

**The History of Corporate Ownership in China**

(First Draft, 19 September, 2002)

William Goetzmann, Yale University

Elisabeth Köll, Case Western Reserve University

**Introduction**

The historical development of corporate enterprises in China is particularly interesting in the context of the current trend towards the globalization of Western-style corporate governance. Roughly a century ago, during the last great period of globalization, China’s Imperial government promulgated a set of laws that created modern, Western-style limited liability corporations. The government was clearly responding to competition from foreign business enterprise in China, however, the new corporate structure collided in interesting ways with an existing business framework based on family firms and state patronage. In this paper, we examine the emergence of corporate ownership in China from the final decades of the Qing empire in the late 19<sup>th</sup> century to the early Republican period in the 1910s and 1920s. By analyzing the actual process of incorporation, the development of the legal and financial environment, and the role of the state, we ask whether this “top-down” approach, i.e. the central government laying out a legal and institutional framework for corporate enterprises based on Western models with the expectation that it will work as it did in the West, is a viable solution to the creation of corporate ownership, structures, and institutions in an environment traditionally dominated by family business and business under state patronage. Based on business records from turn-of-the-century Chinese corporations, this paper argues that the government’s “top-

down” approach created a framework which only insufficiently promoted the system of corporate capitalism. As our analysis shows, Chinese business institutions essentially imitated the form of Western corporate institutions without fully installing essential structures and features of the corporate system according to our Western interpretation.

This paper is structured as follows. After discussing the changing role of government governance in companies in the 19<sup>th</sup> century in the first part of this paper, the second part is dedicated to the Company Law in 1904 and its impact on the development of corporate business structures. In the third section we examine the issue of control and ownership by exploring the role of shareholders, their rights and representation, investment opportunities, capital markets, investment behavior, and the role of the government. The conclusion will discuss the question as to what extent specific social and institutional factors prevented historically the acceptance of a corporate capitalist system in Chinese business as ordered by the government. Considering the “top-down” approach of the current Chinese government and the governments of other emerging markets from around the world, this discussion will also allow us to comment on the introduction and acceptance of corporate capitalist structures and the role of the government in business in the 21<sup>st</sup> century.

## **I. Business Institutions in 19<sup>th</sup> China: State Governance through Patronage and Sponsorship**

Before the introduction of China’s first Company Law in 1904 and the founding of the Republic in 1911, family businesses, many of them of substantial size and scope, were the central institutions for domestic private economic activities in Ming and Qing China. The largest and most successful of these enterprises also relied upon some form of state sponsorship. All of the famous mercantile

family firms such as those of the Yangzhou salt merchants or the Huizhou merchants in the pawnshop business operated under and were dependent on imperial patronage. Family businesses had a long tradition in China, but only changes in business law, which came about first in the treaty ports and then by 1904 in the rest of China, were conducive to the incorporation of those private business institutions.

By contrast, foreign corporate enterprise developed vigorously in Chinese treaty ports during the late 19<sup>th</sup> Century. Shares of foreign-registered corporations doing business in China began trading in Shanghai in the 1870's, and the Shanghai stock exchange served as a conduit for domestic and foreign investment in China for the next 70 years. While Chinese domestic corporations did not trade on this colonial stock exchange, the evolution of a domestic Chinese corporate code and domestic capital markets must be studied against a backdrop of a colonial business that was regarded by the Chinese government both as a foreign competitor to domestic business and, eventually, a useful structure for imitation.

The processes of competition and very limited imitation began well before the formal introduction of the corporate code in 1904. Indeed, the first attempts to build large-scale industrial enterprises on the Western model were undertaken by concerned government officials after the end of the Taiping Rebellion in 1864. In the wake of this major political crisis the Qing government had experienced a substantial weakening of its central authority. As one would expect, whatever little industrialization there had existed in China before 1895 was characterized by a focus on heavy industries serving the government's military and defense purposes.<sup>1</sup> This circumstance was directly linked to the program of the so-called Self-Strengthening Movement in which concerned government officials — mostly politically powerful provincial governor-generals — attempted to

revive the national economy and military after the devastating Taiping Rebellion during the Tongzhi Restoration period between 1862 and 1874.

When Li Hongzhang (1823-1901) was appointed governor-general of Zhili and Imperial Commissioner of the Northern Ports in 1870, he became the most ardent proponent of the Self-Strengthening Movement. One significant part of his plan was to acquire knowledge from the West – including knowledge of Western industrial and financial practices. He secured permission from the imperial government to send Chinese students to study in France in the 1870's. One of them, his protégé, reformer Ma Jianzhong, made a careful study of Western railroad finance in 1879, and proposed the adoption of public bond issues for infrastructure development in China.<sup>2</sup>

Together with moderately reform-minded officials and political authorities such as Zeng Guofan (1811-1872) and Zuo Zongtang (1812-1885), Li Hongzhang demanded that the Chinese government should strive to improve its military equipment and technology in order to defend against the Western powers who had displayed their military superiority so forcefully at China's expense. However, these government officials were not proponents of launching an industrial revolution or a modern economy in China. On the contrary, they wanted to restore the traditional economy, including agriculture and commerce, and were not planning on “enhancing the strength and wealth of the country at the cost of its traditional institutions”.<sup>3</sup>

Thus the initial establishment of industrial enterprises at the time has to be interpreted as a step towards regaining military strength and national pride without contesting the status quo of government and society, rather than as a step towards planned economic development. In order to

---

1 Feuerwerker, “Economic Trends in the Late Ch'ing Empire”; Chen Zhen and Yao Luo, *Zhongguo jindai gongye shi ziliao*, vol.1, pp. 4-5; Eastman, *Family, Fields and Ancestors*, pp. 172-173. For a detailed history of the Jiangnan Arsenal see Cornet, *État et Enterprises en Chine*.

<sup>2</sup> Bailey, Paul, 1998, *Strengthen the Country and Enrich the People: The Reform Writings of Ma Jianzhong (1845-1900)*, Curzon, Durham East Asian Series No. 2, Surrey. P. 14.

