

# ALIBABA: A CASE STUDY OF SYNTHETIC CONTROL

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*Alibaba, the NYSE-traded Chinese e-commerce giant, is currently valued at over \$700 billion. But Alibaba’s governance is opaque, obscuring who controls the firm. We show that Jack Ma, who now owns only about 5%, can effectively control Alibaba by controlling an entirely different firm: Ant Group. We demonstrate how control of Ant Group enables Ma to dominate Alibaba’s board. We also explain how this control gives Ma the indirect ability to disable (and perhaps seize) VIE-held licenses critical to Alibaba, providing him with substantial additional leverage. Alibaba is a case study of how corporate control can be created synthetically with little or no equity ownership via a web of employment and contractual arrangements.*

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## INTRODUCTION

Alibaba Group Holding Limited (Alibaba) conducted one of the world's largest IPOs on the New York Stock Exchange in 2014<sup>1</sup> and by early 2021 was worth around \$700 billion.<sup>2</sup> Founded by Jack Ma (Ma) and others, by the end of 2020 Alibaba had become one of China's most valuable publicly traded companies,<sup>3</sup> as well as the world's second-largest e-commerce firm<sup>4</sup> and the ninth most valuable firm in the world.<sup>5</sup>

Alibaba has a unique governance structure: a majority of Alibaba's board is appointed by the so-called Alibaba Partnership (the Partnership), consisting of several dozen individuals.<sup>6</sup> Thus, as is widely understood, the Partnership controls Alibaba.<sup>7</sup> More probing analysis shows this power is actually concentrated in the hands of several people, as the Partnership itself is effectively controlled by a small Partnership Committee, of which Ma is a perpetual member.<sup>8</sup>

In this Article, we dig even deeper into Alibaba's control arrangements, and reveal a surprising fact: Ma, who now owns less than 5% of Alibaba,<sup>9</sup>

<sup>1</sup> See Lucinda Shen, *These Are The 9 Biggest IPOs of All Time*, FORTUNE (Apr. 26, 2019), <https://fortune.com/2019/04/26/biggest-ipos-history-uber/>.

<sup>2</sup> See *Alibaba Group Market Cap*, YCHARTS, [https://ycharts.com/companies/BABA/market\\_cap](https://ycharts.com/companies/BABA/market_cap) (last visited Feb. 12, 2021). This valuation is down slightly from a peak of more than \$800 billion in October 2020.

<sup>3</sup> See Dawn Lim et al., *U.S. Weighs Adding Alibaba, Tencent to China Stock Ban*, WALL ST. J. (Jan. 7, 2021), <https://www.wsj.com/articles/u-s-considers-adding-alibaba-tencent-to-china-stock-ban-11609961075>.

<sup>4</sup> See *Largest e-commerce companies by market cap*, COMPANIESMARKETCAP.COM, <https://companiesmarketcap.com/e-commerce/largest-e-commerce-companies-by-market-cap/> (last visited Feb. 14, 2021) (listing Alibaba as second only to Amazon).

<sup>5</sup> See *Largest Companies by Market Cap*, COMPANIESMARKETCAP.COM, <https://companiesmarketcap.com/> (last visited Feb. 14, 2021).

<sup>6</sup> See *infra* Part II.A.

<sup>7</sup> See Li Yuan, *Jack Ma Is Retiring From Alibaba. He Won't Go Far*, N.Y. TIMES (Sept. 10, 2019), <https://www.nytimes.com/2019/09/10/business/alibaba-jack-ma-retire.html> (noting that the Partnership is "a group of a few dozen employees with tremendous power over the company's board and leadership . . ."). See also Liza Lin, *Alibaba's Daniel Zhang to Succeed Jack Ma as Chairman Next Year*, WALL ST. J. (Sep. 10, 2018), <https://www.wsj.com/articles/daniel-zhang-to-succeed-jack-ma-as-alibaba-chairman-1536542559>.

<sup>8</sup> See Yu-Hsin Lin & Thomas Mehaffy, *Open Sesame: The Myth of Alibaba's Extreme Corporate Governance and Control*, 10 BROOK. J. CORP. FIN. & COM. L. 437, 454 (2016).

<sup>9</sup> See *infra* Part II.A.

effectively controls Alibaba—control that would persist even if Ma’s equity stake declined further.<sup>10</sup> The reason is that Ma’s control over Alibaba actually derives from his control of a different firm, Ant Group Co. (Ant Group),<sup>11</sup> which is based on assets spun out of pre-IPO Alibaba.<sup>12</sup>

In particular, we show that Ma can use Ant Group to (1) effectively control the Partnership Committee, and thus the Partnership, and ultimately Alibaba’s board; and (2) at least temporarily cut off (and perhaps seize) critical licenses held in Alibaba’s VIEs,<sup>13</sup> giving Ma substantial holdup leverage over Alibaba in addition to his effective control of Alibaba’s board. Ma’s control of Ant Group gives him the power to affect the pay and employment of every member of Alibaba’s current board, every Alibaba executive, and the Alibaba and Ant Group executives who own Alibaba’s VIEs.<sup>14</sup> Alibaba is thus a case study of what we call “synthetic control,” in which an entrepreneur wields corporate control via a web of contractual and employment relationships rather than via equity.

Whether this is good news or bad news for investors depends on one’s beliefs about Ma’s future objectives. Investors who trust Ma to steer Alibaba to deliver value for American shareholders should be relieved.<sup>15</sup> Investors

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<sup>10</sup> As will be explained, one of the links in Ma’s chain of control is the Alibaba Partnership’s right to appoint a majority of Alibaba’s board. See *infra* Part II.A. This right can be eliminated by Alibaba shareholders with approval of 95% of the shares being voted. See *infra* note 54. If all shares were voted, Ma could defeat such a proposed change with slightly more than 5% of Alibaba’s shares. However, not all shares would be voted, enabling Ma to prevail with far fewer shares. Moreover, other members of the Alibaba Partnership, who own about 3% of Alibaba’s equity (see *infra* Part II.A), would join Ma in voting their shares to defeat any attempt to strip the Partnership of its power, either out of self-interest or because Ma can pressure them to do so (see *infra* Part II.B). Thus, Ma’s equity ownership could decline further without putting his control at risk.

<sup>11</sup> Until recently, the company’s legal Chinese name had been Zhejiang Ant Small and Micro Financial Services Group Co. Ltd. See Stella Yifan Xie, *Jack Ma’s Fintech Giant Ant to Drop ‘Financial’ From Its Name*, WALL ST. J. (June 22, 2020), <https://www.wsj.com/articles/jack-mas-fintech-giant-ant-to-drop-financial-from-its-name-11592822997>. However, the company changed its Chinese name to “Ant Technology Group Co.” and now seeks to be referred to in English as “Ant Group Co.” See *id.* In this Article, we use the name “Ant Group.” In July 2020, Ant Group announced it would conduct a concurrent IPO in Hong Kong and Shanghai. See *infra* note 32. Our Article is based on information about Ant Group’s governance arrangements that was publicly available as of October 2020.

