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What Is the Main Agency Problem?
---The Governance Scandal of Mingxing Electric Power Co. Ltd.**

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China's Corporate Governance: What Is the Main Agency Problem?

---The Governance Scandal of Mingxing Electric Power Co. Ltd.

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Abstract

This paper studies a case of corporate governance scandal of MXEP. The analysis shows that there was an institutional vacancy in MXEP corporate governance during the period. We find that the internal disciplining mechanism of two-board system was not effective especially when MXEP's majority shareholder was the private group and the major reason of MXEP corporate governance failure was not caused by lack of autonomy inside the company, but short of checking and balancing power for its top management.

By reviewing the process of China's SOE reform as well as the major policies, I find that too much attention has been paid to decreasing government intervention while the constraining mechanism for manager's power discretion has been relatively neglected in the reform course. This one sided focus on decreasing government intervention have made management discretion become the major agency problem of China's corporate governance.

There are two implications we may get from these analysis. The first one is that government intervention and the market internal logic may be complements rather than substitutes at least in current China's condition. The second one is that the recent reform measures, including the implementation of revised laws as well as shareholding reform, cannot strengthen the monitoring role on top management in the perspective of internal governance. So we think that China should explore new way to improve the internal corporate governance for restricting on the authority abuse of top management.

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I. Introduction

With the development of China's economy as well as its emerging capital market, the issue of China's corporate governance, especially the related problems of the reformed SOEs, have been a hot issue of academic research and policy debate. After a number of public corporate scandals such as Guangxia (Yinchuan) Industry Co. Ltd, Lantian Co. Ltd. occurred since 2000, combined with no evident efficiency improvement of listed SOEs, scholars as well as the government officials started to examine more closely than ever the issue of Chinese corporate governance.

Firstly, in academic research, we may ask that what the central agency problem, the largest shareholders or the managers, in China's SOEs is. The seminal work in the field of corporate governance by Berle and Means (1932) advances that, in practice, managers of a firm pursue their own interests rather than the interests of shareholders. In recent years, another important view promoted by La Porta, Lopez de Silanes, Shleifer, and Vishny (1998) assert that the central agency problem in large corporations is to restrict expropriation of minority shareholders by controlling shareholders. Is this the case in China's corporate governance?

Secondly, in policy practices, should China quicken the process of SOE privatization, or still keep state as the controlling shareholders or let the state play some roles in SOEs' governance? Moreover, very recently, China has taken a series measures, in which the most significant ones are the revisions of the Corporate Law and Securities Law as well as the shareholding reform to improve the situation of the corporate governance. Although it's too soon to assess the effectiveness of the revised laws, but we may ask that if the government took the right remedial steps to correct the unsatisfied shortcoming existed in China's reformed SOEs, i. e if the policy measures adequately capture the context and experience of China's listed firms.

For these issues, there are quite a lot of studies from the perspective of institutional changes. For example, Pistor et al. (2004) found that the so called ideal laws transplanted from western countries couldn't work as expected in transition economies. Allen et al. (2005) pointed out that in China's corporate governance, a series informal rules binding with financing from the informal channels rather than commercial banks

or capital market, has been playing a major role, while Ayyagari (2007) suggested that the role of reputation and relationship based financing and governance mechanisms in financing the fastest growing firms in China is likely to be overestimated. One of the major lessons from these kinds of research was that the corporate governance would not automatically develop as a natural response to comprehensive privatization programs and shifts in formal control rights (Sonja et al., 2008). It seems that literatures agreed that there is a gap between actual corporate governance and the related laws' stipulations especially in transition economies. Based on those established studies, one of an important question we may ask is: what has been mainly attributed to China's deficient corporate governance mechanisms? Moreover, what kinds of institutions that actually shape and influence social behavior in China's corporations?

This paper studies on the governance problems of Sichuan Mingxing Electric Power Co. Ltd (MXEP hereafter), which is a reformed SOE before a private company became the largest shareholder in 2003 and a listed firm in Shanghai Securities Exchange (the Exchange code of the company is 600101). We find that the lack of restricting mechanisms on top management in the company is the major reason of the scandal. Two implications we may get from the MXEP case. Firstly, in the backdrop of the market initially designed to help SOEs to financing their investment and the newly established framework of laws and regulations still need time to be work efficiently, the government intervention is essential in running this market. Secondly, the two board system (board of directors and board of supervisors) as well as independent director institution have not worked as expected in Chinese corporate governance. For exploring the major policy reasons of the governance failures like MXEP, the paper then review the major policies of China's SOE reform from a new angle of what problems have been emphasized. I find that disciplining managers' power discretion has been relatively neglected in the reform process while increasing the autonomy of corporations has been emphasized. From the above case analysis and policy reviews, it seems that the recent revision of laws and the shareholding reform could do little for coping with the problem of lacking checking and balancing power for managers' behaviors. Finally, I listed the implications as well as the policy recommendations according the analysis.

The rest of the paper is organized as follows. Section 2 is the recent background of

China's corporate governance environment; Section 3 gives the introduction of the case company as well as its scandal; Section 4 analyses the main contributing factor of the corporate governance deficiency of the case company; section 5: reviews the related government policies in the process of China's SOE reform; section 6 are conclusions and implications.

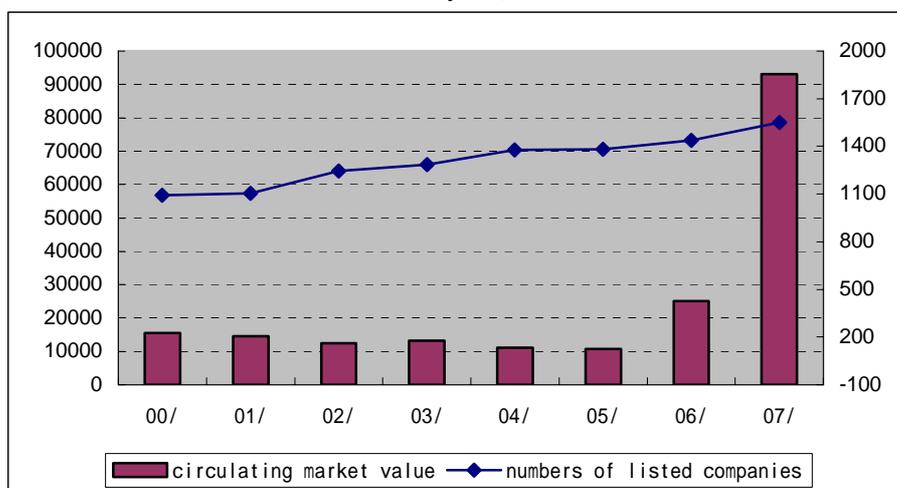
II. Recent Background of China's Corporate Governance Improvement

2.1 Development of China's Stock Market

The so-called jump-starting Chinese capital market had been quite active during its first decade due to the government's effort to encourage the reformed state-owned enterprises (SOEs) to be listed on the market. Many of the SOEs were restructured to joint stock companies under the guidance of the Corporate Law, which was executed since 1994, and then undertook initial public offerings (IPOs) and listed on the Shanghai or Shenzhen Exchanges, which were set up in 1990 and 1991 successively.

Entering in the new century, China's stock market experienced a relatively long period of setbacks since 2001 to 2005, against the backdrop of both domestic as well as worldwide corporate scandals. After that, the stock market entered a new booming stage since 2006 and the stock index increased dramatically especially in 2007. To the end of July 2008, there are 1614 companies (including the companies who issued A and B shares), in which most of them are reformed SOEs, listed on the exchanges and the market value of these companies is RMB 18,188.46 billion in China's capital market (see Chart 1 for detailed information).

