF CHINA, *supra* note 5, at 164-68 (observing that non-financial conglomerates in Mainland China that control financial companies have grown in recent years, but are mostly not subjected to group-wide supervision, and contrasting this regulatory approach with financial holding company regulatory regimes in other jurisdictions, including the United States, EU, and Japan); *id.* at 169-71 (stating that the "savage growth" of non-financial conglomerates that control financial companies through risky means "must be treated as an acute disease"); see also *infra* notes 249, 266-282 and accompanying text (describing recent policy actions proposed and taken by the PBOC and other agencies that would increase regulation over or augment the structure of certain FCCs).

Mainland China's FCC-controlled financial firms and their non-financial affiliates. In 2018, PRC regulators seized the assets of a massive, opaquely-structured FCC that controlled numerous financial companies and reportedly relied upon false financial transactions between these entities and affiliates to fuel growth.<sup>12</sup> Shortly thereafter, the PBOC and the PRC's top banking regulator both warned that other FCCs were using financial firm affiliates to fund company expansion through inappropriate intra-group transactions.<sup>13</sup>

These warnings came to a head in mid-2019 when Baoshang Bank, controlled by a massive FCC called Tomorrow Group, was taken over by the PBOC and the China Banking and Insurance Regulatory Commission ("CBIRC") in response to "severe credit risks" – Mainland China's first bank takeover in twenty years – and shortly thereafter, the deposit insurance fund incorporated by the PBOC took over 150 interbank negotiable certificates of deposit issued by Baoshang Bank.<sup>14</sup> Indeed, much of Baoshang Bank's lending volume was reportedly to other Tomorrow Group companies.<sup>15</sup> Over forty percent of its liabilities were interbank

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<sup>12</sup> See Guo Tingbing, *In Depth: A Maze of Capital Leads to Anbang's Aggressive Expansion*, CAIXIN (Apr. 30, 2017), <https://www.caixinglobal.com/2017-04-30/a-maze-of-capital-leads-to-anbangs-aggressive-expansion-101084940.html> [<https://perma.cc/RT4T-HPXB>].

<sup>13</sup> See *China Official Says Crackdown on Murky Conglomerates Isn't Over*, BLOOMBERG (Jan. 16, 2018), <https://www.bloomberg.com/news/articles/2018-01-17/china-official-says-crackdown-on-murky-conglomerates-isn-t-over> [<https://perma.cc/7C9X-P36R>] (reporting that Shuqing Guo, chairman of the China Banking Regulatory Commission, stated that some conglomerates structured through complex ownership structures used affiliate banks as "ATM machines"); PEOPLE'S BANK OF CHINA, *supra* note 5, at 170 (finding that "some non-financial enterprises obtain credit funds, manipulate profits, and transfer or hide assets through loans and guarantees from financial institutions they own . . . [which] are used as cash machines").

<sup>14</sup> See Cheng Leng, *China's State Insurance Fund to Take over Baoshang NCDs from July 8 – Sources*, REUTERS (July 4, 2019), <https://www.reuters.com/article/china-banks-baoshang/chinas-state-insurance-fund-to-take-over-baoshang-ncds-from-july-8-sources-idUSL4N24516F> [<https://perma.cc/B6JL-U2L5>] (citing regulators); see also IMF, *People's Republic of China: 2019 Article IV Consultation*, 8, Country Report No. 19/266 (Aug. 2019), <https://www.imf.org/en/Publications/CR/Issues/2019/08/08/Peoples-Republic-of-China-2019-Article-IV-Consultation-Press-Release-Staff-Report-Staff-48576> [<https://perma.cc/3PGQ-4ZNY>].

<sup>15</sup> See Xia Guobei & Leng Cheng, *Troubled Tomorrow Group Selling Control of Baoshang Bank*, CAIXIN (June 7, 2018), <https://www.caixinglobal.com/2018-06-07/troubled-tomorrow-group-selling-control-of-baoshang-bank-101266629.html> [<https://perma.cc/6GNF-5T97>] (discussing the close relationship between Baoshang Bank and Tomorrow Group).

debts<sup>16</sup>—its distress increased funding costs for banks and non-financial institutions heavily reliant on interbank markets by sparking market-wide fears.<sup>17</sup> The PBOC responded by injecting over 400 billion yuan (over \$60 billion U.S. dollars (“USD”)) into interbank markets.<sup>18</sup>

Then in early 2020, long-standing financial difficulties at another FCC—HNA Group, headquartered in Hainan province—triggered local government involvement. Regulators had already intervened to support the heavily-indebted conglomerate’s ability to raise funds in 2018,<sup>19</sup> but after the coronavirus pandemic’s severe impact on

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<sup>16</sup> See Wu Hongyuran, Timmy Shen & Teng Jing Xuan, *Exclusive: Baoshang Bank’s Creditors Get Added Backstop on Deposits, Debts Worth Over 50 Million Yuan*, CAIXIN (May 27, 2019), <https://www.caixinglobal.com/2019-05-27/exclusive-baoshang-banks-creditors-get-added-backstop-on-deposits-debts-worth-over-50-million-yuan-101420491.html> [<https://perma.cc/62LW-HKNL>].

<sup>17</sup> See Andrew Galbraith & Cheng Leng, *China’s Baoshang Bank Takeover Raises Contagion Fears*, REUTERS (May 27, 2019), <https://www.reuters.com/article/us-china-banks-regulator-ncd/chinas-baoshang-bank-takeover-raises-contagion-fears-idUSKCN1SX0QT> [<https://perma.cc/YM5Q-KJ8A>] (reporting that “[t]he seizing of Baoshang fanned concerns about indebted small banks across the country, pushing up yields on some negotiable certificates of deposit (NCD) issued by regional banks by more than 10 basis points”); Gabriel Wildau & Yizhen Jia, *Regional Lenders: China’s Most Dangerous Banks*, FIN. TIMES (July 30, 2018), <https://www.ft.com/content/24e2a368-7b4b-11e8-bc55-50daf11b720d> [<https://perma.cc/8P8A-E6UJ>] (reporting that many of Mainland China’s regional banks rely heavily on interbank markets for funding). Mainland China’s bank-sponsored wealth management products, which are mostly issued by small and medium joint-stock banks but operated off-balance sheet by non-bank affiliates, channel both bank and non-bank funds into a range of assets, including money market instruments, bonds, and equity assets. Torsten Ehlers, Steven Kong & Feng Zhu, *Mapping Shadow Banking in China: Structure and Dynamics*, 14-15 (Bank for Int’l Settlements, Working Paper No. 701, 2018), <https://www.bis.org/publ/work701.pdf> [<https://perma.cc/C93N-23MH>].

<sup>18</sup> See Anjani Trivedi & Shuli Ren, *China’s Lehman Moment Is Drawing Closer*, BLOOMBERG (June 19, 2019), <https://www.bloomberg.com/opinion/articles/2019-06-19/china-s-lehman-moment-is-drawing-closer> [<https://perma.cc/DN62-5A8B>]. Throughout this Article, the 2017 conversion rate of 6.759 yuan to \$1 USD reported by the OECD is used to convert yuan volumes into approximate USD. *Exchange Rates*, OECD, <https://data.oecd.org/conversion/exchange-rates.htm> [<https://perma.cc/EN97-WXXY>]. In instances where the yuan and Japanese yen are converted, a 16.585 yen to 1 yuan conversion rate is used, according to the OECD report of 112.166 yen to \$1 USD conversion rate for 2017. *Id.* In instances where the yuan and Euro are converted, a 7.637 yuan to 1 euro conversion rate is used, as the OECD reports a 0.885 euro to \$1 USD conversion rate for 2017. *Id.*

<sup>19</sup> See *China Prepares State Support for HNA Fundraising*, BLOOMBERG (June 15, 2018), <https://www.bloomberg.com/news/articles/2018-06-15/china-is-said-to-prepare-state-support-for-hna-fundraising> [<https://perma.cc/TF3Z-SVZG>] (reporting that, in June 2018, a “senior official at the People’s Bank of China led a

HNA Group in 2020, the Hainan provincial government established a working group made up of local authorities to help the FCC restructure its sizable debts to a number of large banks.<sup>20</sup> Most recently, the FCC Alibaba and its affiliate Ant Financial have been subject to a range of high-profile regulatory actions, discussed in depth below.

In order to improve understanding of the complex, multi-sector conglomerates at the center of these recent events, this Article analyzes the economic, legal, and policy origins of Mainland China's FCCs, as well as what differentiates their structure and regulation from financial groups and mixed conglomerates in the EU, Japan, and the United States. Unlike older research that contrasts financial conglomerate regulation in the EU, Mainland China, and the United States,<sup>21</sup> this Article focuses on conglomerates that both control two or more types of large financial companies and also conduct substantial non-financial business activities. This Article also fills research gaps stemming from the fact that most Chinese FCCs emerged relatively recently and operate across financial sector verticals (for example, banking and insurance), so their significance

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meeting with three regulators, the Hainan provincial government, HNA Co-Chairman Chen Feng and the group's biggest creditor, instructing attendees to support HNA's future bond issues").

<sup>20</sup> Haihang Jituan (海航集团) [HNA Group], *Hainansheng Haihang Jituan Lianhe Gongzuozu Jiang Quanmian Xiezu Quanli Tuijin Benji Tuanfeng Xian Huajie Gongzuo* (海南省海航集团联合工作组将全面协助全力推进本集团风险化解工作) [*Hainan Province's HNA Group Joint Working Group Will Fully Assist the Group's Risk Resolution Work*], XUEQIU (雪球) (Feb. 29, 2020), <https://xueqiu.com/2701143866/142553597> [https://perma.cc/N2UB-8KHY] (reporting that the working group was established in late February 2020). In mid-March 2020, HNA Group announced that the working group was helping HNA Group address governance and debt problems facing the conglomerate, and that, with the support of policymakers, it was in the process of restructuring debts with a number of large banks. Haihang Jituan (海航集团) [HNA Group], *Haihang Jituan Yu Bufen Zhaiquan Yinhang Daibiao Juxing Zuotanhui* (海航集团与部分债权银行代表举行座谈会) [*HNA Group Held a Symposium with Representatives of Some Creditor Banks*], WEIXIN (微信) [WECHAT] (Mar. 13, 2020), <https://mp.weixin.qq.com/s/el8WWmYEVmWmZn3UHMjmQ> [https://perma.cc/DC28-N97R]. According to one report quoting inside sources, by mid-March 2020, the working group was, "play[ing] a dual role of rescue and supervision . . . allowing the government to channel necessary funding and asset merger services to HNA." Dave Makichuk, 'No Bailout' for Troubled HNA Group, ASIA TIMES (Mar. 3, 2020), <https://asiatimes.com/2020/03/no-bailout-for-troubled-hna-group/> [https://perma.cc/8R28-G5T2].

<sup>21</sup> See Kuan-Chun Chang, *From Zero to Something: The Necessity of Establishing a Regulatory System of Financial Conglomerates in China*, 11 ASIAN-PAC. L. & POL'Y J. 1, 69-93 (2009).

is accordingly not emphasized in earlier, sectoral-focused studies on Mainland China's financial system structure.<sup>22</sup>

Part II examines the Leninist origins of the PRC's first SFCCs, which emerged in the 1980s, and how legal and regulatory changes of the 1980s and 1990s facilitated FCC growth during the 2000s. Part III estimates the role FCCs play in Mainland China's modern financial system, while also identifying regulatory reasons for and organizational drivers of complex FCC structures that may pose potential financial market risks, as well as recent regulatory steps taken in response by the PBOC. Part IV contrasts structures of Mainland China's FCCs with those of state-owned entities and corporate groups in the EU, Japan, and the United States, examining how these jurisdictions' policy frameworks prevent organizations similar to Mainland China's large FCCs from emerging. Part V concludes, summarizing challenges that FCCs will pose to regulators moving forward.

## II. HOW DECADES OF LEGAL AND POLICY CHANGES SPURRED THE FORMATION OF CHINA'S FIRST FCCS

Mainland China's first FCCs formed in the late 1980s. Their origins can be traced to the PRC's 1950s to 1970s embrace of a Lenin-inspired, centrally-planned economic system, through which almost all financial and commercial activities were coordinated by the state, as well as 1980s policy shifts guided by an embrace of cross-sector horizontal integration aimed at achieving a "socialist commodity economy."<sup>23</sup> Against this backdrop, most large FCCs emerged in the

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<sup>22</sup> See generally DOUGLAS J. ELLIOTT & KAI YAN, *THE CHINESE FINANCIAL SYSTEM: AN INTRODUCTION AND OVERVIEW* (2013) (analyzing the Mainland China financial system primarily along categories that reflect financial industry sub-sectors); Franklin Allen & Jun "QJ" Qian, *China's Financial System and the Law*, 47 *CORNELL INT'L L.J.* 499 (2014) (examining the Mainland China financial system across banking, stock markets, bond markets, investment industry, asset managers, and the shadow financial sector); Franklin Allen, Jun "QJ" Qian & Xian Gu, *An Overview of China's Financial System*, 9 *ANN. REV. FIN. ECON.* 191 (2017) (analyzing the PRC financial system across: the banking and intermediation sector; financial markets; the shadow financial sector; and foreign sectors).

<sup>23</sup> The founding of the PRC's political and economic system was highly influenced by the Soviet Union's. See Wu Jinglian (吴敬琏), *Zhongguo Jingji Gaige Sanshi Nian Licheng de Zhidu Sikao* (中国经济改革三十年历程的制度思考) [Thoughts on the Reform of China's 30-Year Economic System], *Keji yu Jingji Huaba* (科技与经济画报) [*ECON. SCI.*], no.5, 2008, at 285. Indeed, the PRC's embrace

2000s, thanks to 1990s legal and policy shifts formalizing company structures and securities markets, as well as efforts throughout the 2000s to channel more private capital into the financial sector. This Part profiles legal reforms, policy actions, and economic events that enabled PRC corporate groups to gain control of two or more of nine types of financial companies<sup>24</sup> and thus become FCCs. In particular, this Part focuses on the origins of Mainland China's ten largest FCCs as of 2017,<sup>25</sup> and on how these major FCCs gained control of banks, insurers, and "trust and investment companies,"<sup>26</sup> which have served as financing vehicles for numerous FCCs' commercial and industrial business lines.

*a. Born from Lenin's "State Syndicate": Origins of FCCs*

Shortly after the PRC's founding, its policymakers embraced Vladimir Lenin's vision for a "State Syndicate,"<sup>27</sup> through which "[a]ll citizens become employees and workers of a single countrywide state 'syndicate.'"<sup>28</sup> By 1956, the PRC had adopted Leninist socialism "with drums beating and gongs clanging," as economist Wu Jinglian writes, and all urban nonagricultural

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of Lenin's "State Syndicate" resulted in the mid-1950s establishment of a "centrally-planned economic system." See JINGLIAN WU, UNDERSTANDING AND INTERPRETING CHINESE ECONOMIC REFORM 9, 12 (2015). Later, the PRC's central government implemented a series of policies between 1958 and 1978 that decentralized administrative power from the central government to subcentral authorities, forming a decentralized planned economic system. These developments, however, did not change the nature of the PRC's planned economy. See *id.* at 43, 54-55.

<sup>24</sup> According to this Article's definition, FCCs control two or more types of the following financial firms: banks, certain large non-bank lending companies, certain large non-bank payments companies, fund companies, futures companies, insurers, internal financial companies, securities companies, and "trust and investment companies." See PEOPLE'S BANK OF CHINA, *supra* note 5 and accompanying text.

<sup>25</sup> Based on data used in this Article's analysis and its definition of an FCC, Mainland China's ten largest FCCs as of 2017 were Alibaba, Anbang Group, CITIC Group, China Huaneng Group, China Resources, China Merchants Group, Evergrande Real Estate, Ping An Group, Tomorrow Group, and Funde Group. For information on the sources and methodology used to identify these FCCs, see *infra* note 196 and accompanying text.

<sup>26</sup> For an overview of the functions of modern-day trust and investment companies, see MCKINSEY & CO., *infra* note 215 and accompanying text.

<sup>27</sup> See JINGLIAN WU, CHINA'S LONG MARCH TOWARD A MARKET ECONOMY 83-84 (2005).

<sup>28</sup> VLADIMIR LENIN, *The State and Revolution*, in 25 V. I. LENIN COLLECTED WORKS 381, 473 (Stepan Apresyan & Jim Riordan eds., 1964).

industries were transformed into a single, giant enterprise—the “state syndicate.”<sup>29</sup> Indeed, Wu explains that each of the thousands of state-owned enterprises (“SOEs”) that emerged was not considered a stand-alone entity, but rather, a “grassroots production unit for cost accounting” within a “highly integrated system of the party, the state, and the economy” that spanned many sectors.<sup>30</sup> From 1959 to 1978, SOEs accounted for over eighty-six percent of the PRC’s total industrial output.<sup>31</sup> Policymakers encouraged SOEs to expand operations across various industries,<sup>32</sup> resembling the cross-sector expansion FCCs would embrace decades later.

The PRC’s 1950s embrace of a Leninist “state syndicate” also resulted in the establishment of a “mono-bank” system through which the PBOC was the PRC’s only bank,<sup>33</sup> serving both commercial bank and central bank functions.<sup>34</sup> This aligned with Lenin’s vision for “a single giant State Bank, with branches in every rural district, in every factory.”<sup>35</sup> By the 1960s, the PBOC was essentially the only source of industrial and commercial credit in the PRC.<sup>36</sup> Similar to operational and commercial activities of SOEs, its

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<sup>29</sup> UNDERSTANDING AND INTERPRETING CHINESE ECONOMIC REFORM, *supra* note 23, at 83-84.

<sup>30</sup> *Id.* at 84.

<sup>31</sup> See BECKY CHIU & MERVYN K. LEWIS, REFORMING CHINA’S STATE-OWNED ENTERPRISES AND BANKS 189 (2006).

<sup>32</sup> See, e.g., MAO TSE-TUNG, *Instructions (June-September 1958)*, in SELECTED WORKS OF MAO TSE-TUNG: VOLUME VIII (1990).

<sup>33</sup> See CHIU & LEWIS, *supra* note 31, at 188-89.

<sup>34</sup> See Franklin Allen, Xian Gu & Jun “QJ” Qian, *People’s Bank of China: History, Current Operations and Future Outlook* 5-6 (2017), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3018506](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3018506) [<https://perma.cc/T2GA-ZK7U>] (noting that under this law and regulation, the PBOC was made responsible for “[i]ssuing currency, managing the treasury, administering financial activities, maintaining financial stability and restoring the economy and rebuilding the country” and also for “(1) printing and issuing banknotes and bonds and adjusting currency circulation; (2) allocating wealth and providing short-term and long-term loans and investment; (3) analyzing and monitoring the financial management of government offices, state-owned enterprises and cooperatives by managing cash and transferring money; (4) managing foreign currency, noble metals, and the balance of payments and settlements; (5) taking charge of financial administration and supervising private institutions, public-private institutions and foreign organizations involving the financial industry; (6) managing treasury and cash outflow of the fiscal budget; (7) issuing treasury bonds; (8) leading specialized banks and state-owned insurance companies; (9) other relevant financial issues”).

<sup>35</sup> See CHIU & LEWIS, *supra* note 31, at 189 (quoting A.W. SAMANSKY, CHINA’S BANKING SYSTEM: ITS MODERN HISTORY AND DEVELOPMENT 1 (1981)).

<sup>36</sup> See *id.*

lending and monetary policy decisions were ultimately decided by the State Council,<sup>37</sup> “the highest organ of state administration” in the PRC.<sup>38</sup> By the late 1970s, the PRC had transformed into a large, cross-sector “state syndicate” that inherently mixed commercial and financial activities.<sup>39</sup>

*b. The 1980s: The First FCC Emerges from Financial System Shifts and SOE Reforms*

Starting in 1978, the PRC began a decade of sweeping economic policy changes resulting in dramatic transformations to its financial system and SOEs. The economic model that came about—“socialism with Chinese characteristics”—aimed to achieve economic modernization through pragmatic reforms, although it remained explicitly guided by Leninism.<sup>40</sup> This decade would give rise to SFCCs, whose business activities, like that of the PRC’s “state syndicate,” spanned multiple sectors and aligned with national policy objectives.

Between 1979 and 1984, the PRC’s mono-banking system was split-up, and major pillars of financial intermediation were handed over to newly-created, state-controlled entities. Four major state-owned banks (“SOBs”) were formed.<sup>41</sup> Previously-established rural credit cooperatives (“RCCs”) morphed into SOB “grassroots”

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<sup>37</sup> See Allen, Gu & Qian, *supra* note 34, at 6-7.

<sup>38</sup> SUSAN V. LAWRENCE & MICHAEL F. MARTIN, CONG. RSCH. SERV., R43303, CHINA’S POLITICAL INSTITUTIONS AND LEADERS IN CHARTS 2 (Mar. 20, 2013) (quoting XIANFA art. 57, §1 (1982) (China)), <https://fas.org/sgp/crs/row/R43303.pdf> [<https://perma.cc/HK25-BAFX>].

<sup>39</sup> See Yingyi Qian & Jinglian Wu, *China’s Transition to a Market Economy: How Far across the River?* 4-5 (Stan. Ctr. for Int’l Dev., Working Paper No. 69, 2000), <https://kingcenter.stanford.edu/sites/default/files/publications/69wp.pdf> [<https://perma.cc/4JHC-M8AR>] (observing that “the essential point of Lenin’s [State Syndicate] remained valid for both pre-reform and post-reform China”).

<sup>40</sup> Marxism-Leninism was a component of one of the “Four Cardinal Principles,” introduced by Deng Xiaoping in a 1979 speech that guided “socialism with Chinese characteristics.” See William A. Joseph, *Ideology and Chinese Politics*, in *POLITICS IN CHINA: AN INTRODUCTION* 129, 156 (William A. Joseph ed., 2010).

<sup>41</sup> The large SOBs established during this time are the Agricultural Bank of China, Bank of China, China Construction Bank, and the Industrial and Commercial Bank of China. See CHIU & LEWIS, *supra* note 31, at 191-92.

units,<sup>42</sup> state-influenced urban credit cooperatives (“UCCs”) were launched,<sup>43</sup> and the PBOC’s role as a central bank was reaffirmed by the State Council.<sup>44</sup> The People’s Insurance Company of China (“PICC”) was founded as the PRC’s only insurance company and would remain as such until the late 1980s.<sup>45</sup>

Although securities markets were undeveloped,<sup>46</sup> policymakers increasingly allowed small businesses to form.<sup>47</sup> Private sector growth accelerated after 1983 under Deng Xiaoping’s policy of “don’t argue; try bold experiments and blaze new trails” and related national-level guidelines, which enabled medium- to large-scale private enterprises to grow,<sup>48</sup> even though the private sector would

<sup>42</sup> RCCs are another form of loan-making depository institution that date back to the 1950s, when their ownership structure at that time was unclear; although by the 1960s and 1970s, RCCs were managed by “people’s communes.” See KUMIKO OKAZAKI, RAND, NAT’L SEC. RSCH. DIV., BANKING SYSTEM REFORM IN CHINA: THE CHALLENGES OF MOVING TOWARD A MARKET-ORIENTED ECONOMY 10 (2007), [https://www.rand.org/content/dam/rand/pubs/occasional\\_papers/2007/RAN\\_D\\_OP194.pdf](https://www.rand.org/content/dam/rand/pubs/occasional_papers/2007/RAN_D_OP194.pdf) [<https://perma.cc/V5A3-EVCG>]. Starting in the late 1970s, RCCs “were transformed into the ‘grass-roots unit’ of the [Agricultural Bank of China],” an SOB. *Id.*

<sup>43</sup> UCCs are depositories that emerged to primarily serve privately-owned enterprises and individuals. The first UCC was established in 1979. See *id.* at 9-10; see also Nicholas Loubere & Heather Xiaoquan Zhang, *Co-operative Financial Institutions and Local Development in China*, 3 J. COOP. ORG. & MGMT. 32, 34 (2015) (explaining that UCCs were “set-up and run by local people, institutions and governments” and “worked closely with local governments” when making loans).

<sup>44</sup> See Allen, Gu & Qian, *supra* note 34, at 7-8.

<sup>45</sup> See SWISS RE CORPORATE HISTORY, A HISTORY OF INSURANCE IN CHINA 31-32 (2017), [https://www.swissre.com/dam/jcr:eb1aba5f-05ca-4bd4-bfe6-d42a6ed6b8c5/150Y\\_Markt\\_Broschuere\\_China\\_Inhalt.pdf](https://www.swissre.com/dam/jcr:eb1aba5f-05ca-4bd4-bfe6-d42a6ed6b8c5/150Y_Markt_Broschuere_China_Inhalt.pdf) [<https://perma.cc/4HZZ-L97M>].

<sup>46</sup> See NICOLAAS GROENWOLD, YANRUI WU, SAM HAK KAN TANG & XIANG MEI FAN, THE CHINESE STOCK MARKET: EFFICIENCY, PREDICTABILITY AND PROFITABILITY 10 (2004) (explaining that in the early 1980s, joint stock structures were limited to some instances of “co-operative shareholding” established by township and village enterprises in southern coastal provinces).

<sup>47</sup> In the early 1980s, there were over 178,000 *ge-ti* (“个体”) shops and locations in Mainland China that together employed over two million people. Each of these entities could technically only hire up to seven people, but by 1983, some employed over 100 people. Xiaohong Chen, *Private Enterprises, and the Growth of Small and Medium-Sized Enterprises*, in THIRTY YEARS OF CHINA’S REFORM 276, 283-84 (Wang Mengkui ed., 2012).

<sup>48</sup> See UNDERSTANDING AND INTERPRETING CHINESE ECONOMIC REFORM, *supra* note 23, at 184 (citing Deng Xiaoping, *Excerpts from Talks Given in Wuchang, Shenzhen, Zhuhan and Shanghai*, in 3 SELECTED WORKS OF DENG XIAOPING 374 (1993)). In 1983, a nationwide “three-nots” policy was also issued in response to large-scale business operations emerging across the PRC: “It is not convenient to promote these, they are not allowed to be publicized openly, and we should not be in a hurry to shut them down.” See Xiaohong Chen, *supra* note 47, at 284-85.

not be legalized until 1988.<sup>49</sup> Yet capital markets remained immature,<sup>50</sup> and SOB lending volume was capped by the State Council and largely restricted to SOEs.<sup>51</sup>

To fuel large-scale investments and equipment imports, state-owned “trust and investment companies” (“TICs”), from which the first SFCCs would emerge, were established.<sup>52</sup> The first—China International Trust and Investment Corporation (“CITIC”)—was founded with state funds in 1979.<sup>53</sup> By 1982, hundreds of TICs—all state-controlled—were operational.<sup>54</sup> TICs raised capital from institutional sources, such as governments and international investors, and used those funds to make loans and investments across sectors.<sup>55</sup>

The establishment of TICs was a necessary ingredient for the formation of the first FCCs. Another was the gradual proliferation of joint-stock ownership structures for private and public sector enterprises, accelerated by local-level policy actions between 1984 and 1986,<sup>56</sup> which enabled thousands of joint-stock companies to

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<sup>49</sup> It was not until 1988 that the PRC Constitution was amended to permit the private sector to exist. See UNDERSTANDING AND INTERPRETING CHINESE ECONOMIC REFORM, *supra* note 23, at 59-60.

<sup>50</sup> See Grace Xing Hu, Jun Pan & Jiang Wang, *Chinese Capital Market: An Empirical Overview* 3-4 (Nat'l Bureau Econ. Rsch., Working Paper No. 24346, 2018), <http://web.mit.edu/people/junpan/CCM.pdf> [<https://perma.cc/R5VX-NZ8W>] (discussing the initial stage of the PRC's significant but slow period of transforming into a more market-oriented economy after 1976, beginning with the emergence of common stocks in the early 1980s).

<sup>51</sup> See CHIU & LEWIS, *supra* note 31, at 191-92.

<sup>52</sup> See Zhaohui Hong & Ying Yan, *Trust and Investment Corporations in China* 2 (Fed. Rsrv. Bank Cleveland, Working Paper No. 97-06, 1997), <https://www.clevelandfed.org/en/newsroom-and-events/publications/working-papers/working-papers-archives/1997-working-papers/wp-9706-trust-and-investment-corporations-in-china.aspx> [<https://perma.cc/A84K-GMZK>] (noting that “[b]efore TICs were formed, most of the firms in China had only one resource for all their financial needs—the state-owned banks”); GREGORY C. CHOW, *THE CHINESE ECONOMY* 297 (2d ed. 1987) (observing that the first TIC was established in part to “import advanced technology and equipment”).

<sup>53</sup> See QIN XIAO, *THE THEORY OF THE FIRM AND CHINESE ENTERPRISE REFORM: THE CASE OF CHINA INTERNATIONAL TRUST AND INVESTMENT CORPORATION* 93 (2004).

<sup>54</sup> See ANDREW COLLIER, *SHADOW BANKING AND THE RISE OF CAPITALISM IN CHINA* 77 (2017).

<sup>55</sup> See *id.* at 76-77.

<sup>56</sup> In 1984, the Shanghai Municipal Government established securities regulations, facilitating private company stock ownership, and enabling an electronics company to issue stock, marking for the first private sector share issuance in the PRC's history. See KANG YONG, LU SHI & ELIZABETH D. BROWN,

emerge.<sup>57</sup> Then in 1986, the State Council stimulated the conversion of SOEs into joint-stock companies,<sup>58</sup> and explicitly encouraged the development of horizontally-integrated, multi-sector conglomerates through its “Provisions on Several Issues Concerning Further Promoting Horizontal Economic Integration” (“1986 Provisions”).<sup>59</sup> With the goal of achieving a “socialist commodity economy,” the 1986 Provisions supported “horizontal economic union” between enterprises through a number of approaches, including multi-sector conglomerates.<sup>60</sup>

Following the spirit of these provisions, CITIC’s CEO proposed to the State Council in 1986 that CITIC be permitted to reorganize as a “socialist group company” with a banking subsidiary.<sup>61</sup> In 1987, the State Council allowed CITIC to transform into a multi-tiered conglomerate called “CITIC Group,”<sup>62</sup> launch a wholly-owned national commercial bank,<sup>63</sup> and reorganize its many divisions into

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CHINESE CORPORATE GOVERNANCE: HISTORY AND INSTITUTIONAL FRAMEWORK 6 (2008), [https://www.rand.org/pubs/technical\\_reports/TR618.html](https://www.rand.org/pubs/technical_reports/TR618.html) [<https://perma.cc/2LXU-JSAK>]. By 1986, other local governments had also issued rules to govern the issuance of private company stocks to the public. See Basile Cuigniez, *The Chinese Stock Market: Historical Evolution and Current Trends* 19 (2017) (M.S. Dissertation, Universiteit Gent), [https://lib.ugent.be/fulltxt/RUG01/002/376/724/RUG01-002376724\\_2017\\_0001\\_AC.pdf](https://lib.ugent.be/fulltxt/RUG01/002/376/724/RUG01-002376724_2017_0001_AC.pdf) [<https://perma.cc/P8LP-TZZN>].

<sup>57</sup> By 1986, over 6,000 companies across the PRC had issued stock, and over-the-counter stock markets were operating in several big cities. Cuigniez, *supra* note 56, at 19.

<sup>58</sup> The State Council’s *Regulations on Deepening Enterprise Reform and Enhancing the Vitality of Enterprises* allowed many SOEs to be converted into joint-stock companies. See Hu, Pan & Wang, *supra* note 50, at 4; FAN ZHANG, *THE INSTITUTIONAL EVOLUTION OF CHINA: GOVERNMENT VS. MARKET* 100 (2018) (noting that according to the regulations, “local governments could pick some large and medium-sized SOEs to carry out experiments on changing the SOEs to shareholding companies,” and “[b]y the end of 1986, about 6,000 shareholding companies had been set up nationwide”).

<sup>59</sup> *Guanyu Jinyibu Tuidong Hengxiang Jingji Lianhe Ruogan Wenti De Guiding* (关于进一步推动横向经济联合若干问题的规定) [Provisions on Several Issues Concerning Further Promoting Horizontal Economic Integration] (promulgated by the State Council, Mar. 23, 1986, effective Mar. 23, 1986) 1987 LAW Y.B. CHINA 1, 267 (China), [http://www.pkulaw.cn/fulltext\\_form.aspx?Db=qikan&gid=1510038015](http://www.pkulaw.cn/fulltext_form.aspx?Db=qikan&gid=1510038015) [<https://perma.cc/5GPA-3WHX>].