<sup>12</sup> See *infra* Parts I, II.A., and III.B.

<sup>13</sup> We define and discuss VIEs in Part III.

<sup>14</sup> We assume that Ma exerts control over individuals only through identifiable employment-related carrots and sticks. This assumption substantially understates Ma’s actual power. All of these individuals are co-founders of Alibaba, were later hired by Ma, or were later appointed to their positions with his consent. Thus, even if Ma lacked financial levers over them, these individuals would likely follow Ma’s instructions, out of gratitude, friendship, loyalty, and respect, at least as long as they were not unduly burdened. For an argument that directors in U.S. firms are often beholden to CEOs for similar reasons, see JESSE FRIED & LUCIAN BEBCHUK, *PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION* 31–33 (Harvard University Press, 2004).

<sup>15</sup> For an argument that founders may wish to ensure their control to benefit all investors, see Zohar Goshen & Assaf Hamdani, *Corporate Control and Idiosyncratic Vision*, 125 YALE L.J. 560, 576 (2016) (explaining why even investors who genuinely intend to consume no private benefits may nevertheless insist on retaining control).

concerned that a founder owning less than 5% of Alibaba's equity might one day siphon off substantial value for himself and his friends should worry.<sup>16</sup>

Whatever the answer, Alibaba makes clear that the separation of ownership from control in public firms, which has been at the center of all corporate governance debates in the last few decades, can arise without either pyramidal ownership structures or dual-class shares.<sup>17</sup> In particular, while entrepreneurs can use dual-class stock to control firms with only a tiny amount of equity,<sup>18</sup> we show that an entrepreneur can control a firm without any equity, but rather via a combination of charter provisions and arrangements external to the firm and independent of its capital structure.

The Article's roadmap is as follows: Part I describes Alibaba's business and structure, and Ant Group's control arrangement. Part II explains how Ma effectively controls Alibaba's board via his control of Ant Group. Part III explains how Ma's control over Ant Group enables him to hold hostage the critical licenses held in Alibaba's VIEs. Part IV describes potential constraints on Ma.

## I. ALIBABA AND ANT GROUP

We describe Alibaba's corporate and business structure and then Ant Group's current control arrangement.

### A. *Alibaba's Corporate and Business Structure*

Alibaba is a Cayman-domiciled company governed by its articles of association and the Companies Law of the Cayman Islands.<sup>19</sup> Its headquarters is in Hangzhou, China (PRC),<sup>20</sup> hometown of founder Ma.<sup>21</sup> Alibaba's equity trades as American Depository Shares (ADSs) on the New York

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<sup>16</sup> For an argument that entrenchment of founders can harm public investors, see Lucian A. Bebchuk & Kobi Kastiel, *The Untenable Case for Perpetual Dual-Class Stock*, 103 VA L. REV. 585, 603 (2017). We describe possible constraints on Ma, including on his ability to siphon off value, in Part IV.

<sup>17</sup> For an analysis of classical approaches to separating ownership and control in public firms, see Lucian A. Bebchuk et al., *Stock Pyramids, Cross-Ownership and Dual Class Equity: The Mechanisms and Agency Costs of Separating Control From Cash-Flow Rights*, in CONCENTRATED CORPORATE OWNERSHIP 445–60 (R. Morck, ed., 2000). For an analysis of the use of shareholder agreements to reallocate control in public firms, see Gabriel Rauterberg, *The Separation of Voting and Control: The Role of Contract in Corporate Governance* (Working Paper, 2020), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3637204](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3637204).

<sup>18</sup> See generally Lucian A. Bebchuk & Kobi Kastiel, *The Perils of Small-Minority Controllers*, 107 GEO. L.J. 1453 (2019).

<sup>19</sup> See Alibaba Grp. Holding Ltd., Annual Report (Form 20-F) (2020) at 68 [hereinafter *Alibaba Form 20-F* (2020)].

<sup>20</sup> See *id.* at 68. We use “China” or “PRC” to denote Mainland China, excluding the Special Administrative Region of Hong Kong.

<sup>21</sup> See *Jack Ma*, ENCYCLOPEDIA BRITANNICA (Apr. 8, 2021), <https://www.britannica.com/biography/Jack-Ma>.

Stock Exchange (NYSE).<sup>22</sup> The firm is considered a foreign private issuer (FPI) under U.S. securities law and NYSE listing rules.<sup>23</sup> In 2019, Alibaba completed a secondary listing in Hong Kong.<sup>24</sup>

Alibaba's main business is providing internet platforms for retail and wholesale commerce both in China and elsewhere.<sup>25</sup> It also offers cloud

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<sup>22</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 213. Alibaba was originally planning to list on the Hong Kong Stock Exchange (HKEx). See Prudence Ho, Telis Demos & Juro Osawa, *Alibaba Is in Talks With Hong Kong Stock Exchange Over Ownership Structure*, WALL ST. J. (Aug. 18, 2013), <https://www.wsj.com/articles/SB10001424127887324139404579019843695560418>. Hong Kong was the preferred option because Alibaba's online platform Alibaba.com had been listed on the HKEx, *see id.*, and because of Hong Kong's proximity to mainland China. See Reuters Staff, *Top shareholders back Alibaba's controversial corporate structure*, Reuters (Sept. 27, 2013), <https://www.reuters.com/article/us-alibaba-ipo/top-shareholders-back-alibabas-controversial-corporate-structure-idINBRE98Q08N20130927> ("As a company with most of our business in China, it was natural for Hong Kong to be our first choice."). Alibaba first sought to list with a dual-class structure giving the Alibaba Partnership (discussed *infra* in Part II.A.) board control, but this proposal conflicted with the HKEx's policy against dual-class arrangements. See Prudence Ho & Juro Osawa, *Hong Kong's IPO Dilemma*, WALL ST. J. (Aug. 28, 2013), <https://blogs.wsj.com/moneybeat/2013/08/28/hong-kong-ipo-dilemma/>. When the HKEx rejected its initial proposal to allow a dual-class share scheme (*see* Lin & Mehaffy, *supra* note 8, at 441), Alibaba proposed allowing the Partnership to nominate a majority of the board's directors. See Shen Wei & Angus Young, *Dual Share Plan in Context: Making Sense of Hong Kong's Decision Not to Embrace Alibaba's Listing*, 26 INT'L CO. & COM. L. REV. 4, 5 (2015). When talks between Alibaba and the HKEx fell apart, Alibaba approached the New York Stock Exchange and Nasdaq, which both approved this approach. See Telis Demos, Juro Osawa & Jacob Bunge, *Alibaba: NYSE, Nasdaq Approve Partnership Structure Proposal*, WALL ST. J. (Oct. 21, 2013), <https://www.wsj.com/articles/SB10001424052702303672404579149981322056134>. Alibaba eventually chose the NYSE, and went public with this arrangement. See *infra* Part II.A. Hong Kong eventually revised its listing rules in 2018 to allow for dual-class share structures. See Kenan Machado & Saurabh Chaturvedi, *Asian Exchanges Woo Firms With Two Classes of Stock – But Investors, Companies Are Wary*, WALL ST. J. (Jan. 25, 2018), [https://www.wsj.com/articles/asian-exchanges-woo-firms-with-two-classes-of-stock-but-investors-companies-are-wary-1516864916?mod=searchresults\\_pos16&page=1](https://www.wsj.com/articles/asian-exchanges-woo-firms-with-two-classes-of-stock-but-investors-companies-are-wary-1516864916?mod=searchresults_pos16&page=1).