Chart 1: The Development of China's Securities Market
(Unit of the market value: RMB billion yuan)



Data Resource: CSRC statistics: <http://www.csrc.gov.cn>

2.2 Recent Major Measures Aimed to Improve China's Corporate Governance

Against the policy backdrop of continue strengthening the SOE reforms, the listed companies with state or state agency as their majority shareholders have seen many changes in recent years. The most significant one of this is that some of the shares originally owned by state or state agency were approved to sell to private companies, mainly in order to further reduce the government intervention in companies' operation and make the companies independent players.

Another two main measures were taken by the government in recent years to emphasize the issue of corporate governance of listed companies. One is the revision of the Corporate Law and Securities Law. The other is the shareholding reform.

The revised laws have been put into practice since January 1, 2006. The revision of the laws added stipulations of punishment for misbehaving corporate shareholders and substantiated the rules of procedures for share-holders' meeting as well as board meeting. Meanwhile the revised law gave more power to board of supervisors and established institution of supervisors' board meeting and also added the requirement of independent directors in listed companies. The revision of the Securities Law focused on the protection of shareholders' right to information. In line with enhancing the corporate governance of listed companies, the new Securities Law also allows investors to sue misbehaving listed companies or their majority shareholders.

In 2005, the government decided to reform the split share structure, which aimed to transform the original non-tradable shares (state shares and so-called legal person share hold by other enterprises) to tradable shares by a variety of reform arrangements the listed companies made according their own shareholding and financial situations. Until 2007, almost all listed companies finished their shareholding reforms.

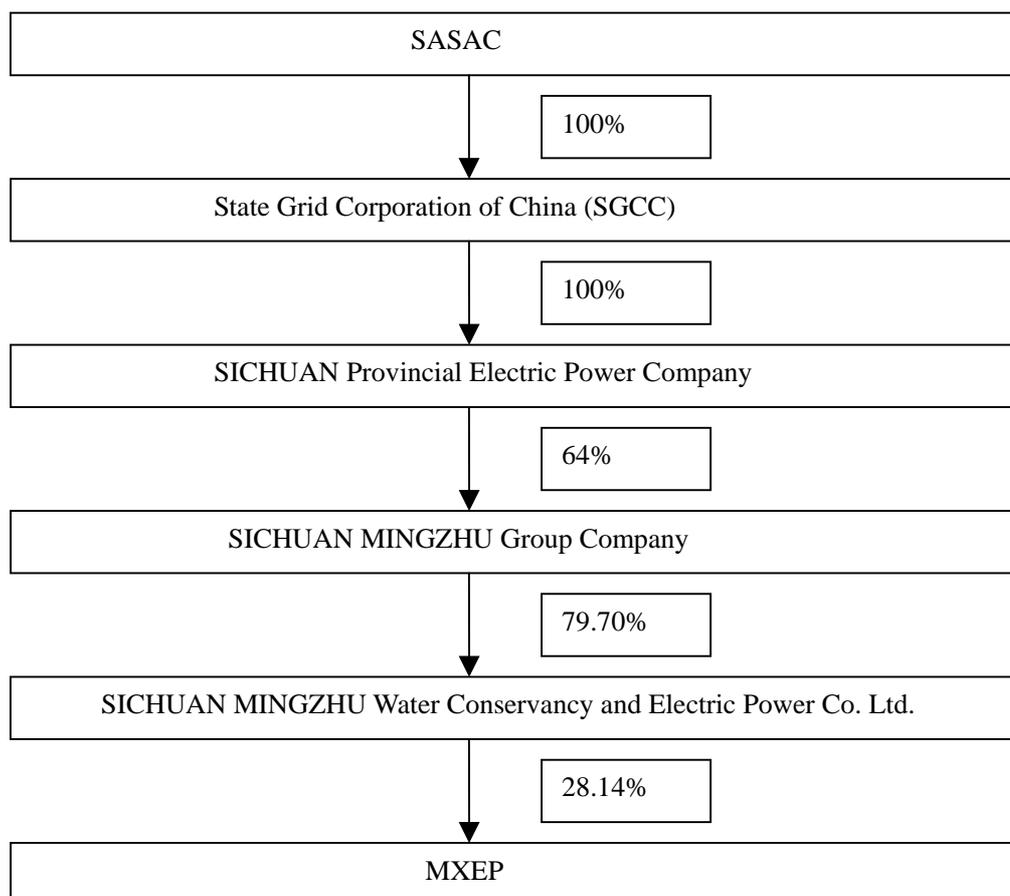
III. About the Case Company and its recent scandal

3.1 Introduction profile of the Company

Sichuan Mingxing Electric Power Co., Ltd located in Suining City, China's south west Sichuan Province. The former identity of MXEP is Suining Electric Power Company, which was a wholly state owned company before 1988. In Apr. 1988, as sole founder, Suining Electric Power Company reformed itself and established Suining Electric Power Co., Ltd, according to the document of "*Suggestions Concerning Expanding Experiments of Joint-stock Companies on Large and Medium-Sized Enterprises Owned by the Whole People*", which was published by Sichuan Provincial Government. Later in the same year, the company issued 2,9000 thousands shares at the price of RMB 1 yuan per share to local public, approved by Suining Branch of People's Bank of China. In June 1997, the shares issued in 1988 were approved by China's Securities Regulation Committee (CSRC) as well as Sichuan provincial government to be listed on Shanghai Securities Exchange (SSE).

The main businesses of MXEP include production of provision electricity, tap-water and natural gas for Suining citizens. The registered capital amounts RMB 264.896 million yuan. The current controlling shareholder is Sichuan Mingzhu Water Conservance and Electric Power Co. Ltd., who is a holding company of Sichuan Mingzhu Group Company, the majority shares of the latter ultimately hold by State Grid Corporateion of China (SGCC) (see chart 2). MXEP now have total 11 branch, subsidiary or holding companies and employs about 2,473 workers.

Chart 2: The Current Shareholder Structure of MXEP



3.2 Financing Activities in the capital market

After listing on SSE, MXEP had twice seasoned issues by right offer, which had been very popular in China's capital market, in 1999 and 2001 respectively (see table 1 of timeline about MXEP). In March 1999 (the stock price of the company was between RMB 12.53 to 13.55 yuan in this month), MXEP offered its then existing shareholders to have right to buy 2 shares with the price of RMB 12.5 yuan for their every 10 shares. It turned out that state shareholder gave up part of its right and the legal person shareholders gave up all of their right to buy the offered stocks and the total amount of RMB 152.25 million yuan was raised. In August 2001 (the stock price ranged between RMB 14.75 to 15.65 yuan in the month), the company again had a right offer arrangement which offered 3 shares at the price of RMB 15 yuan to the then existing shareholders for their every 10 shares. Similarly, this time state shareholder bought 10%

of its offering and legal person shareholders again gave up all of their right to buy new shares (see table 2 for the changes of shareholder structure) and the company raised RMB 350.422 million yuan by this offering.

3.3 Changes of the equity ownership

Table 2 and Chart 3 show changes of the company's shareholder structure after its listing in SSE. We may find the fact that the share percentage hold by different categories (state shares, legal person shares and public shares) of shareholders has been changed several times. The first two changes were caused by legal person shareholders and state shareholders gave up all of or part of their rights to buy seasoned right offers in 1999 and 2001 respectively.

The third change occurred in 2003 when Shenzhen Minglun Group Company (Minglun hereafter) bought out 35.78 million state shares from local government agency of SASAC, Suining Xingye Asset Management Company and 12 million legal person shares from Suining Exlectic Material Company, and then became the largest shareholder with the 28.14% of MXEP total shares. After this buy-out, the percentage of state shares decreased to 7.99% while the legal person shares increased to 36.06%. The state agency deducted state shares by this buy-out because Minglun was a private company.