<sup>60</sup> *Id.*

<sup>61</sup> See YONGJIN ZHANG, *CHINA’S EMERGING GLOBAL BUSINESSES* 139-40 (2003).

<sup>62</sup> *See id.*

<sup>63</sup> *See id.* at 140 (reporting that this bank’s establishment required State Council approval); Margot Schueller, *Financial system reform in China* in *THE INTERNATIONAL*

subsidiaries.<sup>64</sup> This marked the formation of Mainland China's first FCC, as CITIC Group controlled multiple types of financial companies, as well as large subsidiaries operating across a range of non-financial sectors.<sup>65</sup>

This structure exemplified the 1986 Provisions, as did the State Council's 1987 decision to allow a non-financial conglomerate to establish a "finance company of an enterprise group."<sup>66</sup> By year-end, seven of such internal financial companies had been formed, each of which was funded by deposits from its own affiliates and conducted intra-group lending.<sup>67</sup> Around this time, several new joint-stock regional banks were also established,<sup>68</sup> some of which were controlled by entities conducting substantial levels of non-financial activities.<sup>69</sup> For example, China Merchants Bank, established in 1987, was wholly-owned by China Merchants Group – an SOE primarily involved in shipping.<sup>70</sup>

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HANDBOOK ON FINANCIAL REFORM 73, 76-77 (Maximilian J.B. Hall ed., 2003) (noting that this bank was established in 1987 and wholly-owned by CITIC).

<sup>64</sup> See QIN XIAO, *supra* note 53, at 104.

<sup>65</sup> See *id.* at 104-05; YOUNGJIN ZHANG, *supra* note 61, at 140.

<sup>66</sup> Guanyu Zujian He Fazhan Qiye Jituan De Jidian Yijian (关于组建和发展企业集团的几点意见) [Several Opinions on the Formation and Development of Enterprise Groups] (promulgated by State Econ. & Trade Comm'n & State Econ. Restructuring Comm'n, Dec. 16, 1987, effective Dec. 16, 1987), art. 16, [http://www.pkulaw.cn/fulltext\\_form.aspx?Db=chl&Gid=810e5e624a7f2348bdfb&keyword=关于组建和发展企业集团的几点意见&EncodingName=&Search\\_Mode=accurate&Search\\_IsTitle=0](http://www.pkulaw.cn/fulltext_form.aspx?Db=chl&Gid=810e5e624a7f2348bdfb&keyword=关于组建和发展企业集团的几点意见&EncodingName=&Search_Mode=accurate&Search_IsTitle=0) [https://perma.cc/KR7P-ETK4].

<sup>67</sup> See NICHOLAS R. LARDY, CHINA'S UNFINISHED ECONOMIC REVOLUTION 74-75 (1998).

<sup>68</sup> See *id.* at 69-70 (listing eight regional banks established during the late 1980s, including Guangdong Development Bank, Shenzhen Development Bank, Merchants Bank, and Shanghai Pudong Development Bank); Chunhang Liu, *Reform and Opening Up of the Banking Industry in THIRTY YEARS OF CHINA'S REFORM* 254, 255 (Wang Mengkui ed., 2012) (explaining that Shenzhen Development Bank, Merchants Bank, and Shanghai Pudong Development Bank, and three other banks "set up with ownership by shareholders" were established in the late 1980s). Some regional banks were able to establish significant presences outside their home locality. See LARDY, *supra*, at 67.

<sup>69</sup> See CHIU & LEWIS, *supra* note 31, at 192 (explaining that many of the regional banks formed in the late 1980s were owned by "state-affiliated agencies or large enterprises, local government bodies or private companies").

<sup>70</sup> *History, CHINA MERCHANTS GROUP*, <http://www.cmhk.com/en/ac/history/history/index.shtml> [https://perma.cc/YE94-YB5U].

In the late 1980s, the State Council allowed new insurance companies to emerge to compete with PICC.<sup>71</sup> One was a Shenzhen-based joint-stock regional insurer called Ping An Insurance Company, established by a consortium that included China Merchants Group.<sup>72</sup> Around the same time, China Merchants Group also gained control of a Hong Kong insurance company.<sup>73</sup> Thus China Merchants Group, having expanded into banking and insurance, became the PRC's second SFCC. Later, in the 2000s, Ping An Insurance Company transformed into a privately-controlled corporate group called Ping An Insurance (Group) Company of China, Ltd. ("Ping An Group") and became one of the PRC's largest PFCCs, controlling a range of financial and non-financial businesses.<sup>74</sup>

*c. The 1990s: Economic Shifts, Legal Changes, and an Embrace of the "Socialist Market Economy" Set the Stage for Rapid 2000s FCC Formation*

By 1990, about half of the PRC's industrial output was still attributable to SOEs.<sup>75</sup> Throughout the subsequent decade, a number of legal changes, market structure shifts, and SOE reforms were initiated in response to both the PRC's early 1990s embrace of a "socialist market economy" and spats of market turmoil.

<sup>71</sup> See Qixiang Sun, Lingyan Suo & Wei Zheng, *China's Insurance Industry: Developments and Prospects in HANDBOOK OF INTERNATIONAL INSURANCE: BETWEEN LOCAL DYNAMICS AND LOCAL CONTINGENCIES* 597, 601-02 (J. David Cummins & Bertrand Venard eds., 2007) (observing that the State Council's 1985 *Interim Regulations on the Administration of Insurance Enterprises* enabled the establishment of new insurance companies).

<sup>72</sup> *Ping An Insurance Becomes Goldman Sachs' First Principal Investment in China*, GOLDMAN SACHS, <https://www.goldmansachs.com/our-firm/history/moments/1994-ping-an.html> [https://perma.cc/W9F4-THU6].

<sup>73</sup> See Changyuan Lin, *Financial Conglomerates in China* 16-17 (Ctr. for Int'l L. Stud., Working Paper No. 2003020011, Oct. 14, 2003), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=446840](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=446840) [https://perma.cc/3ULN-HNH6].

<sup>74</sup> See *History*, PING AN, <https://www.pingan.cn/en/about/history.shtml> [https://perma.cc/E8VX-3KZB]; see also *infra* note 169 and accompanying text (examining when Ping An Group gained control of substantial non-financial businesses).

<sup>75</sup> See NICHOLAS R. LARDY, *MARKETS OVER MAO: THE RISE OF PRIVATE BUSINESS IN CHINA* 75 (2014), [https://piie.com/publications/chapters\\_preview/6932/03iie6932.pdf](https://piie.com/publications/chapters_preview/6932/03iie6932.pdf) [https://perma.cc/AQT3-54PA].

Although only one lasting FCC emerged in the 1990s, the legal and policy groundwork necessary for FCC growth throughout the 2000s was set during this time, and many financial companies later acquired by FCCs were established.

*i. Securities Markets Expand and New Banks Form, while the "Socialist Market Economy" Spurs the Company Law and Private Sector Growth*

In order to legitimize flourishing informal securities markets, two national stock markets—the Shanghai and Shenzhen stock exchanges—were formed in 1990.<sup>76</sup> By 1992, the number of participating brokerage firms doubled to over eighty.<sup>77</sup> During this time, the State Council also approved the formation of the PRC's first futures exchange, spurring the formation of many futures companies and numerous regional derivatives exchanges.<sup>78</sup> Several securities and futures companies that emerged during the late 1980s and early 1990s would later be controlled by FCCs.<sup>79</sup>

As securities markets grew and joint-stock companies proliferated, national-level policymakers, including General Secretary Jiang Zemin and PBOC Governor Zhu Rongji, endorsed the establishment of a "socialist market economy."<sup>80</sup> This economic

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<sup>76</sup> See Damian Tobin & Ulrich Volz, *The Development and Transformation of the Financial System in the People's Republic of China* 16 (ADB Institute, Working Paper No. 825, Mar. 2018), <https://www.adb.org/sites/default/files/publication/411136/adbi-wp825.pdf> [https://perma.cc/C92M-8LU5].

<sup>77</sup> See CARL E. WALTER & FRASER J.T. HOWIE, *PRIVATIZING CHINA: THE STOCK MARKETS AND THEIR ROLE IN CORPORATE REFORM* 155 (2003).

<sup>78</sup> See Donald Lien & Bo Yang, *Futures Markets in the People's Republic of China: Development and Prospective*, 11 AM. J. CHINESE STUD. 25, 29-30 (2004).

<sup>79</sup> For example, China Merchant Securities Co. Ltd., controlled by China Merchants Group, was established in 1991. *Company Profile*, CMS, <http://www.newone.com.cn/ws/html?arg=en/AboutUs&>; see also *infra* notes 86-88 and accompanying text.

<sup>80</sup> See KJELD ERIK BRØDSGAARD & KOEN RUTTEN, *FROM ACCELERATED ACCUMULATION TO SOCIALIST MARKET ECONOMY IN CHINA* 101-02 (2017) (citing Zhonggong Zhongyang Guanyu Jianli Shehui Zhuyi Shichang Jingji Tizhi Ruogan Wenti De Jueding (中共中央关于建立社会主义市场经济体制若干问题的决定) [Central Committee of the Communist Party of China, Decision on Certain Issues concerning the Establishment of the Socialist Market Economy] (Promulgated by Cent. Comm. of the Communist Party of China, Nov. 14, 1993, effective Nov. 14, 1993) [hereinafter 1993 Socialist Market Economy Decision],

model was incorporated into the PRC's constitution in 1993 by the National People's Congress ("NPC"),<sup>81</sup> and its key feature was the "modern enterprise" (essentially, corporations) system, which enabled the conversion of large SOEs into profit-maximizing joint-stock companies with equity ownership rights allotted to both state and non-state entities.<sup>82</sup> The embrace of a "socialist market economy" also enabled private firms to play a larger role in the economy, and opened the door to SOE privatization.<sup>83</sup>

Against this backdrop, in 1992, the PBOC approved the establishment of two new national commercial banks wholly owned by SOEs, and then, in 1995, enabled the conversion of these banks into joint-stock institutions, bringing the total number of national, non-SOB commercial banks to four.<sup>84</sup> One of these new banks, Huaxia Bank, was initially owned by a state-owned steel

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[http://pkulaw.cn/fulltext\\_form.aspx?Db=chl&Gid=4cbd93d7254ee66fbdfb&keyword=中共中央关于建立社会主义市场经济体制若干&EncodingName=&Search\\_Mode=accurate&Search\\_IsTitle=0](http://pkulaw.cn/fulltext_form.aspx?Db=chl&Gid=4cbd93d7254ee66fbdfb&keyword=中共中央关于建立社会主义市场经济体制若干&EncodingName=&Search_Mode=accurate&Search_IsTitle=0)  
[<https://perma.cc/GY6D-5FAV>].

<sup>81</sup> The NPC is a nearly 3,000-member legislative body that usually meets for about ten days each year. For more information on the NPC, see SUSAN V. LAWRENCE & MICHAEL F. MARTIN, CONG. RSCH. SERV., R41007, UNDERSTANDING CHINA'S POLITICAL SYSTEM 31 (2013), <https://fas.org/sgp/crs/row/R41007.pdf> [<https://perma.cc/P7BH-QFDE>]. As legal scholars note, as was the case with this PRC Constitution amendment, the NPC translates the policy preferences of senior officials into "state will" "through legal procedure." See Jianfu Chen, *The Transformation of Chinese Law – From Formal to Substantial*, 37 HONG KONG L.J. 689, 721 n.173 (citing Liu Zheng (刘政), *Wei Jianshe You Zhongguo Tese de Shehuizhuyi Tigong Geng Youli de Xianfa Baozhang* (为建设有中国特色的社会主义提供更有力的宪法保障) [*Further Constitutional Protection for the Construction of Socialism with Chinese Characteristics*], 2 ZHONGGUO FAXUE (中国法学) [LEGAL SCI. IN CHINA] 5, 6 (1993)). This Constitutional change was adopted during the First Session of the Eighth NPC. See *id.*

<sup>82</sup> See BRØDSGAARD & RUTTEN, *supra* note 80, at 102 (citing 1993 Socialist Market Economy Decision, *supra* note 80); see also Wu Jinglian, Ma Guochuan, Xiaofeng Hua & Nancy Hearst, *The Failure of State-Owned Enterprise Reforms Under Market Socialism, in WHITHER CHINA? RESTARTING THE REFORM AGENDA* 71 (Wu Jinglian & Ma Guochuan eds., 2016) (observing that "institutional innovations in the large SOEs" taken in accordance with the 1993 *Socialist Market Economy Decision* were carried out "with a view to establishing a modern enterprise (that is, corporate) institution").

<sup>83</sup> See BRØDSGAARD & RUTTEN, *supra* note 80, at 103, 105-06; see also Jianfu Chen, *supra* note 81, at 721 (observing that the embrace of the "socialist market economy must first and foremost be seen as a license to practice capitalism in the economic sphere").

<sup>84</sup> See LARDY, *supra* note 67, at 66-69. Besides the large SOBs, CITIC's bank and the Bank of Communications were the PRC's first two national banks, established in 1986 and 1987, respectively. See *id.* at 64-66, 250 n.36.

conglomerate known as Shougang Group.<sup>85</sup> Another one, China Everbright Bank, was established by China Everbright Group<sup>86</sup>—an SOE that began as a TIC and operated technology, infrastructure, and construction businesses<sup>87</sup>—which would soon also gain control of a securities company,<sup>88</sup> marking the formation of the PRC's third SFCC. Problematic transactions between the two newly-established national banks and their intra-group affiliates soon led to government-ordered restructurings and Shougang Group's loss of a majority stake in Huaxia Bank,<sup>89</sup> a sign of troubles to come for FCCs.<sup>90</sup>

Most notably, the PRC's embrace of a "socialist market economy" led to the passage of the Company Law of the People's Republic of China at the end of 1993.<sup>91</sup> This law eased and formalized the process through which joint-stock companies could form<sup>92</sup>—a critical precondition to the growth in PFCCs that began roughly a decade later. The proliferation of joint-stock companies was further enabled by 1992 and 1993 State Council actions that established the State Council Securities Commission ("SCSC") and the China Securities Regulatory Commission ("CSRC"),<sup>93</sup> and also standardized accounting rules and the process for listing on the PRC's growing stock markets under a regulatory framework led by

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<sup>85</sup> See *id.* at 67-68. Shougang Group would later become an SFCC. See *infra* Appendix A (listing major FCCs as of 2017).

<sup>86</sup> See LARDY, *supra* note 67, at 67.

<sup>87</sup> See Changyuan Lin, *supra* note 73, at 14 (listing various business activities of China Everbright Group in 1994); WU XIAOQIU, CHINESE SECURITIES COMPANIES: AN ANALYSIS OF ECONOMIC GROWTH, FINANCIAL STRUCTURE TRANSFORMATION, AND FUTURE DEVELOPMENT 29 (2014) (noting that China Everbright Group first emerged as a TIC).

<sup>88</sup> See *id.*

<sup>89</sup> See LARDY, *supra* note 67, at 67-68; see also NEIL C. HUGHES, CHINA'S ECONOMIC CHALLENGE: SMASHING THE IRON RICE BOWL 48 (2015) (observing that China Everbright Group retained control of its newly-formed bank).

<sup>90</sup> By the late 2010s, several large FCCs were engaged in high levels of problematic intra-group transactions. See *supra* notes 12-15 and accompanying text.

<sup>91</sup> See BRØDSGAARD & RUTTEN, *supra* note 80, at 105-06 (citing Gongsì Fa (公司法) [Company Law] (promulgated by Standing Comm. Nat'l People's Cong., Dec. 1993; rev'd by Standing Comm. Nat'l People's Cong., Aug. 2004), [http://www.npc.gov.cn/wxzl/gongbao/2014-03/21/content\\_1867695.htm](http://www.npc.gov.cn/wxzl/gongbao/2014-03/21/content_1867695.htm) [<https://perma.cc/5ZY9-3DVJ>]).

<sup>92</sup> See Zhao Youg Qing, *The Company Law of China*, 6 IND. INT'L & COMP. L. REV. 461, 467 (1996) (citing Company Law, *supra* note 91, art. 8).

<sup>93</sup> See Tobin & Volz, *supra* note 76, at 4.

these newly-formed entities.<sup>94</sup> Although the CSRC's powers were initially quite limited in scope,<sup>95</sup> during the late 1990s, it gained a range of securities and futures markets regulatory authorities<sup>96</sup> and absorbed the SCSC.<sup>97</sup>

*ii. Further Banking System, Insurance Industry, and SOE Reforms Enable FCC Formation*

By the mid-1990s, banking assets were flooding into stocks, which in turn resulted in stock market bubbles, and bank lending volume was insufficient.<sup>98</sup> In response, the Law of the People's Republic of China on Commercial Banks ("Commercial Bank Law") was passed in 1995, which allowed for non-financial company control of banks – a critical precondition to future FCC growth – but required that: (1) loans to a single "borrower" not exceed ten percent of a bank's capital; (2) banks not invest in securities firms or TICs; (3) unsecured loans not be extended to a bank's "related persons"; (4) secured loans to "related persons" be extended at or above prevailing market rates; and (5) regulators first approve of any transaction that will result in a change of "shareholders" holding over ten percent (later lowered to five percent or more) of a bank's shares or capital.<sup>99</sup> In 1995, the NPC also passed the

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<sup>94</sup> See CHIU & LEWIS, *supra* note 31, at 194; Gupiao Faxing Yu Jiaoyi Guanli Zanzing Tiaoli (股票发行与交易管理暂行条例) [Interim Provisions on the Administration of the Issuing and Trading of Stocks] (promulgated by State Council, Apr. 22, 1993, effective Apr. 22, 1993) (China), <http://www.lawinfochina.com/Display.aspx?lib=law&ID=1334> [<https://perma.cc/Q7JR-P8QY>].

<sup>95</sup> See Tobin & Volz, *supra* note 76, at 18-19.

<sup>96</sup> See STEPHEN GREEN, CHINA'S STOCKMARKET: A GUIDE TO ITS PROGRESS, PLAYERS AND PROSPECTS 157-58 (2003) (explaining that in 1997, due to changes brought about by the National Financial Work Conference, "[securities market] regulatory powers were concentrated in the CSRC and local governments were sidelined," and that, by this time, "the PBOC . . . was forced to hand over its powers to the CSRC"); Lien & Bo Yang, *supra* note 78, at 30 (explaining that the CSRC gained oversight authority over the futures market in 1994).

<sup>97</sup> See Tobin & Volz, *supra* note 76, at 4.

<sup>98</sup> See Liping Xu & Yu Xin, *Thorny Roses: The Motivations and Economic Consequences of Holding Equity Stakes in Financial Institutions for China's Listed Nonfinancial Firms*, 10 CHINA J. ACCT. RES. 105, 109 (2017); HUGHES, *supra* note 89, at 48-49.

<sup>99</sup> Zhonghua Renmin Gongheguo Shangye Yinhang Fa (中华人民共和国商业银行法) [Law of the People's Republic of China on Commercial Banks]

Insurance Law of the People's Republic of China ("Insurance Law"), which allowed non-financial companies to control insurers, but included a requirement that regulators approve of any transactions resulting in changes to owners of ten percent or more (later lowered to five percent) of the shares of a joint-stock insurer.<sup>100</sup> Unlike the Commercial Bank Law, it did not address related party transactions.<sup>101</sup>

This omission, as well as the Commercial Bank Law's narrow restrictions on intra-group dealings, meant that the laws did not significantly curb the ability of a non-financial conglomerate to engage in intra-group transactions conducted on preferential

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(promulgated by the Standing Comm. of the 8th Nat'l People's Congress, May 10, 1995, effective July 1, 1995), art. 15, 24, 40, 43, [http://www.law-lib.com/law/law\\_view.asp?id=260](http://www.law-lib.com/law/law_view.asp?id=260) [<https://perma.cc/58HV-F7WN>]. In December 2003, the Commercial Bank Law was amended, and regulatory authority over banks was transferred to the newly-formed China Banking Regulatory Commission ("CBRC"). See WEI WANG, CHINA'S BANKING LAW AND THE NATIONAL TREATMENT OF FOREIGN-FUNDED BANKS 140-41 (2013). As part of the December 2003 amendments, Article 24 was amended to require that transactions resulting in a change of shareholders holding five percent or more of a bank's shares or capital first be approved by regulators—the threshold was originally over ten percent. *Zhonghua Renmin Gongheguo Shangye Yinhang Fa* (中华人民共和国商业银行法) [Law of the People's Republic of China on Commercial Banks] (2003), art. 24, [http://www.npc.gov.cn/zgrdw/englishnpc/Law/2007-12/12/content\\_1383716.htm](http://www.npc.gov.cn/zgrdw/englishnpc/Law/2007-12/12/content_1383716.htm) [<https://perma.cc/A2GE-4AM9>]. Also, many references to the People's Bank of China in the Commercial Bank Law were changed to a "regulatory authority under the State Council." For example, contrast Article 15 of the 1995 Commercial Bank Law with that of the 2003 version. The CBRC, the "regulatory authority under the State Council" mentioned in the 2003 Commercial Bank Law, was established pursuant to the Law on Banking Regulation and Supervision, passed in 2003 by the NPC, which resulted in a 2003 State Council notice that established the CBRC. See *China Banking Regulatory Commission*, CHINA BANKING NEWS, <http://www.chinabankingnews.com/china-banking-regulatory-commission/> [<https://perma.cc/3HLV-GQPN>]; *Guowuyuan Guanyu Jigou Shezhi de Tongzhi* (国务院关于机构设置的通知) [Notice of the State Council on the Setup of Institutions], GUOWUYUAN (国务院) STATE COUNCIL (Mar. 21, 2003), [http://www.gov.cn/gongbao/content/2003/content\\_62041.htm](http://www.gov.cn/gongbao/content/2003/content_62041.htm) [<https://perma.cc/9L5F-XTCT>].

<sup>100</sup> *Zhonghua Renmin Gongheguo Baoxian Fa* (中华人民共和国保险法) [Insurance Law of the People's Republic of China] (promulgated by the Standing Comm. of the 8th Nat'l People's Congress, June 30, 1995, effective Oct. 1, 1995), art. 91, [http://www.npc.gov.cn/wxzl/wxzl/2000-12/05/content\\_4644.htm](http://www.npc.gov.cn/wxzl/wxzl/2000-12/05/content_4644.htm) [<https://perma.cc/86FA-5G9S>]. The threshold was lowered to five percent in 2009. See LOVELLS, AMENDMENTS TO THE PEOPLE'S REPUBLIC OF CHINA INSURANCE LAW: TIME FOR A COMPLETE OVERHAUL OR SIMPLY A CONSOLIDATION? § 7.2 (2009), [https://www.hoganlovells.com/~media/hogan-lovells/pdf/publication/amendmentstotheprcinsurance-law\\_pdf](https://www.hoganlovells.com/~media/hogan-lovells/pdf/publication/amendmentstotheprcinsurance-law_pdf) [<https://perma.cc/UV98-WQ8T>].

<sup>101</sup> See LOVELLS, *supra* note 100, § 7.1 (explaining that the Insurance Law did not substantially address related party transactions until 2009).

terms<sup>102</sup> – in other words, a mixed conglomerate could support intra-group growth via transactions with a financial firm affiliate priced below prevailing market-wide risk-based prices.<sup>103</sup> FCCs would later take advantage of these weak regulatory guardrails to engage in high levels of these transactions.<sup>104</sup> FCCs would also grow by taking advantage of the absence of a clear definition of “shareholder,”<sup>105</sup> and due to the fact that the Commercial Bank Law allowed for certain changes of actual control over a bank to take place without regulatory approval.<sup>106</sup> Moreover, while the Insurance Law generally prohibited insurance companies from controlling non-insurance businesses, exceptions to that rule were soon granted – Ping An Insurance Company established a securities company in 1995 and acquired a TIC in 1996.<sup>107</sup>

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<sup>102</sup> See Kuan-Chun Chang, *The Supervision of Financial Conglomerates In China In The Post WTO Era – The Challenges Of Risk Concentration And Risk Contagion*, 11 U. MIAMI INT’L & COMP. L. REV. 1, 30 (2003) (explaining that the Commercial Bank Law and other rules “fail[ed] to provide a concrete firewall between banks and their affiliates” and did not regulate several “types of transactions between affiliates that can adversely affect the condition of banks”); see also Zhonghua Renmin Gongheguo Shangye Yinhang Fa (中华人民共和国商业银行法) [Law of the People’s Republic of China on Commercial Banks] (promulgated by the Standing Comm. of the 8th Nat’l People’s Congress, May 10, 1995, effective July 1, 1995), art. 40, [http://www.law-lib.com/law/law\\_view.asp?id=260](http://www.law-lib.com/law/law_view.asp?id=260) [<https://perma.cc/58HV-F7WN>] (providing a relatively narrow definition of “related persons”).

<sup>103</sup> Financial markets regulators associate high levels of these types of transactions within a mixed conglomerate with an increased risk that the conglomerate will lack sufficient financial resources vulnerable to withstand macroeconomic or idiosyncratic shocks. TRIPARTITE GRP. BANK, *supra* note 3, at 20-23 (explaining the risks of high intra-group exposures within a financial conglomerate); *id.* at 36-37 (explaining why intra-group exposures are particularly risky for mixed conglomerates); see also *infra* note 252 and accompanying text.

<sup>104</sup> For example, Tomorrow Group’s Baoshang Bank engaged in high levels of intra-group transactions. See *supra* note 15 and accompanying text.

<sup>105</sup> Haier Group, for example, gained control of a bank through separate investments made by five of its affiliates. See *infra* notes 133-135 and accompanying text.

<sup>106</sup> See IMF, *People’s Republic of China: Detailed Assessment Report: Basel Core Principles for Effective Banking Supervision*, Country Report No. 12/78, at 40 (Apr. 2012), <https://www.imf.org/external/pubs/ft/scr/2012/cr1278.pdf> [<https://perma.cc/T9KQ-H2BT>].

<sup>107</sup> See Sun, Suo & Zheng, *supra* note 71, at 605 (explaining that China Ping An Insurance (Group) Company Ltd.’s expansions into non-financial business lines exemplified one of several exceptions made to the newly-passed Insurance Law); *History*, *supra* note 74.

Despite regulatory shifts, new bank formation still required PBOC approval,<sup>108</sup> and few new joint-stock banks were established in the five years after the Commercial Bank Law's passage.<sup>109</sup> Indeed, the four large SOBs still accounted for roughly eighty-five percent of banking assets in 1995.<sup>110</sup> Yet by 1996, the PRC had entered a banking crisis, and twenty-four percent of SOB lending volume was non-performing (meaning that loans were "overdue, idle, or simply bad").<sup>111</sup> The next year, PRC stock markets crashed,<sup>112</sup> and the non-performing loan rate across its financial sector rose to over twenty-eight percent.<sup>113</sup> During the late 1990s, many TICs failed, including one of the PRC's largest,<sup>114</sup> prompting policymakers to suspend the operations of almost all TICs and require that remaining TICs reapply for licenses.<sup>115</sup> Four state-owned asset management companies that acquired SOB non-performing loans were also established.<sup>116</sup> Although these entities

<sup>108</sup> Zhonghua Renmin Gongheguo Shangye Yinhang Fa (中华人民共和国商业银行法) [Law of the People's Republic of China on Commercial Banks] (promulgated by the Standing Comm. of the 8th Nat'l People's Congress, May 10, 1995, effective July 1, 1995), art. 11, [http://www.law-lib.com/law/law\\_view.asp?id=260](http://www.law-lib.com/law/law_view.asp?id=260) [<https://perma.cc/58HV-F7WN>].

<sup>109</sup> See HUGHES, *supra* note 89, at 58-59 (reporting that "[a]t the end of 1999, there were just eleven shareholder banks").

<sup>110</sup> See LARDY, *supra* note 67, at 224.

<sup>111</sup> See Chunhang Liu, *supra* note 68, at 257 (reporting the nonperforming loan ratio by using "the Chinese standard for classifying bad loans").

<sup>112</sup> See WALTER & HOWIE, *supra* note 77, at xxvi.

<sup>113</sup> See Chunhang Liu, *supra* note 68, at 257.

<sup>114</sup> See COLLIER, *supra* note 54, at 77-78.

<sup>115</sup> See JIANBO LOU, AN OVERVIEW OF PRC TRUST LAW AND TRUST BUSINESS 2, [http://shintakuhogakkai.jp/activity/pdf/vol40\\_China2.pdf](http://shintakuhogakkai.jp/activity/pdf/vol40_China2.pdf) [<https://perma.cc/3VG8-AEDC>] (observing that TIC operations were suspended in by 2000); Touzi Guanchazhe (投资观察者) [Investment Observer], *Zhongguo Xintuoshi Shang Liuci Zhengdun Dashiji* (中国信托史上六次整顿大事记) [Six Major Events in the History of China Trust], SOHU (搜狐) [SOHU] (May 16, 2016), [https://m.sohu.com/a/75610386\\_372392/](https://m.sohu.com/a/75610386_372392/) [<https://perma.cc/NZD3-M5XF>] (reporting that by 2001 only sixty TICs were authorized to operate in the PRC due to the 1999-2000 restructuring of the industry, which resulted in hundreds of TICs being closed). The 1999-2001 restructuring of the TIC industry resulted from policy initiatives decided upon at the 1997 National Financial Work Conference convened by senior national policymakers. See Dai Xianglong (戴相龙), *Daixianglong Huiyi 1993 Nian Dao 2000 Nian Jinrong Zhixu Banian Dazhengdun* (戴相龙回忆 1993 年到 2000 年金融秩序八年大整顿) [Dai Xianglong Recalls the Eight-Year Overhaul of the Financial Order from 1993 to 2000], JINRONGJIE (金融界) [JR.COM] (July 17, 2018), <http://bank.jrj.com.cn/2018/07/17112124824468.shtml> [<https://perma.cc/7U9W-RF89>].

<sup>116</sup> See Delin Zhang, *Reform and Development of State-Owned Enterprises, in THIRTY YEARS OF CHINA'S REFORM* 217, 225-26 (Wang Mengkui ed., 2012).

would later transform into FCC-like entities,<sup>117</sup> no new major FCCs besides China Everbright Group formed in the 1990s. Yet two significant late 1990s crisis responses set the stage for FCC growth during the 2000s.

First, in the midst of financial markets turmoil, a new type of joint-stock commercial bank was created through the consolidation of UCCs.<sup>118</sup> These depository institutions had proliferated throughout the 1980s, and accounted for five times as much private lending volume as the SOBs in 1996,<sup>119</sup> even though UCCs' financial assets equaled just four percent of the SOBs'.<sup>120</sup> Yet by 1999, UCCs' balance sheets were seriously distressed—with a non-performing loan ratio of thirty-seven percent.<sup>121</sup> In response, 2,300 of these institutions were soon consolidated into over ninety “city commercial banks”<sup>122</sup>—joint-stock commercial banks primarily owned by urban non-financial company, individual, and local government shareholders.<sup>123</sup> Some of these banks would be acquired by PFCCs in the 2000s.<sup>124</sup>

The second, late 1990s policy driver of 2000s FCC growth was the SOE reform strategy of “grasp the large and let go of the small” (“抓大放小,” or *zhuadafangxiao* in Chinese), first endorsed by national policymakers in 1995.<sup>125</sup> At the time, forty percent of SOEs

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<sup>117</sup> See PEOPLE'S BANK OF CHINA, *supra* note 5, at 63 (observing that these asset management vehicles maintain investments in both non-financial and financial entities).

<sup>118</sup> See LARDY, *supra* note 67, at 72.

<sup>119</sup> See *id.* at 71-72.

<sup>120</sup> See *id.* at 224 (reporting that the 1995 total assets of UCCs totaled 303 billion yuan, while the total assets of the four major SOBs totaled 8.056 trillion yuan).

<sup>121</sup> See Chunhang Liu, *supra* note 68, at 259.

<sup>122</sup> See HUGHES, *supra* note 89, at 59.

<sup>123</sup> See LARDY, *supra* note 67, at 72.

<sup>124</sup> See *infra* notes 131-137, 154 and accompanying text.