<sup>23</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 64, 222.

<sup>24</sup> See Stu Woo, *Alibaba Shares Enjoy a Strong Start in Hong Kong*, WALL ST. J. (Nov. 26, 2019), <https://www.wsj.com/articles/a-strong-open-sesame-for-alibaba-in-hong-kong-11574746859>. See also Alibaba Form 20-F (2020), *supra* note 19, at 158.

<sup>25</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 69–74. Within China, Alibaba supports retail commerce through Taobao.com and Tmall.com. See *id.* Taobao is China's largest mobile commerce platform., *id.* at 71, connecting merchants (generally individuals or small businesses) to consumers. Merchants can create listings and storefronts for free, and then pay to direct traffic from the platform's search engine, advertise on third-party affiliates, or upgrade storefronts with advanced capabilities. *Id.* at 83. Taobao also includes an active social media component, connecting users with merchants, influencers, and other customers. Search results on Taobao Marketplace, the platform's "top-level traffic funnel," directs users to a variety of content—including products sold on Tmall. *Id.* Tmall is the world's largest third-party e-commerce platform for major brands and retailers. *Id.* In addition to Taobao and Tmall, Alibaba's e-commerce businesses include Freshippo (a proprietary grocery chain, involving online and offline stores); AliExpress (a cross-border platform that connects international customers with Chinese merchants); Alibaba.com (Alibaba's first business, an international wholesale platform); 1688.com (a domestic wholesale platform); Lazada (a platform for brands and retailers in Southeast Asia); and Ele.me (a food delivery service). See *Our Businesses*, ALIBABA, <https://www.alibabagroup.com/en/about/businesses> (last visited Dec. 21, 2020). Alibaba also operates Alimama, a "monetization platform" that provides marketing services to its e-commerce merchants. See Alibaba Form 20-F (2020), *supra* note 19, at 84.

computing,<sup>26</sup> digital media, and entertainment services.<sup>27</sup> Alibaba is a holding company: it has few assets other than shares of its wholly-owned offshore (non-China) subsidiaries.<sup>28</sup> These offshore subsidiaries, in turn, are themselves holding companies that directly or indirectly own shares in downstream subsidiaries. The most economically critical of these downstream subsidiaries are onshore (China-based and domiciled) and part of so-called WFOE-VIE arrangements that we describe in Part III.

Figure 1 below is a simplified diagram of Alibaba's structure, taken from one of the company's 2020 securities filings.<sup>29</sup> Below the dotted line are Alibaba's key operating businesses, all based and domiciled in China. The four entities at the bottom are VIEs, each of which is connected to a WFOE one row up.

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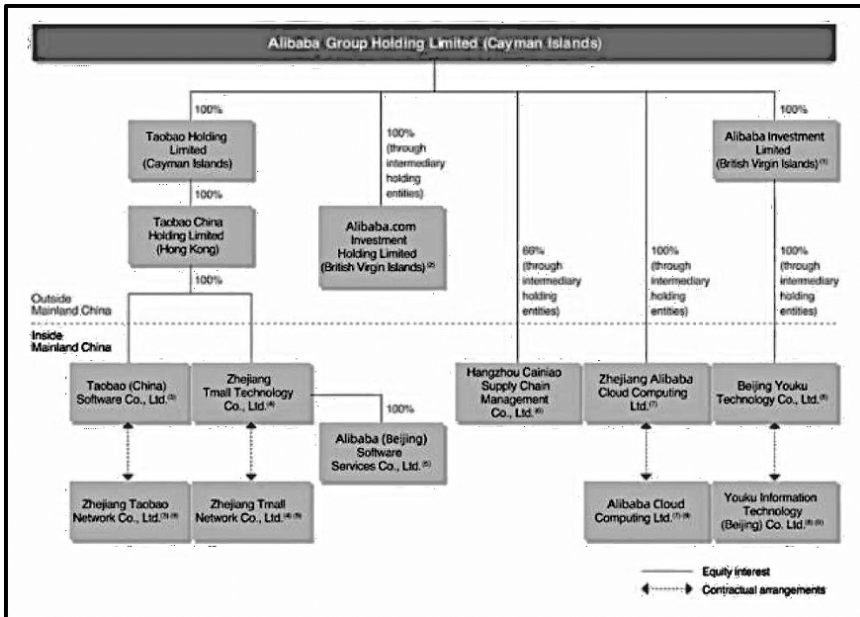
<sup>26</sup> Alibaba Cloud Computing is the world's third largest (and Asia Pacific's largest) "Infrastructure as a Service" provider by revenue. *See* Alibaba Form 20-F (2020), *supra* note 19, at 72. In addition to serving as the backbone for Alibaba's e-commerce businesses, this business offers a suite of other products and services comparable to that of Amazon Web Services. *See Alibaba Cloud Product Comparison for AWS Professionals*, ALIBABA CLOUD (Feb. 7, 2018), [https://www.alibabacloud.com/blog/alibaba-cloud-product-comparison-for-aws-professionals\\_444958](https://www.alibabacloud.com/blog/alibaba-cloud-product-comparison-for-aws-professionals_444958).

<sup>27</sup> Alibaba's digital media and entertainment businesses are run primarily by Youku, the third largest long-form video platform in China by number of monthly users. *See* Alibaba Form 20-F (2020), *supra* note 19, at 73. In addition to Youku, Alibaba maintains other content platforms that provide digital news feeds, literature, and music to consumers over the internet: Alibaba Pictures (an "Internet-driven integrated platform that covers content production, promotion and distribution, intellectual property licensing and integrated management, cinema ticketing management and data services for the entertainment industry"); Damai (an online ticketing platform); and Shuqi (an online literature distribution and reading platform). *See id.* at 91. Alibaba also operates several "innovation initiatives," including DingTalk, a "business efficiency app" akin to Slack. *See id.* at 92.