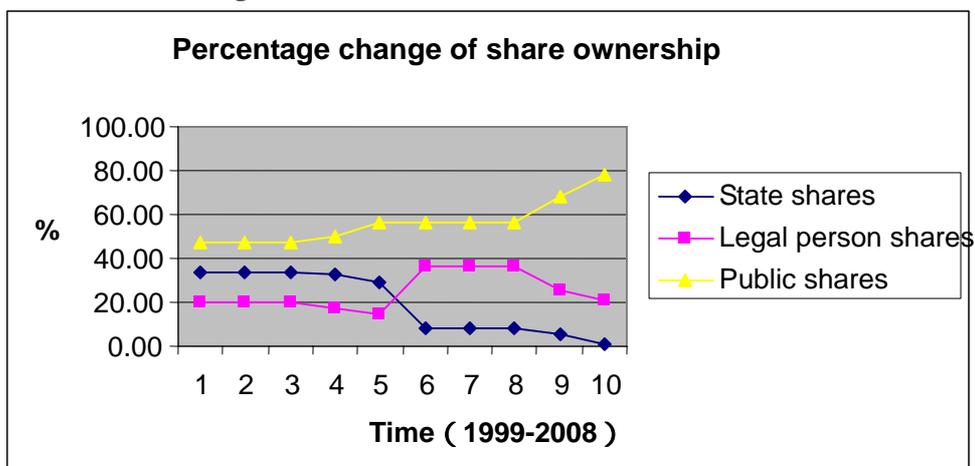
Table 2: The changes of shareholder structure of MXEP (thousands shares)

	Changes of shareholder structure						
	Total shares	State shares	legal person shares	Public shares	Percentage of state shares	Percentage of legal person shares	Percentage of public shares
19970626	61,823.20	20,705.60	12,117.60	29,000	33.49	19.60	46.91
19971231	86,552.48 ^(a)	28,987.40	16,964.64	40,600	33.49	19.60	46.91
19981231	129,828.72 ^(b)	43,481.76	25,446.96	60,900	33.49	19.6	46.91
19991231	146,443.86	47,916.90	25,446.96	73,080	32.72 ^(c)	17.38 ^(c)	49.90 ^(c)
20011231	169,805.37	49,354.41	25,446.96	95,004	29.06 ^(d)	14.99 ^(d)	55.95
20031231	169,805.37	13,574.41	61,226.96	95,004	7.99 ^(e)	36.06 ^(e)	55.95
20041231	203,766.50 ^(f)	16,289.29	73,472.35	114,005	7.99	36.06	55.95
20051231	264,896.45 ^(g)	21,176.07	73,472.35	148,206.32	7.99	36.06	55.95
20071231	324,178.98 ^(h)	18,486.53	83,382.97	222,309.48	5.70 ^(h)	25.72 ^(h)	68.58 ^(h)
20080630 ⁽ⁱ⁾	324,178.98	2,277.59	67,174.02	254,727.38	0.70 ⁽ⁱ⁾	20.72 ⁽ⁱ⁾	78.58 ⁽ⁱ⁾

Notes:

- (a) The reason of the increase of total shares is that MXEP distributed stock dividends in the middle of the year.
- (b) The company distributed stock dividends again in the middle of 1998.
- (c) The company had rights offer this year, which turned out the state shareholder bought 51% of its newly offering shares with assets investment and the legal person shareholder gave up all of its rights to buy its offering shares.
- (d) MXEP had another rights offer in 2001, which turned out the state shareholder bought 10% of its newly offering share with cash and again the legal person shareholder gave up all of its rights to buy its offering shares.
- (e) Approved by the local government, 35.78 million state shares originally held by Suining Xingye Assets Operating Company and 12 million legal person shares originally held by Suining Electric Material Company were bought out by Shenzhen Minglun Group Company. Consequently, the percentage of legal person shares increased to 36.06% of the total shares from that of 14.986% previous year and correspondingly the percentage of state shares in total shares decreased to 7.99% from 29.065% previous year.
- (f) In 2004, the company exercised its profit distribution arrangement of financial year 2003 which included stock dividends as well as stock increase transferred by capital conservation.
- (g) The Profit distribution arrangement in 2004 financial year, which include stock dividends (10:1) and added shares transferred by capital conservation (10:4), was implemented in July 2005.
- (h) By implementing the shareholder reform arrangements.
- (i) It should be noted that the newly added tradable shares after one year moratorium now should be classified to public shares but it doesn't actually mean the change of shareholders unless the shareholders sell the shares on the market.
- (j) Some of original legal person as well as state shares became tradable after the one year moratorium required by the reform package, so basically those shares changed to be public shares after that but still hold by original shareholders.

Chart 3: The changes of shareholder structure



The fourth alteration of shareholder structure occurred in February 2007 when MXEP made its share split reform arrangement, which original shareholders of non-tradable shares might make their shares tradable at the expenses of paying 1 of their share and presenting 4 shares transferred by surplus reserves to existing public shareholders' every 10 shares. The total shares then increased, meanwhile the percentage of state shares as well as legal person shares decreased. A year later in February 2008, after the expiry date of trading moratorium required by CSRC, the original non-tradable shareholders may trade their holdings in the market so some of original non-tradable shares became tradable public shares but still hold by original shareholders. Table 3 shows MXEP's share structure as of Jun 30th 2008.

Table 3: Share Ownership as of June 30, 2008

Name of substantial shareholders	Property of the shareholder	Number of shares (in thousands)	Percentage to total of shares	Shares subject to trading moratorium
Sichuan Mingzhu Water Conservancy and Electric Power Co. Ltd	State holding company	65,069.997	20.07	65,069.997
Suining Xingye Asset Operating Company	State agency	18,486.534	5.70	2,227.585
Suining Xingyuan Technology Co. Ltd	State holding company	18,312.969	5.65	2,104.020

3.4 Profitable Performance of the Company

Financial data showed that the earning indicators of MXEP had a sharp decline in 2005 and continued the weak profitable performance in 2006 financial year. During 2005 to 2006 financial year, it took a RMB 377.15 and 289.90 million yuan from its net income respectively for its bad-loans, debt and investment loss caused by a series of behaviors of securing credit for its related companies, aggressive expanding of investment in different industries under the control of Minglun Group. MXEP also reported a substantial drop of its net assets in these two years (see table 4, Chart 4 and Chart 5).

On April 30th, 2007, MXEP announced that it would be signed by “ST (Special Treatment, used for reminding investors of the risky stocks, which means that the company’s shares may be forced to de-list from the Exchange if it continue to fail of making profit in the next financial year)” since May 8, 2007 by SSE because of its loss of net profit successively in 2005 and 2006 financial year according the SSE regulation of “The Rules of Listing Stocks”.

In March 2008, the company announced in its 2007 annual report that it made a net profit of RMB 88.85 million yuan in its 2007 financial year mainly by selling some of its investment project or equity as well as restructuring its sub-ordinate company of Sichuan Wantong Gas Joint Stock Company. The risky sign of “ST” was got rid of before its stock name in SSE since March 2008.