<sup>3</sup> Wright, *The Last Stand of Chinese Conservatism*, p. 153.

secure control over this policy, any industrial enterprise founded before 1895 required not only sanction or permission but even active supervision and sponsorship from the government and its agents, the official bureaucrats. Notable examples of this promotion of industrial enterprises under government sponsorship in the 1860s and 1870s included the Jiangnan Arsenal (Jiangnan zhizao ju) and the China Merchants' Steamship Navigation Company (Lunchuan zhaoshang ju), both in Shanghai, as well as the Kaiping Coal Mines (Kaiping meikuang) near Tianjin. Curiously, the China Merchants' Steamship Navigation Company evolved from a business proposal by Yung Wing, a Yale College graduate, who, like Ma Jianzhong drew upon his experience overseas to propose innovations in Chinese enterprise. Feuerwerker notes that the idea of beating the West at its own game, that is, adopting Western-style corporate business practices to government-controlled enterprise was present in Wing's initial conception. Quoting Wing's autobiography, "No foreigner was to be allowed to be a stockholder in the company. It was to be a purely Chinese Company managed and worked by Chinese exclusively."<sup>4</sup>

All three enterprises self-evidently demonstrate the immediate goals of the Self-Strengthening Movement: the Jiangnan Arsenal was to improve China's military strength by manufacturing modern arms, the steamship company was to facilitate the grain transport for the government as well as make China less dependent upon foreign-owned transportation companies, while the mines were supposed to provide the power for national transportation facilities and limited private consumption.<sup>5</sup> This strategy was certainly not an ambitious program aimed at nation-wide industrialization through private initiatives. In order to stress their close relationship with the government's agenda, these new industrial enterprises carried the character *ju* for governmental bureau in their names instead of the characters for factory (*chang*) or industrial company (*gongsi*)

---

<sup>4</sup> Quoted in Feuerwerker, *China's Early Industrialization*, Harvard University Press, Cambridge, 1958. p. 97.

which would have indicated a private business concern. While each of these firms was funded in part by the issuance of shares to Chinese merchants, they were not floated on a public capital market in the manner we understand today, nor indeed were they funded through a public issue in the manner used by foreign-registered corporations in Shanghai at the time. Although a public share market for domestic Chinese companies existed in fits and starts from the 1880's, the domestic Chinese capital market in the late 19<sup>th</sup> Century did not attract enough public investment to fund large-scale operations such as mines, railways, and factories.<sup>6</sup> Despite this competitive financial disadvantage, these new enterprises, initiated by Chinese government officials, operated on a much larger scale than traditional private manufacturing and transportation businesses and thus faced tremendous new challenges in regard to financial and personnel management and technology.

One way to overcome the predicament of lack of public markets would have been to establish the new enterprises as government monopolies similar to the economic strategy of the Meiji government in Japan during the 1870s and 1880s. However, given its strained financial situation, the Qing government could not provide sufficient funds available for such investment. In addition, the machinery, the technological and managerial procedures of the new enterprises required expertise which government officials with their administrative background could not provide.<sup>7</sup>

---

5 See Feuerwerker, *China's Early Industrialization*; Chi-kong Lai, "The Qing State and Merchant Enterprise"; Carlson, *The Kaiping Mines*.

6 See Zhu, Yingui, 1998, "Three Market Crashes and Shanghai Securities Market in Late 1880's and Early 1900's," *China Economy History Research*, Issue 3, 58-70. Also McElderry, 2001, "Shanghai Securities Exchanges: Past and Present," *Occasional Paper Series of the Asian Business History Centre, University of Queensland*. A time-series comparison of prices of domestic and foreign shares can be found in Goetzmann, Ukhov and Zhu, 2001, "China and the World Financial Markets 1870-1930: Modern Lessons from Historical Globalization," Working Paper, International Center for Finance, Yale School of Management.

7 For a general introduction see Wellington Chan, "Government, Merchants and Industry to 1911". On Japan's industrial development see Hirschmeier, *The Origins of Entrepreneurship in Meiji Japan*, and Smith, *Political Change and Industrial Development in Japan*.

In order to solve these problems, the new industrial enterprises established in the 1870s and 1880s took the form of government-sponsored enterprises, known as *guandu shangban* (government supervision and merchant management) enterprises. The bureaucratic term for this type of enterprise had its origin in the traditional set-up of the government's salt monopoly where merchants had provided capital and management while government officials had been in control of production and trade quotas. Under the new scheme for large-scale industrial enterprises, private investors, mostly merchants, were expected to put up the capital and to manage their investment under the supervision of government officials. This arrangement meant that apart from some financial sponsorship through government loans, the merchants bore all the financial risks of the enterprise which often became joint-stock operation. In addition, they were required to work under the thumb of supervising government officials who often followed their own, not necessarily government-directed business agenda and who introduced bribes, corruption, and inflexible management into these enterprises. Albert Feuerwerker and Guohui Zhang have shown in detail the manifold problems these industrial government enterprises encountered due to the peculiar financial and managerial arrangements.<sup>8</sup> Not surprisingly, the financial profit for the private investors in these *guandu shangban* enterprises in the 1870s and 1880s was rather limited.

For example, as Lai Chi-Kong has shown, the China Merchants' Steamship Navigation Company attempted for a short while to consolidate the government-business cooperation with its new joint-stock structure between 1872 and 1884, but continued under dominant government influence in the following years.<sup>9</sup> In the privatization process after 1895, the supervising director of the company appointed by the government, Sheng Xuanhuai (1849-1916), became an appointee of the board of directors. As Feuerwerker has shown, it was more a change in name than in fact, as

---

<sup>8</sup> Feuerwerker, *China's Early Industrialization*; Guohui Zhang, "The Emergence and Development of China's Modern Capitalist Enterprises".

Sheng Xuanhuai, while supervising director, had already acquired substantial shares in the company.<sup>10</sup>

During this period of timid state-directed industrial efforts, Li Hongzhang became in his position as government official and personal supervisor/sponsor the most powerful patron of *guandu shangban* enterprises. The China Merchants' Steamship Navigation Company, the Kaiping Mines, and the Shanghai Cotton Cloth Mill were all under his official sponsorship which actually translated his political power in the government into the opportunity to establish his own sphere of economic influence and to control these enterprises in a quasi-monopoly situation. This is not to say that Li Hongzhang's patronage had a completely negative impact on these enterprises. As Chi-kong Lai has shown for the China Merchants' Company, in the beginning Li's sponsorship in fact secured sufficient financial support and autonomy for the merchant managers.<sup>11</sup> Only when Li Hongzhang was eventually unable to prevent the government from assuming more direct control of the management, did the company encounter problems. Extraction, mismanagement, and misuse of funds accompanied the government's growing intervention in the enterprise, leading to decreasing merchant investment. In general, lack of auditing procedures and absence of distinction between private and company funds characterized these government-sponsored enterprises as much as any family business at the time.