<sup>28</sup> *See id.* at 122. These wholly-owned direct and indirect offshore holding company subsidiaries include companies domiciled in the Cayman Islands, British Virgin Islands, and Hong Kong. *See id.*

<sup>29</sup> *See id.*

FIGURE 1: ALIBABA'S CORPORATE STRUCTURE



### B. Ant Group and its Control

Ant Group is a privately-held, China-domiciled fintech company operating Alipay, an online payment service spun out of pre-IPO Alibaba.<sup>30</sup> In September 2019, Alibaba converted a profit-sharing interest in Ant Group into a 33% equity stake.<sup>31</sup> In July 2020, Ant Group announced it would conduct a concurrent IPO in Hong Kong and Shanghai.<sup>32</sup> The IPO was blocked by Chinese regulators in November 2020 but may go forward in the future.<sup>33</sup>

Alibaba's June 2019 securities filings indicate that Ma controlled a majority of the voting interests in Ant Group a few months before the Septem-

<sup>30</sup> For a discussion of this spinout, see *infra* Part III.B.

<sup>31</sup> See Lulu Yilun Chen, *Alibaba Snags 33% of Jack Ma's Ant as Portfolio Tops \$83 Billion*, BLOOMBERG (Sept. 24, 2019), <https://www.bloomberg.com/news/articles/2019-09-24/alibaba-closes-acquisition-of-a-third-of-jack-ma-s-ant-financial?ref=IRXjXN7s>; Alibaba Grp. Holding Ltd., Report of Foreign Private Issuer (Form 6-K) (Nov. 13, 2019).

<sup>32</sup> See Sherisse Pham, *Jack Ma's Ant Group chooses China for its IPO*, CNN BUSINESS (July 21, 2020), <https://www.cnn.com/2020/07/20/tech/ant-financial-jack-ma-ipo-hnk-intl/index.html>.

<sup>33</sup> See, e.g., Keith Zhai et al., *How billionaire Jack Ma fell to earth and took Ant's mega IPO with him*, REUTERS (Nov. 5, 2020), <https://www.reuters.com/article/ant-group-ipo-suspension-regulators-idUSL8N2HQ002>; Xie Yu, *With Ant IPO in Limbo, Funds Let Investors Cash Out*, WALL ST. J. (Nov. 11, 2020), [https://www.wsj.com/articles/with-ant-ipo-in-limbo-funds-let-investors-cash-out-11605085858?modHP\\_lead\\_pos5](https://www.wsj.com/articles/with-ant-ipo-in-limbo-funds-let-investors-cash-out-11605085858?modHP_lead_pos5).

ber 2019 transaction.<sup>34</sup> As we discuss in more detail in the following paragraph, Ma also controlled a majority of the voting interests in Ant Group immediately before the aborted IPO in late 2020. We thus infer that Ma controlled a majority of Ant Group's voting interests between the September 2019 transaction and the aborted IPO.<sup>35</sup>

Prior to the planned IPO, 50.52% of Ant Group's equity was held by two investment vehicles, Hangzhou Junhan and Hangzhou Junao,<sup>36</sup> which were controlled by Hangzhou Yunbo, the General Partner of both entities. In August 2020, Ma transferred equity interests in Yunbo to Eric Jing, Simon Hu, and Fang Jiang.<sup>37</sup> Each received a 22% interest in Yunbo, leaving Ma with 34%.<sup>38</sup> This transfer and its effects indicate that Ma had previously owned all of Hangzhou Yunbo's equity. Along with this equity transfer, Ma and the other three shareholders entered into a "Concert Party Agreement" providing that all matters related to Ant Group—including the exercise of voting rights for all shares held by Junhan and Junao as well as the nomination of directors and supervisors to Ant Group's board—would be decided by a two-thirds majority vote of the Yunbo shareholders.<sup>39</sup> Ma's 34% interest provides him with an effective veto over the decisions of Yunbo. More importantly, in the event of a disagreement among the shareholders, all votes will be cast "in accordance with the decision of" Ma.<sup>40</sup> Before the planned IPO, Ma thus controlled 50.52% of Ant Group's equity.<sup>41</sup>

Had Ant Group's planned IPOs in Hong Kong and Shanghai gone forward, Ma's control would not have been significantly affected. The company

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<sup>34</sup> These filings reported that Ma owned 100% of the general partner of two PRC limited partnerships (Hangzhou Junao and Hangzhou Junhan) that together own over 70% of the equity issued by Ant Group and through this general partner personally controls a "majority of the voting interests" in Ant Group. See Alibaba Grp. Holding Ltd., Annual Report (Form 20-F) (2019) at 23, 191–92 [hereinafter Alibaba Form 20-F (2019)].

<sup>35</sup> In Alibaba's summer 2020 securities filings, Alibaba reported that Ma personally controlled "approximately 50% of the voting interests" of Ant Group. See Alibaba Form 20-F (2020), *supra* note 19, at 29. Thus, Ma might not have controlled a majority of the voting interests between the September 2019 transaction and the aborted IPO. But this seems unlikely, given his control of a majority of the voting interests at both endpoints of this period.

<sup>36</sup> See Ant Group Co. Ltd., Prospectus (Oct. 27, 2020) at 161, 292, <https://www1.hkexnews.hk/listedco/listconews/sehk/2020/1026/2020102600165.pdf> [hereinafter Ant Prospectus]. Junhan holds a 29.86% stake, and Junao a 20.66% stake. See *id.* at 145.

<sup>37</sup> See Ant Prospectus, *supra* note 36, at 140. As will be discussed *infra* in Part II.B, Ma's control of Alibaba is effected through his domination of the Alibaba Partnership, which in turn is effected through his domination of the Alibaba Partnership Committee. Eric Jing, Ant Group's Executive Chairman, is a member of the Alibaba Partnership Committee. Simon Hu, Ant Group's CEO, and Fang Jiang, Alibaba's Chief People Officer, are members of the Alibaba Partnership. See also Ant Prospectus, *supra* note 36, at 299 ("Each of Mr. Eric Jing, Mr. Simon Hu, Mr. Xingjun Ni, Mr. Joe Tsai, Mr. Li Cheng, and Ms. Fang Jiang is a partner of the Alibaba Partnership.").

<sup>38</sup> See *id.* at 140.

<sup>39</sup> See Ant Prospectus, *supra* note 36, at 292.

<sup>40</sup> See *id.*

<sup>41</sup> Ant Group's 2020 IPO prospectus does not mention any agreement over the allocation of board seats, which could in principle have deprived Ma of actual control notwithstanding his control of a majority of voting interests. See Ant Prospectus, *supra* note 36, at 161, 292.



planned to issue “H Shares” in Hong Kong and “A Shares” in Shanghai. The total number of shares offered in each market would represent approximately 11% of Ant Group’s total outstanding shares.<sup>42</sup> Immediately following the planned IPO, Yunbo’s stake would have been diluted to 39.55%.<sup>43</sup>

While Yunbo’s stake would have been reduced to less than a majority of the shares, Ma would have still controlled Ant Group. Alibaba’s post-IPO ownership would have been 31.77%.<sup>44</sup> Thus, to the extent Ma controls Alibaba (as we argue below), Ma would have controlled a total of 71.32% of Ant’s voting shares. Even if Alibaba had remained “neutral” in a control contest, Ma would still have controlled Ant Group: Yunbo could quickly buy 10.45% of the shares (perhaps by having Ant Group issue it more shares) and no other party could acquire 50%.