Table 4: Major Financial Data of MXEP from 1997 to 2007 (RMB thousands yuan for others and Yuan for Earning and equity per share)

	Sales Revenue	Net Profit	Total Assets	Equity	Earning per Share	Net assets per share	ROE (%)
1997	146,490	50,708	276,063	223,666	0.553	2.550	22.23
1998	194,971	78,155	340,227	292,310	0.527	2.250	29.96
1999	206,840	83,109	663,014	580,535	0.532	3.960	18.26
2000	243,471	80,377	942,934	606,113	0.516	4.140	13.26
2001	248,242	78,322	1,362,256	991,661	0.426	5.800	7.29
2002	325,413	78,727	1,425,359	1,030,440	0.476	5.880	7.85
2003	408,878	103,243	2,294,338	1,141,650	0.452	5.560	6.88
2004	547,644	84,140	2,586,968	1,220,695	0.413	5.960	6.56
2005	549,246	-255,833	2,265,096	965,182	-0.970	3.640	-23.20
2006	641,465	-159,124	2,085,979	813,748	-0.600	3.070	-17.99
2007	519,348	88,852	2,101,009	922,598	0.270	2.850	10.15

Chart 4: Revenue and net profit from 1997 to 2007

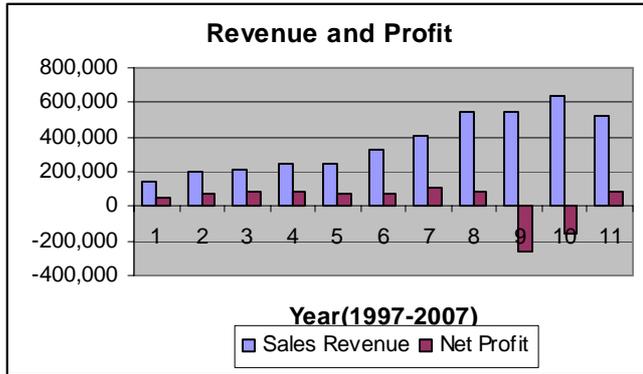
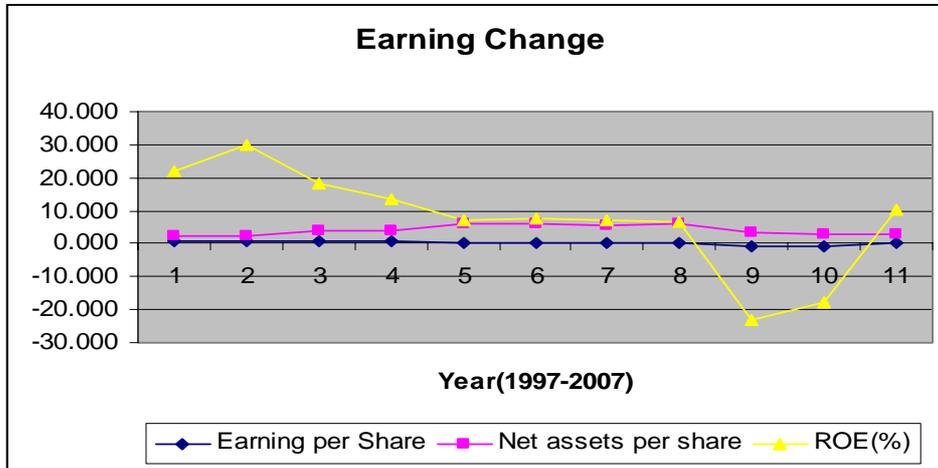


Chart 5: Earning Changes from 1997 to 2007



3.5 MXEP’s Governance Scandal

In July 2004, Sichuan Regulation Bureau of CSRC sent *A Notice of Risk Reminding* to MXEP, which said that some problems had been found from the company’s 2003 annual report. These problems included that its investment (especially in real estate and foreign trade industry which were not the main businesses of MXEP) increased substantially and a big amount increase of bank loans (the balance sheet showed the net increase of RMB 500 million yuan loans during the financial period) in 2003 financial year. In Oct. 2004, the Bureau sent “ *A Notice for Rectify and Reform Within the Specified Time*” to MXEP and demanded the company take measures to control its investment and management risks. The notice put forward the following three problems existed in the company. The first one is about an investment project, Jiemei Center invested by one of its subsidiary companies named Mingxin Kangqiao Co. Ltd., in

which MXEP had 55.5% of shares. It was found that not only this project required a still more capital investment, but also the property right of the project was not registered by the subsidiary company and so it put MXEP's claim in the company at jeopardy. The second problem said that two of MXEP's holding companies, Mingxin Kangqiao Co. Ltd. and Mingxin Shangshe Co. Ltd. had been having abnormal frequent short-term loan activities to other companies, which the related information of those activities had not disclosed to the public. The third problem advanced by the notice said that MXEP had serious flaws in its internal governance mechanisms reflected by un-efficient control of businesses, loan activities and investment for its two subsidiaries.

In 2005, MXEP was involved in a series law suits by Bank of Communication, Huaxia Bank, Shanghai Pufa Bank, Guangzhou Development Bank and China Agriculture Bank for either itself or its subsidiary company's guarantee loans for other companies. The shares held by Minlun Group were then frozen by courts in turn because of the suits. The public investors as well as regulators then found that MXEP had never disclosed these security loan activities and the decision of these activities had not been approved by the board of directors. In Nov. 2005, MXEP made an announcement of finding that two companies, one is HangKang Yili Co. Ltd and the other is Tianjin Jiechao Import and Export Co. Ltd had borrowed its capital of total RMB 143.35 million yuan in the previous month, which Minglun Group provided security for this debt. The announcement said that both the debtors and guarantee provider failed to return the debt on schedule and MXEP had filed a suit for the debtors and its largest shareholder, Minglun Goup. .

On Dec. 15, 2005, CSRC Sichuan Branch announced that it put on file for investigating MXEP's series behaviors against *Securities Law of People's Republic of China*. On Dec. 29, 2005, MXEP made a public disclosure about Yimng Zhou's being detained by Suining Security Institution in the simple reason that he was suspected to have embezzled huge amount of capital from MXEP. It soon announced that other directors and key managements came from Minglun Group in MXEP were also detained by local Security Institution. According to the preliminary result of investigation made by Suining Security Office, it is estimated that MXEP has capital loss of about RMB 476 million yuan caused by the majority shareholder's behavior of malicious external

investment, being credit guarantees for other companies against the related laws and regulations, false trading and having made short-term loans against laws.

In 2006, MXEP had a series announcements about its involvement of law suits for its several security credit for other companies and said that the company only had heard of the security loan behaviors after it received the legal statement from the related courts and the activities were the illegal behaviors of Zhou Yiming as well as Minglun Group because the board never discussed nor had a resolution for these activities.

In September 2006, Suining Intermediate People's Court entrusted an auction agency for auctioning the shares held by Minglun Group according the related laws. SICHUAN MINGZHU Water Conservancy and Electric Power Co. Ltd won the bid and became the largest shareholder (see chart 4 for the current shareholders' structure of the company) of MXEP thereafter.

Required by the regulators and directed by the new largest shareholder, MXEP took series measures, including revising its corporate bylaws and information disclosure rules, selling some of its investment projects and establishing its internal financial management rules, to improve its internal governance.

IV. Analysis on MXEP case

4.1 The Institutional Feature of the MXEP Case

The corporatization of MXEP represents a typical reform track of China's SOEs, which is "Gufen Hua" at first and then privatization. As we see in the column of "Related Backgrounds" in table 1, it's easy to be found that the framework of laws and rules regulating China's listed SOEs as well as capital market barely came into exit in the process of along with the development of the capital market. For example, although China's established Shengzhen and Shanghai Securities Exchange in 1990 and 1991 successively, the first company law governing the organization and operation of joint stock companies just has executed since 1994. MXEP listed in SSE in 1997, but the first China's Securities Law, regulating issuing and transacting stocks, had not come out until 1998. Lots of administrative regulations and procedures played important roles before the law was implemented. As we mentioned in previous part, the found of MXEP was

decided by Suining municipal government and guided by a document published by Sichuan provincial government. Furthermore, the so-called administrative power has been still effective even after the laws being put into practice. Again from table 1, we see the transfer of MXEP's largest shareholder in 2003 was mainly decided by Suining government rather than the board or shareholders' conference. From these facts, we may say that China's capital market has been governed by a mixture system which consists of administrative functions and market rules.