In order to attract private investment from merchants who had become less and less willing to risk their money in government-sponsored enterprises in the 1880s, the government devised a compromise and promoted a more attractive kind of cooperation for merchants in the form of

---

9 Lai Chi-kong, "The Qing State and Merchant Enterprise."

10 See Feuerwerker, *China's Early Industrialization*, especially pp. 161-64; Lai Chi-kong, "The Qing State and Merchant Enterprise"; Lai Chi-kong, "Lunchuan Zhaoshangju jingying guanli wenti"; Zhu Yingui, *Guojia ganyu jingji yu Zhong Ri jindaihua*; Quan Hansheng, *Hanyeping gongsi shilue*; Zhongguo Kexueyuan Shanghai Jingji Yanjiusuo, *Hengfeng shachang de fazhan yu gaizao*.

11 Chi-kong Lai, "Li Hung-chang and Modern Enterprise", p. 238.

*guanshang heban* (official and merchant joint management) enterprises. According to this new arrangement, merchants were to be more in control of the capital invested and of the management. However, this move by the government towards more flexibility and private financial as well as managerial involvement never really materialized and did not trigger the desired outpouring of investment funds. In fact, the dissatisfaction of the merchants grew during the early 1890s and was even acknowledged by government officials.<sup>12</sup>

Certainly, the now more restrained presence of the government in *guanshang heban* enterprises still offered private investors some advantage in regard to official protection against inconvenient national as well as foreign competition. Nevertheless, creating an encouraging investment climate for private activity in the industrial sector would first require the more drastic step of abolishing the general protectionist mechanism against private enterprises in China, namely, the government policy which did not allow Chinese nationals independently to open private industrial enterprises anywhere in the empire.

The turning point came in 1895 when we witness a new phase of industrial entrepreneurship in China.<sup>13</sup> From that year on, enterprises in light industry and in the consumer goods industry were founded in greater numbers with a significant shift from government sponsored enterprises to enterprises with private involvement in ownership and management. For example, a boom in establishing cotton mills with full Chinese ownership took place after 1895. Between 1890 and 1894 only a total of five cotton spinning mills had been successfully established (all but one with government involvement), while by 1916 thirty new mills were in operation, all of them under private merchant management (*shangban*).<sup>14</sup> The statistics of weaving mills is even more

---

12 Wellington Chan, "Government, Merchants and Industry to 1911", pp. 434-35.

13 Quan Hansheng, *Zhongguo jingjishi yanjiu*, vol.2, p. 715.

14 Du Xuncheng, *Minzu zibenzhuyi yu jiu Zhongguo zhengfu*, pp. 286-292. All the mills included in this statistic have a starting capital of at least 10,000 yuan.

impressive. While only one factory in private management was operating in 1897, by 1916 81 private weaving mills were in business.<sup>15</sup>

In another important sector, 35 mining enterprises were founded between 1895 and 1911 as private enterprises (*shangban*) in contrast to nine mining enterprises in total government ownership (*guanban*), ten other enterprises under joint government-merchant management (*guanshang heban*), and only two as government supervision-merchant management operations (*guandu shangban*).<sup>16</sup> As the government withdrew from direct involvement in the enterprises remaining under joint management, new forms of private business operations developed, now supported by structural aspects of incorporation, limited liability, and legal accreditation. The incentives for increased industrial activity and the changing ownership conditions did not originate in deliberate government reforms out of concern for a weak national economy; rather, they resulted from events in connection with China's foreign policy.

The Treaty of Shimonoseki at the end of the Sino-Japanese war in 1895 for the first time granted foreigners permission to engage in manufacturing operations in Chinese treaty ports. As Shao Xunzheng has pointed out, since permission had been given to foreigners for building factories in China, it was impossible for the government to prevent its own nationals from engaging in industry any longer. However, Shao stresses that the fall of Li Hongzhang from power in 1895 was also a vital factor.<sup>17</sup> Li Hongzhang's personal patronage of such enterprises as the Kaiping Mines, the Shanghai Arsenal, and the China Merchants' Steamship Navigation Company had been a crucial reason for their success. Li Hongzhang was powerful not only in Beijing near his power base in Zhili province, but also in Shanghai. There he exerted his influence in the appointment of

---

15 Ibid., pp. 293-304. Many of the listed weaving mills also dyed cloth as part of their business operations. Only five of the 86 new weaving operations established between 1902 and 1916 were under government management (*guanban*).

16 Du Xuncheng, *Minzu zibenzhuyi yu jiu Zhongguo zhengfu*, pp. 460-70.

17 Shao Xunzheng, "Guanyu yangwupai minyong qiye", p. 369.

the Shanghai circuit intendant (*daotai*), the most senior official in Shanghai's administration, and worked successfully for his operations by networking through fellow provincials, colleagues, and fellow examination graduates.<sup>18</sup> Through these formal and informal relationships Li Hongzhang was able to gain support from Shanghai and Jiangsu officials as well as from merchants and gentry members who either were attracted by Li's financial awards or by their own vested interests in the enterprises. In short, as long as Li Hongzhang was in power, the operations under his supervision were protected through his patronage and thus also through their exceptional monopoly status.

Despite the fall of Li Hongzhang and his monopolistic restrictions and the opening of the industrial realm to private initiatives, it took more than a decade before China was to experience substantial industrialization in regard to the number of factories and their output, and it was not until the post-1900 Qing reforms that the imperial court openly encouraged private business and industrial enterprise.<sup>19</sup> Establishing factories for light industry production, transportation or banking businesses required considerable private capital investment from merchants or businessmen. Even without interference from the government and influential officials, the risk of investing private capital in major industrial operations such as cotton spinning mills or silk filatures was still considerable in the early twentieth century. Without an open and accessible capital market for domestic shares, the raising of capital was still one of the major problems in founding private enterprises, with the exception of family businesses which recruited their capital from kinship and native-place networks.