<sup>125</sup> ZHONGGONG ZHONGYANG (中共中央) [CENT. COMM. OF THE COMMUNIST PARTY OF CHINA], ZHONGGONG ZHONGYANG GUANYU ZHIDING GUOMIN JINGJI HE SHEHUI FAZHAN “JIUWU” JIHUA HE 2020 NIAN YUANJING MUBIAO DE JIANYI (中共中央关于制定国民经济和社会发展“九五”计划和 2010 年远景目标的建议) [PROPOSAL OF THE CENTRAL COMMITTEE OF THE COMMUNIST PARTY OF CHINA ON FORMULATING THE NINTH FIVE-YEAR PLAN FOR NATIONAL ECONOMIC AND SOCIAL DEVELOPMENT AND THE VISION OF 2010] 20 (Sep. 28, 1995), <https://www.ndrc.gov.cn/fggz/fzzlgh/gjzgh/200709/P020191029595683696918.pdf> [<https://perma.cc/AB3M-ZV48>]. As Chiu and Lewis explain, this policy was “officially implemented after its confirmation at the Fifteenth Party Congress in October 1997 and the Ninth National People’s Party Congress in March 1998.” CHIU & LEWIS, *supra* note 31, at 66-67.

were losing money,<sup>126</sup> and many had more debts than assets.<sup>127</sup> Within five years, over 10,000 small and medium SOEs were converted into privately-controlled joint-stock companies largely owned by management.<sup>128</sup> Concurrently, about 1,000 large SOEs were restructured, primarily through the consolidation of SOEs into bigger, joint-stock SOEs.<sup>129</sup> Central state organs encouraged many of these large SOEs to form expansive, multi-sector corporate groups, the growth of which was supported by preferential credit and equity market access policies.<sup>130</sup>

*d. The 2000s: Most FCCs are Born*

By 2000, the economic, policy, and legal conditions necessary for the growth of FCCs had been established: struggling city commercial banks sought capital injections, large SOEs were expanding across sectors in the spirit of *zhuadafangxiao* and the 1986 Provisions, and legal changes stemming from the “socialist market economy” were driving the growth of equity markets, joint-stock companies, and demand for insurance by businesses and individuals. These and other early 2000s developments—including policymakers’ commitment to sector-based regulation, the growth of e-commerce, policy changes that attracted more private capital into the financial system, and a resurgence of TICs—enabled many more large FCCs to emerge.

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<sup>126</sup> See UNDERSTANDING AND INTERPRETING CHINESE ECONOMIC REFORM, *supra* note 23, at 157.

<sup>127</sup> See Zhang, *supra* note 116, at 225.

<sup>128</sup> See CHIU & LEWIS, *supra* note 31, at 68-69.

<sup>129</sup> See *id.* at 66-67. In response to high losses at SOEs, in 1998 Premier Zhu Rongji announced that the government would work to turn large and medium-sized SOEs into profit-making entities within three years. See CHIU & LEWIS, *supra* note 31, at 74; Zhang, *supra* note 116, at 225-26. Yet from 2001 to 2005, the PRC’s SOEs as a whole experienced losses each year. See Xin Li & Kjeld Erik Brødsgaard, *SOE Reform in China: Past, Present and Future*, 31 COPENHAGEN J. ASIAN STUD. 54, 60 (2013).

<sup>130</sup> See CHIU & LEWIS, *supra* note 31, at 67.

i. *PFCCs Form and SFCCs Grow as Insurance and Securities Markets Restructure, and TICs are Revived*

As the 2000s began, newly-formed city commercial banks needed capital.<sup>131</sup> In the early 2000s, Haier Group, a fast-growing appliance manufacturing conglomerate,<sup>132</sup> gained control of the Bank of Qingdao,<sup>133</sup> which had been established through the consolidation of twenty-one UCCs in 1996.<sup>134</sup> It did so through five subsidiaries, each of which acquired ten percent stakes,<sup>135</sup> illustrating the weakness of Commercial Bank Law restrictions on ownership concentration and complexity. By 2001, the private industrial and technology conglomerate Tomorrow Group, which emerged thanks to securities market and SOE reforms of the 1980s and early 1990s,<sup>136</sup> gained control of Baoshang Bank and Tai'an Bank, also taking advantage of a wave of city commercial bank restructuring.<sup>137</sup>

To improve regulatory oversight over an increasingly complex banking system, the China Banking Regulatory Commission

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<sup>131</sup> See Chunhang Liu, *supra* note 68, at 259.

<sup>132</sup> See BILL FISCHER, UMBERTO LAGO & FANG LIU, *REINVENTING GIANTS: HOW CHINESE GLOBAL COMPETITOR HAIER HAS CHANGED THE WAY BIG COMPANIES TRANSFORM* 47 (2013).

<sup>133</sup> See JEANNIE JINSHENG YI & SHAWN XIAN YE, *THE HAIER WAY: THE MAKING OF A CHINESE BUSINESS LEADER AND A GLOBAL BRAND* 108 (2003). Pursuant to the PRC's Commercial Bank Law, the PBOC would have needed to approve this acquisition. See *supra* note 108 and accompanying text.

<sup>134</sup> See BANK OF QINGDAO CO., LTD., *GLOBAL OFFERING* 121 (2015), <https://www1.hkexnews.hk/listedco/listconews/sehk/2015/1120/ltn20151120019.pdf> [<https://perma.cc/2HWR-NF8Y>].

<sup>135</sup> See YI & YE, *supra* note 133, at 108.

<sup>136</sup> See Dan Wei (但伟), *Mingtianxi Wanzhuan Shangshi Gongsi* (明天系玩转上市公司) [*Tomorrow Group's Fun with Listed Companies*], SOHU (搜狐) [SOHU.COM] (Feb. 7, 2017), <http://roll.sohu.com/20130408/n371904827.shtml> [<https://perma.cc/U7RG-N5ZU>].

<sup>137</sup> See Su Longfei (苏龙飞), *Mingtianxi, Anbangxi, Haihangxi, Fuxingxi . . . Mingying Jinrong 28 Jutou Mingdan Ji Chigu Quan Jiemi* (明天系、安邦系、海航系、复星系 . . . 民营金融 28 巨头名单及持股图全揭秘) [*Tomorrow, Anbang, HNA, Fosun . . . The List of 28 Private Financial Giants and Their Shareholding Charts Will Be All Revealed*], XINCAIFU (新财富) [NEW FORTUNE] (Jul. 9, 2019) [hereinafter *New Fortune FCC history*], [https://mp.weixin.qq.com/s?\\_\\_biz=MjM5MTA5MjE3Nw==&mid=2651726309&idx=1&sn=84e93cc7ea2fdeceaa27924c4b5b85a5&chksm=bd405d5b8a37d44d7888233aeb035e167fd0ecb9b9c719df56307acd656686ba7e72b83e5817](https://mp.weixin.qq.com/s?__biz=MjM5MTA5MjE3Nw==&mid=2651726309&idx=1&sn=84e93cc7ea2fdeceaa27924c4b5b85a5&chksm=bd405d5b8a37d44d7888233aeb035e167fd0ecb9b9c719df56307acd656686ba7e72b83e5817) [<https://perma.cc/G7V5-ZHUX>].

("CBRC") was established in 2003.<sup>138</sup> It soon implemented new restrictions on intra-group transactions that expanded the definition of "related party" relative to the Commercial Bank Law, but capped these transactions at a high level and still relied upon unclear terminology, thereby impeding effectiveness and enabling further FCC growth.<sup>139</sup> Also, as a reaction to the growing number of non-financial corporate groups that controlled numerous financial companies, the China Insurance Regulatory Commission ("CIRC"),<sup>140</sup> CBRC, and CSRC issued guidelines in 2004 endorsing

<sup>138</sup> The CBRC was established pursuant to NPC-approved State Council actions in 2003. See *China Banking Regulatory Commission*, *supra* note 99. Its establishment was authorized by Article 9 of the Insurance Law. See *Zhonghua Renmin Gongheguo Baoxian Fa* (中华人民共和国保险法) [Insurance Law of the People's Republic of China] (promulgated by the Standing Comm. of the 8th Nat'l People's Congress, June 30, 1995, effective Oct. 1, 1995), art. 9, [http://www.npc.gov.cn/wxzl/wxzl/2000-12/05/content\\_4644.htm](http://www.npc.gov.cn/wxzl/wxzl/2000-12/05/content_4644.htm) [<https://perma.cc/86FA-5G9S>].

<sup>139</sup> A 2004 CBRC rule required that credit extended by a bank to "related parties" not exceed fifty percent of net capital. *Shangye Yinhang Yu Neiburen He Gudong Guanlian Jiaoyi Guanli Banfa* (商业银行与内部人和股东关联交易管理办法) [*The Administrative Measures for the Connected Transactions between the Commercial Banks and their Insiders or Shareholders*] (promulgated by China Banking Regul. Comm'n, Apr. 2, 2004, effective May 1, 2004) art. 32, <http://www.lawinfochina.com/display.aspx?lib=law&id=3500&CGid=> [<https://perma.cc/QZQ5-7K7U>]. It also expanded the Commercial Bank Law's definition of "related party" to include legal persons under direct or indirect "control" by the same organization controlling a bank. Compare *id.*, art. 6-8 with *Zhonghua Renmin Gongheguo Shangye Yinhang Fa* (中华人民共和国商业银行法) [Law of the People's Republic of China on Commercial Banks] (2003), art. 40, [http://www.law-lib.com/law/law\\_view.asp?id=260](http://www.law-lib.com/law/law_view.asp?id=260) [<https://perma.cc/58HV-F7WN>]. See also Mary Ip, *Chinese Financial Markets: Regulators and Current Laws in CHINA'S CAPITAL MARKETS: CHALLENGES FROM WTO MEMBERSHIP* 297, 321 (Kam C. Chan et al. eds., 2007) (explaining that the CBRC's 2004 regulations "amplified the description of 'connected persons'"). Yet what constituted "control" remained ambiguous, enabling preferential "related party" transactions to continue. See IMF, *People's Republic of China: Financial System Stability Assessment*, Country Report No. 11/321, at 41 (Nov. 2011), <https://www.imf.org/external/pubs/ft/scr/2011/cr11321.pdf> [<https://perma.cc/JJ66-Q2CX>] (explaining that "no legal requirement [existed] to identify ultimately beneficial owners and clients of banks" and suggesting that "[r]ules for identifying related parties . . . need to be strengthened"). Moreover, a fifty percent threshold is relatively high, and therefore undermined the rule's effectiveness. See MARK A. DEWEAVER, ANIMAL SPIRITS WITH CHINESE CHARACTERISTICS: INVESTMENT BOOMS AND BUSTS IN THE WORLD'S EMERGING ECONOMIC GIANT 112 (2012).

<sup>140</sup> The CIRC was established in 1998 by the State Council. *Guowuyuan Guanyu Chengli Zhongguo Baoxian Jianshu Guanli Weyuanhui de Tongzhi* (国务院关于成立中国保险监督管理委员会的通知) [*Notice of the State Council on the Establishment of China Insurance Regulatory Commission*] (promulgated by State Council, Nov. 11, 2014,

increased cross-agency regulatory coordination, but reaffirming a commitment to sector-based regulation.<sup>141</sup> Although the State Council officially approved CITIC Group and China Everbright Group to be classified as financial holding companies in 2002,<sup>142</sup> no group-wide regulatory regimes were established,<sup>143</sup> enabling further FCC growth.

Against this regulatory backdrop and amidst securities market reforms, beginning in 2001, Tomorrow Group gained control of several securities companies,<sup>144</sup> becoming the PRC's first PFCC.<sup>145</sup> China Huaneng Group, a state-owned utility company, also emerged as a SFCC during this time after gaining control of a securities company and its fund management subsidiary,<sup>146</sup> one of

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effective Nov. 11, 1998), <https://law.lawtime.cn/d471199476293.html> [<https://perma.cc/839Z-7DDZ>].

<sup>141</sup> Zhongguo Yinhangye Jiandu Guanli Weiyuanhui, Zhongguo Zhengquan Jiandu Guanli Weiyuanhui, Zhongguo Baoxian Jiandu Guanli Weiyuanhui (中国银行业监督管理委员会、中国证券监督管理委员会、中国保险监督管理委员会) [China Banking Regul. Comm'n, China Sec. Regul. Comm'n & China Ins. Regul. Comm'n], *San Da Jinrong Jianguan Jigou Jinrong Jianguan Fengong Hezuo Beiwanglu* (三大金融监管机构金融监管分工合作备忘录) [*Memorandum of Cooperation on Financial Supervision of Three Major Financial Supervisory Agencies*] art. 8 (Jun. 2004), <http://business.sohu.com/2004/06/28/21/article220752183.shtml> [<https://perma.cc/VG7C-WZ5T>].

<sup>142</sup> See Jin Sheng, *China's Financial Holding Companies: Mixed Operation and Separate Supervision* 5 (Nat'l Univ. of Sing. Ctr. for Banking & Fin. L. Working Paper, Feb. 3, 2016), [https://law.nus.edu.sg/cbfl/wp-content/uploads/sites/5/2020/07/CBFL-WPS-1601-SJ02\\_SHENG-Jin.pdf](https://law.nus.edu.sg/cbfl/wp-content/uploads/sites/5/2020/07/CBFL-WPS-1601-SJ02_SHENG-Jin.pdf) [<https://perma.cc/6GGT-TEEH>].

<sup>143</sup> See Tang Shisheng (汤世生), *Taiwan Jinkong Moshi Dui Dalu Jinrong de Jiejian* (台湾金控模式对大陆金融的借鉴) [*Learning in Mainland Financial Markets from Taiwan Financial Holding Company Model*], ZHONGGUO FAZHAN GUANCHA (中国发展观察) CHINA DEV. WATCH 43 (2011), <https://doc.mbalib.com/view/9f9156ac61a0dbe2abf87dd94beef4b2.html> [<https://perma.cc/SW8Z-P42R>] (reporting that the PBOC proposed draft regulations for holding companies in 2000 and 2005, but ultimately abandoned those plans).

<sup>144</sup> See New Fortune FCC history, *supra* note 137.

<sup>145</sup> Ping An Group did not become a PFCC until after it gained control of numerous non-financial companies. See *infra* note 169 and accompanying text.

<sup>146</sup> See *Gongsi Jianjie* (公司简介) [*Company Introduction*], CHANGCHENG JIJIN, (长城基金) [GREAT WALL FUND] <http://www.ccfund.com.cn/main/zjcc/gsjj/index.shtml> [<https://perma.cc/N89R-M2NR>] (noting that Great Wall Securities, controlled by China Huaneng Group, was founded in 2001); ZHONGGUO CHANGCHENG ZHENGQUAN GUFEN YOUXIAN GONGSI, (中国长城证券股份有限公司) [CHINA GREAT WALL SECURITIES CO. LTD.], CHANGCHENG ZHENGQUAN GUFEN YOUXIAN GONGSI SHOU CI GONGKAI FAXING GUPIAO ZHAOGU SHUOMINGSHU (长城证券股份有限公司首

the first of such firms to emerge in the PRC.<sup>147</sup> Overall, the number of fund management companies grew to over fifty-eight by 2006.<sup>148</sup>

Also in the early 2000s, PBOC regulatory changes allowed TICs to reemerge as a powerful force in Chinese financial markets.<sup>149</sup> As a result, by 2004, TIC assets had rebounded to 278.4 billion yuan, and then reportedly rose to 1 trillion and 14 trillion yuan in 2007 and 2014, respectively.<sup>150</sup> In 2003, a TIC controlled by recently-restructured Ping An Group – which by then was the PRC's second-largest life insurer – received regulatory approval to acquire a regional bank.<sup>151</sup> China Resources – an SOE with business activities spanning construction, consumer products, energy, and healthcare that had grown under *zhuadafangxiao*<sup>152</sup> – also gained control of a TIC in 2006.<sup>153</sup> In 2009, it became one of Mainland China's largest SFCCs after regulators allowed it to assume an over seventy-five percent ownership stake in a struggling city commercial bank.<sup>154</sup>

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次公开发行股票招股说明书) [CHINA GREAT WALL SECURITIES CO. LTD. INITIAL PUBLIC OFFERING PROSPECTUS] 71-72 (2018), <http://www.cgws.com/cczq/tzzgx/xxpl/201905/P020190508581655383249.pdf> (reporting that by 2003, China Huaneng Group and its affiliates controlled over fifty percent of Great Wall Securities).

<sup>147</sup> The PRC's first fund management companies were established in 1998. See Franklin Allen, Jun "QJ" Qian, Meijun Qian & Mengxin Zhao, *A Review of China's Financial System and Initiatives for the Future*, in CHINA'S EMERGING FINANCIAL MARKETS: CHALLENGES AND OPPORTUNITIES 3, 48 (James R. Barth et al. eds., 2009).

<sup>148</sup> *Id.*

<sup>149</sup> See JIANBO LOU, *supra* note 115, at 13-14.

<sup>150</sup> *Id.* at 14.

<sup>151</sup> See *History*, *supra* note 74 (noting that in February 2003, Ping An Insurance Company was restructured into a holding company, Ping An Insurance (Group) Company of China, Ltd., that went public the following year); *Ping An Plans to Buy Fujian Bank*, CHINA DAILY (Nov. 26, 2003), [http://www.chinadaily.com.cn/en/doc/2003-11/26/content\\_284939.htm](http://www.chinadaily.com.cn/en/doc/2003-11/26/content_284939.htm) [<https://perma.cc/9NY7-CH86>] (reporting that in November 2003, Ping An Group, through its TIC subsidiary, gained control of Fujian Asian Bank in Fujian province).

<sup>152</sup> See *Company at a Glance*, CHINA RES., <http://en.crc.com.cn/whoware/companyataglance/> [<https://perma.cc/5HX5-CXLG>].

<sup>153</sup> See *Gongsi Jianjie* (公司简介), [Company Introduction], HUARUN XINTUO (华润信托) [CR TRUST], <https://www.crctrust.com/gsjj/index.html> [<https://perma.cc/A58V-85SA>].

<sup>154</sup> *Zhongguo Yinjianhui Guanyu Huarun Gufen Youxian Gongsi Rugu Zhuhai Shi Shangye Yinhang Gudong Zige de Pifu* (中国银监会关于华润股份有限公司入股珠海市商业银行股东资格的批复) [Reply of the China Banking Regulatory Commission on CR Trust's Qualifications to Become a Shareholder of Zhuhai Commercial Bank], ZHONGGUO YINJIANHUI (中国银监会) [CBRC] (Apr. 23, 2009),

Another driver of PFCC formation was insurance industry growth brought about in part by an increase in private risk-taking stemming from the PRC's embrace of a "socialist market economy."<sup>155</sup> Between 1999 and 2004, total Mainland China insurance industry assets grew from 260.4 billion to 1.112 trillion yuan, and by 2003, there were twenty-two domestic insurance companies, versus thirteen in 2000 and just four in 1991.<sup>156</sup> One new insurer was Anbang Property and Casualty Insurance Co., Ltd., which was founded in 2004 and later reorganized into a PFCC called Anbang Insurance Group Co., Ltd. ("Anbang Group").<sup>157</sup> Funde Sino Life Insurance Co., Ltd., also launched in the early 2000s,<sup>158</sup> would later become a subsidiary of the PFCC Funde Holding Group Co., Ltd. ("Funde Group"),<sup>159</sup> established in 2007.<sup>160</sup>

In 2006, the State Council's "Several Opinions on the Reform and Development of the Insurance Industry" accelerated insurance sector growth by supporting restructuring, acquisitions, and mergers within the industry.<sup>161</sup> Several insurers controlled by

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<http://www.cbirc.gov.cn/cn/view/pages/governmentDetail.html?docId=275791&itemId=867&generaltype=1> [<https://perma.cc/9RNH-BNEU>].

<sup>155</sup> The embrace of the "socialist market economy" in 1993 by national policymakers resulted in individuals and businesses increasingly assuming financial risks, thus fueling insurance demand. See Sun, Suo & Zheng, *supra* note 71, at 602-03.

<sup>156</sup> See *id.* at 603, 606.

<sup>157</sup> See *Anbang Insurance Group (China)*, PUB. OPS. INT'L, <https://www.publicopinions.net/index.php/directory/the-200-certified-winners-of-the-sustainable-development-award-2018-2019/1935-anbang-insurance-group-china.html> [<https://perma.cc/WG9Q-8HGG>] (noting that the CIRC granted approval for Anbang Property & Casualty Insurance Co., Ltd. to restructure as a holding group and that, in 2012, Anbang Insurance Group Co., Ltd. was founded); New Fortune FCC history, *supra* note 137 (providing a timeline of Anbang Group's financial company acquisitions and its expansion into non-financial business lines, particularly hotel management).

<sup>158</sup> See *Company Profile*, SINO LIFE INS. CO., <https://www.sino-life.com/ensinolife/> [<https://perma.cc/8DRC-9VCH>].

<sup>159</sup> See *infra* Appendix A.

<sup>160</sup> *Jituan Jianjie (集团简介)* [Group Introduction], FUDE KONGGU JITUAN (富德控股集团) [FUDE HOLDING GRP.], <http://www.fundegroup.com/web/introduction.aspx> [<https://perma.cc/PUW9-PYPJ>].

<sup>161</sup> New Fortune FCC history, *supra* note 137; Guowuyuan (国务院) [State Council], Guowuyuan Guanyu Baoxianye Gaige Fazhan de Ruogan Yijian (国务院关于保险业改革发展的若干意见) [Some Opinions of the State Council on the Reform and Development of the Insurance Industry] (Jun. 15, 2006), [http://www.gov.cn/zwggk/2006-06/26/content\\_320050.htm](http://www.gov.cn/zwggk/2006-06/26/content_320050.htm) [<https://perma.cc/D2T5-HZXN>].

Tomorrow Group were established shortly thereafter.<sup>162</sup> HNA Group—an airline company that had acquired SOE assets<sup>163</sup>—similarly established an insurance company joint venture,<sup>164</sup> becoming a PFCC.<sup>165</sup>

Also in 2006, the CIRC formally allowed insurance companies to invest in up to two banks.<sup>166</sup> Shortly thereafter, Ping An Group—still the PRC's second-largest life insurer<sup>167</sup>—gained control of two Mainland China banks.<sup>168</sup> By this time it had morphed into a PFCC that controlled a range of significant non-financial subsidiaries with business lines spanning e-commerce, hotel management, electronics manufacturing, and expressway maintenance.<sup>169</sup>

<sup>162</sup> See New Fortune FCC history, *supra* note 137.

<sup>163</sup> See David Barboza & Michael Forsythe, *Behind the Rise of China's HNA: The Chairman's Brother*, N.Y. TIMES (Mar. 27, 2018), <https://www.nytimes.com/2018/03/27/business/hna-group-deals-china.html> [<https://perma.cc/G4HU-BXXR>].

<sup>164</sup> See *Da Shiji* (大事记) [Major Events], DINGCHENG RENSHOU (鼎诚人寿) [DINGCHENG LIFE], <https://www.dingchenglife.com.cn/c/2019-09-23/485307.html> [<https://perma.cc/9L9F-F8W7>].

<sup>165</sup> HNA Group had already acquired a futures company in 2003. See *Haihang Jituan Caiwu Youxian Gongsì* (海航集团财务有限公司) [HNA Group Finance Co., Ltd.], QINGKE YANJIU (清科研究) [PEDATA.COM], [https://m.pedata.cn/ep/detail\\_254369410.html](https://m.pedata.cn/ep/detail_254369410.html) [<https://perma.cc/Y4ER-7H6E>].

<sup>166</sup> *Guanyu Baoxian Jigou Touzi Shangye Yinhang Guquan de Tongzhi* (关于保险机构投资商业银行股权的通知) [Notice on Insurance Institutions Investing in Equity of Commercial Banks] (Oct. 16, 2006), [http://www.gov.cn/jrzq/2006-10/16/content\\_414876.htm](http://www.gov.cn/jrzq/2006-10/16/content_414876.htm) [<https://perma.cc/625U-SWGT>].

<sup>167</sup> See PING AN INS. (GRP.) CO. OF CHINA, LTD., ANNUAL REPORT 2009, at 3 (2010), <https://www1.hkexnews.hk/listedco/listconews/sehk/2010/0427/ltn201004271085.pdf> [<https://perma.cc/XP9U-8U6D>].

<sup>168</sup> See *History*, *supra* note 74.

<sup>169</sup> Although Ping An Insurance Company of China gained control of financial companies throughout the 1990s, it did not become an FCC until after it both reorganized as Ping An Group and gained majority equity interests in several principal subsidiaries engaged in non-financial businesses across a number of sectors between 2007 and 2009. Compare PING AN INS. (GRP.) CO. OF CHINA, LTD., *supra* note 167, at 144-46 (listing various non-financial companies in which Ping An Group, by 2009, controlled over fifty percent of equity interest, including three manufacturers, a consulting company, two IT companies, and three hotel management businesses) with PING AN INS. (GRP.) CO. OF CHINA, LTD., ANNUAL REPORT 2007, at 121-23 (2008), <https://www1.hkexnews.hk/listedco/listconews/sehk/2008/0326/ltn20080326457.pdf> [<https://perma.cc/5W3K-AGM2>] (presenting a list of principal subsidiaries of Ping An Group as of December 2007, which only includes three non-financial companies—two property managers and one expressway management company—in which Ping An Group controlled over fifty percent of equity interest). In 2004, Ping An became a publicly listed company in which U.K. and U.S. banks held major

ii. Mainland China's First Internet PFCC Forms

As Mainland China's private sector grew, so did a new online retailer called Alibaba<sup>170</sup> which, in 2004, built out a payments processing system called Alipay that allowed it to facilitate online payments as the custodian of buyer and seller funds.<sup>171</sup> Alipay soon morphed into a mobile payments service with tens of millions of users, prompting the PBOC to create a new regulatory framework for these activities—Alipay received Mainland China's first Payments Business License in May 2011.<sup>172</sup> That same month, Tenpay Payment Technology Co., Ltd. ("Tenpay"), a company controlled by Tencent Holdings Ltd. ("Tencent"), an online gaming, music, and social network company, also received one of these licenses.<sup>173</sup> In 2013, Alipay and Alibaba's financial services

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stakes, but for which the largest shareholder was a Shenzhen municipal government investment vehicle. See Christine Chan, *HSBC to Strengthen Grip on Ping An*, S. CHINA MORNING POST (Jun. 8, 2004), <https://www.scmp.com/article/458658/hsbc-strengthen-grip-ping> [https://perma.cc/7UEQ-2G4K]; see also *History*, supra note 74. By 2020, Ping An Group's Healthcare and Technology unit operated China's largest online healthcare platform, known as Ping An Good Doctor. See Eric Ng, *Ping An Good Doctor, China's Largest Health Care Platform, Reports Jump in Users Amid Coronavirus, Smaller than Expected Annual Loss*, S. CHINA MORNING POST (Feb. 12, 2020), <https://www.scmp.com/business/article/3050074/ping-good-doctor-chinas-largest-health-care-platform-reports-jump-users> [https://perma.cc/8M2X-J26P].

<sup>170</sup> See DUNCAN CLARK, ALIBABA: THE HOUSE THAT JACK MA BUILT 131 (2016). Alibaba was incorporated in 1999, but before then it had already been conducting business for several years, and at the time of its incorporation had over 28,000 customers. *Id.* at 102.

<sup>171</sup> See Julia Wu, *A Brief History of Jack Ma's Ant Financial - the \$150B Unicorn*, HACKERNOON (Aug. 6, 2019), <https://hackernoon.com/the-story-of-ant-financial-4t2aq3zh8> [https://perma.cc/F3KG-2TJE].

<sup>172</sup> *Gongsi Licheng* (公司历程) [Our History and Timeline], MAYI JITUAN (蚂蚁集团) [ANT GRP.], <https://www.antfin.com/history.htm> [https://perma.cc/JZS6-33AG]. Notably, in 2011, Alipay was spun off into a company directly controlled by Alibaba's CEO. See Huang Yuntao & Kevin Soh, *Alipay Gets License to Set Up E-payment System*, REUTERS (Mar. 26, 2011), <https://www.reuters.com/article/us-alipay/alipay-gets-licence-to-set-up-e-payment-system-idUSTRE74P26120110526> [https://perma.cc/KJV2-KB8L].

<sup>173</sup> See *Guanyu Caifutong* (关于财付通) [About Tenpay], CAIFUTONG (财付通) TENPAY, <https://www.tenpay.com/v3/helpcenter/about/about.shtml> [https://perma.cc/9MGR-AJAX]. Tenpay Payment Technology Co., Ltd. (财付通支付科技有限公司) is also known as Tenpay, and it is reportedly over ninety-five percent owned by Tencent Computer (深圳市腾讯计算机系统有限公司 or 腾讯计算机 in Chinese). *Caifutong Zhifu Keji Youxian Gongsi* (财付通支付科技有限公司) [Tenpay], TIANYANCHA (天眼查) TIANYANCHA,

businesses – including a sizable non-bank consumer micro-lending service – were restructured into a new company soon rebranded as Ant Financial, which later expanded its non-bank credit product offerings.<sup>174</sup> Ant Financial remained seventy-five percent owned by Alibaba management and employees,<sup>175</sup> thus this Article treats Alibaba as effectively maintaining control of Ant Financial as Alipay's annual payments processing volume grew to over \$1 trillion USD in 2015.<sup>176</sup>

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<https://www.tianyancha.com/company/2313221010>. Since 2005, Tencent has controlled Tencent Computer through contractual agreements, even though it lacks direct equity ownership in the company. See TENCENT HOLDINGS LTD., 2005 ANNUAL REPORT 80, 83 (2006), <http://cdc-tencent-com-1258344706.image.myqcloud.com/storage/uploads/2019/11/09/d530cf0097fd788ce2ff5d0583e6dcb4.pdf> [<https://perma.cc/37ZG-2F46>]; TENCENT HOLDINGS LTD., *infra* note 181, at 261, 263.

<sup>174</sup> Ant Financial's formation process began in 2013, and by 2014, in addition to Alipay and investment platforms, Ant Financial also operated Ant Credit, a non-bank lending service. See Ant Fin. Servs. Grp., *Official Launch of Ant Financial Services Group Brings New Financial Ecosystem to China*, BUS. WIRE (Oct. 16, 2014), <https://www.businesswire.com/news/home/20141016005260/en/Official-Launch-of-Ant-Financial-Services-Group-Brings-New-Financial-Ecosystem-to-China> [<https://perma.cc/9CLX-7JJS>]. By Q1 2014, Ant Credit "had loaned RMB190 billion for more than 700,000 small and micro-businesses." IFC, *Ant Financial Services Group and Goldman Sachs 10,000 Women Launch First Internet-Based Gender-Finance Program in China to Boost Women Entrepreneurship*, INT'L FIN. CORP. (Jan. 27, 2015), <https://ifcext.ifc.org/IFCExt/pressroom/IFCPressRoom.nsf/0/5DFDA58BCBFE71B685257DDA00303B14?OpenDocument> [<https://perma.cc/G74W-Q3HH>]. By 2017, Ant Financial operated five non-bank consumer and business lending services. See CITIGROUP, *BANK OF THE FUTURE: THE ABCS OF DIGITAL DISRUPTION IN FINANCE* 39 (2018), <https://www.citibank.com/commercialbank/insights/assets/docs/2018/The-Bank-of-the-Future/2/> [<https://perma.cc/72EM-ZFG8>]. Additionally, by 2017, Ant Financial also controlled two Chongqing-based non-bank small consumer loan companies that in 2017 issued over 200 billion yuan in asset-backed securities. See Yan Qinbo (闫沁波), *Mayi Jinfu Jiang Zai Chongqing Sheli Xiaofei Jinrong Gongsi* (蚂蚁金服将在重庆设立消费金融公司) [*Ant Financial Sets Up a Consumer Finance Company in Chongqing*], 21 CAIJING (21 财经) [21 FINANCE] (Feb. 5, 2018), [http://epaper.21jingji.com/html/2018-02/06/content\\_80272.htm](http://epaper.21jingji.com/html/2018-02/06/content_80272.htm) [<https://perma.cc/2SBB-5SGD>]. For the purposes of this Article, all of the consumer and business small loan services provided by Ant Financial are treated as one financial company, while Ant Financial's two Chongqing-based small loan businesses are together treated as one financial company.

<sup>175</sup> See ANT FIN., ANT FINANCIAL (2016), <https://www.alibabagroup.com/en/ir/pdf/160614/12.pdf> [<https://perma.cc/NF4T-QXMH>].