4.2 The Role of the Largest Shareholder in the Corporate Governance of MXEP

There had been twice important shareholder changes since MXEP's listing in SSE, one is that state shareholder, Suining Xingye Asset Operating Company and state-owned legal person shareholder, Suining Municipal Electric Power and Material Company together sold 28.138% of MXEP's total shares to a private company, Shenzhen Minglun Group Co. Ltd. In this process, 72.51% of state shares (which took 21.08% of total shares of MXEP) and almost 50% of state-owned legal person shares (which was 7.07% of the company's total shares) were dropped out. Another important change is that another state owned company, Sichuan Mingzhu Water Conservancy and Electric Power Co. L. td took over the shares which had been hold by Minglun Group after the corporate scandal

The most significant change of largest shareholder occurred in March 2003, when Shenzhen Minglun Group Company, a large multi-business private investment shareholding company established in 1997 bought 3,578 state shares and 12,000 thousands legal person shares and then became the largest shareholder of MXEP. Later in June 2003, Minglun reshuffled the board and sent 5 persons to either as directors or as top managements of the listed company. MXEP's development strategy had become much more aggressive all of the sudden after this change. The company revised its corporate bylaws, in which the limitation on board decision about external investment was changed to no more than 30% of the company's net assets from that of 8%. In Aug. 2003, it invested RMB 270 million yuan to become the largest shareholder of Mingxing Kangqiao Co. Ltd and hence involved in real estate industry. One month later, it invested RMB 150 million yuan to found Mingxing Trading Company aimed to engage

in foreign trade businesses.

Obviously, the change point of MXEP's investment and financing behaviors started from the transfer of the majority shareholder from the state agency to private Minglun Group in 2003. The background of the company's privatization is that China's SOEs, especially the small and medium ones were experiencing the "strategic adjustment in the distribution of the state economy" guided by the government's 1999 principle of deepening SOE reform. Most of the small and medium SOEs were privatized in this process. The Fourth Plenum of the Chinese Communist Party's 15th Central Committee held in September 1999 adopted a "decision" that calls for "strategic adjustment" of the state sector by "withdrawing what should be withdrawn". Due to this policy issuance, the privatization process was becoming politically more acceptable (Tenev, Zhang and Brefort, 2002). According the announcement of State-owned Assets Supervision and Administration Commission (SASAC) that was established in March 2003, the number of state-owned and state-controlled enterprises declined from 238,000 in 1998 to 150,000 in 2003¹. The number of employees in SOEs decreased from 71,310,000 at the end of 1997 to 41,310,000 at the end of 2003²

We find that the behaviors of the private majority shareholder were more unfavorable to the minority shareholders than that of the state agency or state holding company. I think this is most probably because that there is almost no effective discipline power for the key manager, Zhou Yimin. Secondly, it is evidently that the influence of the majority shareholder in the company's decision making process was very powerful.

4.3 The Role of Board in MXEP Corporate Governance

Theoretically, directors in a company's board represent the interest of different shareholders. According the corporate law, the mission of the board is to select the CEO, monitor management, and vote on important decisions such as investment, mergers & acquisitions, changes in remuneration of the CEO, etc. It's also worth to be mentioned here that the role of a board chairman in the decision making of a China's company is different with that of other countries. In China, a chairman of a board is generally sent

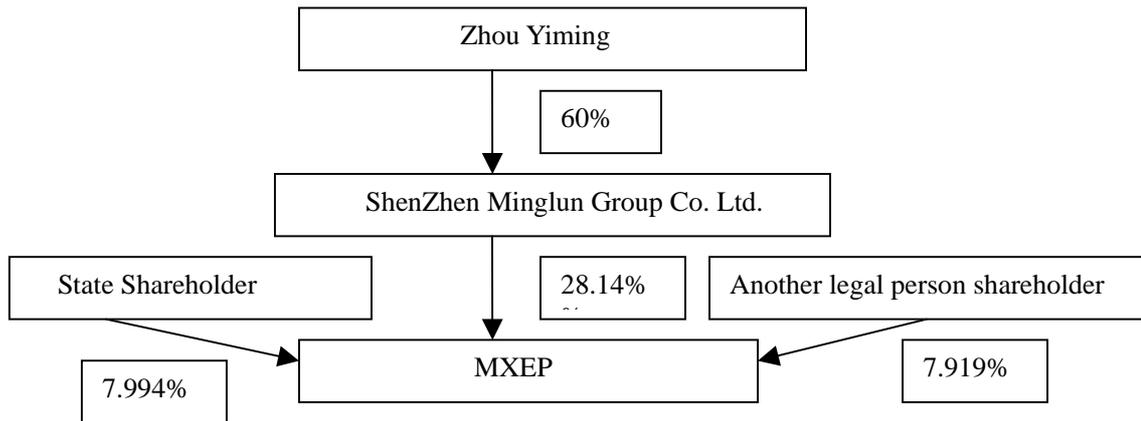
¹ China Daily, Page 11, Sep 30, 2004, SOE Reform Heads in a Right Direction .

² This number was given by Shao Ning, who is a vice director of SASAC, on Oct. 10, 2004 when he made a presentation in Qinghua University.

by a controlling shareholder to be in charge of managing and operating businesses and thus is a real first management in a company and a CEO is like a second agent selected by board chairman for helping the later to implement the corporate strategy (Zhao Zhenyu, et. al, 2007).

In the case of MXEP , firstly, Board Chairman, Zhou Yiming, was the actual dominator of the company (see Chart 6) . Secondly, other top management, including General Manager Zhou Xiuhua, were the board members, in which most of them came from Zhou Yiming’s Minglun Group and Zhou had a decisive influence for the selection of the directors as well as other top management. The board was totally captured by the management of the company in this case.

Chart 6: The Actual Dominator of MXEP



Source: MXEP 2003\2004\2005 Annual Report

Form 2003 and 2006 annual reports of MXEP, we may find that almost all directors were changed following the transfer of the largest shareholder. In 2003, after Minglun Group became the dominate shareholder, 9 of the 11 former directors, all 2 independent directors and 5 directors in the supervising board were replaced by new ones. After Sichuan Mingzhu Water Conservancy Projects and Electric Power Ltd gained the position as a controlling shareholder of MXEP, all of 7 directors and 4 independent directors, 3 of 5 directors in supervising board in 2005 were removed and the new ones

were put into the positions. The twice changes of board members showed that the selection of directors was decided by the largest shareholder. We also find that this is always the case in China's listed firms if we look at the directors' replacement following by a change of a majority shareholder.

In the case of MXEP, the board failed to play the role of monitoring the behavior of the management supposed by both the related theory as well as the corporate law.

Required by CSRC regulatory rules³, MXEP introduced independent director institution in 2002 (two people were elected to be independent directors in May 28 of the year). In June of 2003, the number of independent directors was increased to four people. The previous two independent directors left off the company and other 4 fresh people were elected following the change of the largest shareholders. Intuitively, We cannot help but suspecting the degree of independency of these "independent" directors. It turned out that there was almost no voice from these independent directors during 2003-2004, when MXEP made risky external investments, being credit guarantors for other companies against the related laws and regulations etc.

Similar as the independent directors, if we compare the related information disclosed in its 2002 and 2003 annual report, all of 5 directors in supervising board were also changed after the transfer of the largest shareholder. Furthermore, if we look at the member structure of the supervising board disclosed in 2004 annual report, except one of supervising director named Shui Goumin, who was the general manager of the state shareholder, Suining Xingye Asset Operating and Management Company and did not hold a management position in MXEP, all other 4 supervising directors concurrently hold a management posts such as vice chairman of the board, director of administrative affairs etc. and with the chairman of supervising board simultaneously hold the position of Vice Chairman of the board of the company. In another word, 80% supervising directors concurrently were under the lead of the CEO. That is why the role of supervisory board is traditionally very weak in supervising the behavior of management in listed firms and it even became weaker after the introduction of independent director institution (CFA Institute, 1999, 2007, etc.)

³ In August 2001, the CSRC issued specific guidelines on the qualifications of independent directors of listed companies, namely, the "Guideline on Establishment of Independent Director System in Listed Companies."

During the scandal of MXEP, the board or directors had no monitoring or discipline role for the management. Actually, during 2003 to 2005, the board was controlled by the key person, Mr. Zhou Yiming, who was then also the decision maker of MXEP. Obviously, there was an institutional vacancy in the internal governance of the company. Some empirical studies also find that this situation widely existed in China's listed firms. For example, Li Wei-an and Sun Wen (2007) found that the responsibility and obligation of directors and independent extent of board has no significant influence on firms' operating performance.