There were, however, instances during this post-1900 period when the potential for full development of a Chinese share market appeared. Lee En-han documents the evolution of the Chinese Railway Rights Recovery Movement from 1904 to 1911, a period in which a number of

---

<sup>18</sup> Yuen-sang Leung, "The Shanghai-Tientsin Connection".

<sup>19</sup> See also David Faure, *China and Capitalism*, pp. 46-48.

domestic Chinese rail companies were chartered and capitalized in the wake of nationalistic zeal to recover the rail concessions made to foreign development firms.<sup>20</sup> Nineteen major provincial railway companies were formed with Chinese capital raised through a combination of public share issuance, domestic, and overseas Chinese merchant investment and provincial government sponsorship. In some cases, these firms were given development rights that were stripped from foreign entities. Virtually all of these ventures foundered in the late Qing or early Republican period; some for political reasons associated with the suspension of their charters by the Imperial government, others from lack of capital, mismanagement and problems. The process of their failure itself is interesting. Lee En-han documents aggressive proxy contests challenging managerial expropriation.

The Dasheng enterprises reveal the strengths and weaknesses of industrial enterprises founded in the wake of 1895 and the transition that came about with the privatization process. Dasheng was originally conceived as a regional enterprise in the form of a *guanshang heban* operation; it was officially initiated by Zhang Zhidong who would lend his support as the patron in the beginning. However, in contrast to the previous system under Li Hongzhang, Zhang Zhidong who represented the *guan* or official side in the enterprise, did not represent the government as a corporate body but acted as an individual official. In this position he offered patronage and ineffective official protection for the enterprise, but not much else.<sup>21</sup>

One could say that the watering down of government patronage to individual official patronage eventually led to the complete disappearance of involvement by individual officials in the enterprise. Zhang Zhidong was unable to offer Dasheng vital financial support, and without financial leverage his official influence faded from the picture. The originally government-

---

<sup>20</sup> Han, Lee-En, *China's Quest for Railway Autonomy: 1904-1911*. Singapore University Press, Singapore, 1977.

sponsored enterprise thus became soon a privatized operation under the strong impact of the founder's family without ever developing into a family business. Registered officially as a shareholding company with limited liability in 1907, Dasheng then grew into a major industrial complex with considerable financial success and a substantial life-span.

## **II. The Power of the Law? Chinese Company Legislation in 1904**

In the wake of the late Qing reforms, China's first Company Law (*gongsi lü*) was issued by the newly created Ministry of Commerce on January 21, 1904, based on Japanese and English company laws, but in much abbreviated form. The government's main goal was to encourage the establishment of Chinese companies modeled on Western corporate structures which would be able to compete with the foreign companies producing and selling goods in China. With regard to existing Chinese company structures, the company law was supposed "to overcome the constraints of the partnership" which, lacking the limited liability concept, in William Kirby's words "could be limiting, but not limited".<sup>22</sup> According to the Company Law, businesses in the form of partnerships with unlimited or limited liability, joint-stock companies with unlimited or limited liability, and sole proprietorships with unlimited liability were allowed to register.<sup>23</sup> Between 1904 and 1908, some 272 companies had registered with the Chinese government, over half of them as joint-stock companies with limited liability.<sup>24</sup>

Here are some examples of how existing Chinese businesses responded to the new Company Law. The Nanyang Brothers Tobacco Company was registered under English law in Hong Kong in 1905 and later as a joint-stock company with the Beijing government under Chinese

---

<sup>21</sup> Elisabeth Köll, *From Cotton Mill to Business Empire: The Emergence of Regional Enterprise in Modern China*. Harvard East Asian Monographs, forthcoming.

<sup>22</sup> Kirby, "China Unincorporated", p. 47.

<sup>23</sup> *Da Qing xinfaling (Gongsi lü)*, 2:a.

law in 1918.<sup>25</sup> The management of the company, especially its debts and credit arrangements, had always been problematic because of the use of former compradors, since it was never clear whether they acted as agents or principals. With the new holding structure of the business company Sherman Cochran documents a managerial innovation in the appointment of a financial controller in 1919 who was responsible for reorganizing the company's finances.<sup>26</sup>

Many families opted not to register their firms for fear of losing control over management and equity. Even those family firms that registered with the Chinese government (and most family firms in the treaty ports did not), did not necessarily give up their family business structure. The Yong'an (Wing On) company, famous for its department stores in Shanghai and founded by the Guo family in Hong Kong in 1907, is example of a large family business that was registered under English law and continued to exist as a joint-stock limited liability company in 1912. The family exerted its strong financial control over the company's shareholding structure.<sup>27</sup> As Kubo Toru and Wellington Chan have shown, despite taking the company public, the Guo brothers were able to achieve almost a consolidation between ownership and control through shareholdings from extended family, overseas and native place networks, interlocking directorships and inter-company loans.<sup>28</sup>

Needless to say, the treaty ports, not rural areas, became preferred locations for Chinese to establish their new incorporated enterprises. Chinese merchants and businessmen valued the cooperation with compradors or foreign brokerages in the treaty ports in order to gain access to new financial sources and foreign products and technology. In addition, many of the Chinese

---

24 Wellington Chan, *Merchants, Mandarins and Modern Enterprise*, pp. 180-82.

25 Cochran, *Big Business in China*, pp. 56, 100-101.

26 Ibid., pp. 151-152.

27 Shanghai Shehui Kexueyuan Jingji Yanjiusuo, *Shanghai Yong'an gongsi*, p. 7.

28 Wellington Chan, "The Origins and Early Years of the Wing On Company Group", p. 89; Kubo Toru, "Kindai Chugoku mengyo no chitai kozo", pp. 36-38.

investors used the presence of foreign settlements and their special legal administration in order to register their companies under the protection of foreign legal statutes.

The role of the imperial government in the registration process was not dominant but remarkably restrained. According to the 1904 law, businessmen had to register their companies with the local chamber of commerce first before the registration would then be forwarded to the central government in Beijing. As a clear affirmation of the much more visible hand of the Republican government, this practice was abolished in the law's 1914 revised and expanded form when registration now had to take place directly with the government.