In what follows, we explain that Ma’s control over Ant Group has enabled him to dominate Alibaba’s board (Part II) and given him a way to hold Alibaba up by depriving it, at least temporarily, of assets critical to its business (Part III).

## II. MA’S EFFECTIVE CONTROL OVER ALIBABA’S BOARD

Below we explain that an entity called the Alibaba Partnership controls Alibaba’s board. We then show how Ma effectively controls the Alibaba Partnership.

### A. *The Alibaba Partnership Controls Alibaba’s Board*

Alibaba currently has a single class of shares. In early July 2020, Ma owned 4.8% of the shares.<sup>45</sup> Other directors and executives, including cofounder Joe Tsai (Tsai), owned about 2.6%, and SoftBank owned 24.9%.<sup>46</sup> Were it not for the special voting arrangements we describe below, SoftBank would be the largest shareholder and, absent coordination among other shareholders, could dominate Alibaba’s board.<sup>47</sup>

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<sup>42</sup> See *id.* at 22–23. Ant Group planned to float 5.5% of its total outstanding shares in each market. The dual listing was anticipated to raise upwards of \$34 billion. See Julie Zhu & Scott Murdoch, *Investors line up for Ant Group’s record \$34.4 billion IPO*, REUTERS (Oct. 26, 2020), <https://www.reuters.com/article/ant-group-ipo/investors-line-up-for-ant-groups-record-34-4-billion-ipo-idUSKBN27B1CG>.

<sup>43</sup> See Ant Prospectus, *supra* note 36, at 57, 145. This ownership stake would be split between the Mainland-traded A Shares (38%) and Hong Kong-traded H Shares (1.55%). See *id.* at 161.

<sup>44</sup> See *id.* at 145, 161.

<sup>45</sup> See Alibaba Form 20–F (2020), *supra* note 19, at 191.

<sup>46</sup> *Id.*

<sup>47</sup> In March 2020, SoftBank announced that it intended to sell about \$14 billion of its Alibaba shares (around 10% of its stake) as part of an effort to shore up its businesses battered by the COVID-19 pandemic. See Lulu Chen & Giles Turner, *SoftBank Plans to Sell \$14 Billion in Alibaba Shares*, BLOOMBERG (Mar. 23, 2020), <https://www.bloomberg.com/news/articles/2020-03-23/softbank-is-said-to-plan-14-billion-sale-of-alibaba-shares>. After this sale,

However, as is well understood, Alibaba's articles of association give Lakeside Partners, L.P., commonly known as the "Alibaba Partnership" (the Partnership),<sup>48</sup> the power to appoint a simple majority of Alibaba's directors.<sup>49</sup> The Partnership selects these directors by majority vote of the partners from nominees selected by the Partnership Committee, which we describe below.<sup>50</sup> As of early July 2020, there were 36 partners: Ma, 27 Alibaba executives (including Tsai), and eight executives of Ma-controlled Ant Group.<sup>51</sup> All but one (Tsai) appear to be Chinese nationals. At IPO in 2014, there were 30 Partners.<sup>52</sup>

This power gives the Partnership perpetual control of the board<sup>53</sup> regardless of the partners' collective equity ownership.<sup>54</sup> Separately, a voting

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SoftBank will still be Alibaba's largest shareholder. Alibaba Form 20-F (2020), *supra* note 19, at 191.

<sup>48</sup> For an explanation of the origins and purposes of the Partnership, see Lin & Mehaffy, *supra* note 8, at 451-52. The story goes that Ma, a former English teacher, gathered 17 of his friends and former students in his Hangzhou apartment in 1999, and together they founded Alibaba. *Id.*, at 451. Alibaba was incorporated four months later, at which point the founders became shareholders. See Russell Flannery, *Inside Alibaba: Vice Chairman Joe Tsai Opens Up About Working With Jack Ma and Jonathan Lu*, FORBES (Jan. 8, 2014), <https://www.forbes.com/sites/russellflannery/2014/01/08/inside-alibaba-vice-chairman-joe-tsai-opens-up-about-working-with-jack-ma-and-jonathan-lu/?sh=2e3dc52f511b>. The Partnership was created in 2010. See Lin & Mehaffy, *supra* note 8, at 452.

<sup>49</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 42, 175-79. While the Alibaba Partnership has retained the right to nominate a simple majority of Alibaba's Board of Directors since the IPO, the Partnership has generally nominated fewer than half of the directors. At the IPO in 2014, the board was to have nine total directors—four nominated by the Alibaba Partnership, one nominated by Softbank, and four independents. See Alibaba Grp. Holding Ltd., Prospectus (Sept. 22, 2014) at 235 [hereinafter Alibaba Prospectus]. An additional independent director was added in 2015, leaving the Partnership with four out of ten director nominees. See Alibaba Grp. Holding Ltd., Annual Report (Form 20-F) (2015) at 131, 138. In 2016, a fifth independent director was added, and one of the previously independent directors became an Alibaba Partnership nominee. See Alibaba Grp. Holding Ltd., Annual Report (Form 20-F) (2016) at 151 [hereinafter Alibaba Form 20-F (2016)]. This balance of five out of eleven directors being nominated by the Partnership persisted from 2016 through 2019. In 2020, Masayoshi Son—the sole Softbank nominee on the board—stepped down, leaving the board with five of ten directors nominated by the Partnership. See *infra* note 57.

<sup>50</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 177-78.

<sup>51</sup> See *id.* at 178-79. One of the eight from Ant Group (Lucy Peng) was an executive but is now a director. See *infra* note 58. We thus use the term "executive" here to mean executive or director.

<sup>52</sup> See Alibaba Prospectus, *supra* note 49, at 229. The Partnership grew to 34 by 2016, to 36 by 2017, and to 38 by 2019, before shrinking slightly to 36 in 2020. See Alibaba Form 20-F (2016), *supra* note 49, at 156; Alibaba Grp. Holding Ltd., Annual Report (Form 20-F) (2017) at 170 [hereinafter Alibaba Form 20-F (2017)]; Alibaba Form 20-F (2019), *supra* note 34, at 170; Alibaba Form 20-F (2020), *supra* note 19, at 175.

<sup>53</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 42-43. To become a director of Alibaba, the Alibaba Partnership's director nominee must receive a majority vote at the shareholders meeting. However, if the Partnership nominee is not elected by Alibaba shareholders, or is elected but leaves the board, the Partnership may appoint a different person to serve as interim director until the next election. See *id.* at 177. This ensures that a majority of Alibaba's directors will be appointed by the Partnership regardless of the shareholder vote.