4.4 The Role of State Ownership in Corporate Governance

Like some other listed companies in China's capital market, MXEP had been experienced a gradual change from a state-owned enterprise (SOE), a joint-stock company with the state as its largest shareholder to a joint-stock company with a private group company as its block shareholder. The scandal occurred during the private Minglun Group as its majority shareholder. MXEP was bailed out by a state holding company later. After its new largest holder, Sichuan Mingzhu Water Conservancy Projects and Electric Power Ltd took over the company, it gradually get rid of difficulty and return to normal businesses. In MXEP case, both Suining Xingye Asset Operating and Management Company, the former majority shareholder, and the block holder after the scandal are state holding companies. Contrary to conclusions that some literatures (for example: Xu Xiaodong & Chen Xiaoyue, 2003⁴) hold about the unfavorable role of state as a first largest shareholder in listed firms, state holding companies have done a better job for its role in corporate governance compared with the behavior of the private Minglun Group as a majority shareholder. In this case, we also failed to find that established theory that think "redistribution of control rights to private economic actors would limit chances for rent-seeking behavior and other forms of private enrichment (Shleifer Andrei and Vishny, 1994)".

Considering that corporate governance acts as a *monitoring* and *discipline* device for ensuring that management pursues value-maximizing goals, we may find that China's

⁴ One of the main conclusions they had is that firms under the control of the government shareholder have lower value, poorer firm performance and weaker governance than the comparable firms under the control of a non-government shareholder. The paper was published in *Economic Research Journal*, 2003(02).

state shareholders actually have been playing such a role in their holding listed firms, by the way of selecting capable and responsible directors or top management and having a system to assess their proficiency. Although it has been criticized that this system is anti-corporate spirit and has strong government administrative feature, in the environment which the market of professional managers is not in the position, the administrative system of selecting and assessing SOEs' managers is an effective way of monitoring and discipline device for the corporate governance of listed SOEs.

The positive role of a state agency or a state owned company as a majority shareholder in monitoring the behavior of top management in a listed SOE may reflect in following aspects. The traditional managers' assessment and selection mechanism used by state agency or state company for sending a chairman to their holding listed firms is effective in the environment that there are no market of professional managers. Some empirical studies about the effectiveness of corporate governance of reformed SOEs have provided proof for this prediction. For example, Zhao Zhenyu, Yang Zhishu and Bai Chong-en (2007) found that indicators of accounting performance like ROE and EPS have a significant positive relationship with non-routine changes of a chairman of a board in China's listed companies. Unlike some views about the un-effectiveness of the largest shareholders in which most of them are state agency or state owned companies, Lv Jun, Li Zhaoxia and Hu Jie (2008) also found that the majority shareholders in China's listed firms play an effective role in the corporate governance. The probability of adverse selection of top management in reformed SOEs is weakened because their performance in the position is monitored by related state agencies or parent state companies.

4.5 The Implication of the Case

As we already know, Chinese stock market had been regarded as a financing channel for SOEs from its very inception and did not naturally emerge from the market like US Berle-Means companies. The basis of the system was dictated directly by the relation between the government and the market. As we have found in MXEP case, from the reform arrangement and the decision of becoming a public company to the transfer of the majority shareholder, it has to be approved not only by CSRC but also by the local

government. It's long been criticized that the government administrative intervention should be blamed for listed SOEs' disappointing governance situation. We think that this may have been exaggerated in the simple reason that the newly established framework of related laws and regulations has not been effectively worked in the operation of Chinese listed SOEs. If we don't want to leave institutional vacuum in the reform process, the administrative measures of government intervention are still essential. It seems that the government intervention and the market internal logic are complements rather than substitutes in this transition process.

Another point related to the government intervention is the state being a majority shareholder in listed SOEs. Many commentators as well as economists think that this is the main problem which caused the corporate governance failure of the listed SOEs. From MXEP case, we find that the transfer of majority shareholder from state agency, Suining Xingye State Assets Operating Company, to a jump-start private company, Shenzhen Minglun Group Company is the beginning of series wrongdoing of MXEP. On contrary, MXEP had been doing OK before the transfer. Here we do not mean that the state should maintain a leading position for its holdings in listed SOEs, we would rather express that rash privatization may cause more damage.

As we also can see in the process of MXEP case, the board system as well as independent director institution did not act as it had expected. The board of supervisors has just been a matter of form in the governance organization in the company. Still, the failure of MXEP governance mainly caused from the lack of actual internal restricting mechanisms for the top management.

V. What Has Been Missed in the Process of the SOE Reform

From the above analysis, we find that the main contributing factor of MXEP scandal is the institutional vacancy in the internal corporate governance or lack of discipline device for the key management of the company. Some may ask that if MXEP is a special case or it reflects a general internal governance circumstances of a reformed SOE. For understanding this situation, in this section I try to review the major policies Chinese government has been taken in the process of China's SOE reform.

5.1 The Gradual Progress of China's SOE Policies

In order to find the logic in the process of China's SOE reform, a brief review of the related main policies during past 30 years reform is necessary. From my perspective, China's SOE reform can be divided into following three stages.

China has started to reform of its industrial sector since 1984. The first stage may be called pre-corporatization period, which is from middle 1984, marked by the issuance of "*On Regulations of Further Expanding the Autonomy of State-owned Enterprises*", to 1993 when the decision of starting to establish the "modern enterprise system" was made by the Third Plenary Session of 14th Party Congress. The main characteristic in this period is to increase the autonomy of managers for promoting SOEs' efficiency. Furthermore, other two main policy changes (Tenve, Zhang and Brefort, 2002) should also be noticed. One is that variety of contracts under the "contract responsibility system" has introduced beginning in 1987. Directors of enterprises that had entered into this contracting system were given greater control over their enterprises' operations in return for meeting profit remittance targets. Meanwhile, the government also gave the managers of SOEs the authority to rationalize their work force by allocating surplus labor from production to other tasks or training. Another one is, in 1992, the government directly stipulated that contracts under the responsibility system could give managers additional autonomy, including the rights to make production decisions, negotiate prices for outputs and inputs, purchase goods and materials, hire workers and determine wages and bonus for their employees.

The second stage of China's SOE reform is the corporatization process from 1993 to 1998. In this period, the government took further measures to redefine the property rights of SOEs and diversify SOE's ownership. The "*Decision on Issuances Concerning the Establishment of a Socialist Market Economic Structure*" was enacted in 1993, which created the concept of "modern enterprise system". According this concept and with provisions for full separation of the state's exercise of ownership rights from the enterprise's exercise of legal person property right, the Corporate Law was promulgated in the same year and have been put into practice since July 1994. The key words of this period are "gaizhi", which means transferring SOEs to joint stock companies through corporatization, and "shangshi", which means supporting some of the reformed SOEs to

list in Shengzhen or Shanghai Securities Exchanges. The number of listed firms dominated with reformed SOEs increased very rapidly, from 53 in 1992 to 851 in 1998. Meanwhile, the initiative of giving more decision-making freedom to SOE managers had been kept but the conception was changed to be “decreasing government intervention”. For example, in late 1998, the government ordered all party and government administrative organs to sever their links with the enterprises they control (World Bank, 1999).

The third stage of the SOE reform is from 1998 to the present. It might be called “shareholding restructuring” or privatization process. In 1998, the government introduced two types of reform method to SOEs. One is “Zhuda Fangxiao”, which means that regarding the large companies, it converted them into shareholding companies with large government ownership, and for the small companies it allowed them to be owned by private investors. The other is shareholding restructuring, which asked SOEs to market their assets or shareholding that take the form of limited liability or joint stock companies. In the later vein, the reform of share split structure started from 2005 and finished at 2007.