It is difficult to establish the exact date when Chinese enterprises like Dasheng, or more precisely the Dasheng No.1 mill, acquired private, corporate status as a legal entity. After extensive search in various archives it is safe to say that no documents exist that formally dissolved the initial form of the enterprise at its foundation as a *guanshang heban* (official-merchant joint management) operation. The text printed on share certificates from 1897 and from 1903 still stated that the Dasheng spinning mills

... were established in Tongzhou with approval granted by edict in response to a memorial from the Minister of the Southern Ports [i.e. Zhang Zhidong]..., by contract set up for perpetuity to be jointly managed (*yongyuan heban*) by officials and gentry...<sup>29</sup>

In March 1905 the *Dagongbao* newspaper published an announcement which listed the Dasheng No.1 Cotton Mill as approved and registered by the Ministry of Commerce (*shangbu*) together with ten other companies (*gongsi*) established by Dasheng's founder, Zhang Jian.<sup>30</sup> This was the official recognition of the company registration required by the Company Law (*gongsi lü*) as promulgated

---

29 NTFB: doc.247, share certificate from 1897; doc.182, share certificate from 1903. Share certificates from the years 1898 to 1903 with the same text are also kept in the Nantong Municipal Archives (NTD: B 402-111-1).

30 *Dagongbao*, March 4, 1905, 2a-2b; March 6, 1905, 2a.

in 1904.<sup>31</sup> Finally, we know from the published report of the first shareholder meeting in 1907 that the Dasheng No.1 Cotton Mill had now taken on the form of a stockholding company with limited liability (*gufen youxian gongsi*).<sup>32</sup>

What did the shareholders of the newly incorporated companies say? We must not forget that although Dasheng had been operating with private share capital since its establishment in 1898, shareholders had no public forum within the enterprise to voice their suggestions or criticism regarding the company's policies. Thus the new legal status of the company seems to have been met with great enthusiasm from the shareholders. Zheng Xiaoxu (1860-1938), one of the most prominent shareholders with an active career in business and national politics, most notably as a staunch Manchu loyalist<sup>33</sup>, is quoted in the 1907 shareholder report, which documents the lively discussions at Dasheng's first ever shareholder meeting:

Formerly all the organization of this mill was unlimited and untouched by any law<sup>34</sup>.

Now that we have shareholders' meetings, the unlimited and without-law status should be changed into a company that is limited and with a complete law. We should first decide on its name as Dasheng Stockholding Company With Limited Liability (Dasheng *gufen youxian gongsi*).<sup>35</sup>

One would expect that the new share certificates of the Dasheng No.1 mill from 1907 onwards would bear reference to the new legal status of the company — but they do not. The certificates only refer to the Dasheng Spinning and Weaving Company (Dasheng *fangzhi gongsi*)

---

31 The law may be found in Shangwu Yinshuguan Bianyisuo [ed.], *Da Qing Guangxu xin faling*, 'gongsi lü', 10:3b.

32 NTD: B 402-111-445, 13b.

33 For the biography of Zheng Xiaoxu (1860-1938, courtesy name: Zheng Sukan) see Boorman, *Biographical Dictionary of Republican China*, vol.1, pp. 271-275. Zheng Xiaoxu is probably most famous for his Manchu loyalty and his refusal to recognize the Republic of China. Between 1925 and 1932 he served as assistant to the former Xuantong emperor Puyi.

34 To translate 'wufa' with 'illegal' would be beside the point, as there was no company law with required registration before 1904, and thus a company without official registration was not an illegal operation.

35 NTD: B 402-111-445, 12b.

without indicating its new legal status. However, the text on share certificates from the years 1915 and 1919 at least no longer mentions the previous involvement of the government in the establishment of the company.<sup>36</sup>

However, while some companies like Dasheng through incorporation rid themselves of government patronage, some enterprises actively continued to seek and exploit government patronage during the Republican period when political power became even more fragmented. The Lanzhou Mining Company (Beiyang Lanzhou guankuang youxian gongsi) and the Qixin Cement Company (Qixin yanghui gongsi) are examples of such privatized enterprises under rejuvenated patterns of political patronage. Their founder, the government official Zhou Xuexi (1869-1947), enjoyed the political patronage of Yuan Shikai who first as governor-general of Zhili and later as president of the Republic had great influence in the Beijing government. Yuan's support of the Qixin company through partial exemption from custom duties and its placement as major supplier of cement for the government-owned railways fortified the positive relationship between the most successful industrialist in northern China and the Beijing government. Although the establishment of the Nanjing government in 1927 meant a drastic change in the political scenario and thus a shift in the patronage advantages for Zhou Xuexi, his companies were already so well established that they continued their business with success in the 1930s.<sup>37</sup>

In general, the change to limited liability evidently did not evoke great changes in terms of the business organization of Chinese enterprises.<sup>38</sup> The introduction of annual shareholder meetings appears as the most significant result of their legal transformation into a private, incorporated

---

36 NTFB: doc.No.193, share certificate from 1915; doc.No.198, share certificate from 1919.

37 Feuerwerker, "Industrial Enterprise in Twentieth-Century China", in particular pp. 287-302; Carlson, *The Kaiping Mines*, pp. 105-17.

38 For example, after 1907 the name of the company did not give any evidence of the newly acquired limited liability concept, as none of the successive shareholder and company reports or the official company correspondence actually referred to Dasheng as a *youxian gongsi*, a company with limited liability.

companies. The new legal status did not affect the internal managerial or the overall structure of the business. The line of hierarchy was basically unchanged as the department heads were still appointed by the managing director, now in consultation with the board of directors (*dongshiju*).<sup>39</sup>

In addition, according to the stipulations of the 1904 Company Law two auditors (*chazhangyuan*) were appointed to examine the company's finances. However, it should be pointed out that the law did not specify that these auditors had to be independent, only that company directors could not simultaneously serve as auditors for their own companies.<sup>40</sup> This meant that legally auditors could still be selected from the remaining members of the board. For example, in the case of Dasheng auditors were recruited among the board members and thus from within the company management under Zhang Jian's immediate influence.<sup>41</sup> These auditors more or less rubber-stamped Dasheng's annual reports and signed the minutes of the shareholder meetings. We should not interpret their role as controllers who represented the interests of shareholders regarding financial clarity and critical examination. In fact, as part of the management, the auditors were there to defend the financial decisions they had approved on the board earlier on.