<sup>54</sup> See Lin & Mehaffy, *supra* note 8, at 439, 458. The Partnership's nomination and appointment right can be eliminated only if (1) certain provisions of the Partnership agreement are amended without the consent of a majority of those Alibaba directors who are not nominees or appointees of the Partnership and are independent directors within the meaning of

agreement among Ma, Tsai, and SoftBank commits the parties to vote their collective shares for directors nominated by the Alibaba Partnership and, as long as SoftBank owns at least 15% of Alibaba's shares, for one director nominated by SoftBank.<sup>55</sup> As of early July 2020, Alibaba's board consisted of ten members, five of whom were Alibaba Partnership nominees and none of whom was a SoftBank nominee.<sup>56</sup> The remaining Alibaba directors also owe their positions to the Partnership, either directly or indirectly: they were nominated by either Alibaba insiders who were members of the Partnership before Alibaba's IPO, or were nominated by Ma and other members of the Alibaba board thereafter.<sup>57</sup>

### B. Ma Effectively Controls the Alibaba Partnership

We now explain how Ma uses his control of Ant Group to dominate the Alibaba Partnership, which consists almost entirely of Alibaba and Ant Group executives. To see how this works, it is helpful to divide the partners besides Ma into two groups: the eight Ant Group executives and the 27 Alibaba executives.

#### 1. Ma's Control Over Partners Who Are Ant Group Executives

Consider the first group, the eight Ant Group executives. To the extent Ma controls Ant Group, Ma can fire or cause the firing of any of these

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Section 303A of the NYSE Listed Company Manual; or (2) Alibaba's articles of association are amended to provide otherwise by a vote of shareholders representing at least 95% of shares voting. See Alibaba Form 20-F (2020), *supra* note 19, at 177-78. Even a change of control or a merger will not terminate the Partnership's nomination and appointment right. See *id.* at 42-43.

<sup>55</sup> See *id.* at 197. Until mid-2020, the SoftBank director was its head Masayoshi Son, an early backer and business partner of Ma's. In mid-2020, Son announced that he would step down from the board. See Phred Dvorak, *SoftBank CEO Masayoshi Son Quits Alibaba Board*, WALL ST. J. (June 25, 2020), <https://www.wsj.com/articles/softbank-ceo-masayoshi-son-says-he-will-resign-from-board-of-alibaba-11593055958>. Presumably, he will be replaced by another director appointed by SoftBank. Until recently, Ma also served on the board of SoftBank. See Alibaba Form 20-F (2019), *supra* note 34, at 165. In May 2020, Ma announced he would step down. See Kosaku Narioka, *Alibaba Co-Founder Jack Ma to Leave SoftBank's Board*, WALL ST. J. (May 17, 2020), <https://www.wsj.com/articles/alibaba-co-founder-jack-ma-to-leave-softbanks-board-11589770260>.

<sup>56</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 178.

<sup>57</sup> The five current directors not nominated by the Partnership are Chee Hwa Tung (Tung), Walter Teh Ming Kwauk (Kwauk), Jerry Yang (Yang), Börje Ekholm (Ekholm), and Wan Ling Martello (Martello). See Alibaba Form 20-F (2020), *supra* note 19, at 170. All five were nominated by the three-person Nomination Committee, which consists of Tung, Yang, and Ma (who serves as chair). See *id.* at 189. Tung and Yang were put on the board by Ma and the Alibaba Partnership before the 2014 IPO. See Toh Han Shih & Bien Perez, *Tung Chee-hwa set to join Alibaba board*, S. CHINA MORNING POST (June 17, 2014), <https://www.scmp.com/business/companies/article/1534396/tung-chee-hwa-set-join-alibaba-board>; Bloomberg News, *Yahoo founder Jerry Yang plays a key role in Alibaba's listing*, S. CHINA MORNING POST (Sept. 12, 2014), <https://www.scmp.com/business/companies/article/1590503/yahoo-founder-jerry-yang-plays-key-role-alibabas-listing>. All five non-Partnership directors thus owe, directly or indirectly, their positions to Ma.

executives.<sup>58</sup> This would force the fired executive to exit the Partnership.<sup>59</sup> Ma can also increase or decrease any of these executives' pay, title, or responsibilities. Ma can thus dominate all of these partners.

## 2. Ma's Control Over Partners Who Are Alibaba Executives

Next consider the second group, the 27 Alibaba executives. As we explain below, Ma dominates these executives through his control of the Partnership Committee, which (1) directly helps set their pay and (2) indirectly determines their employment situations at Alibaba.

### a. Ma's Control Over the Partnership Committee

The Partnership Committee (the Committee) is subject to elections every five years.<sup>60</sup> Ma and Tsai, as Continuity Partners, are permanent members of the Committee.<sup>61</sup> Each Committee decides whether the next Committee will have five, six, or seven members, and nominates candidates.<sup>62</sup> All of the partners then select from the nominees who will fill the slots not occupied by Ma and Tsai.<sup>63</sup> Accordingly, to the extent that Ma controls the current Committee, he can also control the next Committee.

Currently, the Committee consists of Ma, Tsai, Daniel Zhang (Alibaba CEO and Executive Chair),<sup>64</sup> Jian Wang (Chairman of Alibaba's Technology Steering Committee), and two persons from Ant Group: Lucy Peng and Eric Jing.<sup>65</sup> Wang joined the Committee during 2019–20, expanding it from five to six members.<sup>66</sup>

Before Wang joined the Committee, Ma and the two Ant Group representatives constituted a majority of the five members, enabling Ma (via control of Ant Group)<sup>67</sup> to impose his will. Tsai, described in the financial media

<sup>58</sup> One of the eight Ant Group executives in the Partnership is Lucy Peng, who was formerly Chair and President of Alipay China. See Alibaba Form 20–F (2019), *supra* note 34, at 173. Peng now appears to be connected to Ant Group solely through her director position. See Alibaba Form 20–F (2020), *supra* note 19, at 179; see also *supra* note 49. But because her serving in this position requires Ant Group's (and thus Ma's) approval, Ma still exerts control over her.

<sup>59</sup> See Alibaba Form 20–F (2020), *supra* note 19, at 180.

<sup>60</sup> See Alibaba Form 20–F (2020), *supra* note 19, at 177. Prior to 2020, elections were held every three years. See Alibaba Form 20–F (2019), *supra* note 34, at 171.

<sup>61</sup> See Alibaba Form 20–F (2020), *supra* note 19, at 177.

<sup>62</sup> See *id.* From 2014 through 2019, the Committee was required to consist of at least five partners. In 2020, this rule was changed to require "at least five but no more than seven Partners." See *id.*

<sup>63</sup> See *id.*

<sup>64</sup> In September 2019, Zhang replaced Ma as Alibaba's Executive Chair. Thus, Ma no longer has an executive position at Alibaba. See Lily Kuo, *Jack Ma, China's richest man, steps down as chairman of Alibaba*, GUARDIAN (Sept. 10, 2019), <https://www.theguardian.com/business/2019/sep/10/jack-ma-chinas-richest-man-steps-down-as-chairman-of-alibaba>.