5.2 The Mechanism of Monitoring managers’ behaviors has been neglected

From the above policy sequence, we may find that the whole process of China’s SOE reform is try to free SOEs’ from direct government administration by giving managers more and more power to make their SOEs’ decision, while it seems that there is no concrete policy strategy to remind that the increasing discretion of managers need to have other powers to monitor on it, especially in the environment that market institution is still in the process of building. During the process, not only some of the newly enacted laws are not quite contextual in China’s economic situation, but also some of the articles in text laws are vague and hard to enforce.

In early 1990s, when the efficiency improvement in SOEs remained stagnant and new problem of high debt ratio became the great concern after “shifting from allocation by Ministry of Finance to bank loans for SOE capital distribution, it was realized then that more measures should be taken in the SOE reform. The initial approach of “increasing the autonomy” used in 1980s was reviewed. The general conclusion is that the

contracting responsibility system might have been provided incentives for good performance, but it is failed to penalize bad performance (Pannier, 1996) and the approach was successful in giving SOE managers short-run incentives but fail to let them take a long-run view in running their enterprises⁵ (Weiyang, Zhang, 2004).

Although different opinions emerged in the second period and the different policies were taken, the initial approach of giving managers more freedom has been kept. With the SOEs' bad assets mounted⁶ and the issue of SOE overinvestment⁷ became serious, the government resorted to measures such as the corporatization and letting SOEs to finance from stock market.

The purposes of these policies are often recognized as following. Firstly, commentators criticized the supposed unity of ownership and control in the hands of the state under the old system, with the resultant imposition of non-profit-maximization objectives on enterprise managers through "bureaucratic interference". Secondly, they pointed to the issues of conflicting objectives from multiple state agencies with authority over the enterprises. Thirdly, they pointed to the absence of an effective ultimate principal with an interest in, and ability to, police managers and ensure efficient operations (Clarke, 2003). From these purposes, we can find that corporatization is supposed to separate state ownership from state control and thereby free managers from such interference, so that they can pursue efficient and profitable operations. Attention again was paid on "free managers" without adding feasible corresponding constraints on possible power abuses.

Although two-tier board structures, the Board of Directors and the Board of Supervisors is introduced by the corporate law, but it becomes a common knowledge that it is very weak both in practitioners and academic literatures (Allen et al, 2002; Teven et al, 2002 etc.).

In some extent, those new approaches taken in the third stage of the SOE reform were aimed to solve the problems more outside the SOEs, and less attention was paid to the causative factors of SOE inefficiency inside the SOEs. Moreover, further discretion

⁵ Zhang reviewed this point in an interview conducted by Economy Observation (Jingji Guancha Bao) in Aug. 2004, Economy Observation, Aug 28, 2004.

⁶ About this issue, read Wang Weiguo, 2002, The Bad-Assets of Banks and Corporate Rescue in China.

⁷ Chunlin Zhang, Guoyou Qiye Gaige Yu Guojia Rongzi (SOE reform and State Financing), Journal of Jingji Yanjiu, (Journal of Economic Study), No. 4, 1997.

such as “hiring labors and deciding workers’ wages and bonus” given to SOE managers during this stage made it impossible for corporate insiders such as employees or a subordinate of a company’s CEO to monitor management behaviors. In more and more extent the employees’ fate was up to their managers, given that unemployment gradually became more common along with the SOE reform, especially for average Chinese workers whose jobs are relatively easy to be replaced in the natural environment of the huge population. The point is that enhancing the monitoring role by corporate insiders who have information advantages in the meantime was neglected. Besides, the government control was decreasing in the same time. In this way, the evolution of SOEs’ culture tended toward a direction of emphasizing the authority of managers and reducing constraints power both from the government administration system as well as corporate insiders.

In the old system, both managers and employees of SOEs were under the leadership of the local government. Employees used to have their voice heard by giving the judgment on one who would be promoted to the position of managers to the government. Although managers do had stronger influence in some administration decisions in their enterprises, they would not do something that against the willing of workers because doing that would put their future promotion on danger. As the authority of managers increasing and the function of government decreasing in managing SOEs, workers who have different opinions with their managers have more dangerous to be laid off. In this sense, the extent of workers’ participation in operating SOEs are lower than that of old days, although the entire old system is much less desirable.

The increase of manager’s authority discretion also has a detrimental influence on managers’ paying attention to the interests of shareholders including not only minority shareholders and legal person shareholders, but also state shareholder as well. At least this is partial reason of corporate governance failure in some listed firms as reflected typically in MXEP case as well as other earlier famous cases in China’s capital market such as Guangxia (Yinchuan) Industry Co. Ltd, which nicknamed by observers as “Chinese Enron” and Lantian Co. Ltd⁸ etc..

The so called “insider control” problem became worse off in the privatization stage.

⁸ For more information about Guangxian (Yinchuan) and Lantian, Search for Caijing (Finance) articles in 2001 .

The practices intensified the SOEs' culture of emphasizing the authority of managers.

In research literatures about corporate governance of Chinese listed firms, two main problems often were cited. One is that the parent companies of listed firms arbitrarily expropriate assets or capital of listed firms, and thus harm the interests of minority shareholders. Another is the weak constraint for managers of listed firms (Tenev et al, 2002; Lu Yi, 2003; Wong et al, 2004; etc.). As we can see in the policy measures during the reform process, still much attention was paid to the former one. Moreover, for the first problem, following questions should be further asked. Does the state shareholder generally gain benefits from that? Are the managers in listed firms and their parent firms do so under the pressure of government? It's not hard to gather instances of some managers' gaining their own benefit or doing inside deals without concerning shareholders (including state shareholders) interests. In this sense, at least part of the origin of the first problem is actually caused by the second one.

To conclude this part, although weak constraint for SOEs' managers is not a new issue, the extent of its harmfulness and the degree of its seriousness has been increasing along with the increase of market resources. But it seems the policy designers have relatively neglected this factor in mapping the SOE reform path. This is not only the origin of loss of state assets and public complaints, but also has led the Chinese enterprise cultural to evolve to an undesired way of depressing insiders' role to monitoring power abuses. From this policy analysis, we may easy to understand that the lack of monitoring managers' behavior is in common in China's corporations.

VI. Concluding Discussion

This paper studies a case of corporate governance scandal of MXEP, a former listed SOE and its majority shareholder was transferred to a private group company, Shenzhen Minglun Group Company from a local state agency, Suining Xingye Assets Operating Company. The company had experienced series wrongdoings and thus caused a quite big loss led by its private majority shareholder. It was bailed out by a state holding company affiliated with SGCC after the scandal.

The case analysis shows that there was an institutional vacancy in MXEP corporate

governance during the period. We find that the internal disciplining mechanism of two-board system was not effective especially when MXEP's majority shareholder was the private group. The analysis of the role of the majority shareholders shows that it seems the state shareholder might have played a better check-and-balance role in monitoring the top management.

Although some economists as well as commentators take a view that too much government intervention, especially by the way of being a largest shareholder in listed SOEs, should be blamed for the low level of corporate governance in Chinese listed companies. In MXEP case, it is obviously that the transfer of majority shareholder to be a private company is one of the reasons to cause scandal. Another major reason of MXEP corporate governance failure was not caused by lack of autonomy inside the company, but short of checking and balancing power for its top management.

For understanding more general situation of China's corporate governance, the paper then turn to review the process of China's SOE reform as well as the major policies, considering that China's SOE coporatization has been facilitated by the government with a top-down approach. I find that too much attention has been paid to decreasing government intervention while the constraining mechanism for manager's power discretion has been relatively neglected in the course of SOE reform. This one sided focus on decreasing government intervention have made management discretion become the major agency problem of China's corporate governance. From the policy sequence, it's not hard to know that the lack of monitoring mechanisms on the behavior of top management is in common in China's corporations.