On the whole, it seems that the new legal status of incorporation, which we tend to associate with the form of a 'modern' business enterprise in the Western sense, did not lead to significant improvements with regard to protecting shareholders rights or curbing the power of the managing director. Judging from the complaints at shareholder meetings of Liu Hongsheng's or Zhang Jian's enterprises and their complete ineffectiveness in every respect, with all the potential prospects of openness and accountability through incorporation, shareholders were still placed at a disadvantage. The balance of power did not change in the company. Nonetheless, the shareholders' role in Chinese business in general deserves some further exploration.

---

39 NTD: B 402-111-445, 17a-b.

40 See the law in Shangwu Yinshuguan Bianyisuo [ed.], *Da Qing Guangxu xin faling*, 'gongsi lü', 10:7a-8b.

In line with common business practice used in government-sponsored enterprises, shareholders in companies that had started after 1895 and incorporated relatively early, received guaranteed interest payments at a fixed rate of eight per cent on their share investment. They collected their interest annually in person from the accounting office at the factories.<sup>42</sup> Thus the shares should be rather described as bonds in their financial performance, bearing minimal financial risks for the holders. Only in the early 1920s did Dasheng investors become exposed to the fluctuations of the newly opened stock exchanges. Shares of the Dasheng No.1 mill were traded for the first time by the Shanghai Stock Merchants Association in 1917, but the trading volume of this trading association operating with government approval since late 1914 seems to have been rather limited.<sup>43</sup> When the Shanghai Stock Exchange opened in 1920, shares of the Dasheng No.1 and No.2 Cotton Mill were listed and their market prices regularly reported in the *Shenbao* newspaper.<sup>44</sup>

To be sure, due to the absence of a stock market, shareholders in the 1900s and 1910s did not constitute a clientele who were taking great risks on the company's behalf and who would be inclined to withdraw their investments at short notice. On the other hand, incorporation did not seem to have made the company more attractive to potential investors, even if the aim of attracting investors and thus new capital might have been the main reason for businessmen like Zhang Jian, Liu Hongsheng, or the Rong brothers to register their companies in the first place. The capital of the Dasheng No.1 mill remained unchanged at 1.13 million taels between 1903

---

41 NTDAG: B 402-111-445, 4a.

42 Köll, *From Cotton Mill to Business Empire*, chapter 5. These interest payments with passbooks were called *xizhe*. As Ellen Hertz points out, even in China today dividends from Shanghai's stock market are distributed in person and not through the mail. Hertz, *The Trading Crowd*, p. 37.

43 McElderry, "Shanghai Securities Exchanges: Past and Present", in particular p. 6 and footnote 1 which gives a partial list of the government securities and government shares traded in 1917.

44 *Shenbao*, August 1920.

and 1914.<sup>45</sup> Obviously, the new legal status of limited liability did not attract tremendous interest or create greater trust among investors and did not prompt the management to seek a capital increase through the public offering of new share subscriptions.

In the context of financial control the question arises whether the introduction of the new company legislation changed the process of creating and controlling accounts in Chinese enterprises. According to the stipulations in the 1904 Company Law, corporate companies were required to produce a detailed company report at least once every year. The annual report had to contain a profit and loss statement (*churu zongzhang*), a written statement on the company's commercial situation (*maoyi qingxing jielie*), the exact loss or profit figure, the amount of money paid out as dividends and set aside for reserves as well as a balance of the company's assets and liabilities.<sup>46</sup> Most of the companies complied with all these basic formal requirements in their annual company reports.

In fact, from the existing published and unpublished company records it is clear that companies like Dasheng had fulfilled these basic publication requirements even before the 1904 legislation, and as a general trend accounting practices did not change significantly in the following decades.<sup>47</sup> One would expect certain changes in the reporting style or at least a more detailed, lucid presentation of the accounts as a result of the introduction of new company legislation. However, a look into the Company Law from 1904 reveals that no regulations specified the way company accounts should be compiled and recorded, while the regulations for the annual financial statement were summarized in just two lines.<sup>48</sup> Even the revised Company Law from 1914 under the section

---

45 *DSQXDX*, pp. 18-19, 93-103.

46 See the law in Shangwu Yinshuguan Bianyisuo [ed.], *Da Qing Guangxu xin faling*, 10:9a.

47 See the annual company reports in *DSQXDX*, covering the period between 1899 and 1930.

48 Shangwu Yinshuguan Bianyisuo [ed.], *Da Qing Guangxu xin faling*, 10:9a.

company accounting (*gongsi zhi jisuan*) did not contain any further specification for standardized bookkeeping.<sup>49</sup>

In short, the law required an annual company report, but no uniform system for company accounting. It should be pointed out that in general modern, western-style bookkeeping methods found their way into China only in the 1930s.<sup>50</sup> In general, most companies officially used a standardized, modernized accounting system only in the 1940s.<sup>51</sup> Nevertheless, this is not to say that traditional forms of bookkeeping were inefficient or irrational; even in large-scale industrial enterprises they obviously served their purpose. Companies maintained, at least to the outsider, a complex bookkeeping system which provided some internal control within the branches, factories, and offices.<sup>52</sup>

All these observations confirm William Kirby's analysis of the 1904 Company Law in relation to its very limited impact on the development of Chinese enterprises and modern industries. Only a relatively small number of enterprises registered at all, and of those registered as stockholding companies with limited liability only a few were of substantial size and actually grew into sustainable enterprises.<sup>53</sup> Kirby also mentions the uncertainty of how commercial disputes of corporations would be settled by the imperial court system as a factor, which might have deterred investors and discouraged seeking incorporation.<sup>54</sup> In this sense, the "top-down" approach of the imperial government represented a failed attempt to promote viable Chinese

---

49 Zhongguo Di'er Lishi Dang'anguan [ed.], *Zhang Jian nongshang*, 'Gongsi tiaoli', pp. 46-47.

50 For the introduction of Western-style accounting to China see Gao Zhiyu, *Zhongguo kuaiji fazhan jianshi*, pp. 84-91. From the 1920s onwards the frequent advertising of bookkeeping manuals for industrial and commercial enterprises in newspapers and journals indicates the increasing demand for accounting knowledge. (See, for example, *Shenbaoguan wushi zhounian jinian*, 1922, p. 5 and advertisements without page numbers).