<sup>176</sup> See ZENNON KAPRON & MICHELLE MEERTENS, *SOCIAL NETWORKS, E-COMMERCE PLATFORMS, AND THE GROWTH OF DIGITAL PAYMENT ECOSYSTEMS IN CHINA: WHAT IT MEANS FOR OTHER COUNTRIES* 7 (2017), [https://btca-prod-1.s3.amazonaws.com/documents/284/english\\_attachments/ChinaReportApril2017Highlights.pdf?1492606527](https://btca-prod-1.s3.amazonaws.com/documents/284/english_attachments/ChinaReportApril2017Highlights.pdf?1492606527) [<https://perma.cc/H2YH-C3P2>].

This milestone marked the emergence of Mainland China's first "internet PFCC" ("IFCC")—a subcategory of PFCC that distinctively: (1) operates a large retail payment system (\$1 trillion USD processed annually); and (2) earns much of its revenue from internet-related activities.<sup>177</sup> In 2015, Ant Financial also gained control of a fund management company that it had already partnered with to launch one of the world's largest money market mutual funds.<sup>178</sup> Unlike Ant Financial, Tencent operates a fund management platform but does not control a major retail-oriented fund management company,<sup>179</sup> although throughout the late 2010s both Tencent and Alibaba conducted very high levels of venture capital investing.<sup>180</sup> Tencent-controlled non-bank lender Tenpay Micro Loan launched in 2014, but Tencent did not become an IFCC until 2016 after it both gained control of a bank and its annual payments volume grew to over \$1 trillion USD.<sup>181</sup>

<sup>177</sup> As mentioned above, this Article treats \$1 trillion USD in annual payment processing volume as a threshold for determining whether the financial activities of an FCC are "significant." See *supra* note 5 and accompanying text.

<sup>178</sup> See EO INTELLIGENCE, DECIPHERING THE TRILLION-VALUED UNICORN - ANT FINANCIAL CASE STUDY 7-8 (2019), <https://img2.iyiou.com/ThinkTank/2019-06-21/Ant%20Financial%20Case%20Study.pdf> [<https://perma.cc/6VJ8-UZYG>] (reporting that in 2015, Ant Financial gained control of fifty-one percent of Tianhong Asset Management's total shares). Tianhong Asset Management launched the *Yu'e Bao* money market fund in 2013 via a partnership with Ant Financial. *Id.* at 6-7. By 2014, *Yu'e Bao* was the world's fourteenth largest money market mutual fund. See Gwynn Guilford, *China's \$122 Billion Boom in Shadow Banking is Happening on Phones*, QUARTZ (Feb. 10, 2014), <https://qz.com/175421/chinas-122-billion-boom-in-shadow-banking-is-happenin-g-on-phones/> [<https://perma.cc/A5AX-24DF>].

<sup>179</sup> Tencent's *Licaitong* is an online marketplace for financial products, through which Tencent enables customers to invest in funds established by fund management companies with which it partners, but does not control. See LEON QI, JOHN CHOI & LIZ ZENG, DAIWA CAP. MKTS., DEMYSTIFYING INTERNET FINANCE 11 (2014), [http://asiaresearch.daiwacm.com/eg/cgi-bin/files/China\\_Financials\\_and\\_Internet\\_sectors\\_140312.pdf](http://asiaresearch.daiwacm.com/eg/cgi-bin/files/China_Financials_and_Internet_sectors_140312.pdf) [<https://perma.cc/XB4R-ES7Q>].

<sup>180</sup> See Savannah Dowling, *Huge Rounds, Heated Competition: How Tencent & Alibaba Are Defining VC in China*, CRUNCHBASE NEWS (Jan. 21, 2018), <https://news.crunchbase.com/news/huge-rounds-heated-competition-tencent-alibaba-defining-vc-china/> [<https://perma.cc/9CQ6-DY8G>] (reporting that Tencent's and Alibaba's participation in venture capital funding rounds grew dramatically from 2013 to 2017, totaling over 200 and 100 investments, respectively).

<sup>181</sup> Tenpay Micro Loan (深圳市财付通网络金融小额贷款公司 or 财付通小贷 in Chinese), which was founded in 2013 and lends to small and medium enterprises, is ultimately controlled by Shenzhen Shiji Kaixuan Technology Co. Ltd. (深圳市世纪凯旋科技有限公司), a company that, through contractual agreements rather than

iii. 2010s Banking System Policy Decisions Enable Further PFCC Growth

A series of 2010s policy decisions enabled Tencent and other privately-owned conglomerates to expand into banking. First, in 2010, the State Council issued “Some Opinions on Encouraging and Guiding the Sound Development of Private Investment,” calling for more private capital in the financial services industry.<sup>182</sup> The PBOC also once again decided not to implement holding company regulations for FCCs, although in 2011 it again proposed introducing such regulations for some conglomerates.<sup>183</sup> Then in 2012, the CBRC issued “Suggestions on the Implementation of Encouraging and Guiding Private Capital to Invest in the Banking Sector,” which affirmed that “private enterprises may invest in

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equity ownership, is controlled by Tencent. See *Shenzhen Shiji Kaixuan Technology Co. Ltd.* (深圳市财付通网络金融小额贷款公司) [Tenpay Micro Loan], TIANYANCHA (天眼查) TIANYANCHA, <https://www.tianyancha.com/company/2325765626> (providing information on the nature of Tenpay Micro Loan’s business and the company’s origins, and reporting that the firm is over seventy percent owned by Shenzhen Shiji Kaixuan Technology Co. Ltd.); TENCENT HOLDINGS LTD., 2019 ANNUAL REPORT 261, 263 (2020), <https://cdc.tencent.com-1258344706.image.myqcloud.com/uploads/2020/04/02/ed18b0a8465d8bb733e338a1abe76b73.pdf> [<https://perma.cc/D2BF-U56L>] (reporting that while Tencent “does not have legal ownership in equity” of Shenzhen Shiji Kaixuan Technology Co. Ltd., “under certain contractual agreements . . . [Tencent] and its other legally owned subsidiaries control [Shenzhen Shiji Kaixuan Technology Co. Ltd.]”). Tencent gained control of a bank in 2014. See *infra* note 192 and accompanying text. The volume of Tencent’s WeChat Pay transactions first exceeded \$1 trillion USD in 2016. See KAPRON & MEERTENS, *supra* note 176, at 7. Tencent launched WeChat Pay in 2013 by integrating Tenpay into its WeChat platform, and WeChat Pay payments and transfers are routed through Tenpay. See *About Tenpay*, *supra* note 173.

<sup>182</sup> Guowuyuan (国务院) [State Council], *Guli He Yindao Minjian Touzi Jiankang Fazhan de Ruogan Yijian* (鼓励和引导民间投资健康发展的若干意见) [Some Opinions on Encouraging and Guiding the Sound Development of Private Investment], art. 18 (2010), [http://www.gov.cn/zw/gk/2010-05/13/content\\_1605218.htm](http://www.gov.cn/zw/gk/2010-05/13/content_1605218.htm) [<https://perma.cc/SX6T-BCU7>].

<sup>183</sup> See DELOITTE, JINRONG HUNYE JINGYING ZHENGSHI MAIRU XINPIANZHANG (金融混业经营正式迈入新篇章) [MIXED FINANCIAL COMPANIES HAVE OFFICIALLY ENTERED A NEW CHAPTER] 1-2 (2020), <https://www2.deloitte.com/content/dam/Deloitte/cn/Documents/financial-services/deloitte-cn-fsi-financial-holding-company-supervision-zh-200119.pdf> [<https://perma.cc/TC5B-RH3D>].

banking financial institutions through establishment, subscription for new stock, transfer of equity, and merger and restructuring.”<sup>184</sup>

Amidst these policy shifts, HNA Group gained a twenty percent stake in Yingkou Coastal Bank in 2010 with approval from the CBRC.<sup>185</sup> That year, the CBRC also published a notice allowing major shareholders to gain ownership interests exceeding twenty percent of shares in some at-risk rural and urban commercial banks, although it also generally restricted a single company from investing in more than two banks.<sup>186</sup> Yet at the same time, the CBRC accelerated efforts to merge troubled RCCs into joint-stock rural commercial banks<sup>187</sup> and thus, in the following years, Tomorrow Group expanded investments in two rural commercial banks, while Anbang Group acquired a thirty-five percent share of Chengdu Rural Commercial Bank.<sup>188</sup> Overall, between 2002 and 2013, private ownership of joint-stock banks increased from eleven to forty-five percent and private ownership of city commercial banks increased from nineteen to fifty-six percent.<sup>189</sup>

<sup>184</sup> *Guanyu Guli He Yindao Minjian Ziben Jinru Yinhangye de Shishi Yijian* (关于鼓励和引导民间资本进入银行业的实施意见) [Suggestions on the Implementation of Encouraging and Guiding Private Capital to Invest in the Banking Sector], CHINA BANKING REGUL. COMM’N (May 26, 2012), [http://www.cbrc.gov.cn/chinese/home/docDOC\\_ReadView/35AF2AE678A0439BA5E296C3137A5652.html](http://www.cbrc.gov.cn/chinese/home/docDOC_ReadView/35AF2AE678A0439BA5E296C3137A5652.html) [https://perma.cc/Q5N4-468W].

<sup>185</sup> *Zhongguo Yinjianhui* (中国银监会) [China Banking Regul. Comm’n], *Zhongguo Yinjianhui Guanyu Choujian Yingkou Yanhai Yinhang de Pifu* (中国银监会关于筹建营口沿海银行的批复) [Reply of the China Banking Regulatory Commission on the Establishment of Yingkou Coastal Bank], ZHONGGUO YINJIANHUI (中国银监会) [CHINA BANKING & INS. REGUL. COMM’N] (Oct. 25, 2010), <http://www.cbirc.gov.cn/cn/view/pages/ItemDetail.html?docId=272901&itemId=4110&generaltype=1> [https://perma.cc/YSL8-FHW5].

<sup>186</sup> *Zhongguo Yinjianhui* (中国银监会) [China Banking Regul. Comm’n], *Zhongguo Yinjianhui Bangongting Guanyu Jiaqiang Zhongxiao Shangye Yinhang Zhuyao Gudong Zige Shenhe de Tongzhi* (中国银监会办公厅关于加强中小商业银行主要股东资格审核的通知) [Notice of the General Office of the China Banking Regulatory Commission on Strengthening the Qualification Review of Major Shareholders of Small and Medium-sized Commercial Banks], ZHONGGUO YINJIANHUI (中国银监会) [CHINA BANKING & INS. REGUL. COMM’N], <http://www.cbirc.gov.cn/cn/view/pages/governmentDetail.html?docId=278643&itemId=863&generaltype=1> [https://perma.cc/327A-UPUS].

<sup>187</sup> See MICHAEL F. MARTIN, CONG. RSCH. SERV., R42380, CHINA’S BANKING SYSTEM: ISSUES FOR CONGRESS 4 (2012), <https://fas.org/sgp/crs/row/R42380.pdf> [https://perma.cc/TQ29-KMHU].

<sup>188</sup> See New Fortune FCC history, *supra* note 137.

<sup>189</sup> See Qingmin Yan (阎庆民), *Yinjianhui Zhuxi Yanqingmin Tan Minying Yinhang Shidian Gongzuo* (银监会副主席阎庆民谈民营银行试点工作) [Qingmin Yan, Vice Chairman of the CBRC, Talks About the Pilot Work of Private Banks],

Yet until 2014, no Mainland China-based banks had been established entirely with private capital in the PRC.<sup>190</sup> That year, the CBRC approved the establishment of five pilot privately-owned banks.<sup>191</sup> The first of the pilot banks, WeBank, was established in 2014 and is controlled by Tencent.<sup>192</sup> Two other pilot banks established in 2015 were also backed by PFCCs: 1) MYbank, controlled by Ant Financial; and 2) Shanghai Huarui Bank, controlled by JuneYao Group, an FCC that also controls a range of non-financial business including a namesake airline and several consumer goods retailers.<sup>193</sup> The CBRC soon formalized the process by which privately-owned banks are formed by issuing related

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ZHONGGUO YINJIANHUI (中国银监会) [CHINA BANKING & INS. REGUL. COMM'N] (Mar. 11, 2014), <http://www.cbirc.gov.cn/cn/view/pages/ItemDetail.html?docId=44777&itemId=915&generaltype=0> [https://perma.cc/845L-4T8T].

<sup>190</sup> Before 2014, Mainland China only had one bank founded by private capital—Minsheng Bank. See Xinhua, *China Regulator Approves Operation of Private Webank*, CHINA DAILY (Dec. 13, 2014), [http://www.chinadaily.com.cn/business/2014-12/13/content\\_19080267.htm](http://www.chinadaily.com.cn/business/2014-12/13/content_19080267.htm) [https://perma.cc/9E5F-3ZGC]. However, Minsheng Bank was not entirely founded by private capital. See *About CMBC*, CHINA MINSHENG BANK (Jan. 1, 2013), <http://en.cmbc.com.cn/CMBCToday/AboutCMBC/IntroductiontoCMBC/index.htm> [https://perma.cc/62VR-D8MN] (noting that Minsheng Bank was the “first national joint-stock commercial bank initiated and founded mainly from non-public enterprises”).

<sup>191</sup> See Jamil Anderlini, *China Opens Door to Private Banks*, FIN. TIMES (Mar. 11, 2014), <https://www.ft.com/content/7096239e-a8e0-11e3-bf0c-00144feab7de> [https://perma.cc/WSH2-AT2M].

<sup>192</sup> See Yang Ge, *Online Banks Tied to Tencent, Alibaba Bulk Up 1 Yuan at a Time on Microloans*, CAIXIN (Jun. 7, 2017), <https://www.caixinglobal.com/2017-06-07/online-banks-tied-to-tencent-alibaba-bulk-up-1-yuan-at-a-time-on-microloans-101099195.html> [https://perma.cc/WSH2-AT2M] (reporting that WeBank is 30 percent owned by Tencent). A mid-2017 New Fortune article reported that Tencent controlled WeBank; see *infra* note 197 and accompanying text.

<sup>193</sup> See Jiang Xueqing, *Micro Firms Handed a Boost, Thanks to New Breed of Private Banks*, CHINA DAILY (Jan. 22, 2019), <http://www.chinadaily.com.cn/a/201901/22/WS5c46805aa3106c65c34e5cb6.htm> [https://perma.cc/4HC9-2T8T] (reporting that MYBank is thirty percent owned by Ant Financial); *Huarui Bank*, JUNEYAO, <http://www.en.juneyao.com/hrbank/index.jhtml> [https://perma.cc/HXP6-5X66] (reporting that Shanghai Huirui Bank formally started operation in May 2015). A mid-2017 New Fortune article reported that Ant Financial controlled MYbank while JuneYao Group controlled Shanghai Huirui Bank as well as a TIC. See *infra* note 197 and accompanying text. For information on JuneYao Group’s non-financial business lines, see Appendix A, and *Group Introduction*, JUNEYAO, <http://www.en.juneyao.com/GroupIntroduction.jhtml> [https://perma.cc/V58X-E52S].

licensing procedures and regulatory requirements in 2015.<sup>194</sup> By 2017, the CBRC approved the establishment of seventeen privately-owned banks including Jiangsu Suning Bank, backed by consumer goods retailer Suning.com Co., Ltd. (“Suning Commerce Group”),<sup>195</sup> marking the formation of another PFCC.<sup>196</sup>

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<sup>194</sup> CBRC, *Guidance on Promoting the Development of Private-owned Banks*, GOV.CN (June 22, 2015), [http://www.gov.cn/zhengce/2015-06/22/content\\_5042920.htm](http://www.gov.cn/zhengce/2015-06/22/content_5042920.htm) [<https://perma.cc/5WU6-PMDR>].

<sup>195</sup> See Li Dongmei, *Chinese Retailer Suning Launches Private Internet Bank*, CHINA MONEY NETWORK (June 19, 2017), <https://www.chinamoneynetwork.com/2017/06/19/chinese-retailer-suning-launches-private-internet-bank> [<https://perma.cc/DM9J-WADB>]; *Suning Tesco*, Suning, <https://www.suningholdings.com/cms/suningdqtxtdata/index.htm> [<https://perma.cc/R76A-5RV3>]. Given the PBOC’s classification of Suning Commerce Group as a “de-facto financial holding company,” as well as thresholds used in foreign regulatory regimes to determine that a non-financial firm controls a bank, this Article treats Jiangsu Suning Bank as being controlled by Suning Commerce Group. See PEOPLE’S BANK OF CHINA, *supra* note 5, at 169; *infra* notes 315-320, 345-349 and accompanying text (explaining how twenty-five and twenty percent ownership stakes held by a non-financial company in a bank are used by U.S. and EU financial regulators, respectively, to determine whether a heightened regulatory regime is appropriate). Suning.com Co., Ltd. is also called Suning Commerce Group (苏宁云商集团股份有限公司). See *Suning Tesco*, *supra*.

<sup>196</sup> By 2017, Suning Commerce Group also controlled Suning Financial Services, which offers non-bank consumer and business loans. See MANCY SUN, PIYUSH MUBAYI, TIAN LU & STANLEY TIAN, GOLDMAN SACHS, *THE RISE OF CHINA FINTECH* 66 (2017), <https://hybg.cebnet.com.cn/upload/gaoshengfintech.pdf> [<https://perma.cc/7JDY-SN4V>]. In 2017, Suning Financial Services reportedly offered \$24.3 billion USD loans. See Zhou Pengfeng (周鹏峰), *Minying Jinkong Yangben Zhi Suning Jinrong: Sanzudingli You Youhuo You Tiaozhan* (民营金控样本之苏宁金融：三足鼎立有诱惑有挑战) [*Suning Finance, a Specimen of Private Finance: A Three-Legged Stand with Temptations and Challenges*], 21 JINGJIWANG (21 经济网) [21JINGJI.COM] (Sep. 1, 2018), <http://www.21jingji.com/2018/9-1/wMMDEzODBfMTQ0NzIwMQ.html> [<https://perma.cc/64GA-3MWP>]. For the purposes of this Article, Suning Financial Services and its various financial affiliates, including numerous regional non-bank lending subsidiaries, are collectively treated as one “company that, through one or more non-bank lending businesses, conducts a high level of financial intermediation,” one of the nine types of financial companies considered in this Article’s categorization of FCCs. See *supra* note 5 and accompanying text (providing the methodology used in this Article to classify FCCs); *Shanghai Suning Jinrong Fuwu Jituan Youxian Gongsi* (上海苏宁金融服务集团有限公司) [*Shanghai Suning Financial Services Group Co., Ltd.*], TIANYANCHA (天眼查) TIANYANCHA, <https://www.tianyancha.com/company/3403000763> (reporting that Shanghai Suning Financial Services Group, also known as Suning Financial Services, controls numerous provincial non-bank small business lending subsidiaries, as well as various other financial companies that do not correspond to the nine types of financial companies considered in this Article’s categorization of FCCs).

### III. THE SIGNIFICANCE, STRUCTURE, AND REGULATION OF FCCs IN MAINLAND CHINA

FCCs play a critical role in Mainland China's financial system across various industry verticals, including banking, payments, insurance, and fund management. This Part presents estimates of the extent to which financial companies controlled by FCCs participate in key segments of Mainland China's financial markets. It also examines causes of and policy issues related to FCC organizational complexity that compound the difficulty of identifying, assessing, and regulating the financial market risks posed by Mainland China's FCCs.

#### *a. Mainland China's FCCs Are Significant Across Financial Industry Verticals*

Appendix A provides a list of large FCCs used to estimate the scope of financial services activities conducted by Mainland China's FCC-controlled firms. These FCCs were identified using data from several prominent Chinese financial news and data aggregation services—including New Fortune, Wind, and TianYanCha—as well as an analytical framework provided in the PBOC's 2018 Financial Stability Report.<sup>197</sup> Importantly, given the prevalence of complex

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<sup>197</sup> Appendix A is primarily sourced from mid-2017 New Fortune publications that list financial companies controlled by the PRC's largest state-owned and privately-owned conglomerates, ranked by financial assets. Su Longfei (苏龙飞), *Zhongguo Minying Jinrong Quanli Bang TOP100: Mayun Jingran Zhi Pai Diwu, Naxie Ren Bi Ta Geng* (中国民营金融权力榜 TOP100: 马云竟然只排第五, 哪些人比他更有权力?) [*Top 100 of China's Private Financial Power List: Jack Ma Is Only Fifth, Who Is More Powerful than Him?*], XIN CAIFU (新财富) [NEW FORTUNE] (July 11, 2017), [https://mp.weixin.qq.com/s/A\\_y9igKA7A8Rnt0WQYScag](https://mp.weixin.qq.com/s/A_y9igKA7A8Rnt0WQYScag) [<https://perma.cc/N3K9-TBFH>]; Su Longfei (苏龙飞), *Yang Qi Jinrong Quanli Bang: ZhaoShangju, Huarun, Guojia Dianwang, Yancao Zonggongsi.....Jiemi 23 Da Shiye YnagYnagYnagYnagYangYnag Qi Jinrong Quan Buju* (央企金融权力榜: 招商局、华润、国家电网、烟草总公司.....揭秘 23 大实业央企金融全布局!) [*List of Financial Powers of Central-Government-Owned Enterprises: China Merchants, China Resources, State Grid, Tobacco Corporation . . . Unveiled the Full Layout of 23 Major Industrial Central-Government-Owned Enterprises!*], XIN CAIFU (新财富) [NEW FORTUNE] (July 13, 2017) [collectively hereinafter New Fortune 2017 Reports], [https://mp.weixin.qq.com/s/4\\_Ay3Hc2vOhuwk1d06Y7zg](https://mp.weixin.qq.com/s/4_Ay3Hc2vOhuwk1d06Y7zg) [<https://perma.cc/9H2D-GJKS>]. Besides Tencent, all conglomerates listed in the New Fortune 2017 Reports that are also included in Appendix A are those that conform with this Article's definition of an FCC because, as of 2016-17: (1) each

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conglomerate controlled two or more of the nine types of financial companies considered in this Article's approach to identifying FCCs; (2) financial companies controlled by each conglomerate collectively accounted for over \$10 billion USD (about 70 billion yuan) in financial assets; and (3) each conglomerate operated large non-financial business lines. *See supra* note 5 and accompanying text. Capital leasing companies listed in the New Fortune 2017 Reports, however, are excluded from estimates of FCC-controlled financial companies set forth in Appendix A, as these are not one of the nine types of financial companies considered in this article's approach to identifying FCCs. Also, even though the New Fortune 2017 Reports indicate that Tencent's 2017 financial assets were below the \$10 billion USD threshold, this article still considers it an FCC because of the scale of its payment system. *See id.* For an overview of the sources used to determine if a conglomerate listed in the New Fortune 2017 Reports operated large non-financial business lines in 2016-17, see *infra* note 407. Notably, given the close relationship between Alibaba and Ant Financial, this Article treats Alibaba as an FCC rather than Ant Financial, the entity listed in the New Fortune 2017 Reports. *See supra* notes 174-176 and accompanying text. Appendix A also includes four FCCs not listed in the New Fortune 2017 Reports: CITIC Group, China Everbright Group, Shougang Group, and Suning Commerce Group. The PBOC has categorized CITIC Group, China Everbright Group, and Suning Commerce Group as "de-facto financial holding companies." *See PEOPLE'S BANK OF CHINA, supra* note 5, at 168-69. This Article treats Suning Commerce Group as controlling two financial companies that are types considered in this article's approach to identifying FCCs. *See supra* notes 195-196 and accompanying text (listing financial companies controlled by Suning Commerce Group). This article treats CITIC Group as controlling seven of these financial companies: CITIC Bank (which together with AiBank and CITIC Bank's subsidiaries, including China CITIC Bank International, is treated as a single financial company), CITIC Trust, CITIC Securities (which together with its financial company subsidiaries, besides CITIC Futures, is treated as one financial company), CITIC Futures, CITIC-Prudential Fund Management Co., Ltd., CITIC Finance Co., Ltd. (an internal financial company), and CITIC-Prudential Life Insurance Co., Ltd. *See* CITIC LTD., ANNUAL REPORT 2017, at 175, 336-39 (2018), <https://www.citic.com/ar2017/download%20center/en/e00267.pdf> [<https://perma.cc/8BYZ-2UMY>] (reporting CITIC Group as the parent company of CITIC Ltd., which at the time held fifty percent or more shares in each of CITIC Bank, CITIC-Prudential Life Insurance Co., Ltd., CITIC Trust, and CITIC Finance Co., Ltd.); *Group Structure*, CITIC INT'L FIN. HOLDINGS LTD. (Dec. 15, 2017), <http://www.citicfh.com/eng/structure/index.htm> [<https://perma.cc/5ED3-XPXZ>] (reporting that CITIC Bank, through a subsidiary, as of December 2017 controlled seventy-five percent of China CITIC Bank International); *Gongsi Jianjie* (公司简介) [*Company Profile*], ZHONGXIN BAOCHENG (中信保诚) CITIC-PRUDENTIAL FUND MGT. CO., LTD., <https://www.citicprufunds.com.cn/pc/companyInfo> [<https://perma.cc/73DA-Y6A7>] (explaining that CITIC-Prudential Fund Management Co., Ltd, founded in 2005, is a joint-venture of CITIC Trust and Prudential Group Co, Ltd.); CITIC SEC., 2017 ANNUAL REPORT 12, 54, 106 (2018), <http://www.citics.com/newsite/en/FinancialInformation/FinancialReport/201804/P020180420605294602805.pdf> [<https://perma.cc/B5NQ-STJH>] (reporting that in 2017 CITIC Securities controlled CITIC Futures as well as other financial companies, and that 16.5 percent of CITIC Securities shares were ultimately controlled by CITIC Group, by far the largest shareholder). Given the close relationship between CITIC Group and CITIC Securities, this article treats CITIC Securities as being controlled by CITIC Group. *See id.* (detailing numerous

significant CITIC Securities related party transactions with CITIC Group); Nisha Gopalan, *How CLSA Had the Life Squeezed out of It*, BLOOMBERG (Jan. 9, 2020), <https://www.bloomberg.com/opinion/articles/2020-01-09/clsa-losing-identity-threatens-citic-s-global-ambitions> [<https://perma.cc/X7FH-X4J3>] (referring to CITIC Securities as a unit of CITIC Group); Zhonggong Zhongxin Jituan Weiyuanhui (中共中信集团委员会) [CCP CITIC Group Committee], *Zhonggong Zhongxin Jituan Weiyuanhui Guanyu Xunshi Zhenggai Qingkuang de Tongbao* (中共中信集团委员会关于巡视整改情况的通报) *CCP CITIC Group Committee Announcement on Inspection and Rectification*, Zhonggong Zhongyang Jilü Jiancha Weiyuanhui (中共中央纪律检查委员会) [Central Commission for Discipline Inspection of the Communist Party of China] (Apr. 27, 2016), [www.ccdi.gov.cn/special/zyxszt/2015dsl\\_zyxs/agls\\_2015dsl\\_zyxs/201605/t20160501\\_78340.html](http://www.ccdi.gov.cn/special/zyxszt/2015dsl_zyxs/agls_2015dsl_zyxs/201605/t20160501_78340.html) [<https://perma.cc/2P44-SAXV>] (indicating that CITIC Securities acts as a subsidiary of CITIC Group). This article treats China Everbright Group as controlling seven financial companies that are types considered in this article's approach to identifying FCCs. *Zhongguo Guangda Jituan Gufengongsi* (中国光大集团股份公司) [*China Everbright Group*], TIANYANCHA (天眼查), <https://www.tianyancha.com/company/210456243> (reporting that China Everbright Group owns fifty percent or more shares of each of Everbright Sun Life Insurance Co., Everbright Xinglong Trust Co., Ltd., China Everbright International Trust & Investment Corporation, and Everbright Financial Holding Asset Management Co., Ltd.—which either directly or through subsidiaries controls several fund companies and is, for purposes of this Article, treated as a single financial company); CHINA EVERBRIGHT BANK, 2017 ANNUAL REPORT 65, 67-68 (2018), [http://www.cebbank.com/site/gdywwz/Investor%20Relations/Financial%20Reports/H\\_Share81/66410664/2018042722274447511.pdf](http://www.cebbank.com/site/gdywwz/Investor%20Relations/Financial%20Reports/H_Share81/66410664/2018042722274447511.pdf) [<https://perma.cc/2M5Y-YKJ4>] (reporting that in 2017 China Everbright Group and its state owner Central Huijin Investment Ltd. together controlled over fifty percent of China Everbright Bank's shares); EVERBRIGHT SEC. CO., LTD., ANNOUNCEMENT OF ANNUAL RESULTS FOR THE YEAR ENDED DECEMBER 31, 2017, at 106 (2018), <http://www.ebscn.com/upload/20180327/20180327083850883.pdf> [<https://perma.cc/DL3V-3R8L>] (reporting that as of December 2017, China Everbright Group was the controlling shareholder of Everbright Securities Company Limited, which is, together with its subsidiaries, treated as a single financial company in this article, with the exception of Everbright Futures Co., Ltd., which this Article treats as a separate financial company). This Article also treats Shougang Group as a FCC, even though it is not explicitly mentioned by the PBOC. See *Shougang Jituan Youxian Gongsi* (首钢集团有限公司) [*Shougang Group Limited Company*], TIANYANCHA (天眼查) [TIANYANCHA], <https://www.tianyancha.com/company/672482> (reporting that Shougang Group controls one internal financial company and a fund company that controls other financial companies but for purposes of this article is treated as a single financial company); *infra* note 200 (explaining that in mid-2017 Shougang Group controlled over 20 percent of Huaxia Bank, a large bank). This Article's counts of financial companies controlled by Suning Commerce Group and the two large IFCCs include payments and non-bank lending companies that are not included in tallies presented in the New Fortune 2017 Reports. See *supra* notes 5, 174, 181 and accompanying text (explaining the circumstances under which these types of financial companies are included in this Article's counts of financial companies controlled by an FCC as well as how many of these types of companies are controlled by the IFCCs).

FCC organizational structures that rely on cross-shareholding and ownership pyramids,<sup>198</sup> as well as the lack of public information on ownership relationships between opaquely organized FCCs and non-listed banks and insurers, it can be difficult to determine whether a particular financial firm is controlled by an FCC. This Article largely relies on mid-2017 New Fortune investigative reports to make these determinations, which were critical to producing Figure 1 and Table 1 below.<sup>199</sup>

*i. Banking: FCC-Controlled Banks Account for One-Quarter of Banking Assets Held Outside the Large SOBs*

According to the estimate presented in Figure 1,<sup>200</sup> by mid-2017, FCC-controlled banks accounted for about thirteen percent of Mainland China's commercial banking assets, while banks

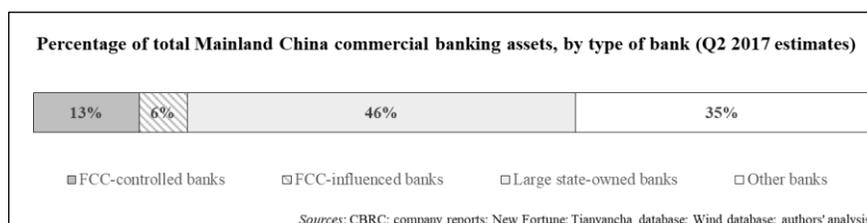
<sup>198</sup> For an explanation of these ownership structures that enable an FCC to control a financial company even though it does not directly own the majority of shares, see *infra* notes 225-228 and accompanying text.

<sup>199</sup> See New Fortune 2017 Reports, *supra* note 197 and accompanying text.

<sup>200</sup> Appendix B lists all banks included in this analysis, and was primarily developed by cross-referencing Appendix A's list of FCCs with New Fortune's lists of banks controlled by Mainland China's largest conglomerates in 2016-17, using each conglomerate's respective ownership share in the bank(s) it controlled. See New Fortune 2017 Reports, *supra* note 197 and accompanying text. For the four FCCs identified in this Article but not listed in the New Fortune 2017 Reports, the following sources are used to determine each FCC's ownership stake in its respective bank affiliate: CITIC LTD., *supra* note 197 and accompanying text; HUA XIA BANK CO., ANNUAL REPORT 2017, at 64 (2018), <http://www.hxb.com.cn/en/images/abouthuaxiabank/investorrelationship/informationdisclosureannualreport/2018/07/13/81C01D5A8B7C45D21CA6DF1FC D7B2D6C.pdf> [<https://perma.cc/XT7J-2F3Q>] (reporting that in mid-2017, Shougang Group controlled 20.28 percent of Huaxia Bank); CHINA EVERBRIGHT BANK, *supra* note 197 and accompanying text. Suning Commerce Group is excluded from Appendix B because it did not establish a bank until mid-2017. For each of the banks listed in Appendix B, Wind data was used to determine Q2 2017 banking assets, except in three instances where data limitations necessitated that 2016 Wind data be used, and one instance where 2015 data, as reported by New Fortune, was used. See *Wind Financial Terminal*, WIND, <https://www.wind.com.cn/en/wft.html> [<https://perma.cc/GA68-RLD5>]; *infra* note 408 and accompanying text. SOB and total commercial bank assets data used to produce Figure 1 was obtained from the CBRC website. *Yinhangye Jianguan Tongjizhibiao Yuedu Qingkuangbiao (2017 Nian)* (银行业监管统计指标月度情况表(2017年)) [*Monthly Statistics Fact Sheet*], ZHONGGUO YINHANG BAOXIAN JIANDUGUANLI WEIYUANHUI (中国银行保险监督管理委员会) [CHINA BANKING & INS. REGUL. COMM'N] (Feb. 1, 2018), <http://www.cbirc.gov.cn/cn/view/pages/ItemDetail.html?docId=146945&itemId=954&generaltype=0> [<https://perma.cc/J53C-YPVH>].