There are two implications we may get from these analysis. Firstly, from MXEP case, we think that government intervention and the market internal logic may be complements rather than substitutes at least in current China's condition. In that way we think that Chinese government should keep play a major role in SOEs at least for a relatively long time, given that insufficient effective institution to discipline the discretion of top management and the professional managers' market still need time to be mature. Therefore, I think that more attention be paid on the expropriation of powerful management rather than government intervention in institutional perspective and more anti-director rules and mechanism should be established in future policy

design. A practical start point of this may be the promotion of employees' participation in monitoring top management.

Secondly, although it is too early to evaluate the effects of the recent revisions of China's *Company Law* and *Securities Law*, in which legislators tried to increase the degree of "company autonomy" and encouraged companies to deal with their problems by internal negotiation rather than resort to law or government administration intervention, we may find it would not facilitate to improve the situation in cases like MXEP, not mention that it is still a long way to go for China to make the book law effective in practice. As to the shareholding reform, although it may help to the formation of pricing function of the capital market, it may not improve the situation of corporate governance because it seems that the reform cannot strengthen the monitoring role on top management in the perspective of internal governance. It has been expected that shareholding reform may facilitate the merger and acquisition activities, and thus may give managers more pressure to maximize the interest of shareholders. But according Aoki (2003)'s implication of "institutional binding" and Jone (1994)'s thinking about China's business culture, either from China's corporate law, which is the combination of Japanese model and German style of corporate governance and the fact of bank dominated financing system, or from the culture tradition of pursuing harmonious business environment, it may be unrealistic to rely the M & A market to play monitoring role on management from outside governance.

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Table 1: The Timeline of Mingxing Electric Power case

Year	Main Events	Related Backgrounds
1988	<ul style="list-style-type: none"> Guided by the local government, SuiNing Electricity Company reformed itself and found “SuiNing Electric Power Shareholder Limited Company” in April this year, which is the former identity of the case company In May of 1988, the reformed company was approved to issue 29,000,000 shares at the price of RMB 1 yuan per share 	<ul style="list-style-type: none"> China’s SOE reform started from 1984, marked by the issuance of “On Regulations of Further Expanding the Autonomy of State-owned Enterprises.” From 1987, the “contracting responsibility system” was introduced to SOEs, and managers in SOEs were given more freedom in management.
1990		The establishment of Shenzhen Securities Exchange and the Shanghai Securities Exchange.
1994		The Company Law of PRC started to execute since July 1 this year.
1997	On June 27 th , the shares issued in 1988 were approved to be listed on Shanghai Stock Exchange and the first day price in SSE was 23.08 yuan per share	
1998	Sent each shareholders 3 extra shares (like a stock split) as well as 1 share transferred from capital conservation (like stock dividends) for every 10 existing shares	<ul style="list-style-type: none"> Securities Law of PRC was enacted East Asian financial crisis
1999	MXEP had rights issue with the rate of 10 old shares could get another 2 shares with the price of RMB 12.5 per share, and there were 16,615,140 shares offered this time and total RMB 152,250 thousands yuan was raised.	<ul style="list-style-type: none"> The CPC Central Committee released a document on several important issues related to SOE development and reform, indicating that SOE reform entered another phase of "strategic adjustment in the distribution of the state economy."

		<ul style="list-style-type: none"> • Securities Law of PRC had been exercised since July 1 this year.
2001	Another rights issue which ten of existing share rights entitled a shareholder to buy 3 more shares at a subscription price of 15 yuan per share and there had 350,422 thousands yuan been raised.	
2002		CSRC published “The Guidance for Corporate Governance of Listed Firms”
2003	<ul style="list-style-type: none"> ● In March, Suining Municipal government decided to sale 47,780 thousands shares at the total price of RMB 0.38 billion yuan to Shenzhen Minglun Group Company who therefore hold 28.14% of total MXEP shares and became the largest shareholder of MXEP ● The new board showed up after the sale and then some of the rules in MXEP’s Corporate Regulations were re-wrote, e.g. the limitation on board decision for outside investment was changed from no more than 8% to 30% of the company’s total net assets ● In the second half of this year, the new board decided to invest RMB 270,000 thousands yuan to become a major shareholder of Mingxing Kangqiao Co. Ltd., a former subsidiary wholly-controlled by Minglun Group and invested in real estate projects. 	China established State-owned Assets Supervision and Administration Commission (SASAC)
2004	<ul style="list-style-type: none"> ● MXEP decided to as a major investor, invest RMB1,100 million yuan to establish “Sichuan Minglun Chemical Co. Ltd.” ● MXEP guaranteed a loan of RMB 1,000 million yuan for its sub-branch, Minglun Kangqiao Co. Ltd and warned by CSRC Sichuan Branch for this behavior ● MXEP received a Risk Warning Notice from CSRC Sichuan Branch on July 29 and after investigation on the company’s outside investment and guarantee behaviors, the Branch demanded it cope with the problems in a limited period. 	The debate about loss of state-owned assets in the process of SOE reform has been initiated by Larry Lang, professor of HongKong Chinese University
2005	<ul style="list-style-type: none"> ● All shares owned by Minglun Group were frozen (from July 11th to the same day the next year) by Shenyang Branch of China Communication Bank because Minglun had guaranteed a loan for a company which then could not return the debt. ● In Dec., CSRC Sichuan Branch put MXEP on file for investigation and prosecution, three directors who came from Minglun were detained by Suining Municipal Public Security Bureau for their criminal acts of diverting capital from MXEP; ● On Dec. 5th, The right of controlling shareholder was entrusted in the second largest shareholder Suining Xineye Assets Management and Operation Company for one year ● On Dec. 30th, Zhou Yiming, the president of the 	<ul style="list-style-type: none"> ● CSRC and China Bank Regulation Committee co-published “The Notice Concerning Standardizing the Behaviors of Guaranteeing for Other Companies” ● CSRC enacted “Managing Arrangements on Shareholding Incentives of Listed Companies” ● Shareholding reform started with two batch of listed firms for experiments and then was widely carried by more and more listed companies ● CSRC, SASAC, Ministry of Finance, People’s Bank of China and Ministry of Commercial

	board of directors was also detained for his criminal act of embezzling funds from MXEP	Business co-published file named “Guiding Views on Shareholding Reform of Listed Companies” ● CSRC Published “Managing Arrangements on the Reform of Shareholding Separation”.
2006	<ul style="list-style-type: none"> ● On Jan 16th, MXEP announced that it was estimated that it would have a considerable loss in 2005 for the simple reason that the company have to deduct a big sum of allowance for the losses caused by its security credit for other company, the embezzlement capital by its largest shareholder as well as two major risky investments. ● On Sep, the 28.14% of total shares originally hold by Minlun was auctioned and got by Sichuan Mingzhu Water Conservancy Projects and Electric Power Ltd, who then became the new controlling share holders of MXEP. 	<ul style="list-style-type: none"> ● The revised Corporate Law of PRC and Securities Law of PRC have been executed since Jan. 1. ● The shareholding reform were spread in listed companies and there were 1269 listed companies completed or in the process of the reform at the end of the year.
2007	<ul style="list-style-type: none"> ● On April 30, 2007, it announced that the company would be signed by prefix of “ST” before its name in SSE because of the consecutive loss in 2005 and 2006 financial years since May 8,2007 ● Implemented the shareholder reform, which the arrangement is that non-tradable shareholders transfer their one share and another 4 bonus share from deduction of corporate reserve fund to tradable shareholders’ every 10-share. The reform then increased MXEP’s total shares to 324,178,977 and also changed the shareholder structure which includes not only all shares became tradable but also the further decrease of shares hold by state or legal persons. 	The year saw the most active transaction in China’s stock market history and the benchmark Shanghai Composite Index hiked its all time high on Oct. 16.
2008	<ul style="list-style-type: none"> ● SSE decided to get rid of the company’s “ST” before its stock name since March 3rd, 2008 	