51 NTB: E 124/1334, pp. 6-17, 19-20.

52 Köll, "Controlling Modern Business in China" in *Journal of Asian Business*, vol14, No.1, 1998, pp. 41-56.

53 Kirby, "China Unincorporated", p. 48.

54 Ibid.

corporate enterprises due to the continuing weaknesses of the legal framework and capital market.

### **III. Characteristics of Corporate Ownership and Control in early 20<sup>th</sup> Century China**

So, why did people bother to register their companies at all? The fact that Zhang Jian also registered the No.2 branch mill in Chongming with the Ministry of Commerce as early as 1905, two years before this mill was even ready to go into operation, shows that he was actively interested in having his industrial companies registered with the government.<sup>55</sup> Obviously the expectation that incorporation would make the company more attractive to potential investors must have played a role.

The most significant aspect of Chinese companies' incorporation is whether the new Company Law and its requirements like shareholder meetings really led to an empowerment of the shareholders with a simultaneous decrease in personal influence of the company founders and directors. The minutes of the meetings prove that the shareholders were only vaguely familiar with the Company Law and with the new implications that limited liability brought for the enterprise and for their personal involvement with regard to rights and obligations. But it appears that there was a general consensus among those shareholders who voiced their opinion at the first meeting in 1907, that the law supported their claims as owners and provided them with a tool to control the corporate management — or so they thought.

In this spirit, shareholders used their newly won influence to protest for the first time publicly against the reduction of their share profit caused by Dasheng's generous donations to Zhang Jian's welfare and educational projects which in return reduced their dividends.<sup>56</sup> Again,

---

<sup>55</sup> *Dagong Bao*, February 28, 1905, 2b.

<sup>56</sup> NTD: B 402-111-445, 20b.

Zheng Xiaoxu, as a concerned and critical shareholder but with no financial leverage in form of majority shareholding, expressed his opinion in a very outspoken way:

Subsidies spent on the costs of the Normal School ... are the virtues of the general manager [i.e. Zhang Jian] himself and have nothing to do with the company. Now in accordance with the law, we have to discuss separately new regulations for the allocation of bonuses.<sup>57</sup>

Obviously, Zheng interpreted the law as a new protective mechanism for the benefit of shareholders against arbitrary bonus allocation (to managers) and fund distribution by the managing director (*zongli*). However, since Zhang Jian as the managing director of the Dasheng mills had never been forced to seek appointment by a director's board but had automatically slipped into this position when transforming Dasheng from a government-sponsored into a private enterprise, Zheng Xiaoxu's criticism could not endanger Zhang Jian's position in any way.

In fact, the 1907 shareholder report is an excellent document for revealing Zhang Jian's authoritarian management of Dasheng and the simultaneous ineffectiveness of the shareholders' criticism and demands for change. The 1907 document, in recognition of the No.1 mill's incorporation, contains eight clauses composed by Zhang Jian as the managing director for the regulation of issues such as managing working capital, reserves, and the election of members of the board.<sup>58</sup> Interestingly enough, there is no regulation for the election of the managing director. Reading his response to shareholders' complaints in the context of the discussions at the meeting, his words are defensive, and instead of addressing some of the shareholders' complaints, he appeals to their integrity and moral conscience. Several other shareholders continued to voice questions in

---

<sup>57</sup> Ibid.

<sup>58</sup> Ibid., 9a-12b.

regard to bonus allocation and salaries for the managers; Zhang Jian never replied in person but had other members of the board explain Dasheng's, i.e. his personal, position.

Let us now further investigate shareholding in the context of incorporation and the identity of the shareholders and their investments in 1907. The legal regulations in the Company Law of 1904 required on registration of the company a statement of how many people were providing the capital, their names and addresses, and the overall amount of capital and number of shares.<sup>59</sup> These regulations concerned the initial setup and changes in the shareholding due to expansion and growth as would occur over time. Periodic shareholding inventories are thus invaluable sources for the examination of shareholding structure and the practice of disguising personal accounts in the form of business accounts. In the case of Dasheng the relatively detailed 1903 record shows that, first of all, most of the Dasheng shares were not held under the personal name of a shareholder, but under a business name, that is, in the name of a *tang* (family trust) or *ji* (business). For example, Zhang Jian's son, Zhang Xiaoruo, held shares under the account names of Zhang Xu, Zhang Liang, Zhang Wu, Zhang Chen, and the Zunsu *tang*, but also under Ruo *ji*, Xiao *ji*, and Xuyin *ji*. Of course, if we take into consideration that Zhang Xiaoruo was only five years old in 1903, it is very clear that these were in fact Zhang Jian's own accounts for his personal assets. One has to suspect that in reality Zhang Jian was the actual owner behind many more business accounts which cannot be clearly identified from the record, because in the majority of cases the entry under the personal name (*xingming*) of the shareholder is left blank. For example, the account listed as holding shares under the business name Fengsi *tang* was in fact the account representing the charity land (*yizhuang*) in possession of Zhang Jian's own family. Zunsu *tang* is an account associated with Zhang Jian's family residence in Haimen county. It is only possible to gain this information from Zhang Jian's obituary in 1926, where the distribution of his personal assets is described; the actual ownership is

not clear from the company's shareholding register.<sup>60</sup> Needless to say, also investors from outside the family circle are listed with their investments under the names of business accounts.