<sup>65</sup> See Alibaba Form 20–F (2020), *supra* note 19, at 177–79.

<sup>66</sup> See Alibaba Form 20–F (2019), *supra* note 34, at 171–73 (reporting as Committee members in June 2019 all of the July 2020 Committee members except Wang).

<sup>67</sup> See *supra* Part II.B.1.

as Ma's "indispensable right-hand man and alter ego,"<sup>68</sup> was presumably another ally.

That Ma agreed to add Wang as a sixth member suggests that Ma did not see this as a threat to his control. It is easy to see why. Even if Tsai turned against him, Zhang and Wang would be unlikely to join Tsai. Zhang and Wang appear to work at Alibaba's headquarters in Hangzhou. Tsai's family life is centered in the United States and his Asia business base is Hong Kong,<sup>69</sup> not Hangzhou. Joining Ma is thus more natural for Zhang and Wang than joining Tsai. Moreover, a bloc with Tsai would constitute no more than half of the Committee and would break if any bloc member defected and gave Ma majority control. Because there is little to gain and much to lose from opposing Ma, opposition is unlikely.<sup>70</sup>

*b. The Partnership Committee's Levers Over Alibaba Executives*

Control of the Partnership Committee enables Ma to dominate Alibaba executives via two levers.

First, the Partnership Committee helps set the pay of partners who are Alibaba executives.<sup>71</sup> Ma can thus use his control of the Partnership Committee to exert influence over every such partner, including the two Alibaba

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<sup>68</sup> See Adam Lashinsky, *This Executive is Alibaba Chairman Jack Ma's Alter Ego*, *FORTUNE* (Apr. 4, 2017), <https://fortune.com/2017/04/04/data-sheet-jack-ma-joe-tsai/>.

<sup>69</sup> Kevin Acee, *Column: Is Joe Tsai the man to Net another big-league team for San Diego?*, *SAN DIEGO UNION TRIB.* (Oct. 27, 2017), <https://www.sandiegouniontribune.com/sports/columnists/kevin-acee/sd-sp-acee-joe-tsai-nba-nhl-san-diego-1028-story.html>.

<sup>70</sup> Ma has always dominated the Partnership Committee. Before Ma dominated the Committee via two Ant Group-affiliated members, he did so through his position as Executive Chair of Alibaba. From the IPO through part of 2016, the Committee consisted of Ma, Tsai, Peng (of Ant Group), Jonathan Lu (CEO, then Vice Chair) and Ming Zeng (a Senior Vice President). Both Lu and Zeng reported to Ma, directly or indirectly, as Executive Chair. Lu was replaced as CEO by Zhang in 2015 and exited the Committee (and the Partnership) in 2016, apparently because he lost Ma's confidence. Michael B. Kelley & Jay Yarow, *Alibaba's CEO Replaced*, *BUSINESS INSIDER* (May 7, 2015), <https://www.businessinsider.com/alibabascio-replaced-2015-5> (noting "early speculation" that "Lu is out because he lost the confidence of Ma"). He was replaced on the Committee by new CEO, Daniel Zhang. See Alibaba Form 20-F (2017), *supra* note 52, at 171. Zeng exited the Committee in 2016 and was replaced by Jing. Compare Alibaba Form 20-F (2016), *supra* note 49, at 157, with Alibaba Form 20-F (2017), *supra* note 52, at 173. He left the Partnership by 2019. Compare Alibaba Grp. Holding Ltd., Annual Report (Form 20-F) (2018) at 176 [hereinafter Alibaba Form 20-F (2018)], with Alibaba Form 20-F (2019), *supra* note 34, at 173.

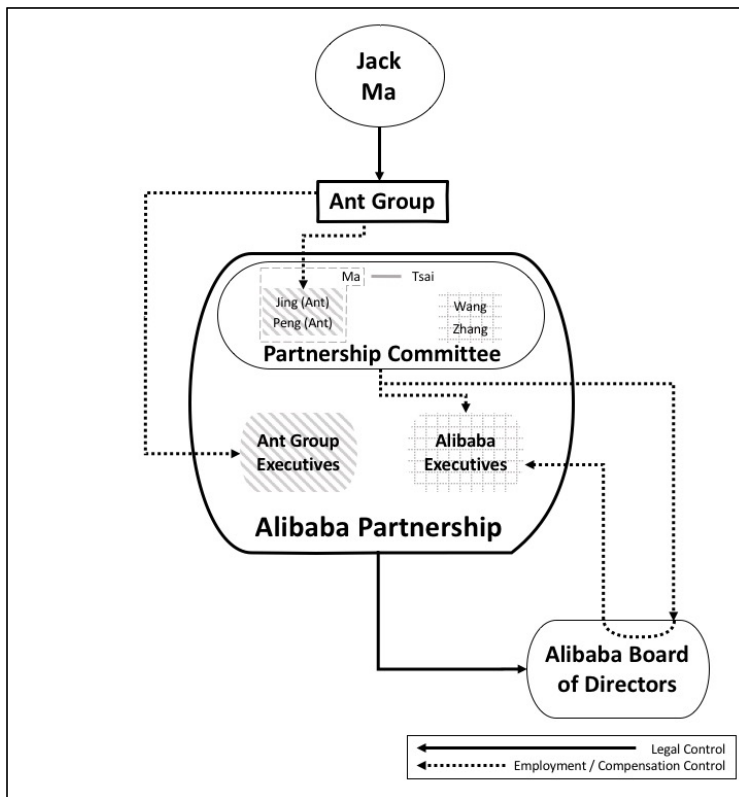
<sup>71</sup> The Committee is responsible for "allocating the relevant portion of the annual cash bonus pool for all partner members of management." See Alibaba Form 20-F (2020), *supra* note 19, at 177. Amounts payable to Partners who are executive officers of Alibaba, Alibaba directors, or members of the Partnership Committee are subject to approval by the compensation committee of Alibaba's board. See *id.* But members of the compensation committee who are Partnership-appointed directors occupy their board seats because they have been nominated by the Partnership Committee. See *id.* They cannot expect to be re-nominated by the Partnership Committee if they fail to go along with its (that is, Ma's) wishes.

executives (besides Tsai) serving on the Partnership Committee (Zhang and Wang).<sup>72</sup>

Second, Ma's control of the Partnership Committee gives him indirect influence over Alibaba executives' employment conditions. The reason is that the Partnership-chosen Alibaba directors, who constitute a majority of the board, need the approval of the Ma-controlled Partnership Committee to be renominated.<sup>73</sup> These directors can be expected to treat unfavorably (for example, by demoting or failing to promote) any executive disliked by the Committee.<sup>74</sup>

Figure 2 depicts Ma's chain of control via Alibaba's board.

FIGURE 2: ALIBABA—MA'S CONTROL VIA BOARD



<sup>72</sup> The Partnership Committee also controls the nomination of new partners to the Partnership. See Lin & Mehaffy, *supra* note 8, at 453.

<sup>73</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 177.