“influenced” by FCCs—meaning that an FCC held twenty percent or more of shares, but there is no clear indication that as of mid-2017 it controlled the bank—accounted for almost six percent of commercial banking assets.

Figure 1: FCC-Controlled and FCC-Influenced Banks Account for Almost 20 Percent of Mainland China Commercial Banking Assets by 2017



Of the twenty-two banks controlled by FCCs in early 2017, the largest were China Merchants Bank, CITIC Bank, China Everbright Bank, and Ping An Bank.<sup>201</sup> Overall, in mid-2017, FCC-controlled banks accounted for at least twenty-four percent of Mainland China commercial banking assets not controlled by large SOBs,<sup>202</sup> totaling 23 trillion yuan (approximately \$3.4 trillion USD).<sup>203</sup>

#### ii. Payments: IFCCs Operate Major Retail Payments Systems

According to a J.P. Morgan analysis, fifty-four percent of Mainland China's 2018 e-commerce spending by value took place via digital wallet mobile payments services.<sup>204</sup> Moreover, a 2018 study reported that digital wallet mobile payments services accounted for forty percent of Mainland China's retail in-person

<sup>201</sup> See *infra* Appendix B. This table excludes a bank controlled by Suning Commerce Group.

<sup>202</sup> See *supra* Figure 1 (grouping the Mainland China banking assets by FCC-controlled banks', FCC-influenced banks, large state-owned banks and “other banks”).

<sup>203</sup> See *infra* Appendix B. For conversion rate, see *Exchange Rates*, *supra* note 18.

<sup>204</sup> *E-commerce Payments Trends: China*, J.P.MORGAN (2019) <https://www.jpmorgan.com/merchant-services/insights/reports/china> [<https://perma.cc/JC8S-2XN7>].

spending.<sup>205</sup> Across e-commerce and in-person spending, over ninety percent of Q4 2018 mobile payments were executed via services provided by the PRC's two IFCCs, Tencent and Alibaba.<sup>206</sup> Taken together, these findings suggest that payments companies controlled by the PRC's two IFCCs accounted for forty to fifty percent of Mainland China's retail payments in 2018.<sup>207</sup>

*iii. Insurance, Fund Management, and TICs: FCCs Have Sizable Market Shares*

By 2017, several FCCs played a very large role in the PRC's insurance industry. Indeed, as Table 1 illustrates, data compiled by S&P Global Ratings and New Fortune together suggest that in early 2017, FCC-controlled life insurance companies accounted for over one-third of life insurance policies written in Mainland China.<sup>208</sup>

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<sup>205</sup> SUKRITI BANSAL, PHILIP BRUNO, OLIVIER DENECKER, MADHAV GOPARAJU & MARC NIEDERKORN, GLOBAL PAYMENTS 2018: A DYNAMIC INDUSTRY CONTINUES TO BREAK NEW GROUND 8 (2018), <https://www.mckinsey.com/~media/McKinsey/Industries/Financial%20Services/Our%20Insights/Global%20payments%20Expansive%20growth%20targeted%20opportunities/Global-payments-map-2018.ashx> [https://perma.cc/J33R-LUFF].

<sup>206</sup> JOSHUA YOUNGER, ALEX YAO, KATHERINE LEI & ARTHUR LUK, J.P. MORGAN, A CASE STUDY IN ALTERNATIVE PAYMENTS: LESSONS FROM THE CHINESE EXPERIENCE 7 (2019).

<sup>207</sup> This figure is estimated using data reported by other sources. See *supra* notes 204-206 and accompanying text.

<sup>208</sup> To produce Table 1, each of the PRC's twenty-five largest life insurance companies and their respective market share, as reported by S&P Global Ratings, was cross-referenced against insurers that, according to the New Fortune 2017 Reports, were controlled by FCCs listed in Appendix A. See *infra* Appendix A; New Fortune 2017 Reports, *supra* note 197; S&P GLOBAL, CHINA'S TOP 25 INSURERS 39 (2017), <https://www.spratings.com/documents/20184/0/China%27s+Top+25+Insurers/5f4d65c5-130c-4027-83dd-dd3eec5b8796> [https://perma.cc/DVJ6-K6N3].

TABLE 1: 2017 ESTIMATED MARKET SHARE OF FCC-CONTROLLED LIFE INSURERS

Insurance Company	Chinese Name	FCC that Controls the Insurers (est. mid-2017 ownership stake)	Market Share of Q1 2017 Life Insurance Policies Written
Ping An Life Insurance	平安人寿	Ping An Group (99.5%)	13.2%
Anbang Life Insurance	安邦人寿	Anbang Group (100%)	9.0%
Huaxia Life Insurance	华夏人寿	Tomorrow Group (93%)	5.3%
Funde Sino Life Co. Ltd.	富德生命	Funde Group (81%)	3.9%
Tianan Life Insurance	天安人寿	Tomorrow Group (40%)	2.6%
Evergrande Life Insurance	恒大人寿	Evergrande Group (50%)	1.0%
Qianhai Life Insurance	前海人寿	Baoneng Group (100%)	1.0%
Estimated total market share of FCC-controlled life insurers			36.0%

The PRC's large FCCs also play a major role in fund management. Most significantly, Ant Financial's money market fund is one of the largest in the world, with over one trillion yuan in assets under management in 2018.<sup>209</sup> The fund assets of other FCCs listed in Appendix A are also substantial, and totaled over one trillion yuan at year-end 2016.<sup>210</sup> Moreover, both IFCCs also serve as important channels through which retail investors invest in bank-administered wealth management products<sup>211</sup> that are similar to MMFs. Serving as funding vehicles to various financial institutions, these wealth management products collectively accounted for 22.2 trillion yuan in assets under management by 2019.<sup>212</sup>

By year-end 2016, the total assets of TICs controlled by FCCs listed in Appendix A likely equaled about seven trillion yuan,<sup>213</sup> and Mainland China's TIC assets reportedly totaled 23 trillion yuan in

<sup>209</sup> See YOUNGER, YAO, LEI & LUK, *supra* note 206, at 9.

<sup>210</sup> The total asset value of FCC-controlled funds was calculated by summing the 2016 fund assets reported by New Fortune for funds it reported as controlled by FCCs listed in Appendix A. See New Fortune 2017 Reports, *supra* note 197; see *infra* Appendix A.

<sup>211</sup> See YOUNGER, YAO, LEI & LUK, *supra* note 206, at 11-12.

<sup>212</sup> See *id.*; Ehlers, Kong & Zhu, *supra* note 17.

<sup>213</sup> The total asset value of FCC-controlled TICs was calculated by summing the 2016 TIC assets reported by New Fortune for TICs it reported as controlled by FCCs listed in Appendix A. See New Fortune 2017 Reports, *supra* note 197; see *infra* Appendix A.

mid-2017.<sup>214</sup> Thus, overall, TICs controlled by Mainland China's FCCs likely accounted for about 30 percent of total TIC assets in early 2017. These TICs largely serve either as funding vehicles through which assets of wealthy individuals or businesses are used to finance high-risk projects, or as a conduit through which banks and other financial firms can invest in asset classes that they would otherwise not be able to purchase due to regulatory reasons.<sup>215</sup>

*b. Understanding FCC Organizational Complexity and Related Regulatory Challenges*

The PBOC's 2018 Financial Stability Report flagged the rapid growth of non-financial conglomerates controlling two or more types of financial firms as a potential risk to the Chinese economy, warning that these groups' complex structures can enable excessive financial leverage, impede supervision, and enable corporate groups to circumvent regulations on improper intra-group transactions.<sup>216</sup> This Section identifies drivers and characteristics of FCC organizational complexity, explores how the PBOC and market observers believe FCC structures contribute to regulatory challenges, and examines the potential impact of recent regulatory shifts aimed at addressing some of these issues.

*i. Cross-Shareholding & Pyramids: Characteristics of Many FCC Structures*

During the early 2000s, as sweeping legal and policy changes and economic turmoil helped drive many FCCs to form, the Organisation for Economic Co-operation and Development ("OECD") found that PRC regulators were understaffed and ill-

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<sup>214</sup> BOSTON CONSULTING GRP., CHINA TRUST INDUSTRY REPORT 2 (2018), [http://image-src.bcg.com/Images/BCG-China-Trust-Report-Feb-2018\\_ENG\\_tcm52-188092.pdf](http://image-src.bcg.com/Images/BCG-China-Trust-Report-Feb-2018_ENG_tcm52-188092.pdf) [<https://perma.cc/8XS5-SZGQ>].

<sup>215</sup> PING AN TRUST CO. & MCKINSEY & COMPANY, THE COMING TRANSFORMATION OF CHINA'S TRUST INDUSTRY – CHINA TRUST INDUSTRY REPORT 2013, at 4 (2013), <http://www.mckinseychina.com/wp-content/uploads/2013/12/mckinsey-china-the-coming-transformation-of-chinas-trust-industry.pdf?5c8e08> [<https://perma.cc/FGV3-ASZJ>].

<sup>216</sup> PEOPLE'S BANK OF CHINA, *supra* note 5, at 169-70.

equipped to conduct proper industry oversight.<sup>217</sup> Accordingly, some of the large FCCs that emerged in the 2000s were established through opaque webs of shell companies and non-publicly-listed financial institutions.<sup>218</sup> Indeed, up until regulations were tightened in 2018,<sup>219</sup> rules aimed at restricting a single entity from controlling more than one bank and one insurer were systematically circumvented through regulatory arbitrage whereby complex FCC structures were used to exert control over numerous financial institutions.<sup>220</sup> This problem was exacerbated by unclear definitions

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<sup>217</sup> See OECD, CHINA IN THE WORLD ECONOMY: THE DOMESTIC POLICY CHALLENGES 50 (2002).

<sup>218</sup> See Michael Forsythe, *Behind China's Anbang: Empty Offices and Obscure Names*, N.Y. TIMES (Sep. 1, 2016), <https://www.nytimes.com/2016/09/02/world/asia/china-anbang-insurance.html> [<https://perma.cc/Y2BP-7SL5>] (reporting on Anbang Group's complex web of business units); David Barboza, *Behind a Chinese Powerhouse, a Web of Family Financial Ties*, N.Y. TIMES (July 18, 2017), <https://www.nytimes.com/2017/07/18/business/dealbook/hna-debt-deal-hain-airlines.html> [<https://perma.cc/UW3Q-7F4N>] (reporting on the conglomerate structure of HNA Group).

<sup>219</sup> In 2018 and 2019, the CBRC, CIRC, and CSRC tightened supervisory loopholes that enabled corporate groups to control numerous financial companies. Shangyeyinhang Guquan Guanli Zhanxing Banfa (商业银行股权管理暂行办法) [Interim Measures for the Administration of Equities of Commercial Banks] (promulgated by China Banking Regul. Comm'n, Jan. 5, 2018, effective Jan. 5, 2018), <http://www.cbirc.gov.cn/cn/view/pages/governmentDetail.html?docId=265032&itemId=861&generaltype=1> [<https://perma.cc/UE7B-MXWS>]; Baoxiangongsi Guquan Guanlibanfa (保险公司股权管理办法) [Measures for the Administration of Equities of Insurance Companies] (promulgated by China Insurance Regulatory Commission, Apr. 10, 2018, effective Apr. 10, 2018), <http://www.cbirc.gov.cn/cn/view/pages/ItemDetail.html?docId=372940&itemId=928&generaltype=0> [<https://perma.cc/R74E-TKWH>]; Zhengquangongsi Guquan Guanliguiding (证券公司股权管理规定) [Provisions on the Administration of Equities of Securities Companies] (promulgated by China Securities Regulatory Commission, July 5, 2019, effective July 5, 2019), <http://www.csrc.gov.cn/pub/zjhpublic/zjh/201907/P020190705633045079946.pdf> [<https://perma.cc/6K9K-LLPA>].

<sup>220</sup> See Tian Jing (田静), *Jituan Nei Jinrongjigou Jianguan Mianlin de Tiaozhan Yu Duice* (集团内金融机构监管面临的挑战与对策) [*Challenges and Countermeasures Faced by Group Financial Institutions*], 98 BIJIAO (比较) [COMP. STUD.] 228, 228 (2018), <http://bijiao.caixin.com/2019-01-16/101370632.html> [<https://perma.cc/6DUP-3GP7>]; PEOPLE'S BANK OF CHINA, *supra* note 5, at 170; see also Peng Qinqin & Liu Xiao, *Party's Over for China's Financial Holding Companies*, CAIXIN (Nov. 20, 2017), <https://www.caixinglobal.com/2017-11-20/partys-over-for-chinas-financial-holding-companies-101173771.html> [<https://perma.cc/TX7B-5DTT>] (observing that rules restricting a single company and its affiliates from collectively controlling more than one bank were "widely circumvented" throughout the 2010s).

of critical legal terms such as “shareholder,” enabling FCCs to circumvent regulatory barriers to bank and insurer acquisitions.<sup>221</sup>

By December 2017, the PRC was “materially non-compliant” with international regulatory best practices related to monitoring the transfer of significant bank ownership stakes, as Mainland China regulators had, according to the IMF, “no systematic process for regularly receiving/collecting information on names and holdings of all significant shareholders or those that exert controlling influence [over banks].”<sup>222</sup> Indeed, during this time, the ultimate controlling shareholders of some large FCCs were unknown entities.<sup>223</sup> This outcome was enabled by highly-complex webs of pyramid structures and cross-shareholdings<sup>224</sup> —organizational approaches through which an FCC’s ultimate controlling shareholder is able to control a financial firm despite only directly owning a minority of its voting rights.

Through pyramid structures, a controlling minority shareholder of a holding company can exert control over a financial firm in which that holding company maintains a controlling stake.<sup>225</sup> Complex FCCs generally utilize multi-tiered pyramid structures,<sup>226</sup> thereby compounding the gap between an FCC parent company’s share of cash flow rights and the extent of its control over a financial firm. Cross-shareholding, on the other hand, occurs when companies own stakes in each other, which in other words means

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<sup>221</sup> See *supra* notes 105-107 and accompanying text. For example, Haier established five different companies to gain control over a bank. See *supra* note 135 and accompanying text.

<sup>222</sup> IMF, *People’s Republic of China: Financial Sector Assessment Program: Detailed Assessment of Observance of Basel Core Principles for Effective Banking Supervision*, Country Report No. 17/403, at 256 (Dec. 2017), <https://www.imf.org/en/Publications/CR/Issues/2017/12/26/Peoples-Republic-of-China-Financial-Sector-Assessment-Program-Detailed-Assessment-of-45516> [<https://perma.cc/UY7Q-FULY>].

<sup>223</sup> For example, in 2017, HNA Group’s largest shareholder was essentially an unknown person. See *Who Owns HNA, China’s Most Aggressive Dealmaker?*, FIN. TIMES (June 2, 2017), <https://www.ft.com/content/8acfe40e-410b-11e7-9d56-25f963e998b2> [<https://perma.cc/JSC8-WLYA>].

<sup>224</sup> See PEOPLE’S BANK OF CHINA, *supra* note 5, at 169-70; Tian Jing, *supra* note 220, at 228.

<sup>225</sup> See Lucian Bebchuk, Reinier Kraakman & George Triantis, *Stock Pyramids, Cross-Ownership, and Dual Class Equity: The Creation and Agency Costs of Separating Control from Cash Flow Rights* 1, 5-7 (Nat’l Bureau of Econ. Rsch., Working Paper No. 6591, 1999), <https://www.nber.org/papers/w6951> [<https://perma.cc/WCY9-VVXF>].

<sup>226</sup> See PEOPLE’S BANK OF CHINA, *supra* note 5, at 169-170; Tian Jing, *supra* note 220, at 228.

that each company indirectly owns some of its own shares.<sup>227</sup> An FCC can use cross-shareholding to allocate voting shares in such a way that greatly reduces the number of shares it must own to control an affiliated financial firm.<sup>228</sup>

According to the PBOC, Mainland China's FCCs have exerted control over financial companies by using a mix of cross-shareholding and pyramid structures.<sup>229</sup> Indeed, by 2018, the ownership structures of some FCCs were highly complex and involved dozens of corporate levels.<sup>230</sup> Opaque and complex structures of FCCs have exacerbated financial risks and impeded effective supervision, for reasons explained below.

ii. *FCC Complexity Impedes Effective Capital Regulation*

Capital acts as the "first line of defense against losses" for financial institutions,<sup>231</sup> and regulatory requirements related to capital levels aim to ensure that an institution's capital is high enough to absorb significant losses.<sup>232</sup> Higher capital levels also reduce the likelihood that linkages between multiple financial firms will result in one entity's failure triggering failures of others.<sup>233</sup> In late 2018, the PBOC warned that complex ownership structures within Mainland China's FCCs create the risk that banks and

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<sup>227</sup> See Bebhuck, Kraakman & Triantis, *supra* note 225, at 7-8.

<sup>228</sup> See GUIDO FERRARINI, CORPORATE OWNERSHIP AND CONTROL LAW REFORM AND THE CONTESTABILITY OF CORPORATE CONTROL 11 (2000), <https://www.oecd.org/corporate/ca/corporategovernanceprinciples/1931676.pdf> [<https://perma.cc/J5AP-F2UM>] (explaining that "cross-[share]holdings allow [a] company involved to place into friendly hands a number of its own shares, thereby reducing the investment required to the controllers to keep control of the relevant company").

<sup>229</sup> PEOPLE'S BANK OF CHINA, *supra* note 5, at 169 (observing that some "de-facto financial holding companies...invest in financial institutions through multilayered shareholding and cross-holdings").

<sup>230</sup> *Id.*

<sup>231</sup> Hal S. Scott, *Reducing Systemic Risk Through the Reform of Capital Regulation*, 13 J. INT'L ECON. L. 763, 764 (2010).

<sup>232</sup> See *Why Do Banks Need to Hold Capital?*, EUROPEAN CENT. BANK (May 3, 2019), [https://www.bankingsupervision.europa.eu/about/ssmexplained/html/hold\\_capital.en.html](https://www.bankingsupervision.europa.eu/about/ssmexplained/html/hold_capital.en.html) [<https://perma.cc/28HT-LEDU>].

<sup>233</sup> See *Testimony Before the Comm. on Banking, Housing, and Urban Affairs U.S. Senate*, 114<sup>th</sup> Cong. (Jun. 7, 2016) (written statement of Hal S. Scott, Director, Comm. on Cap. Mkts. Regul.), [https://www.banking.senate.gov/imo/media/doc/060716\\_Scott%20Testimony.pdf](https://www.banking.senate.gov/imo/media/doc/060716_Scott%20Testimony.pdf) [<https://perma.cc/R4MC-676L>].

insurance companies will be undercapitalized.<sup>234</sup> Similarly, 2019 research by economists at Chongqing University of Technology determined that effective capital regulation for PRC mixed conglomerates is impeded by “the prominent phenomenon of multi-level shareholding and cross-shareholding.”<sup>235</sup>

Consistent with these observations, international banking regulators and central banks agree that complex ownership structures can enable financial groups to obfuscate their capital adequacy.<sup>236</sup> Indeed, complex cross-shareholding webs between Anbang Group affiliates enabled the FCC to misrepresent to regulators that it quintupled its capital within just a few months as it dramatically expanded its ownership of banks and launched an investment fund.<sup>237</sup> A related problem is that the complex ownership structures of Mainland China’s FCCs can enable widespread multiple leveraging,<sup>238</sup> meaning that funds raised by one entity within a corporate group are used as capital to support risk-taking in separate but affiliated business units.<sup>239</sup>

These issues are compounded by a lack of adequate regulatory coordination. As FCCs formed in the 2000s, contact between relevant regulators was limited to periodic meetings conducted pursuant to guidance that did not address multiple leveraging.<sup>240</sup>

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<sup>234</sup> PEOPLE’S BANK OF CHINA, *supra* note 5, at 169 (observing that “layered shareholding and cross-holdings” are “driv[ing] up the overall leverage ratio” at some financial institutions).

<sup>235</sup> Chenyuan Zhao & Qiumin Yu, *A Summary of Risks in China’s Financial Holding Companies*, 10 MOD. ECON. 1385, 1390 (2019), [https://www.scirp.org/pdf/ME\\_2019051515361999.pdf](https://www.scirp.org/pdf/ME_2019051515361999.pdf) [<https://perma.cc/5U6N-5FDR>].

<sup>236</sup> See BASEL COMM. ON BANKING SUPERVISION, PRINCIPLES FOR THE SUPERVISION OF FINANCIAL CONGLOMERATES 28-29 (2012), <https://www.bis.org/publ/joint29.pdf> [<https://perma.cc/J5AP-F2UM>].

<sup>237</sup> See Ding Feng & Jia Huajie, *In Depth: What’s Driving Insurer Anbang’s Big Bang?*, CAIXIN (Feb. 4, 2015), <https://www.caixinglobal.com/2015-02-04/whats-driving-insurer-anbangs-big-bang-101012703.html> [<https://perma.cc/7MHP-7BAD>].

<sup>238</sup> PEOPLE’S BANK OF CHINA, *supra* note 5, at 162 (observing that “increased leverage” has emerged within holding companies that own financial institutions “due to investment with non-proprietary funds”); Zhao & Yu, *supra* note 235, at 1389-90.

<sup>239</sup> See HEIDI MANDANIS SCHOONER & MICHAEL W. TAYLOR, GLOBAL BANK REGULATION: PRINCIPLES AND POLICIES 213-14 (2010).

<sup>240</sup> See Deng Zhongfeng & Cing Yangbin, *Analysis on Double Leverage Risk of Financial Holding Conglomerates*, 257 N. ECON. & TRADE 80, 82 (2006) (observing that, during this time, the only agreement between the CBRC, CIRC, and CSRC to

The PBOC found that “regulatory gaps” brought about by “sectoral regulation” enabled FCCs to “make repeated capital injection[s] in the disguise of a shell company.”<sup>241</sup>

Also, as the financial activities of almost all FCCs were not subject to consolidated supervision at a holding company level, there was no group-wide or mid-tier holding company constraints on leverage.<sup>242</sup> In late 2018 the PBOC also observed that some FCCs had invested in financial institutions with borrowed funds, thereby increasing leverage.<sup>243</sup> Multiple leveraging was exacerbated during the 2010s by the wide-spread practice of FCCs conducting offshore debt issuances backed by a domestic affiliate’s cash flow,<sup>244</sup> and until 2018 CIRC regulatory action, this debt could be omitted from leverage calculations.<sup>245</sup>

Additionally, non-bank micro-lending companies controlled by IFCCs could make loans with funds raised through the recycling of asset-backed security cash flows and the issuance of other forms of debt instruments, leading to high leverage, and these entities have also collaborated with banks to make jointly-issued loans, causing concerns from regulators and market observers over capital adequacy and risk contagion.<sup>246</sup> For example, Alibaba affiliate Ant

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facilitate coordinated supervision of financial conglomerates limited coordination to periodic joint meetings, and that no formal regulations existed to facilitate such coordination); Zhang Yuzhe, Wu Hongyuran & Teng Jing Xuan, *China to Roll Out Financial Holding Company Regulations Later This Year*, CAIXIN (Jun. 3, 2018), <https://www.caixinglobal.com/2018-06-03/china-to-roll-out-financial-holding-company-regulations-later-this-year-101261859.html> [https://perma.cc/T58L-Z4HP] (reporting that between 1999 and 2018, there was a “lack of consensus between government agencies on who should regulate financial holding companies and how they should do so”).

<sup>241</sup> PEOPLE’S BANK OF CHINA, *supra* note 5, at 169.

<sup>242</sup> See Zhao & Yu, *supra* note 235, at 1389-90.

<sup>243</sup> PEOPLE’S BANK OF CHINA, *supra* note 5, at 169.

<sup>244</sup> See Zhao & Yu, *supra* note 235, at 1390; see also Julie Zhu, *Buying Overseas, Chinese Conglomerates Leverage Offshore Assets for Financing*, REUTERS (Apr. 28, 2017), <https://www.reuters.com/article/us-china-capitaloutflows-financing/buying-overseas-chinese-conglomerates-leverage-offshore-assets-for-financing-idUSKBN17T3EG> [https://perma.cc/XA3R-HN2E].

<sup>245</sup> See Yang Qiaoling & Han Wei, *China Clamps Down on Insurers’ Overseas Financing*, CAIXIN (Feb. 13, 2018), <https://www.caixinglobal.com/2018-02-13/china-clamps-down-on-insurers-overseas-financing-101211049.html> [https://perma.cc/V9SK-JEAX].

<sup>246</sup> See HUANG QIFAN (黄奇帆), JIEGOUXING GAIGE: ZHONGGUO JINGJI DE WENTI YU DUICE (结构性改革: 中国经济的问题与对策) [STRUCTURAL REFORM: PROBLEMS AND SOLUTIONS OF CHINESE ECONOMY] 91 (2020); Zhou Jueshuo (周夔铄), *Daxing Hulianwang Qiye Jinru Jinrong Lingyu de Qianzai Fengxian Yu Jianguan* (大型互联网企

Financial's leverage ratio is reportedly well over sixty times assets as a result of the lending activity of Chongqing-based non-bank online consumer lending affiliates,<sup>247</sup> which were lightly-regulated at the provincial level but made loans worth over 300 billion yuan with just 3 billion yuan in capital.<sup>248</sup> Notably, the PBOC in 2017 constrained ABS issuance by these entities, and in November 2020, along with other agencies, issued draft "Interim Measures for the Administration of Online Petty Loan Business (Draft for Soliciting Opinions)," which, among other things, would require that: (i) the balance of proceeds raised by a non-bank micro-loan company operating an online non-bank micro-loan business through issuing bonds, ABS products, or other forms of standardized debt assets not exceed four times its net assets; and (ii) for a single jointly-issued loan, the capital contribution made by a non-bank micro-loan company operating an online non-bank micro-loan business not fall below thirty percent.<sup>249</sup>

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业进入金融领域的潜在风险与监管) [*The Potential Risk and Regulation of Large Internet Enterprises Entering the Financial Sector*], CAIXIN (Nov. 1, 2020), <http://opinion.caixin.com/2020-11-01/101621303.html> [<https://perma.cc/HY26-N7TC>]; Wu Hongyuran, Hu Yue & Han Wei, *In Depth: Cheers and Fears in \$283 Billion Bank-Tech Lending Tie-Up*, CAIXIN (Oct. 27, 2019), <https://www.caixinglobal.com/2019-10-27/in-depth-cheers-and-fears-in-283-billi-on-bank-tech-lending-tie-up-101475874.html> [<https://perma.cc/C5BM-ZA8D>].

<sup>247</sup> See Liu Caiping, Zhang Yuzhe, Yue Yue, Wei Yiyang & Han Wei, *Why Ant Group's IPO May Stay on Ice for a While*, NIKKEI ASIA (Nov. 10, 2020), <https://asia.nikkei.com/Spotlight/Caixin/Why-Ant-Group-s-IPO-may-stay-on-ice-for-a-while> [<https://perma.cc/68KB-4SK7>].

<sup>248</sup> See *id.*; HUANG QIFAN, *supra* note 246, at 91.

<sup>249</sup> See *China Cracks Down on Online Micro-Lending Firms with New Rules*, REUTERS (Dec. 1, 2017), <https://www.reuters.com/article/us-china-regulations-loans/china-cracks-down-on-online-micro-lending-firms-with-new-rules-idUSKBN1DV4OU> [<https://perma.cc/9GEJ-7RXE>]; Wangluo Xiaoe Daikuan Yewu Guanli Zanzing Banfa (Zhengqiu Yijian Gao) (网络小额贷款业务管理暂行办法(征求意见稿)) [*Interim Measures for the Administration of Online Petty Loan Business (Draft for Soliciting Opinions)*], ZHONGGUO YINBAOJIANHUI (中国银保监会) [CHINA BANKING & INS. REGUL. COMM'N] (Nov. 2, 2020), <http://www.cbirc.gov.cn/cn/view/pages/ItemDetail.html?docId=938821&itemId=951> [<https://perma.cc/ZS5E-HUC5>]; see also Aries Poon & Rebecca Isjwara, *China's Leverage Caps on Microlenders Bring Ant's Regulatory Risk to Forefront*, S&P GLOB. MKT. INTEL. (Sep. 16, 2020), <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/china-s-leverage-caps-on-microlenders-bring-ant-s-regulatory-risk-to-forefront-60376685> [<https://perma.cc/7QEJ-532H>]. The November 2020 measures, once finalized, may only have a limited impact on the leverage of Ant Financial's non-bank online consumer lending affiliates, which have largely already shifted to a partnership model whereby most lending is underwritten by partner financial institutions. *Id.*

iii. *Potentially Problematic Intra-Group Transactions and FCC Interconnectivity*

According to the PBOC, by 2018, certain banks and insurers controlled by FCCs had morphed into “cash machines” for the de-facto controlling persons, the ultimate beneficiaries, or affiliated non-financial enterprises, yet through complex structures that took advantage of a sector-based regulatory approach, these activities were hidden from regulators.<sup>250</sup> For example, according to one account, Tomorrow Group appropriated about 150 billion yuan from Baoshang Bank between 2005 and 2017.<sup>251</sup>

Generally, banking regulators across the world prohibit intra-group transactions not conducted at prevailing market rates and limit various forms of intra-group transactions, which can reflect insufficiently diverse exposures, and may stem from pressure by management to support intra-firm growth, a potential source of inadequate risk management.<sup>252</sup> Furthermore, although intra-group transactions are not inherently problematic,<sup>253</sup> high levels of intra-group funding may reduce reliance on external financing, which can serve as a source of private risk-monitoring.<sup>254</sup> Notably, throughout the 2005 to 2015 boom period for FCCs, PRC regulators had in place regulations aimed at ensuring that intra-group transactions between insurers, banks, and securities firms would be conducted at market

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<sup>250</sup> See PEOPLE'S BANK OF CHINA, *supra* note 5, at 170.

<sup>251</sup> See Zhou Xuedong (周学东), *Zhongxiao Yinhang Jinrong Fengxian Zhuyao Yuanyu Gongsu Zhili Shiling – Cong Jieguan Baoshang Yinhang Kan Zhongxiao Yinhang Gongsu Zhili de Guanjian* (中小银行金融风险主要源于公司治理失灵——从接管包商银行看中小银行公司治理的关键) [*Financial Risk of Small and Medium-sized Banks Stems from the Failure of Corporate Governance – An Analysis of the Crucial Determinants of Corporate Governance of Small and Medium-sized Banks based on the Case of Baoshang Bank*] 15 ZHONGGUO JINRONG (中国金融) [CHI. FIN.] 19 (2020).

<sup>252</sup> See SCHOONER & TAYLOR, *supra* note 239, at 121; see also *supra* note 103 and accompanying text.

<sup>253</sup> See BASEL COMM. ON BANKING SUPERVISION, INTRA-GROUP TRANSACTIONS AND EXPOSURES PRINCIPLES ¶ 2 (1999), <https://www.bis.org/publ/bcbs62.pdf> [<https://perma.cc/U9JU-JXX6>] (observing that some intra-group transactions “can facilitate . . . synergies”); see also *id.* ¶ 7 (reporting that most regulatory regimes require that intra-group transactions take place at “arm’s length,” meaning at prevailing market rates).