Even allowing for a considerable margin of error due to the fact that some of the family accounts may not have been identified, clearly control was not tied to majority shareholding in the Dasheng business complex. The 1907 shareholding inventory of the No.1 mill supports this argument with straightforward numbers: The capital stock of 630,000 taels was subscribed by altogether 553 shareholders. The largest single shareholder was the Salt Bureau with its investment of public funds (*gongkuan*) at a value of 23,000 taels or 4 per cent of the total stock capital. Then follows a group of 17 shareholders with investments between 15,000 to 8,000 taels each which gave them ownership of 2.4 per cent to 1.3 per cent of the capital stock each (27 per cent altogether). The remaining capital stock worth 435,000 taels (69 per cent altogether) was subscribed by 535 shareholders who individually owned less than 5,000 taels each in equity. The overwhelming majority of these shareholders owned between one and five shares at 100 taels each. Accounts which can be linked to Zhang Jian's family in one form or another reveal an ownership of 40,300 taels or altogether 6.4 per cent of the total capital stock; a modest percentage even if it was higher than that of the largest single shareholder.<sup>61</sup> This shareholding pattern of a large number of minority shareholders, mostly from the local community and from the director's kinship and social networks, was common among Chinese companies in the early 20<sup>th</sup> century.

It is necessary to point out that holding capital under a business account was a common business practice at least in the late Qing dynasty. In fact, using a business name (*ji* or *hao*) for daily operations and holding property under another name in a trust (*tang*), was a custom already

---

59 Shangwu Yinshuguan Bianyisuo [ed.], *Da Qing Guangxu xin faling*, 'gongsi lü'.

60 Ibid.; *Nantong bao tekan*, October 29, 1926.

61 All following numbers are from NTD: B 402-111-2.

adopted by merchants in the Ming dynasty (1368-1644).<sup>62</sup> The use of front men, names of ancestral halls for individual families or associated groups, and assumed names was a frequent method to conceal ownership and true identity from the government which imposed restrictions on the involvement of gentry members in business.<sup>63</sup> However, since the early twentieth century, gentry investment in industrial enterprises had become a legal and approved activity, and there existed no government taxation of income or capital gains which one would have preferred to avoid. Reasons for concealment now lay in the inappropriate use and transfer of company funds to accounts difficult to detect by auditors and shareholders.<sup>64</sup>

### **Conclusion: Characteristics of Chinese Corporate Ownership Past and Present**

Next to the incorporation process itself, the relationship between control and ownership is one of the central issues for understanding business in China. Recent scholarship has shown that in Chinese businesses under strong family influence the control of equity was rarely separated from the control of management, and that succession disputes were of great significance for the continuity of the company.<sup>65</sup> General consensus exists among historians about the restricted and limited influence of shareholders in China's first stockholding companies like the China Merchants' Steamship Navigation Company. The general scholarly evaluation of Dasheng's situation is much more positive. However, historians like Zhu Yingui have praised Zhang Jian's role in introducing

---

<sup>62</sup> Faure, *China and Capitalism*, p. 17.

<sup>63</sup> See Chan, *Merchants, Mandarins, and Modern Enterprise*, pp. 36-37. Based on her analysis of a court case filed in Hong Kong in 1910, Stephanie Chung points out that the neither *tang* nor *hao* were recognized by the law as legal persons (*faren*). Chung, "Faren' gainian de yizhi", p. 60. Even if this decision was made in the context of a legal system under strong Western influence, it confirms the private nature of the *tang*, *hao*, and *ji* and the legal difficulties in case of litigation.

<sup>64</sup> Dasheng's financial crisis due to this inappropriate transfer of funds is analyzed in detail in Köll, *From Cotton Mill to Business Empire*, chapter 6.

<sup>65</sup> See Faure, "The Control of Equity in Chinese Firms" and Choi, "Competition Among Brothers".

incorporation too uncritically by linking this step automatically to shareholder empowerment and a voluntary power restriction for Zhang Jian who “set himself the boundaries of his influence”.<sup>66</sup>

In contrast, evidence suggests that although the Dasheng No.1 Cotton Mill had adopted the legal form of a limited liability company as early as 1907, it was not managed in such a way as to allow the shareholders to curtail the power of the founder-director. Like the Rong brothers’ companies or Liu Hongsheng’s enterprises, the newly incorporated companies continued traditional business practices and institutions which had been primarily characteristics of Chinese family enterprises. In addition, members of the Zhang family continued to be involved in the financial and managerial organization of the company, even as a hierarchy of salaried executives came into existence to manage the different parts of the business on a day-to-day basis.

Nevertheless, several regulations in the 1904 Company Law helped a new type of business emerge in early twentieth-century China such as the adoption of the limited liability concept, the holding of shareholder meetings, publication of annual company reports and observing existing regulations for accounting.

Until recently, China business historians have tried to capture the essence of Chinese enterprises by focusing on personal relations, in particular in family businesses. Frequently, a business organization has been more or less reduced to the interpretation of being a network, often in the context of a search for the ‘spirit of Chinese capitalism’.<sup>67</sup> Scholars have argued that “kinship and collegiality in China play roles analogous to those played by law and individuality in the West”, and the growth of the Chinese economy has been explained with increased economic opportunities

---

66 Zhu Yingui, “Jindai Zhongguo diyi pi gufenzhi qiye”; Zhu Yingui, “Cong Dasheng shachang kan Zhongguo”, quote p. 59.

67 This approach can be found, for example, in Hamilton and Kao, “The Institutional Foundations of Chinese Business” or in Redding, “Weak Organizations and Strong Linkages”.

and the simultaneous expansion of networks.<sup>68</sup> Of course, business by its nature always involves networks. Considering the emergence of corporate ownership in Chinese companies in the early 20<sup>th</sup> century, the conflict of interest between the founder-director and his shareholders, and divided loyalties between people whose positions relied either upon the authority of the founder or the holding of shares, now becomes the real focus and problem.

To be sure, historically the lack of a statutory framework for business did not mean an absence of substantial and successful enterprises in China. In the same way the insufficient legal and institutional framework for incorporation designed by the Chinese imperial government did not prevent the rise of certain successful incorporated companies, some of them surviving occupation and war. Poor disclosure and weak regulations are well-known and persistent problems of companies and the stock market in contemporary China. Tumultuous shareholder meetings with angry minority shareholders are not unheard of.<sup>69</sup> The question is whether the visible hand of the state will succeed in creating structures of capitalist ownership with more success this time.

---

68 Hamilton, "The Organizational Foundations", in particular pp. 43 (quote), 53-54.

69 "Let 1,000 Casinos Whither" in *Far Eastern Economic Review*, October 18, 2001.