<sup>254</sup> See Stephen Prowse, *Corporate Governance in an International Perspective: a Survey of Corporate Control Mechanisms among Large Firms in the United States, the United Kingdom, Japan and Germany* (1994), <https://www.bis.org/publ/econ41.pdf> [<https://perma.cc/YP6B-M8HV>].

rates and reported to regulators.<sup>255</sup> Yet these rules were regularly circumvented by certain FCCs during the 2010s through regulatory arbitrage, as FCCs' complex structures impeded regulators' ability to categorize affiliated transactions.<sup>256</sup> Moreover, there were legal loopholes that enabled intra-group transactions between insurers and intra-group affiliates until 2019.<sup>257</sup>

Opaque and complex FCC structures can not only mask interconnectivity within corporate groups, but also impede understanding of connectivity between FCCs and other financial institutions. Indeed, information necessary to understand financial relations between various FCC affiliates and external firms may not only be poorly understood by regulators, but also by personnel working within the FCC.<sup>258</sup> Moreover, some FCCs are internationally active—through leveraged transactions conducted via a fund and several other affiliated business entities, HNA Group was able to acquire a ten percent stake in the global financial group

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<sup>255</sup> Zhongguo Baojianhui (中国保监会) [China Ins. Regul. Comm'n], *Baoxian Gongsì Guanlian Jiaoyì Guanli Zhanxing Banfa* (保险公司关联交易管理暂行办法) [Interim Measures for the Administration of Affiliated Transactions of Insurance Companies] (Apr. 4, 2007), <http://bxjg.circ.gov.cn/web/site0/tab5225/info52464.htm> [<https://perma.cc/XBL4-ERXY>]; *Shangye Yinhang Yu Neiburen He Gudong Guanlian Jiaoyì Guanli Banfa* (商业银行与内部人和股东关联交易管理办法) [The Administrative Measures for the Connected Transactions between the Commercial Banks and their Insiders or Shareholders] (promulgated by China Banking Regul. Comm'n, Apr. 2, 2004, effective May 1, 2004) art. 32, [http://www.lawinfochina.com/display.aspx?lib=law&id=3500&CGid=\[https://perma.cc/QZQ5-7K7U\]](http://www.lawinfochina.com/display.aspx?lib=law&id=3500&CGid=[https://perma.cc/QZQ5-7K7U]); ASIA-PACIFIC OFF. OF THE CFA INST. CENTRE FOR FIN. MKT. INTEGRITY, RELATED-PARTY TRANSACTIONS: CAUTIONARY TALES FOR INVESTORS IN ASIA (2009) 14, <https://www.cfainstitute.org/-/media/documents/article/position-paper/related-party-transactions-cautionary-tales-for-investors-in-asia.ashx> [<https://perma.cc/PR52-X7GA>] (the CSRC "banned listed companies from providing loan guarantees to their parents and required the latter to settle their loans to subsidiaries starting in 2006").

<sup>256</sup> See PEOPLE'S BANK OF CHINA, *supra* note 5, at 170-71; see also Xuan Lei, *China Regulator Bars 5 Insurers from Transactions with Shareholders, Affiliates*, S&P GLOB. MKT. INTEL. (Oct. 11, 2017), [https://www.spglobal.com/marketintelligence/en/news-insights/trending/ol4\\_dj\\_ilwt9q8ahtm3naqa2](https://www.spglobal.com/marketintelligence/en/news-insights/trending/ol4_dj_ilwt9q8ahtm3naqa2) [<https://perma.cc/D3NB-W3Y5>].

<sup>257</sup> See Wu Yujian & Denise Jia, *China Revises Rules on Insurers' Related-Party Transactions*, CAIXIN (Sept. 10, 2019), <https://www.caixinglobal.com/2019-09-10/china-revises-rules-on-insurers-related-party-transactions-101460546.html> [<https://perma.cc/RNZ7-TLXB>] (explaining that, through 2019, "rules did not clarify [an] insurance company's management responsibilities on related transactions by subsidiaries, making those in control of the insurer able to use the subsidiaries to bypass regulations to get access to the insurer's premium income").

<sup>258</sup> See Tian Jing, *supra* note 220, at 232; Zhao & Yu, *supra* note 235, at 1390.

Deutsche Bank in 2017.<sup>259</sup> Moreover, HNA Group's structure at the time was so complex that its largest shareholder remained a mystery,<sup>260</sup> causing analysts to fear that the unclear magnitude of HNA Group's size and operations created the risk that any material financial distress at the conglomerate could be transmitted across borders.<sup>261</sup> One prominent scholar has also raised concerns that the interconnectivity between and within IFCCs may drive risk contagion and systemic risk.<sup>262</sup>

*iv. Cross-Subsidization and Unfair Competitions Concerns*

The PBOC has also raised concerns that certain intra-group transactions enable cross-subsidization that both contributes to market risk and could bring about "unfair competition" – a non-financial institution may transfer assets through loans and guarantees made by its financial affiliates within the same FCC, constituting cross-subsidization (meaning that profits from one type of business activity are used to support other business activities).<sup>263</sup> PRC officials fear such intra-group cross-subsidization can enhance the competitive advantages of FCCs and affiliates, which has caused them and other observers to raise market fairness concerns.<sup>264</sup> Other commentators note that certain SFCCs enjoy unfair advantages in

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<sup>259</sup> See Olaf Storbeck., *Deutsche Bank's Biggest Shareholder Pulls Back from German Lender*, FIN. TIMES (Mar. 23, 2019), <https://www.ft.com/content/52f159ea-4cb8-11e9-bbc9-6917dce3dc62>. By March 2019, HNA Group, through its affiliates, only controlled five percent of Deutsche Bank's voting rights, yet had nearly zero economic interest in Deutsche Bank's stock. *Id.*

<sup>260</sup> See *Who Owns HNA, China's Most Aggressive Deal Maker?*, *supra* note 223.

<sup>261</sup> See, e.g., Anjani Trivedi & Julie Steinberg, *How China's Acquisitive HNA Group Fell From Favor*, WALL ST. J. (Nov. 19, 2017), <https://www.wsj.com/articles/how-chinas-acquisitive-hna-group-fell-from-favor-1511118961> [<https://perma.cc/MNU9-CZV4>].

<sup>262</sup> See Zhou Jueshuo, *supra* note 246. Zhou Jueshuo is rumored to be a former PBOC governor. See Eliza Gkritsi, *The Unsigned Op-Eds that Foreshadowed Ant Group IPO Suspension*, TECHNODE (Nov. 9, 2020), <https://technode.com/2020/11/09/china-voices-the-unsigned-op-eds-that-foreshadowed-ant-group-ipo-suspension/> [<https://perma.cc/CNE6-N92W>].

<sup>263</sup> See Tian Jing, *supra* note 220, at 233-35; see also PEOPLE'S BANK OF CHINA, *supra* note 5, at 103, 170; *Cross-Subsidization*, OECD (Aug. 13, 2013), <https://stats.oecd.org/glossary/detail.asp?ID=4968> [<https://perma.cc/Z5GQ-ZUDR>].

<sup>264</sup> See PEOPLE'S BANK OF CHINA, *supra* note 5, at 103; *infra* notes 266-268 and accompanying text; Tian Jing, *supra* note 220, at 233-35.

the form of state support inconsistent with the principle of competitive neutrality.<sup>265</sup>

The PBOC currently appears most concerned that the interaction between financial and non-financial activities within IFCCs will hinder risk monitoring and what it sees as fair competition.<sup>266</sup> Indeed, in December 2020, PBOC Deputy Governor Pan Gongsheng stated that a major focus of the PBOC's late 2020 supervisory interviews of Alibaba affiliate Ant Group (previously named Ant Financial) was eliminating "unfair competition."<sup>267</sup> Relatedly, the PRC's antitrust regulator (the State Administration for Market Regulation) has expressed concern about "unfair competition" by so-called "platform economy" conglomerates—in November 2020, it proposed "Guidelines on Antitrust in the Field of Platform Economy (Draft for Soliciting Opinions)," which, if implemented, would limit horizontal integration and intra-group transactions at multi-sector conglomerates controlling both financial companies and sizable consumer-oriented business lines (such as the IFCCs and Suning Commerce Group).<sup>268</sup>

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<sup>265</sup> See Zhang Chunlin, 'Competitive Neutrality' for SOEs Can Help China At Home and Abroad, CAIXIN (Oct. 16, 2018), <https://www.caixinglobal.com/2018-10-16/competitive-neutrality-for-state-firms-can-help-china-at-home-and-abroad-101335637.html> [<https://perma.cc/3E8D-WXZP>]; see also ORG. FOR ECON. COOP. & DEV., COMPETITIVE NEUTRALITY: MAINTAINING A LEVEL PLAYING FIELD BETWEEN PUBLIC AND PRIVATE BUSINESS 9 (2012), [https://read.oecd-ilibrary.org/industry-and-services/competitive-neutrality\\_9789264178953-en#page1](https://read.oecd-ilibrary.org/industry-and-services/competitive-neutrality_9789264178953-en#page1) [<https://perma.cc/86VS-CKEX>] (explaining that "competitive neutrality occurs where no entity operating in an economic market is subject to undue competitive advantages or disadvantages").

<sup>266</sup> See Guo Shuqing, Party Sec'y & Deputy Governor of the People's Bank of China & CBIRC Chairman, Speech at the Singapore FinTech Festival (Dec. 8, 2020), <https://www.bis.org/review/r201222f.pdf> [<https://perma.cc/E45J-CLZW>].

<sup>267</sup> Xinhua (新华), Zhongguo Renmin Yinhang Fuhangzhang Pan Gongsheng jiu Jinrong Guanli Bumen Yuetan Mayi Jituan youguan Qingkuang da Jizhe Wen (中国人民银行副行长潘功胜就金融管理部门约谈蚂蚁集团有关情况答记者问) [*Pan Gongsheng, Deputy Governor of the People's Bank of China, Answered Reporters' Questions about the Interview with the Financial Management Department about Ant Group*], XINHUA [新华] XINHUA (Dec. 27, 2020), [http://www.xinhuanet.com/2020-12/27/c\\_1126912928.htm](http://www.xinhuanet.com/2020-12/27/c_1126912928.htm) [<https://perma.cc/2XTJ-G4JM>].

<sup>268</sup> See Guanyu Pingtai Jingji Lingyu de Fanlongduan Zhinan (Zhengqiu Yijian Gao) (关于平台经济领域的反垄断指南(征求意见稿)) [*Guidelines on Antitrust in the Field of Platform Economy (Draft for Soliciting Opinions)*] (promulgated by St. Admin. for Mkt. Regul., Nov. 10, 2020), [http://www.samr.gov.cn/hd/zjdc/202011/t20201109\\_323234.html](http://www.samr.gov.cn/hd/zjdc/202011/t20201109_323234.html) [<https://perma.cc/3NE8-F9VA>]; see also Soon Chen Kang & Xiuxi Zhu, *Alibaba in Crosshairs of Growing Antitrust Scrutiny in China*, S&P MKT. INTEL. (Nov. 24, 2020), <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-h>

v. *Recent Regulatory Responses to FCCs*

These developments along with the PBOC's proposed non-bank lending rules discussed above are components of accelerating efforts since 2018 by PRC regulators to constrain the operations of and increase supervision over certain FCCs—particularly the IFCCs. That year, a modest pilot regulatory program for FCCs was introduced, which brought about heightened group-wide risk management standards for the financial operations of three FCCs (as well as two other holding groups).<sup>269</sup> Yet shortly thereafter, the PBOC reported it continued facing the challenge of “regulatory blind spots,” seeking regulatory authority to engage in “holistic, ongoing and look-through supervision” of certain mixed conglomerates.<sup>270</sup> On September 11, 2020, its request culminated in the State Council's issuance of the “Decision of the State Council on Implementing Access Administration of Financial Holding Companies” (“Access Administration Decision”),<sup>271</sup> authorizing the

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eadlines/alibaba-in-crosshairs-of-growing-antitrust-scrutiny-in-china-61345140 [https://perma.cc/JQ9J-DEJB]

<sup>269</sup> In 2018, five corporate groups—China Merchants Group, Shanghai International Group, Beijing Financial Holdings Group, Ant Financial, and Suning Commerce Group—were placed in a pilot regulatory program that entailed more stringent capital requirements and heightened risk management standards for the financial operations of each of these five corporate groups. See Stella Yifan Xie & Chao Deng, *China to Tighten Rules on Five Financial Giants*, WALL ST. J. (Nov. 3, 2018), <https://www.wsj.com/articles/china-to-tighten-rules-on-five-financial-giants-1541246489> [https://perma.cc/9FUK-WVYM] (citing state-run media outlet Xinhua News Agency). Two of these are large FCCs identified in this Article's analysis, while one—Ant Financial—is controlled by Alibaba, another FCC. See *infra* Appendix A. PRC regulators are able to apply group-level supervision principles to the FCC Ping An Group because it is headed by a regulated financial services business, an insurer. See IMF, *People's Republic of China: Financial Sector Assessment Program: Detailed Assessment of Observance of the Insurance Core Principles*, Country Report No. 17/402, at 92-94 (Dec. 2017), <https://www.imf.org/~media/Files/Publications/CR/2017/cr17402.ashx> [https://perma.cc/RMH3-G62P]. All other FCCs identified in this Article, besides Anbang Group, are headed by a non-financial entity. See *supra* note 5 and accompanying text; see *infra* Appendix A. As the IMF observed in 2017, “[w]here there is a non-financial parent entity [controlling a bank or banking sub-group], the CBRC . . . supervises banks or banking sub-groups within the wider group,” but “[a]t present there is no holding company regime in law or regulation” that enables group-wide supervision. IMF, *supra* note 222, at 114.

<sup>270</sup> PEOPLE'S BANK OF CHINA, *supra* note 5, at 170-72.

<sup>271</sup> See Guowuyuan Guanyu Shishi Jinrong Konggu Gongsi Zhunru Guanli de Jueding (国务院关于实施金融控股公司准入管理的决定) [Decision of the State

PBOC to promulgate rules requiring non-financial enterprises and persons controlling two or more types of certain financial institutions to apply to establish a separately capitalized financial holding company subject to PBOC supervision and regulation.<sup>272</sup> The PBOC's regulations, "Interim Measures for the Supervision and Administration of Financial Holding Companies" ("FHC Measures"), mirrored a July 2019 PBOC proposed rule and were implemented in November 2020, requiring "de-facto financial holding companies"—entities that meet criteria set forth in the rules—to apply to the PBOC for approval for formal formation and formal licensing as a PBOC-regulated financial holding company within twelve months.<sup>273</sup>

Under the FHC Measures, however, only a conglomerate with a high proportion of financial assets (eighty-five percent or more of the group's total assets) could be reorganized from the top-down as a "financial holding group" subject to group-wide regulation and

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Council on Implementing Access Administration of Financial Holding Companies] (promulgated by St. Council, Sep. 13, 2020, effective Nov. 1, 2020), [http://www.gov.cn/zhengce/content/2020-09/13/content\\_5543127.htm](http://www.gov.cn/zhengce/content/2020-09/13/content_5543127.htm) [<https://perma.cc/U5SR-N46R>].

<sup>272</sup> *Id.* The types of financial institutions for which a financial holding company would have to be formed include: commercial banks (excluding rural banks), financial leasing companies, TICs, asset managers, securities companies, public funds, futures companies, and insurers. *Id.* A financial holding company will need to be established if a domestic non-financial enterprise, a natural person, or an authorized legal person de-facto controls at least two types of these financial institutions and: (1) if it de-facto controls at least one commercial bank, either total assets of all financial institutions exceed or equal 500 billion yuan, total assets of all financial institutions other than commercial banks exceed or equal 100 billion yuan, or assets under management exceed or equal 500 billion yuan; (2) if it does not control any commercial banks, either total assets of all financial institutions exceed or equal 100 billion yuan or assets under management exceed or equal 500 billion yuan; or (3) if total financial assets do not meet the standards stated in either (1) and (2), but the PBOC deems that a financial holding company should be established. Jinrong Konggu Gongsu Jiandu Guanli Shixing Banfa (金融控股公司监督管理试行办法) [Interim Measures for the Supervision and Administration of Financial Holding Companies] (promulgated by People's Bank of China, Sep. 13, 2020, effective Nov. 1, 2020), art. 6 [hereinafter PBOC FHC Measures], <http://www.pbc.gov.cn/tiaofasi/144941/144957/4093006/index.html> [<https://perma.cc/379P-BBNA>].

<sup>273</sup> Jinrong Konggu Gongsu Jiandu Guanli Shixing Banfa (Zhengqiu Yijian Gao) (金融控股公司监督管理试行办法 (征求意见稿)) [Interim Measures for the Supervision and Administration of Financial Holding Companies (Draft for Soliciting Opinions)] (promulgated by People's Bank of China, Jul. 26, 2019), [http://www.gov.cn/xinwen/2019-07/26/content\\_5415624.htm](http://www.gov.cn/xinwen/2019-07/26/content_5415624.htm) [<https://perma.cc/Q6BZ-42UH>] (China); PBOC FHC Measures, *supra* note 272, art. 13.

supervision.<sup>274</sup> This threshold is hardly met by most Chinese FCCs. For FCCs that do not meet the threshold, financial affiliates controlled by the FCC will likely reorganize into a separately capitalized, PBOC-regulated financial holding company controlled by a domestic non-financial entity.<sup>275</sup> However, it remains to be seen if certain FCC structures could preclude the need for such reorganization.<sup>276</sup> Regardless, most FCCs will likely not be subject to robust group-wide regulation under the new rules,<sup>277</sup> although those that ultimately create PBOC-regulated financial holding companies pursuant to the regulations will be subject to new holding company-level capital regulations,<sup>278</sup> qualitative and quantitative risk management standards,<sup>279</sup> cross-shareholdings restrictions,<sup>280</sup> “penetration supervision” of controlling shareholders and the actual controller,<sup>281</sup> and anti-monopoly regulations.<sup>282</sup>

It remains unclear whether an FCC controlling a “de-facto financial holding company” that requires PBOC licensing under the new rules would, as a whole, be protected by the PRC’s national financial safety net. Were that to be the case, it could weaken market discipline, resulting in moral hazard and excessive risk-taking by affiliated financial institutions.<sup>283</sup> Moreover, the 2019 extension of

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<sup>274</sup> PBOC FHC Measures, *supra* note 272, art. 6.

<sup>275</sup> See *China’s New Rules on Financial Holding Firms to Curb Systemic Risks*, FITCH RATINGS (Oct. 14, 2020), <https://www.fitchratings.com/research/non-bank-financial-institutions/china-new-rules-on-financial-holding-firms-to-curb-systemic-risks-14-10-2020> [<https://perma.cc/5YUG-GL9D>].

<sup>276</sup> See *id.* (noting that “[i]mplementation will be key to the effectiveness of these new regulations”). Indeed, it seems possible that certain ownership structures could enable FCCs to control two or more financial companies but not reorganize those entities within a financial holding company pursuant to the new rule.

<sup>277</sup> However, although it appears that financial holding companies organized pursuant to the rule will not be subject to any clear supervisory benchmarks, the establishment of these entities would likely enable regulators to more closely scrutinize intra-group transactions. See *id.*

<sup>278</sup> PBOC FHC Measures, *supra* note 272, art. 7.

<sup>279</sup> *Id.* art. 24-35.

<sup>280</sup> *Id.* art. 18.

<sup>281</sup> *Id.* art. 40, 41.

<sup>282</sup> *Id.* art. 11, 35, 47.

<sup>283</sup> See TRIPARTITE GRP. BANK, *supra* note 3, at 17 n.9 (suggesting that the real or apparent extension of a safety net over non-financial affiliates of a mixed conglomerate is an undesirable policy outcome); see also GARY H. STERN & RON J.

the national financial safety net to protect 99.98 percent of the corporate creditors of Tomorrow Group's Baoshang Bank as well as likely on average over ninety percent of its other creditors' claims – including large inter-bank creditors – illustrates that the financial operations of certain FCCs may already be viewed by PRC regulators as too-big-to-fail.<sup>284</sup>

In short, the Access Administration Decision and FHC Measures are likely to enhance PBOC oversight authority over the financial operations of most FCCs and modestly limit intra-group transaction volume, but will not directly restrict the ability of FCCs to form through non-financial entities gaining control of multiple large financial companies.<sup>285</sup> Indeed, the new rules arguably legitimize the structure of certain FCCs,<sup>286</sup> even though the two IFCCs – particularly Alibaba – continue to be subject to fierce regulatory scrutiny.<sup>287</sup> In fact, as recent events suggest, FCCs may ultimately enjoy a generous extension of the PRC's national financial safety net.

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FELDMAN, TOO BIG TO FAIL: THE HAZARDS OF BANK BAILOUTS 2 (2004) (explaining that the expansion of the expectation of government protection over creditors results in excessive risk taking and moral hazard).

<sup>284</sup> See Liu Jiefei, *Regulators Move to Restructure Troubled Baoshang Bank*, CAIXIN (Jun. 17, 2019), <https://www.caixinglobal.com/2019-06-17/regulators-move-to-restructure-troubled-baoshang-bank-101427929.html> [<https://perma.cc/7KPC-6FD2>].

<sup>285</sup> PBOC FHC Measures, *supra* note 272, art. 36 (setting forth restrictions on related party transactions for financial holding companies and their holding institutions); *supra* notes 274-82 and accompanying text.

<sup>286</sup> In September 2020, the PBOC noted the economic benefits of certain FCCs to the Chinese economy, observing that some

non-financial enterprises [that] have held several different types of financial institutions through investment . . . have improved resource allocation, reduced cost as well as enriched and improved their financial services through this business model, which was conducive to meeting the demands of various enterprises and consumers and to boosting the capacity of the financial sector for serving the real economy.

See PBC Officials Answer Press Questions on Trial Measures on Regulation of Financial Holding Companies, PEOPLE'S BANK OF CHINA (Sep. 18, 2020), <http://www.pbc.gov.cn/en/3688110/3688172/4048269/4098744/index.html> [<https://perma.cc/Z2J8-4VF4>].

<sup>287</sup> In addition to the restrictions on horizontal integration that the November 2020 SAMR regulations would bring about, a mid-January 2021 draft PBOC rule would effectively mandate anti-trust investigations into and forced divestures by the two IFCCs because of the market concentration enjoyed by their financial affiliates. See Zhongguo Renmin Yinhang Guanyu 《Feiyinhang Zhifu Jigou Tiaoli (Zhengqiu Yijian Gao)》 Gongkai Zhengqiu Yijian de Tongzhi (中国人民银行关于《非银行支付机构条例（征求意见稿）》公开征求意见的通知) [Notice of the

#### IV. HOW FCCs DISTINGUISH MAINLAND CHINA FROM OTHER MAJOR FINANCIAL SYSTEMS

This Part explores how the structure and regulation of Mainland China's FCCs distinguishes its financial markets from those of the EU, Japan, and the United States. First, Chinese SFCCs conduct a much broader range of significant financial and non-financial business activities relative to European, Japanese, or U.S. government-owned entities that offer financial services. Second, EU, Japanese, and U.S. regulatory frameworks either prohibit the structures of most of the PRC's largest FCCs or subject non-financial parent companies and affiliates within somewhat similarly structured entities to higher levels of regulation, while few comparable groups exist in these jurisdictions. Third, although cross-shareholdings and pyramid structures do exist within Japan's and the EU's financial sectors, only in Mainland China are some large mixed conglomerates characterized by both structural features, as well as high levels of intra-group transactions.

*a. Mainland China's SFCCs, Unlike State-Owned Groups in Other Major Markets, Engage in a Wide Range of Financial and Non-Financial Activities*

Mainland China's largest SFCCs conduct a wide range of sizable financial activities but, generally, most of their revenue comes from non-financial business lines.<sup>288</sup> This model does not exist in the United States, where few government-owned companies directly

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People's Bank of China on Public Consultation on the "Regulations on Non-bank Payment Institutions (Draft for Soliciting Opinions)" (promulgated by People's Bank of China, Jan. 20, 2021), <http://www.pbc.gov.cn/rmyh/105208/4166553/index.html> [<https://perma.cc/M63G-UL4D>]; see also Timmy Shen, *China's New Monopoly Rules Put Fintech Giants in the Crosshairs*, CAIXIN (Jan. 22, 2021), <https://www.caixinglobal.com/2021-01-22/chinas-new-monopoly-rules-put-fintech-giants-in-the-crosshairs-101653928.html> [<https://perma.cc/2CH4-ANKM>].

<sup>288</sup> For example, financial services revenue at CITIC Ltd., the major corporate unit of CITIC Group, made up less than forty percent of 2018 revenue. See CITIC LTD., 2018 ANNUAL REPORT 2, 9 (2019) [hereinafter CITIC 2018 ANNUAL REPORT], <https://www.citic.com/uploadfile/2019/0418/20190418044301701.pdf> [<https://perma.cc/C5XJ-FAVB>]. Many SFCCs listed in Appendix A—such as China National Petroleum Corporation and Sinochem Group—are likewise not primarily focused on financial activities.

provide business- or consumer-facing financial services and those that do are often guided by precise financial markets policy objectives and do not operate substantive non-financial business lines. It is also a stark contrast from the Eurozone and Japan, where besides two post office groups that control relatively large financial companies, state-owned institutions that provide a sizable amount of business- or consumer-facing financial services either directly or through affiliates are largely not active in non-financial sectors and predominantly focus on a limited number of financial sector business lines.

One of the few large U.S. federal government-owned financial companies is the Government National Mortgage Association (“Ginnie Mae”),<sup>289</sup> which guarantees principal and interest payments for securities comprised of U.S. government-guaranteed mortgages.<sup>290</sup> In addition to narrowly-focused, federal government-owned financial services entities, the U.S. is also home to some small government-owned entities that directly provide retail financial services, including a North Dakota state government-owned bank,<sup>291</sup> as well as some U.S. state government-owned non-profit

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<sup>289</sup> Fannie Mae and Freddie Mac, two government sponsored enterprises that securitize mortgages, are not considered to be “government-owned,” as both firms are under federal government conservatorship, meaning that the powers of common stockholders have been transferred to a U.S. government agency, but the majority of equity rights have not. See N. ERIC WEISS & DARRYL E. GETTER, CONG. RSCH. SERV., R44525, FANNIE MAE AND FREDDIE MAC IN CONSERVATORSHIP: FREQUENTLY ASKED QUESTIONS 7-8 (May. 31, 2019), <https://fas.org/sgp/crs/misc/R44525.pdf> [<https://perma.cc/A2ZG-3Z25>]. For a list of other U.S. federal government corporations, see KEVIN R. KOSAR, CONG. RSCH. SERV., RL30365, FEDERAL GOVERNMENT CORPORATIONS: AN OVERVIEW (2011), <https://fas.org/sgp/crs/misc/RL30365.pdf> [<https://perma.cc/X66F-BHGG>].

<sup>290</sup> Ginnie Mae is a wholly owned U.S. Government corporation. It securitizes mortgages insured or guaranteed by the U.S. Federal Housing Administration (which guarantees mortgages to first-time and low-income homebuyers), as well as several other U.S. government programs. See *Our Model & Platform*, GINNIE MAE, [https://www.ginniemae.gov/about\\_us/who\\_we\\_are/Pages/our\\_business\\_model.aspx](https://www.ginniemae.gov/about_us/who_we_are/Pages/our_business_model.aspx) [<https://perma.cc/H6MN-FBBA>].

<sup>291</sup> BANK OF N. DAKOTA, ANNUAL REPORT 4 (2018), <https://bnd.nd.gov/annual-report/> [<https://perma.cc/7DE7-C3NY>] (explaining that the Bank of North Dakota is “the only state-owned bank in the country”). The bank’s “primary service is to North Dakota’s financial institutions and state agencies” and it only “deal[s] directly with North Dakota residents . . . to fill a need that is underserved and for which the private sector has requested [their] involvement.” See Eric Hardmeyer, *Why Public Banking Works in North Dakota*, N.Y. TIMES (Oct. 1, 2013), <https://www.nytimes.com/roomfordebate/2013/10/01/should-states-operate-public-banks/why-public-banking-works-in-north-dakota> [<https://perma.cc/T7ZE-W2PF>].

insurance corporations.<sup>292</sup> Yet, unlike Mainland China's SFCCs, these state-owned institutions all almost exclusively conduct financial activities, and are not structured as large multi-layer corporate groups.

In Japan, there are several directly government-owned banks,<sup>293</sup> which unlike Mainland China's SFCCs, are designed to focus on lending to economic sectors deemed by the government to be underserved.<sup>294</sup> Only one of these entities—Shoko Chukin Bank—provides a range of retail-facing financial services and conducts some non-financial business activities.<sup>295</sup> Yet the scope of its non-financial activities is quite small and its lending activities equaled less than two percent of Japan's outstanding commercial bank loans in 2017.<sup>296</sup> Conversely, Japan Post Bank and Japan Post Insurance maintain sizable retail financial services market shares in Japan and are majority-owned by government-controlled Japan Post Holdings—which also controls non-financial businesses such as a postal service—but the government's ownership stake in Japan Post Holdings must fall to around one-third in the coming years under a privatization plan, and the stakes of Japan Post Holdings in Japan Post Bank and Japan Post Insurance are likewise each set to fall to fifty percent or lower.<sup>297</sup>

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<sup>292</sup> See, e.g., *Who We Are*, CITIZENS PROP. INS. CORP., <https://www.citizensfla.com/who-we-are> [<https://perma.cc/NC9J-445H>].

<sup>293</sup> IMF, *Japan Financial System Stability Assessment*, Country Report No. 17/244, at 51 (Jul. 12, 2017), <https://www.imf.org/en/Publications/CR/Issues/2017/07/31/Japan-Financial-System-Stability-Assessment-45151> [<https://perma.cc/VX7F-VPAL>].

<sup>294</sup> See Lev Ratnovski & Aditya Narain, *Public Financial Institutions in Developed Countries – Organization and Oversight* 7-8 (IMF, Working Paper No. 07/227, 2007), <https://www.imf.org/external/pubs/ft/wp/2007/wp07227.pdf> [<https://perma.cc/BB93-K6QC>].

<sup>295</sup> See *New Appearance of Shoko Chukin Bank*, SHOKO CHUKIN BANK, <https://www.shokochukin.co.jp/english/about/company/reborn/>; SHOKO CHUKIN BANK, ANNUAL REPORT 60 (2018), [https://www.shokochukin.co.jp/english/about/company/report/2018/pdf/ar18\\_all.pdf](https://www.shokochukin.co.jp/english/about/company/report/2018/pdf/ar18_all.pdf) [<https://perma.cc/BMQ5-YR6Q>].

<sup>296</sup> See *id.*; Shoko Chukin Bank's Q1 2017 loan balance (9.357 trillion yen) equaled just 1.7 percent of Japan's 2017 outstanding commercial bank loan balance, which the Federal Rsrv. Bank of St. Louis reports was about 539 trillion yen. See *id.*; FED. RESERVE BANK OF ST. LOUIS, ECONOMIC DATA, USE OF FINANCIAL SERVICES, ASSETS: OUTSTANDING LOANS AT COMMERCIAL BANKS FOR JAPAN (June 26, 2018), <https://fred.stlouisfed.org/series/JPNFCSODCXDC> [<https://perma.cc/WQ7U-SSV7>].

<sup>297</sup> See IMF, *supra* note 293, at 9 n.5, 50-1; Hisao Kodachi, *Insurance scandal delays Japan Post privatization by 5 years*, NIKKEI ASIA (Feb. 13, 2020),

In the Eurozone, roughly eight percent of banking assets were held by large public sector institutions in 2015.<sup>298</sup> Approximately sixty percent of these assets belonged to Germany's regional government-owned banks (generally known as *Landesbanken*), such as LBBW, the Eurozone's largest government-owned financial firm.<sup>299</sup> Like Mainland China's SFCCs, *Landesbanken* can be structured as holding companies<sup>300</sup> and may control non-financial firms.<sup>301</sup> Yet as opposed to FCCs, for which non-financial business lines are significant, *Landesbanken* earn over ninety-eight percent of their operating income from financial activities.<sup>302</sup> On the other hand, unlike the *Landesbanken* and the Eurozone's other sizable state-owned financial firms, France's La Banque Postale—the Eurozone's second largest state-owned financial firm, accounting for ten percent of Eurozone 2015 public sector banking assets<sup>303</sup>—is controlled by a state-owned group that earns the majority of its revenue from non-financial business activities.<sup>304</sup> Yet as Table 2 illustrates, that parent group, La Poste, controls a narrower range of

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<https://asia.nikkei.com/Politics/Insurance-scandal-delays-Japan-Post-privatization-by-5-years> [<https://perma.cc/K7RR-PXBZ>]; Taro Fuse & Taiga Uranaka, *Japan Post Insurer Plans \$2.9 Billion Buyback From Parent*, BLOOMBERG (Dec. 16, 2020) <https://www.bloomberg.com/news/articles/2020-12-16/japan-post-insurer-plans-2-9-billion-buyback-to-cut-owner-stake> [<https://perma.cc/3HPV-8X2E>].

<sup>298</sup> See Nicolas Véron, *The Governance and Ownership of Significant Euro-area Banks*, BRUEGEL POLICY CONTRIBUTION, May 2017, at 1, 5, <https://bruegel.org/wp-content/uploads/2017/05/PC-15-2017-290517.pdf> [<https://perma.cc/WZ7E-HJTE>].

<sup>299</sup> See *id.* at 13-15 (reporting data used to calculate German public sector regional and local government-owned banks' share of EU banking assets).

<sup>300</sup> See IMF, *Germany: Financial Sector Assessment Program*, Country Report No. 16/189, at 56 (June 2016), <https://www.imf.org/external/pubs/ft/scr/2016/cr16189.pdf> [<https://perma.cc/WM5B-UQJG>].

<sup>301</sup> For example, BayernLB controls "one of the largest catering firms in Munich." *Group Subsidiaries*, BAYERNLB (JAN. 1, 2021), [https://www.bayernlb.com/internet/en/blb/resp/about\\_us/konzern\\_4/toechter\\_3/toechter\\_2.jsp](https://www.bayernlb.com/internet/en/blb/resp/about_us/konzern_4/toechter_3/toechter_2.jsp) [<https://perma.cc/SR5E-YQNN>].

<sup>302</sup> Data from 2017 shows that Germany's largest *Landesbanken* generated over 73 percent of operating income from interest, and about 25 percent from commissions and financial transactions. DEUTSCHE BUNDESBANK, MONTHLY REPORT 29, 36 (Sept. 2018), <https://www.bundesbank.de/resource/blob/760004/6d8b3367ff98c77e715eac6c7c12bfc7/mL/2018-09-ertragslage-data.pdf> [<https://perma.cc/K5EV-BPXY>].

<sup>303</sup> See Véron, *supra* note 298, at 13-15.

<sup>304</sup> LE GROUPE LA POSTE, 2020 UNIVERSAL REGISTRATION DOCUMENT 8, 12 (2021), [https://le-groupe-laposte.cdn.prismic.io/le-groupe-laposte/8438b095-1a9a-477a-8a25-9699ee41876a\\_GLP2020\\_UDR\\_EN\\_mars\\_2021.pdf](https://le-groupe-laposte.cdn.prismic.io/le-groupe-laposte/8438b095-1a9a-477a-8a25-9699ee41876a_GLP2020_UDR_EN_mars_2021.pdf).

non-financial affiliates than large Chinese SFCCs. Table 2 contrasts business lines of the Eurozone's two largest state-owned financial groups with those of large Chinese SFCCs, as well as large state-owned entities in the United States and Japan that provide financial services.

TABLE 2: FINANCIAL & NON-FINANCIAL BUSINESS LINES OF LARGE GOVERNMENT-OWNED GROUPS ENGAGED IN FINANCIAL SERVICES IN THE EU, JAPAN, THE PRC, AND THE UNITED STATES (FINANCIAL ACTIVITIES IN GREY)

La Poste (France) <sup>305</sup>	LBBW (Germany) <sup>306</sup>	Shoko Chukin Bank (Japan) <sup>307</sup>	Ginnie Mae (U.S.) <sup>308</sup>	China Merchants Group <sup>309</sup>	China National Petroleum Corporation <sup>310</sup>	CITIC Group <sup>311</sup>
Commercial banking	Commercial banking	Commercial banking	Mortgage-backed security guarantees	Commercial banking	Commercial banking	Commercial banking
Insurance	Insurance	Leasing		Securities brokerage	TIC business	TIC business
Securities brokerage	Securities brokerage	Credit card services		Insurance	Insurance	Insurance
Asset management	Asset management	Property management		Asset management	Securities brokerage	Private equity
Payment solutions				Venture capital	Financial leasing	Asset management
Traditional mail				Private equity	Asset management	Securities brokerage

<sup>305</sup> *Id.*; *La Banque Postale and its Subsidiaries*, LA BANQUE POSTALE, <https://www.labanquepostale.com/en/about-us/presentation.subsidiaries.html> [<https://perma.cc/WH8E-86FH>].

<sup>306</sup> *The Subsidiaries of LBBW*, LBBW, [https://www.lbbw.de/group/landesbank-baden-wuerttemberg/subsidiaries/subsidiaries\\_7wong3s3u\\_e.html](https://www.lbbw.de/group/landesbank-baden-wuerttemberg/subsidiaries/subsidiaries_7wong3s3u_e.html) [<https://perma.cc/YU2S-9E99>] (last visited Mar. 13, 2021).

<sup>307</sup> *New Appearance of Shoko Chukin Bank*, *supra* note 295, at 60.

<sup>308</sup> *Our Model & Platform*, *supra* note 290.

<sup>309</sup> *Structure*, CHINA MERCHANTS GRP., <http://www.cmhk.com/en/ac/orst/index.shtml> [<https://perma.cc/XWJ6-SULB>].

<sup>310</sup> *About CNPC*, CPNC, [http://www.cnpc.com.cn/en/aboutnpc/aboutnpc\\_index.shtml](http://www.cnpc.com.cn/en/aboutnpc/aboutnpc_index.shtml) [<https://perma.cc/DR3D-674B>].

<sup>311</sup> *See* CITIC LTD., *supra* note 197, at 11, 23, 29, 37, 48-52, 336-38; CHINA CITIC BANK, 2017 ANNUAL REPORT 57-59 (2018), <https://www1.hkexnews.hk/listedco/listconews/sehk/2018/0427/lt201804272486.pdf> [<https://perma.cc/MZ4A-P693>].

Parcels shipping & logistics				Futures company	Oilfield services	Futures company
Property management				Financial leasing	Equipment manufacturing	Financial leasing
Digital services				Real estate development & management	Chemical product manufacturing	Venture capital
Telecom service				Ports operation & maintenance	Oil / gas exploration & production	Mineral / metal exploration & extraction
				Oil / gas distribution	Chemicals sales & trading	Engineering & construction
				Ship repairing & maintenance	New energy development	Power plant management
				Infrastructure management	Gas pipeline operator	Steel manufacturing
				Ship construction	Engineering & construction	Machinery & truck parts manufacturing
				Toll road management	Oil / gas sales & trading	Ports operation & maintenance
				Food trading and shipping	Oil / gas service stations	Environment services
				Tobacco trading and shipping		Real estate development & management
				Bulk cargo transportation		Helicopter fleet operation
						Publishing
						IT services
						Agriculture
						Food distribution and sales
						Telecom service

*b. Could Mainland China's FCCs Exist Under the EU's, Japan's, or the United States' Regulatory Frameworks?*

Another distinctive characteristic of Mainland China's financial system relative to the world's three other largest is that its FCCs can control relatively large banks and insurers, and can do so without being subject to significant group-wide supervision or regulation.<sup>312</sup> As mentioned above, even an FCC regulated under the FHC

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<sup>312</sup> See PEOPLE'S BANK OF CHINA, *supra* note 5, at 164-70.

Measures, as a whole, largely will not be subject to group-wide regulation and supervision. The analysis below examines why organizations structured similarly to Mainland China's largest FCCs—many of which by 2017 controlled both a bank and an insurer,<sup>313</sup> and could exhibit high levels of intra-group transactions, as explained above—largely do not exist in the EU, Japan, or the United States.

*i. Most FCC Structures Could Not Exist Under the United States' Regulatory Model*

The United States is one of a small number of countries in the world where commercial firm ownership of banks is generally prohibited, albeit with notable exceptions.<sup>314</sup> According to the U.S. Bank Holding Company Act ("BHC Act"), ownership of twenty-five percent or more of a bank's voting securities constitutes control of a bank,<sup>315</sup> and regulators can also utilize subjective tests to determine that owning as little as five percent of voting shares constitutes "control."<sup>316</sup> Once federal regulators determine that an entity "controls" a bank, that entity is considered a "bank holding company" ("BHC")<sup>317</sup> and is subject to a number of holding company-level regulations, including that the BHC serve as a source of strength to its subsidiary bank,<sup>318</sup> adherence to strict caps on intra-

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<sup>313</sup> For a list of the ten largest FCCs as of 2017, *see supra* note 25 and accompanying text. By early 2017, each of these FCCs controlled either: (i) a bank; (ii) one or more insurers; or (iii) a bank and one or more insurers. Seven of the ten largest FCCs controlled a bank and one or more insurers, and only seven FCCs listed in Appendix A do not control either a bank or insurer. *See supra* note 197 and accompanying text.

<sup>314</sup> *See* JAMES R. BARTH, TONG LI, APANARD ANGKINAND, YUAN-HSIN CHIANG & LI LI, INDUSTRIAL LOAN COMPANIES: SUPPORTING AMERICA'S FINANCIAL SYSTEM 35 (2011), <https://assets1b.milkeninstitute.org/assets/Publication/ResearchReport/PDF/ILC.pdf> [<https://perma.cc/ELG7-KZW2>].

<sup>315</sup> 12 U.S.C. § 1841(a)(2) (2019).

<sup>316</sup> 12 C.F.R. § 225.143 (2019).

<sup>317</sup> 12 U.S.C. § 1841(a) (2019).

<sup>318</sup> 12 C.F.R. § 225.4 (2019).

group transactions involving the bank,<sup>319</sup> and compliance with group-wide capital requirements.<sup>320</sup>

By 2016-17, fifteen of the PRC's largest FCCs maintained an ownership stake in a bank greater than twenty-five percent.<sup>321</sup> Thus, these FCCs would be regulated as BHCs at the holding company level under a U.S.-style regulatory model.<sup>322</sup> Yet importantly, the BHC Act also generally restricts BHCs from controlling non-financial companies.<sup>323</sup> Were a regulatory environment similar to that of the U.S.'s enacted across Mainland China, the structures of these fifteen FCCs would be effectively prohibited.

Surely, some U.S. states have permitted the chartering of non-financial company-owned banks, known as "industrial loan companies" ("ILCs").<sup>324</sup> Yet state laws still require that these institutions obtain federal deposit insurance,<sup>325</sup> a process that necessitates an application to and approval by the U.S. Federal Deposit Insurance Corporation ("FDIC"),<sup>326</sup> which has approved no such applications for non-financial company-owned ILCs since 2004, around the time that Wal-Mart's efforts to establish an ILC were fiercely resisted.<sup>327</sup> By 2017, only six non-financial company-

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<sup>319</sup> 12 U.S.C. § 371c (2019) (the aggregate value of intra-group transactions of the bank and its subsidiaries to one affiliate generally may not exceed ten percent, and to all affiliates, generally may not exceed twenty percent).

<sup>320</sup> 12 CFR § 225, app. A.

<sup>321</sup> See *infra* Appendix B.

<sup>322</sup> 12 U.S.C. § 1841 (2019) (defining bank holding company).

<sup>323</sup> 12 U.S.C. § 1843 (2019). Some relatively minor exemptions do exist for foreign banks, merchant banking investments, and investments in companies that conduct activities closely related to the business of banking. See DIV. OF SUPERVISION AND REGUL., BD. OF GOVERNORS OF THE FED. RESRV. SYS., BANK HOLDING COMPANY SUPERVISION MANUAL §§ 3040, 3907, 3020 (2020).

<sup>324</sup> All six non-financial company-owned ILCs are headquartered either in Utah or Nevada. See JAMES R. BARTH & YANFEI SUN, A NEW LOOK AT THE PERFORMANCE OF INDUSTRIAL LOAN COMPANIES AND THEIR CONTRIBUTION TO THE US BANKING SYSTEM 51 (2018), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3197316](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3197316) [<https://perma.cc/H88X-NT7Z>].

<sup>325</sup> See Arthur E. Wilmarth Jr., *Wal-Mart and the Separation of Banking and Commerce*, 39 CONN. L. REV. 1539, 1544-45 (citing, as an example, UTAH CODE ANN. § 7-8-3(4)(b) (2006)).

<sup>326</sup> In 2006, the FDIC implemented a moratorium on approving commercially owned ILC applications. See *id.* at 1549-50 (citing FDIC, Moratorium on Certain Industrial Loan Company Applications and Notices, 71 FED. REG. 43,482, 43,483 (Aug. 1, 2006)).

<sup>327</sup> Numerous U.S. government officials opposed Wal-Mart's early 2000s effort to establish an ILC. See Wilmarth, *supra* note 325, at 1542. The last non-

owned ILCs remained in the U.S.,<sup>328</sup> five of which each had total assets between \$20 million and \$1.4 billion USD, while one had approximately \$9 billion USD in assets.<sup>329</sup> Some of these ILCs are controlled by primarily non-financial U.S. corporate groups that also control other types of financial firms,<sup>330</sup> but overall, these groups each conduct a level of financial intermediation below the thresholds used in this article's FCC definition.<sup>331</sup>

U.S. companies may concurrently control sizable non-financial businesses and large non-bank financial firms, such as insurers.<sup>332</sup> For example, Berkshire Hathaway, Inc. controls freight rail transportation and energy businesses as well as large insurance companies, and some companies it controls are active in derivatives markets.<sup>333</sup> Yet Berkshire Hathaway operates as a holding company

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financial company-owned ILC approved for federal deposit insurance by the FDIC was Target Bank, which subsequently closed. *See* BARTH, LI, ANGKINAND, CHIANG & LI, *supra* note 314, at 24; DAVID W. PERKINS, CONG. RSCH. SERV., R46489, INDUSTRIAL LOAN COMPANIES (ILCs): BACKGROUND AND POLICY ISSUES 3 (2020), <https://fas.org/sgp/crs/misc/R46489.pdf>. In December 2020, the FDIC eased regulations regarding ILC applications for deposit insurance, and in May 2020, it granted conditional approval of applications for two ILCs each controlled by a financial business, rather than a commercial business. *See id.* at 11-12 (reporting that Nelnet and Square, for which the FDIC approved ILC applications in March 2020, are primarily financial companies).

<sup>328</sup> *See* BARTH & SUN, *supra* note 324, at 51.

<sup>329</sup> *See id.* BMW Bank of North America, ultimately controlled by Germany's BMW AG, had over \$9 billion USD in total assets. *See id.*

<sup>330</sup> For example, Harley-Davidson Inc. is the ultimate parent company of the ILC Eaglemark Savings Bank, as well as a Nevada-based insurance company, Harley-Davidson Insurance Services, Inc. *See id.*; *About Us*, HARLEY-DAVIDSON (2020), <https://www.insurance.harley-davidson.com/about-us> [<https://perma.cc/F5YY-PLDG>].

<sup>331</sup> *See supra* notes 5, 329 and accompanying text.

<sup>332</sup> Broadly, this business structure is not prohibited by federal or state laws. *See generally* Lanny A. Schwartz, Hilary S. Seo, Nancy Lee, Allen Mayer & Elena Belov, So, Now You Own a Broker-Dealer!: Regulatory Considerations for Integrating a Brokerage Firm into a Corporate Group (DavisPolk & Oliver Wyman, 2017), [https://www.davispolk.com/files/2017-09-20\\_so\\_now\\_you\\_own\\_broker\\_dealer.pdf](https://www.davispolk.com/files/2017-09-20_so_now_you_own_broker_dealer.pdf) [<https://perma.cc/CAK2-QC7Z>]; BAIRD WEBEL, CONG. RSCH. SERV., R44046, INSURANCE REGULATION: BACKGROUND, OVERVIEW, AND LEGISLATION IN THE 114<sup>TH</sup> CONGRESS (2016), <https://fas.org/sgp/crs/misc/R44046.pdf> [<https://perma.cc/UHE9-HR77>].

<sup>333</sup> *See* BERKSHIRE HATHAWAY, INC., ANNUAL REPORT 2018, at K-1, K-85 (2019), <https://www.berkshirehathaway.com/2018ar/2018ar.pdf> [<https://perma.cc/RA3B-L6RQ>]; *see also* Ryan Tracy, *Regulators Weigh Whether Berkshire Poses Systemic Risk*, WALL ST. J. (Jan. 23, 2014), <https://www.wsj.com/articles/regulators-considering-whether-berkshire-hathaway-poses-systemic-risk-1390491379> [<https://perma.cc/TD7X-65XB>].

with “essentially no centralized or integrated business functions,” and is largely not involved in the day-to-day operations of firms it controls<sup>334</sup>—it does not meet this Article’s definition of an FCC. Most other large U.S. insurers exist within corporate groups that primarily operate within the financial sector<sup>335</sup> and, accordingly, are not structured like an FCC.

This is perhaps in part because, unlike many of the PRC’s FCCs, which integrate the activities of financial and non-financial businesses,<sup>336</sup> U.S. corporate groups that control insurers face stringent regulation of group-wide activities. Material intra-group transactions by an insurer are subject to regulatory review, and such transactions must be conducted at “fair and reasonable” terms.<sup>337</sup> The U.S. state insurance regulators also have the power to examine risks posed to an insurer by its “ultimate controlling party,” and can examine the books and records of that entity and other intra-group affiliates.<sup>338</sup> State regulators must be notified of changes in major insurer shareholders and can actively scrutinize intra-group activity to ensure that it does not threaten insurer-level capital adequacy.<sup>339</sup>

Notably, applying a U.S.-style regulatory regime to Mainland China’s FCCs would result in the two IFCCs being subject to BHC

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<sup>334</sup> BERKSHIRE HATHAWAY, INC., *supra* note 333, at K-1.

<sup>335</sup> For a list of the largest insurers in the United States by market share, see *Facts + Statistics: Insurance Company Rankings*, INS. INFO. INST., <https://www.iii.org/fact-statistic/facts-statistics-insurance-company-rankings> [https://perma.cc/XM5K-GA4F].

<sup>336</sup> Mainland China’s conglomerate structures often foster internal capital markets. See KON SIK KIM, RELATED PARTY TRANSACTIONS IN EAST ASIA 18-19 (European Corp. Governance Inst., Law Working Paper No. 391/2018, 2018), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3141179](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3141179) [https://perma.cc/R24E-LM4T]. Some large FCCs use funds raised from consumers for insurance products to fuel international expansion into non-financial sectors. James T. Addy, *In China, Insurers Sell Risky Products to Fund Risky Investments, Freaking Out Regulators*, WALL ST. J. (Jan. 11, 2017), <https://www.wsj.com/articles/in-china-insurers-sell-risky-products-to-fund-risky-investments-freaking-out-regulators-1484130601> [https://perma.cc/7E9D-JFZL].

<sup>337</sup> NAT’L ASS’N INS. COMM’RS, INSURANCE HOLDING COMPANY SYSTEM REGULATORY ACT (MODEL #440-4) §5 (2015) [hereinafter Model U.S. State Insurance Holding Company Act], <https://www.naic.org/store/free/MDL-440.pdf> [https://perma.cc/5HME-QCBZ].

<sup>338</sup> *Id.* §6. All fifty U.S. states have passed this model legislation. See WEBEL, *supra* note 332, at 19-20.

<sup>339</sup> *Id.* §5; see also Ctr. for Ins. Pol’y & Research, *Group Supervision*, NAT’L ASS’N INS. COMM’RS (Oct. 1, 2019), [https://content.naic.org/cipr\\_topics/topic\\_group\\_supervision.htm](https://content.naic.org/cipr_topics/topic_group_supervision.htm) [https://perma.cc/3Q9P-RR6C].

Act group-wide regulation,<sup>340</sup> as Tencent and Alibaba (through Ant Group) each control over twenty-five percent of a commercial bank's shares.<sup>341</sup> Although WeChat Pay and Alipay are enormous PBOC-regulated services, and the PBOC serves as custodian for user funds for these payment systems,<sup>342</sup> neither of the ultimate controlling groups were subject to group-wide supervision through much of the 2010s.<sup>343</sup> Conversely, in the United States, debit and credit card networks—the dominant channel for non-cash retail payments—are controlled by BHCs.<sup>344</sup>

ii. *Applying EU Rules Would Subject Some Large FCCs to Strict Group-wide Regulation, and Similarly Structured EU Groups are Rare*

Unlike the United States, the EU generally permits corporate groups to concurrently control banks and sizable non-financial companies. However, an EU-based corporate group that conducts substantial non-financial activities while also controlling two or more types of financial firms can be subject to enhanced group-wide regulatory requirements through “supplementary supervision” as a “mixed financial holding company” if the following conditions set forth in EU Directive 2002/87/EC (as amended) are met<sup>345</sup>:

<sup>340</sup> See *infra* Appendix B and accompanying text; see also 12 U.S.C. § 1841.

<sup>341</sup> See *infra* Appendix B; *supra* notes 175, 193 and accompanying text.

<sup>342</sup> See Chen Jia & He Wei, *PBOC Reins in Funds of Payment Platforms*, CHINA DAILY (Jan. 15, 2019), <https://www.chinadaily.com.cn/a/201901/15/WS5c3d169fa3106c65c34e4671.html> [https://perma.cc/NTQ9-C9WN].

<sup>343</sup> See *supra* notes 269-287 and accompanying text.

<sup>344</sup> See STEVEN T. MNUCHIN & CRAIG S. PHILLIPS, *A FINANCIAL SYSTEM THAT CREATES ECONOMIC OPPORTUNITIES: NONBANK FINANCIALS, FINTECH, AND INNOVATION* 215-17 (2018), <https://home.treasury.gov/sites/default/files/2018-08/A-Financial-System-that-Creates-Economic-Opportunities--Nonbank-Financial-s-Fintech-and-Innovation.pdf> [https://perma.cc/FKR3-C5NQ]. Seventy-four percent of non-cash 2017 U.S. consumer transactions were reportedly conducted by credit and debit cards. *Id.* at 221.

<sup>345</sup> A corporate group that meets the EU definition of “mixed financial holding company” is “subject to supplementary supervision at the level of the . . . conglomerate.” See Council Directive 2002/87, art. 5(2), 2003 O.J. (L 35) [hereinafter *Supplementary Supervision Directive*], <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:02002L0087-20140101&qid=1578025064160&from=EN> [https://perma.cc/8H27-GXBR]; see also Michael Gruson, *Consolidated and Supplementary Supervision of Financial Groups*

(1) An otherwise non-regulated EU entity (“Group X”) either exercises a “dominant influence” over, or directly or indirectly owns twenty percent or more of the voting rights or capital of, at least one banking or investment services firm, and at least one insurance sector company;<sup>346</sup>

(2) The balance sheet total of financial sector entities substantially invested in or controlled by Group X [the “Financial Balance Sheet”] equals over forty percent of Group X’s group-wide balance sheet;<sup>347</sup> and

(3) Either: A) Group X’s insurance company assets and its combined banking and investment services firm assets each, as a share of the Financial Balance Sheet, exceed ten percent, while both Group X’s insurance sector solvency requirements and Group X’s combined banking and investment services sector solvency requirements each equal over ten percent of Group X’s total financial sector solvency requirements,<sup>348</sup> or B) the smaller of Group

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in the European Union 42-43 (Inst. for L. & Fin., Working Paper Series No. 19), [https://www.ilf-frankfurt.de/fileadmin/\\_migrated/content\\_uploads/ILF\\_WP\\_019.pdf](https://www.ilf-frankfurt.de/fileadmin/_migrated/content_uploads/ILF_WP_019.pdf) [<https://perma.cc/2CJ8-TJ7P>] (explaining that “the term *mixed financial holding company* [covers] . . . conglomerates headed by a non-regulated entity holding company”).

<sup>346</sup> A “mixed financial holding company” is a “group” – defined to include “undertakings which consist[] of a parent undertaking, its subsidiaries and the entities in which the parent undertaking or its subsidiaries hold a participation” – that is not headed by a “regulated entity” (including banks, insurers, and funds), but which meets the Supplementary Supervision Directive’s definition of a “financial conglomerate,” one criteria of which is that at least one entity within the group “is within the insurance sector and at least one is within the banking or investment services sector.” Supplementary Supervision Directive, *supra* note 345, arts. 2(12), (14)-(15). “Subsidiaries” are defined as either: (i) “any undertaking over which, in the opinion of the competent authorities, a parent undertaking effectively exercises a dominant influence”; (ii) “all subsidiaries of such subsidiary undertakings”; or (iii) an entity that is a “subsidiary undertaking,” as defined in Article 1 of Council Directive 83/349/EEC – including a company for which another entity “has a majority of the shareholders’ or members’ voting rights.” *Id.* art. 2(10) (citing Council Directive 83/349 of the Council of the European Communities, Seventh Council, Jun. 13, 1983 (as amended, Jan. 7, 2013), art. 1, 2003 O.J. (L 193), <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:01983L0349-20130701&from=EN> [<https://perma.cc/WWV6-DFXJ>]). “Participation” is defined to include “direct or indirect ownership of 20% or more of the voting rights or capital of an undertaking.” Supplementary Supervision Directive, *supra* note 345, art. 2(11).

<sup>347</sup> *Id.* art. 2(14)(b)(i) (citing art. 3(1)).

<sup>348</sup> *Id.* art. 2(14)(b)(iii) (citing art. 3(2)).

X's combined banking and investment services company assets or its insurance sector assets exceeds six billion euros.<sup>349</sup>

"Supplementary supervision" brings about a range of reporting obligations and expanded supervisory authorities over a conglomerate, including group-wide capital requirements,<sup>350</sup> risk concentration reporting,<sup>351</sup> restrictions on intra-group transactions,<sup>352</sup> and risk management standards.<sup>353</sup> Entities that do not meet criteria set forth above but earn a large amount of income from financial activities can still be designated as "mixed financial holding companies" by national regulators, subject to the same "supplementary supervision" regime.<sup>354</sup> Additionally, in the EU, "financial holding companies" – defined to mean a corporate group, the subsidiaries of which are "exclusively or mainly" financial companies, at least one of which is a credit institution or investment firm, "and which is not a mixed financial holding company"<sup>355</sup> – are subject to consolidated group-wide regulation, and notably, the term "mainly" can be understood to mean that over 50 percent of a group's revenues are associated with financial firm subsidiaries.<sup>356</sup>

Notably, in 2016, less than one percent of Eurozone banking assets were held by financial holding companies or mixed financial holding companies that were both: (i) ultimately controlled by a non-financial entity or particular family; and (ii) deemed by

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<sup>349</sup> *Id.* art. 2(14)(b)(iii) (citing art. 3(3)).

<sup>350</sup> *Id.* art. 6

<sup>351</sup> *Id.* art. 7.

<sup>352</sup> *Id.* art. 8.

<sup>353</sup> *Id.* art. 9.

<sup>354</sup> *Id.* art. 3(5) (noting that regulators may "in exceptional cases and by common agreement" use income structure, off-balance sheet activities, or total assets under management thresholds to replace the art. 3(2) balance sheet threshold used to determine if an organization's financial activities are significant under art. 2(14)(b)(iii) and therefore whether it meets the definition of "financial conglomerate," a term that, under art. 2(15), includes "mixed financial holding companies").

<sup>355</sup> Regulation (EU) No. 575/2013 of the European Parliament and the Council of the EU of 26 June 2013, art. 4(1)-(3), 4(20), 2003 O.J. (L 176), [https://eba.europa.eu/sites/default/documents/files/documents/10180/501983/3b700c1c-f136-405d-a4b3-b22ea0a062af/CELEX\\_32013R0575R\(02\)\\_EN\\_TXT.pdf](https://eba.europa.eu/sites/default/documents/files/documents/10180/501983/3b700c1c-f136-405d-a4b3-b22ea0a062af/CELEX_32013R0575R(02)_EN_TXT.pdf) [<https://perma.cc/RVW6-N4B2>]. The term "mainly" can refer to when "50% of the equity, consolidated assets, revenues, personnel or another indicator deemed relevant by [a regulator] are associated with subsidiaries that are institutions or financial institutions." *What is Meant with 'Mainly' in the Definition of 'Financial Holding Company'?*, EBA (Nov. 21, 2014), [https://eba.europa.eu/single-rule-book-qa/-/qna/view/publicId/2014\\_796](https://eba.europa.eu/single-rule-book-qa/-/qna/view/publicId/2014_796) [<https://perma.cc/JS9R-9YTX>].

<sup>356</sup> See Gruson, *supra* note 345, at 2-5.

regulators to be “significant” – generally defined as groups or institutions with over thirty billion euros in assets.<sup>357</sup> By late 2019, just five mixed financial holding companies, as defined above, were directly or indirectly supervised by the European Central Bank.<sup>358</sup> Additionally, several non-financial companies controlled one or more “less significant” financial institutions.<sup>359</sup>

Considering the above-mentioned criteria, were an EU regulatory regime implemented in Mainland China, larger FCCs for which financial sector assets make up a sizable share of the group-wide balance sheet, such as CITIC Group<sup>360</sup> and Tomorrow Group (as it existed in 2017<sup>361</sup>), would likely be subject to “supplementary supervision.” Other large FCCs, as structured in 2017, could also

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<sup>357</sup> By 2016, approximately eighty percent (22,118 billion euros) of Eurozone banking assets (27,699 billion euros) were held by “significant institutions” (“SIs”), of which only four – VW Financial Services, Investar/Argenta Bank, RCI Banque, and Precision Capital/BIL – were over fifty percent owned by a non-financial business or a particular family, accounting for 121 billion, 39 billion, 37 billion, and 33 billion euros in total assets, respectively. Véron, *supra* note 298, at 2, 13-15 (listing total Eurozone banking assets and listing assets of and major shareholders in the Eurozone’s largest SIs). SIs generally include all Eurozone financial groups or institutions with total financial assets exceeding thirty billion euros, although some smaller institutions can also be classified as SIs. Regulation (EU) No. 468/2014 of the European Central Bank of 16 April 2014 (SSM Framework Regulation), art. 50-52, 2014 O.J. (L 141), <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0468&from=EN> [<https://perma.cc/7BN4-TJ8N>].

<sup>358</sup> See EUROPEAN CENT. BANK, LIST OF SUPERVISED ENTITIES (Sep. 2019), <https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.listofsupervisedentities201910.en.pdf> [<https://perma.cc/W4W5-FFRW>].

<sup>359</sup> Examples of banks controlled by manufacturing or telecommunications groups include Airbus Bank GmbH; Mercedes-Benz Bank AG; Mercedes-Benz Bank GmbH; Siemens Bank GmbH; and MOBILIS banque. See *id.* at 27, 34, 43, 69, 79.

<sup>360</sup> In 2018, CITIC Ltd.’s total financial services company assets (7.1 trillion Hong Kong Dollars) equaled well over forty percent of its total, group-wide assets (7.7 trillion Hong Kong Dollars). CITIC 2018 ANNUAL REPORT, *supra* note 288, at 2. Additionally, the total assets of both an insurer fifty percent controlled by CITIC Ltd. and CITIC Bank each exceeded over six billion euros. *Id.* at 10, 18. For 2017 currency conversion rates, see *Exchange Rates*, *supra* note 18, and accompanying text.

<sup>361</sup> At year-end 2016, the assets of banks and insurance companies controlled by Tomorrow Group totaled 1.3 trillion and 796 billion yuan (approximately 104 billion euros), respectively, while Tomorrow Group’s total financial sector company assets equaled over three trillion yuan. See New Fortune 2017 Reports, *supra* note 197. For 2017 currency conversion rates, see *Exchange Rates*, *supra* note 18 and accompanying text. A 2017 report describing the conglomerate’s businesses suggests that well over forty percent of Tomorrow Group’s assets were likely financial sector companies at the time. See New Fortune FCC history, *supra* note 137.

seemingly be classified as a “financial holding company” under the EU’s regulatory approach, and would thus be subject to group-wide supervision.

It is doubtful that the business mix and structure of the PRC’s two IFCCs would be permitted in the EU. As of 2019, only nine internet companies had been granted financial licenses by national regulators in the Eurozone, and each of these licenses was quite limited in scope.<sup>362</sup> Moreover, the European Central Bank is reportedly considering an even stricter regulatory regime for internet companies that offer financial services.<sup>363</sup>

*iii. Under the Japanese Model, Some FCCs Could Operate, but the Largest Would Likely be Prohibited*

Japan’s approach towards the regulation of companies structured similarly to Mainland China’s FCCs is also more accommodating relative to the U.S.’s. Corporate groups that control various sizable financial and non-financial companies are subject to differing degrees of regulation by the Financial Supervision Authority (“FSA”)—Japan’s banking, insurance, and securities market regulator—depending on the facts and circumstances surrounding the relationship between a corporate group and the financial companies it controls.

In Japan, if one company owns over fifty percent of shareholder voting rights of another company, then the latter company is considered a subsidiary of the former.<sup>364</sup> A holding company is defined as “a company for which the ratio of the total acquisition value (or other value if it is so listed in the latest balance sheet) of the shares of subsidiary companies to the total assets of said company exceeds fifty percent.”<sup>365</sup> Companies that meet this

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<sup>362</sup> See FIN. STABILITY BD., *supra* note 8, at 7.

<sup>363</sup> See Martin Arnold, *EU Regulators Monitor Big Tech’s Financial Services Foray*, FIN. TIMES (Nov. 11, 2018), <https://www.ft.com/content/27f965da-e5bf-11e8-8a85-04b8afea6ea3> [<https://perma.cc/4HWH-6YJB>].

<sup>364</sup> Banking Act (Act No. 59 of June 1, 1981), art. 2(8), <https://www.fsa.go.jp/common/law/bank01.pdf> [<https://perma.cc/4MNX-QNWX>] (unofficial English translation).

<sup>365</sup> Act on Prohibition of Private Monopolization and Maintenance of Fair Trade (Act No. 54 of April 14, 1947), art. 9(4)(i), [https://www.jftc.go.jp/en/policy\\_enforcement/cartels\\_bidriggings/anti\\_cartel\\_files/The\\_Antimonopoly\\_Act.pdf](https://www.jftc.go.jp/en/policy_enforcement/cartels_bidriggings/anti_cartel_files/The_Antimonopoly_Act.pdf) [<https://perma.cc/8DKM-M7XD>] (unofficial English translation).

definition of a holding company and have at least one bank or insurance company subsidiary are defined as “bank holding companies” (“Japanese BHCs”) and “insurance holding companies” (“Japanese IHCs”), respectively,<sup>366</sup> and their business is restricted to managing subsidiaries under their control.<sup>367</sup>

Certain FCCs—as defined in this Article—can exist under Japan’s regulatory model. An example of such a company is Rakuten, Inc., which engages in a variety of e-commerce and internet services businesses, and also controls large financial companies.<sup>368</sup> Yet although one of its subsidiaries controls a bank and insurance companies,<sup>369</sup> Rakuten, Inc. is not regulated as a Japanese BHC or IHC because it does not meet the Japanese legal definition of a holding company.<sup>370</sup> Nevertheless, in 2017, almost forty percent of Rakuten, Inc.’s total sales reportedly came from financial sector activities.<sup>371</sup> Large non-financial conglomerates can also directly control a Japanese BHC or IHC—for example, Sony Corporation owns over sixty-five percent of Sony Financial Holdings, which controls a bank and insurance companies.<sup>372</sup>

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<sup>366</sup> Banking Act (Act No. 59 of June 1, 1981), art. 2(13), <https://www.fsa.go.jp/common/law/bank01.pdf> [<https://perma.cc/4MNX-QNWX>] (English translation); Insurance Business Act (Act No. 105 of June 7, 1995), art. 2(16), <https://www.fsa.go.jp/common/law/ins01.pdf> [<https://perma.cc/WK5Y-5E64>] (unofficial English translation).

<sup>367</sup> Banking Act (Act No. 59 of June 1, 1981), art. 52-21, <https://www.fsa.go.jp/common/law/bank01.pdf> [<https://perma.cc/4MNX-QNWX>] (English translation); Insurance Business Act (Act No. 105 of June 7, 1995), art. 271-21, <https://www.fsa.go.jp/common/law/ins01.pdf> [<https://perma.cc/WK5Y-5E64>] (unofficial English translation).

<sup>368</sup> See RAKUTEN, ANNUAL SECURITIES REPORT (“YUKASHOKEN-HOKOKUSHO”): FISCAL YEAR ENDED DECEMBER 31, 2017 AND 2018, at 6-7 (2019).

<sup>369</sup> *Announcement of Agreement Regarding Group Reorganization*, RAKUTEN (Feb. 12, 2019), [https://global.rakuten.com/corp/news/press/2019/0212\\_01.html](https://global.rakuten.com/corp/news/press/2019/0212_01.html) [<https://perma.cc/DHB8-5KFS>].

<sup>370</sup> For Japan’s legal definition of a holding company, *see supra* notes 364-365, and accompanying text. The total acquisition value of the shares of Rakuten’s subsidiaries is worth less than half of its total company assets. *See* RAKUTEN, *supra* note 368, at 104, 255 (reporting Rakuten, Inc.’s total assets and its capital investments into its subsidiaries).

<sup>371</sup> *See* Minami Funakoshi & Sam Nussey, *Rakuten Seeks to Boost Financial Services with \$415 Million Asahi Fire & Marine Deal*, REUTERS (Jan. 29, 2018), <https://www.reuters.com/article/us-japan-rakuten/rakuten-seeks-to-boost-financial-services-with-415-million-asahi-fire-marine-deal-idUSKBN1FH0ZX> [<https://perma.cc/4DNH-349H>].

<sup>372</sup> *Sony Financial Group Structure*, SONY FIN. HOLDINGS (Oct. 1, 2020), <https://www.sonyfh.co.jp/en/company/structure.html> [<https://perma.cc/9R3Q-XMNE>].

Japanese non-financial business entities that control financial companies are nevertheless subject to FSA regulations. In Japan, a “major shareholder” of a bank or insurer is generally defined to include a legal person who controls twenty percent or more of voting shares of a bank, insurer, BHC, or IHC.<sup>373</sup> Becoming a “major shareholder” with the intent to remain one for over a year requires regulatory approval,<sup>374</sup> and relative to Mainland China, in recent years, Japan more strictly monitored transfers of bank shares.<sup>375</sup> Additionally, a “major shareholder” can be required to provide regulators with: (i) access to materials that can be used to evaluate the state of a bank’s or insurer’s business;<sup>376</sup> and (ii) the ability to perform on-site inspections of the “major shareholder.”<sup>377</sup> The FSA can also order the “major shareholder” to take measures to ensure the “sound and appropriate management of the business of” a bank

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<sup>373</sup> Banking Act (Act No. 59 of June 1, 1981), arts. 2(9)-(10), <https://www.fsa.go.jp/common/law/bank01.pdf> [<https://perma.cc/4MNX-QNWX>] (English translation); Insurance Business Act (Act No. 105 of June 7, 1995), arts. 2(13)-(14), <https://www.fsa.go.jp/common/law/ins01.pdf> [<https://perma.cc/WK5Y-5E64>] (unofficial English translation).

<sup>374</sup> Banking Act (Act No. 59 of June 1, 1981), art. 52-9(1)-(2), <https://www.fsa.go.jp/common/law/bank01.pdf> [<https://perma.cc/4MNX-QNWX>] (English translation); Insurance Business Act (Act No. 105 of June 7, 1995), arts. 271-10(1)-(2), <https://www.fsa.go.jp/common/law/ins01.pdf> [<https://perma.cc/WK5Y-5E64>] (unofficial English translation).

<sup>375</sup> Compare IMF, *Japan: Financial Sector Assessment Program: Detailed Assessment of Observance of Basel Core Principles for Effective Banking Supervision*, Country Report No. 17/282, at 56-58 (2017) (observing that Japan is “less than compliant” but not “materially non-compliant” with international standards agreed upon by central banks related to monitoring the transfer of ownership of shares in banks) with IMF, *supra* note 222 and accompanying text (explaining that in 2017, the PRC was “materially non-compliant” with these standards).

<sup>376</sup> Banking Act (Act No. 59 of June 1, 1981), art. 52-11, <https://www.fsa.go.jp/common/law/bank01.pdf> [<https://perma.cc/4MNX-QNWX>] (English translation); Insurance Business Act (Act No. 105 of June 7, 1995), arts. 271-12, <https://www.fsa.go.jp/common/law/ins01.pdf> [<https://perma.cc/WK5Y-5E64>] (unofficial English translation).

<sup>377</sup> Banking Act (Act No. 59 of June 1, 1981), art. 52-12, <https://www.fsa.go.jp/common/law/bank01.pdf> [<https://perma.cc/4MNX-QNWX>] (English translation); Insurance Business Act (Act No. 105 of June 7, 1995), arts. 271-13, <https://www.fsa.go.jp/common/law/ins01.pdf> [<https://perma.cc/WK5Y-5E64>] (unofficial English translation).

or insurer,<sup>378</sup> or require the “major shareholder” to divest.<sup>379</sup> Most of Mainland China’s FCCs would be subject to these rules under a Japanese-style regulatory regime.<sup>380</sup>

Moreover, Japan’s Antimonopoly Act prohibits the establishment of a “company which constitutes an excessive concentration of economic power,” thus limiting the scope of any conglomerate’s business activities.<sup>381</sup> Japan’s Fair Trade Commission (“JFTC”) sets definitions for such companies, one of which is a company that controls directly, or through a subsidiary or a “virtual subsidiary,”<sup>382</sup> both: i) a financial company with over fifteen trillion yen in total assets; and ii) a non-financial business with total assets exceeding over 300 billion yen.<sup>383</sup> It seems that by 2017-18 CITIC Group met this definition,<sup>384</sup> and several other large

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<sup>378</sup> Banking Act (Act No. 59 of June 1, 1981), art. 52-14, <https://www.fsa.go.jp/common/law/bank01.pdf> [https://perma.cc/4MNX-QNWX] (English translation); Insurance Business Act (Act No. 105 of June 7, 1995), arts. 271-15, <https://www.fsa.go.jp/common/law/ins01.pdf> [https://perma.cc/WK5Y-5E64] (unofficial English translation).

<sup>379</sup> Banking Act (Act No. 59 of June 1, 1981), art. 52-15, <https://www.fsa.go.jp/common/law/bank01.pdf> [https://perma.cc/4MNX-QNWX] (English translation); Insurance Business Act (Act No. 105 of June 7, 1995), arts. 271-16, <https://www.fsa.go.jp/common/law/ins01.pdf> [https://perma.cc/WK5Y-5E64] (unofficial English translation).

<sup>380</sup> At least twenty-one FCCs own over twenty percent of a bank while at least seventeen FCCs own over twenty percent of an insurer. See New Fortune 2017 Reports, *supra* note 197; see *infra* Appendix B.

<sup>381</sup> FAIR TRADE COMM’N, GUIDELINES CONCERNING COMPANIES WHICH CONSTITUTE AN EXCESSIVE CONCENTRATION OF ECONOMIC POWER, Preface (Nov. 12, 2002), [https://www.jftc.go.jp/en/legislation\\_gls/imonopoly\\_guidelines\\_files/Company\\_Concentration.pdf](https://www.jftc.go.jp/en/legislation_gls/imonopoly_guidelines_files/Company_Concentration.pdf) [https://perma.cc/2RJD-EYR7].

<sup>382</sup> The guidelines generally define a subsidiary as a “company in Japan in which greater than [fifty] percent of its total voting right . . . given to all the stock holders (or all the individual members) is owned by another company.” *Id.* § 1(1)(b). A “virtual subsidiary” is defined as a “company in Japan in which greater than twenty-five percent and fifty percent or less of its total voting right is owned by the company (including those owned by its subsidiaries . . .) and in which its voting rights are the largest among all the holders.” *Id.* § 1(1)(c).

<sup>383</sup> *Id.* § 2(3) (detailing the JFTC’s Type 2 definition of a group that constitutes an “excessive concentration of economic power”).

<sup>384</sup> In 2018, total assets of CITIC Ltd.’s financial services, resources and energy, manufacturing, engineering contracting, and real estate businesses were 7.1 trillion, 132 billion, 135 billion, 55 billion, and 155 billion Hong Kong Dollars, respectively. CITIC 2018 ANNUAL REPORT, *supra* note 288, at 2. In 2018, 1 Hong Kong dollar equaled about 14.1 yen. See *Exchange Rates*, *supra* note 18.

FCCs did as well.<sup>385</sup> Accordingly, these FCCs would likely be subject to regulatory scrutiny and could have been prohibited from forming under a Japan-style regulatory regime.

Another definition used by JFTC is a company group with total assets exceeding 15 trillion yen that controls five or more companies, each of which has revenue exceeding 600 billion yen and operates in a different business area.<sup>386</sup> Business areas are narrowly determined using the Japan Standard Industrial Classification system<sup>387</sup> — examples include “building materials,” “iron and steel products,” and “banks.”<sup>388</sup> Under a third definition, the 15 trillion yen total assets threshold is removed and replaced with conditions that: (i) each of five companies controlled by a conglomerate maintains a 10 percent or higher “sales share” in its respective field of business, or just three, depending on if one company “possesses a substantial position over a principal field of business with extremely vast scale”; and (ii) fields of business in which the company engages are “interrelated.”<sup>389</sup> Financial services such as banking, credit cards, insurance, and securities business are considered interrelated.<sup>390</sup> Thus, if Japan’s regulatory model were applied in Mainland China, Alibaba could potentially be considered a company with “excessive

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<sup>385</sup> In 2017, three other primarily non-financial FCCs (China Everbright Group, China Merchants Group, and Evergrande Group) controlled a bank with over 900 million yuan in assets via an over twenty-five percent ownership stake, and thus likely met this definition. *See supra* note 382 and accompanying text (explaining the JFTC’s “virtual subsidiary” threshold); *see infra* Appendix B; *Exchange Rates, supra* note 18 and accompanying text (providing a 16.595 yen to yuan 2017 conversion rate).

<sup>386</sup> FAIR TRADE COMM’N, *supra* note 381, § 2(2) (detailing the JFTC’s Type 1 definition of a group that constitutes an “excessive concentration of economic power”).

<sup>387</sup> *Id.*, § 2(2)(d) (explaining that, with regards to the JFTC’s Type 1 definition, “[p]rinciple fields of business’ shall be types of industries which are included in the 3-digit classifications of the Japan Standard Industrial Classification and in which shipment volume exceeds 600 billion”).

<sup>388</sup> *See Industrial Classification used in the 2016 Economic Census for Business Activity*, STAT. BUREAU OF JAPAN, <https://www.stat.go.jp/english/data/e-census/2016/industry.html> [<https://perma.cc/DD48-NM63>].

<sup>389</sup> FAIR TRADE COMM’N, *supra* note 381, § 2(4) (detailing the JFTC’s Type 3 definition of a “company that causes an excessive concentration of economic power”). *See also* Eric C. Sibbitt, *A Brave New World for M&A of Financial Institutions in Japan: Big Bang Financial Deregulation and the New Environment for Corporate Combinations of Financial Institutions*, 19 U. PA. J. INT’L ECON. L. 965, 1003-1006 (1998) (explaining that “interrelatedness refers to a situation in which there are trade relations among different fields of business, and goods or services from different fields of business are complementary to or substitutes for one another”).

<sup>390</sup> FAIR TRADE COMM’N, *supra* note 381, § 2(3), list 2.

concentration of economic power” according to this third definition.<sup>391</sup>

*c. Some Large FCCs are Uniquely Characterized by Complex Cross-Shareholding and Pyramid Structures in Which Intra-Group Transactions are Prevalent*

As Part III explained, some of Mainland China’s FCCs grew to be characterized by the widespread, combined usage of pyramid structures and cross-shareholdings within mixed conglomerates that engage in high levels of intra-group transactions. Historically, pyramid structures were prevalent in South and East Asia – particularly Mainland China – as well as some European countries, but are now quite rare in much of the EU, Japan, and the United States.<sup>392</sup> In the United States and Europe, instances of intra-group cross-shareholdings are not common, and cross-shareholdings are on the decline in Japan as well, despite being prevalent in the past.<sup>393</sup>

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<sup>391</sup> In 2018, Alipay accounted for twenty-four percent of third-party internet payments and Ant Financial accounted for over twenty-five percent of MMF assets. See YOUNGER, YAO, LEI & LUK, *supra* note 206, at 7, 9. Data shows that Alibaba also accounts for over half of internet retail sales. See *Alibaba, JD.com Lead in China, but a Few Others Are Making Dents, Too*, EMARKETER (Jun. 2, 2019), <https://www.emarketer.com/content/alibaba-jd-com-lead-in-china-but-a-few-of-hers-are-making-dents-too> [<https://perma.cc/2K8U-6VE9>]. A close “trade relationship” between these financial businesses and Alibaba’s e-commerce business may, under the Japanese regulatory approach, arguably exist. See FAIR TRADE COMM’N, *supra* note 381, § 2(4)(d)(i) (categorizing “trade relationships” as a way in which fields of business can be “interrelated”).

<sup>392</sup> See Bubchuck, Kraakman & Triantis, *supra* note 225, at 7; INSTITUTIONAL S’HOLDER SERVS., REPORT ON THE PROPORTIONALITY PRINCIPLE IN THE EUROPEAN UNION 27 (2007), [https://ecgi.global/sites/default/files/final\\_report\\_en.pdf](https://ecgi.global/sites/default/files/final_report_en.pdf) [<https://perma.cc/FE3T-7JEW>] (finding that some European companies use pyramid structures); Jason W. Howell, *The Dual Class Stock Structure in the United States: A New Dataset and an Examination of Firms Who Leave the Structure 29* (May, 2010) (Ph.D. Dissertation, University of Georgia), [https://getd.libs.uga.edu/pdfs/howell\\_jason\\_w\\_201005\\_phd.pdf](https://getd.libs.uga.edu/pdfs/howell_jason_w_201005_phd.pdf) [<https://perma.cc/CJN4-32BH>] (observing that pyramid structures are rare in the U.S. but common in other countries); Kim, *supra* note 336, at 13 (finding that the “pyramidal ownership structure . . . is relatively rare in the Japanese economy”).

<sup>393</sup> See Howell, *supra* note 392, at 29; INSTITUTIONAL S’HOLDER SERVS., *supra* note 392, at 48; Tatsuhiro Shirakabe, *Corporate Japan Sheds More Cross-Shareholdings*, NIKKEI ASIA (Sep. 5, 2019), <https://asia.nikkei.com/Business/Business-trends/Corporate-Japan-sheds-more-cross-shareholdings> [<https://perma.cc/HWW8-KYGJ>].

Indeed, between 1996 and 2011, in response to a range of policy reforms that facilitated more diversified ownership structures, overall shareholdings by Japanese banks and insurers in other companies dropped precipitously from over thirty-five percent to about seven percent of publicly-traded equity shares.<sup>394</sup> Overall, cross-shareholdings equaled just ten percent of Japan's 2018 stock market capitalization, versus thirty-four percent in 1990.<sup>395</sup> Certainly, some regional banks in Japan still maintain significant cross-shareholding levels.<sup>396</sup> Yet overall, cross-shareholdings are continuing to decline in Japan, reportedly due to recently implemented revisions to its corporate governance code, as well as enhancements to securities regulations, which require that each publicly-listed company disclose its sixty largest investments in other companies and state whether any are cross-shareholdings.<sup>397</sup> These rules aim to help ensure that ownership relationships are better understood not only for publicly-traded large banks, but also at most of Japan's regional banks, of which approximately three-quarters are publicly-listed.<sup>398</sup>

Thus, despite the modest persistence of cross-shareholdings in Japan, Japanese mixed conglomerates are not structured in a way that resembles those of Mainland China's more complex FCCs, which exhibit both cross-shareholding and pyramid structures, as well as relatively high levels of preferential transactions between financial and non-financial affiliates. Indeed, by 2008, survey data showed that significant transactions between related parties—

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<sup>394</sup> See Hideaki Miyajima & Takaaki Hoda, *Ownership Structure and Corporate Governance: Has an Increase in Institutional Investors' Ownership Improved Business Performance?* 11 POL'Y RES. INST., MIN. OF FIN., JAPAN, PUB. POL'Y REV. 361, 367 (2015), [https://www.mof.go.jp/english/pri/publication/pp\\_review/ppr029/ppr029a.pdf](https://www.mof.go.jp/english/pri/publication/pp_review/ppr029/ppr029a.pdf) [https://perma.cc/8RTJ-ZJ3T].

<sup>395</sup> See Shirakabe, *supra* note 393.

<sup>396</sup> See Leo Lewis, *Japan's Cross-Shareholding Still a Tough Habit to Break*, FIN. TIMES (Nov. 17, 2017), <https://www.ft.com/content/4a89c3a0-cadc-11e7-aa33-c63fdc9b8c6c> [https://perma.cc/5MNE-YUJQ].

<sup>397</sup> See Satoshi Uchida, *Governance Demands Chip Away at Japanese Cross-Shareholdings*, NIKKEI ASIA (Jul. 8, 2019), <https://asia.nikkei.com/Business/Business-trends/Governance-demands-chip-away-at-Japanese-cross-shareholdings> [https://perma.cc/AW56-K379].

<sup>398</sup> Seventy-nine regional banks are publicly listed in Japan. See *Regional Banks in Trouble*, JAPAN TIMES (May 11, 2019), <https://www.japantimes.co.jp/opinion/2019/05/11/editorials/regional-banks-trouble/> [https://perma.cc/7GFQ-5WMQ]. In total, Japan has 102 regional banks. *List of Licensed (registered) Financial Institutions*, FSA, <https://www.fsa.go.jp/en/regulated/licensed/index.html> [https://perma.cc/67HX-X3EE] (reporting data from April 2019 and January 2020).

including intra-group transactions, a source of risk for cross-shareholding structures<sup>399</sup> – occurred at less than four percent of Japan’s listed companies.<sup>400</sup> Moreover, transactions between banks and a “related person” not conducted according to prevailing market terms are generally prohibited in Japan, and the term “related person” is defined to include: (i) a bank’s subsidiary or affiliate; (ii) a bank’s major shareholder(s) as well as subsidiaries or affiliates of the major shareholder(s); and (iii) any entity holding over fifty percent of voting rights in the bank and its subsidiaries or affiliates.<sup>401</sup> Conversely, some research finds that by 2015, over ninety percent of listed firms in Mainland China engaged in related party transactions.<sup>402</sup>

EU mixed conglomerates also are not characterized by both pyramid structures and cross-shareholdings, as well as high levels of affiliated transactions. Certainly, in some EU countries such as Spain, pyramid structures are not rare,<sup>403</sup> and can be used to control financial companies.<sup>404</sup> Yet the low, twenty percent investment threshold set by the EU’s Directive 2002/87/EC for determining whether or not a non-financial conglomerate controls a financial institution takes into account whether “dominant influence” exists and both indirect and direct ownership.<sup>405</sup> Thus, from the perspective of whether supplemental supervision is applicable, it appears that there is little difference between using pyramid structures to acquire a bank, insurer, or investment company in the EU versus more direct approaches. Moreover, although EU

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<sup>399</sup> See *supra* notes 252-254 and accompanying text.

<sup>400</sup> See OECD, RELATED PARTY TRANSACTIONS AND MINORITY SHAREHOLDER RIGHTS 31 (2012).

<sup>401</sup> See TATSUO TEZUKA, TAKU ISHIZU, MASAO MORISHITA, SUSUMU TANIZAWA, JAPAN *in* BANKING REGULATION IN 27 JURISDICTIONS WORLDWIDE 77 (Craig Wasserman ed., 2009), [https://www.jurists.co.jp/sites/default/files/tractate\\_pdf/en/200905\\_tezuka\\_is\\_hizu\\_morishita\\_tanizawa.pdf](https://www.jurists.co.jp/sites/default/files/tractate_pdf/en/200905_tezuka_is_hizu_morishita_tanizawa.pdf) [<https://perma.cc/J6CK-Y5XP>]. For definitions of the terms “subsidiary” and “major shareholder,” see *supra* notes 364, 373 and accompanying text.

<sup>402</sup> See Kim, *supra* note 336, at 19 n.62.

<sup>403</sup> See INSTITUTIONAL S’HOLDER SERVS., *supra* note 392, at 27 (finding meaningful prevalence of pyramid ownership structures in Belgium, France, Spain, Luxembourg, and Italy).

<sup>404</sup> See Valentín Azofra & Marcos Santamaría, *Ownership, Control, and Pyramids in Spanish Commercial Banks*, 35 J. BANKING & FIN. 1464 (2011), <https://www.sciencedirect.com/science/article/abs/pii/S0378426610004218> [<https://perma.cc/J6CK-Y5XP>].

<sup>405</sup> See *supra* notes 345-49 and accompanying text.

financial conglomerates can be quite complex (with hundreds of business units), once a corporate group is subject to supplemental supervision pursuant to Directive 2002/87/EC, regulators pay particularly close attention to risks such as multiple leveraging and intra-group conflicts-of-interest.<sup>406</sup>

## V. CONCLUSION

The large role that FCCs play across Mainland China's financial system is globally unparalleled, and presents its regulators with a multifaceted challenge. The complex ownership structures that have emerged within FCCs are difficult to understand, and can create opaque interconnectivity not only within corporate groups but between them. As a result, it may be very difficult to know whether a particular FCC in Mainland China is adequately capitalized, and what impacts its failure would have on the economy.

FCCs emerged in Mainland China not only due to Leninist influences and the embrace of cross-sector integration that gave rise to the first SFCCs, but also thanks to unclear definitions in regulations and laws, insufficiently rigorous supervision, regulatory arbitrage precipitated by gaping legal loopholes, and frequent case-by-case exceptions throughout the 2000s that enabled FCCs to grow through investments in banks and insurers. Simple, time-tested approaches to financial markets regulation, such as ensuring the regular and accurate disclosure of meaningful intra-group transactions and bank and insurer shareholders, as well as implementing sound supervisory frameworks to prevent multiple leveraging, would go quite far in mitigating potential economic risks posed by Mainland China's FCCs. While some recent efforts by regulators may align with these objectives, it seems that late 2020 PBOC regulations have legitimized certain FCC structures, suggesting that FCCs may remain a unique phenomenon of the Chinese financial system for years to come.

Indeed, as this Article's application of the EU's, Japan's, and the United States' respective regulatory frameworks to Mainland

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<sup>406</sup> See Valentina Peleckiene, Kęstutis Peleckis & Gitana Dudzevičiūtė, *New Challenges of Supervising Financial Conglomerates*, 5 INTELL. ECON. 298, 305 (2011), <https://pdfs.semanticscholar.org/c23f/90b99f9730f857d6b9b07440139abcd1c8ca.pdf>.

China's FCCs makes clear, the complexity, size, and cross-sector structures of some of these groups remain far outside the bounds of international norms, and even simple approaches to adequately supervising FCCs may not be easy to implement. This analysis also illustrates important trade-offs as new regulatory approaches for FCCs are considered. More broadly, this Article should serve as a wake-up call to regulators and market participants to be concerned about risks caused by Mainland China's FCCs, and will help those seeking to better understand how the structures and activities of these entities could change as new regulations are promulgated.

## VI. APPENDICES

APPENDIX A: THIRTY-FOUR FCCs (2017)<sup>407</sup>

FCC name	Selected major non-financial business line(s)	Est. number of financial companies controlled
Tomorrow Group	energy; media; technology; tourism; real estate	22
Ping An Group	e-commerce; healthcare; infrastructure; real estate; technology	9
HNA Group	aviation; tourism; real estate	8
CITIC Group	aviation; construction; communications; energy; infrastructure; manufacturing; power generation; metals and minerals production; real estate; transportation	7
China Everbright Group	energy; healthcare; pharmaceuticals; property management; real estate; tourism	7
Alibaba	communications; e-commerce; logistics; information technology	6
China Merchants Group	construction; consumer products; energy; healthcare; logistics; infrastructure; manufacturing; real estate	6
State Grid Corp. of China	power transmission	6
Anbang Group	real estate; tourism	5
Aviation Industry Corp. of China	aviation; manufacturing; military	5
China Huaneng Group	power generation; technology; transportation	5
China Minmetals	metals and minerals production; real estate; transportation	5
China Oceanwide Holdings Group	energy; information technology; real estate; tourism	4
Funde Group	energy; entertainment; logistics; real estate	4
China National Petroleum Corporation	energy; oil/gas production	4
Wanxiang Group	energy; manufacturing	4
Baoneng Group	logistics; manufacturing; real estate; tourism	3
China Baowu Steel Group	energy; steel production	3
China Oil & Foodstuffs Corp.	agricultural products; foodstuffs production; real estate	3
China Resources	construction; consumer products; oil/gas production; power generation; real estate; pharmaceuticals	3
Huaxin Huitong Group	logistics; information technology; real estate; tourism	3
Tencent	communications; e-commerce; entertainment; logistics; information technology	3

<sup>407</sup> For the methodology used to develop this list of FCCs and determine the number of financial companies controlled by each FCC, *see supra* notes 5, 197 and accompanying text. This article only considers nine types of financial companies. *See supra* note 5 and accompanying text. Information on non-financial business lines was compiled using company websites and the following financial data and information sources: Bloomberg; Reuters; TianYanCha; Wind.

China National Offshore Oil Corp.	energy; power generation; oil/gas production	2
China Railway Group	infrastructure; real estate; manufacturing; transportation	2
China Zhongwang Group	manufacturing; metals and minerals production	2
Evergrande Group	construction; consumer products; foodstuffs production; healthcare; manufacturing; real estate; tourism	2
Haier Group	consumer products; manufacturing	2
Hongda Group	chemicals and metals production; logistics; real estate; transportation	2
JuneYao Group	aviation; consumer products; foodstuffs production; tourism; transportation	2
Nanshan Group	aviation; construction; consumer products; manufacturing; metals and minerals production; real estate; tourism	2
Shougang Group	construction; logistics; metals and minerals production; real estate; steel production	2
Sinochem Group	agricultural products; chemicals and metals production; energy	2
State Power Investment Corp.	energy; metals and minerals production; power generation	2
Suning Commerce Group	consumer products; e-commerce; logistics	2

APPENDIX B: TWENTY-ONE FCCs WITH A SIGNIFICANT  
MAINLAND CHINA BANK INVESTMENT (2016-17)<sup>408</sup>

FCC name	Name of bank controlled ("C") or influenced ("I") by FCC as of 2016	Q2 2017 Banking Assets (yuan)	FCC's estimated % of bank shares
China Merchants Group	China Merchants Bank (C)	6,199,690,000,000	29.97%
CITIC Group	CITIC Bank (C)	5,651,216,000,000	65.97%
Funde Holding Group	Shanghai Pudong Development Bank (I)	5,915,395,000,000	20.68%
China Everbright Group	China Everbright Bank (C)	4,033,546,000,000	29.00%
Ping An Group	Ping An Bank (C)	3,092,142,000,000	57.94%
Shougang Group	Huaxia Bank (I)	2,423,098,000,000	20.28%
State Grid Corp. of China	China Guangfa Bank (I)	1,992,227,000,000	20.00%
Tomorrow Group	Baoshang Bank (C)	546,615,738,304	37.56%
	Harbin Bank (C)	546,927,086,000	25.93%
	Guangdong Huaxing Bank (C)	122,867,736,462	27.02%
	Bank of Weifang (C)	103,627,719,616*	38.86%
	Tai'an Bank (C)	60,421,695,162	45.91%
	Shenyang Rural Commercial Bank (C)	39,814,000,000**	30.00%
Evergrande Group	Shengjing Bank (C)	938,711,110,000	27.24%
Anbang Group	Chengdu Rural Commercial Bank (C)	671,305,946,542	35.00%
China National Petroleum Corp.	Bank of Kunlun (C)	301,192,438,996	77.10%
Haier Group	Bank of Qingdao (C)	281,976,231,000	19.06%
China Oil & Foodstuffs Corp.	Longjiang Bank (I)	245,573,282,900	20.00%
China Resources	China Resources Bank (C)	142,236,495,724	75.33%
China Zhongwang Group	Bank of Liaoyang (C)	126,343,524,103	31.46%
Nanshan Group	Yantai Bank (C)	74,305,251,158	34.86%
China Minmetals	Mianyang City Commercial Bank (C)	71,126,740,368	20.00%
Alibaba	MYbank (C)	61,522,357,612*	30.00%
Tencent	WeBank (C)	51,995,491,724*	30.00%
HNA Group	Yingkou Coastal Bank (C)	50,744,737,928	24.80%
JuneYao Group	Shanghai Huarui Bank (C)	30,983,499,686	30.00%

<sup>408</sup> For more information on how this Appendix was developed, see *supra* notes 197, 200 and accompanying text. A "\*" designates that due to mid-year data availability issues, year-end 2016 data, as reported by Wind, was used rather than Q2 2017 banking asset data. A "\*\*" designates that due to data availability issues, 2015 data on banking assets, as reported by New Fortune, was used.