<sup>74</sup> See Lin & Mehaffy, *supra* note 8, at 454. Because Ma determines whether the Partnership-chosen directors are kept on the board, these directors can also be expected to do Ma's bidding on other matters as well. As Part III explains, Ma's control over Alibaba's VIEs gives him a separate and independent source of leverage over Alibaba's directors.

### 3. Can Ma be Removed from the Partnership?

Ma's control of the Alibaba Partnership depends on his control of the Partnership Committee, which in turn depends on remaining a partner. But Ma is at little risk of being forced out of the Partnership, as long as he is alive and not incapacitated.

Any partner, including Ma, can be removed for cause by a vote of the partners.<sup>75</sup> But the likelihood that a majority of the partners will vote to oust Ma is slim: if several partners tried to organize against Ma, he could get them fired or otherwise retaliate against them, whether they work for Ant Group (using his control of Ant Group) or Alibaba (using his control of the Partnership Committee).<sup>76</sup>

Another possible type of forced exit is aging out. Almost all partners must retire at age 60 or upon termination of employment (at Ant Group or Alibaba).<sup>77</sup> However, Ma and Tsai are "Continuity Partners" who can remain partners until age 70 unless they die or become incapacitated.<sup>78</sup> Ma will turn 70 in 2034.<sup>79</sup> Moreover, the age limit for Ma and Tsai can be extended by a majority vote of the partners.<sup>80</sup> The same reasoning that suggests Ma can prevent his expulsion from the Partnership also suggests he could secure majority approval for extending his age limit.

### III. MA'S ABILITY TO SEIZE ALIBABA'S KEY LICENSES

Ma has another source of power over Alibaba: he indirectly controls key licenses undergirding Alibaba's businesses, enabling him to bring Alibaba's operations to a standstill, if not to walk away with valuable assets. Section A describes how these assets are housed in variable-interest-entity (VIE) structures that are connected to Alibaba through legally fragile arrangements. Section B explains how Ma, through his indirect control over the VIEs via Ant Group, can at least temporarily disable these assets, if not permanently expropriate them.

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<sup>75</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 180. By "for cause" we mean "violations of certain standards set forth in the Partnership agreement."

<sup>76</sup> See *supra* Part II.B.2.b; Lin & Mehaffy, *supra* note 8, at 454. In addition, and as we explain in *infra* Part III, Ma could threaten to use his indirect control over the VIEs to throw Alibaba's businesses into disarray.

<sup>77</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 180.

<sup>78</sup> See *id.* Continuity Partners, like ordinary Partners, can of course also choose to resign. See *id.* Before 2018, there was no age limit for continuity members. See Alibaba Form 20-F (2017), *supra* note 52, at 174. Through 2017, there was a possibility that "either two or three partners" could be designated as continuity members. *Id.* However, in 2018, this rule was changed to allow only "one or two" continuity partners. See Alibaba Form 20-F (2018), *supra* note 70, at 177.

<sup>79</sup> See Stu Woo, *Alibaba Sends Jack Ma Off With Birthday Extravaganza*, WALL ST. J. (Sept. 10, 2019), <https://www.wsj.com/articles/alibaba-sends-jack-ma-off-with-birthday-extravaganza-11568127370>.

<sup>80</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 180.

### A. Alibaba's VIEs and Their Legal Fragility

Private Chinese technology firms have long looked to foreign public investors for financing because of the difficulty of conducting public offerings in China.<sup>81</sup> China-registered companies seeking overseas listing must obtain approval from the State Council, a challenge for private firms.<sup>82</sup> Thus, these businesses formed offshore companies, typically domiciled in the Cayman Islands, as overseas listing vehicles.<sup>83</sup>

However, China prohibits foreign ownership and control of firms in strategically sensitive industries, including the internet.<sup>84</sup> Alibaba, as a Cayman-domiciled firm providing internet-based services in China, thus cannot own key assets it needs, including licenses.<sup>85</sup> To work around this problem, Alibaba uses a structure that houses these assets in a China-registered firm owned by Chinese nationals, but then purports to give Alibaba and its foreign investors effective ownership and control over the assets through an elaborate series of contracts.

That structure is a variable-interest entity (VIE) arrangement.<sup>86</sup> Under a VIE arrangement, a foreign-owned firm (such as a foreign-domiciled subsidiary of Alibaba) owns 100% of a China-registered wholly-foreign-owned enterprise (WFOE). The strategically sensitive asset is placed in a China-registered VIE owned by one or more Chinese nationals, usually including the entrepreneur. The WFOE, the VIE and the VIE's owners then enter a series of contracts that purport to enable the WFOE to effectively control the VIE and transfer the profits generated by the VIE to the WFOE.<sup>87</sup> The con-

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<sup>81</sup> See Paul Gillis & Fredrik Oqvist, *Variable Interest Entities in China*, GMT RSCH. GUEST SERIES, 1–2 (Mar. 13, 2019), <https://www.chinaaccountingblog.com/weblog/2019-03-vie-gillis.pdf>; Jesse M. Fried & Matthew Schoenfeld, *Will China Cheat American Investors?*, WALL ST. J. (Dec. 13, 2018), <https://www.wsj.com/articles/will-china-cheat-american-investors-11544744711>; ROBIN HUI HUANG, *SECURITIES AND CAPITAL MARKETS LAW IN CHINA* 53–56 (Oxford University Press, 2014).

<sup>82</sup> Gillis & Oqvist, *supra* note 81, at 1–2. Specifically, the firm would need to obtain approval from the China Securities Regulatory Commission (CSRC), which operates under the control of the State Council.

<sup>83</sup> See *id.* at 2.

<sup>84</sup> See *id.* See also Waishang Touzi Zhunru Tebie Guanli Cuoshi (Fumian Qingdan) (2020 Nianban) (外商投资准入特别管理措施 (负面清单) (2020 年版)) [Special Administrative Measures on Access to Foreign Investment (Negative List) (2020 edition)] (promulgated by the National Development and Reform Commission, June 27, 2020, effective July 23, 2020) at item 17, <http://images.mofcom.gov.cn/lczx/202006/20200627145842336.pdf> (China).

<sup>85</sup> See Alibaba Form 20–F (2020), *supra* note 19, at 123; see also *infra* note 92.

<sup>86</sup> For background, including how VIEs arose in China, see generally Li Guo, *Chinese Style VIEs: Continuing to Sneak under Smog?*, 47 CORNELL INT'L L.J. 569 (2014).

<sup>87</sup> The WFOE typically loans money to the VIE and in connection with this transaction (1) prohibits asset or equity-interest transfers by the VIE; (2) receives call options on the equity interest of the VIE and its assets (both of which can be assigned to third parties, presumably Chinese residents legally able to control the assets) and a right to receive dividends and other distributions declared by the VIE; (3) obtains an irrevocable proxy by the VIE and its current equity holders authorizing any person designated by the WFOE to exercise rights as an equity holder; (4) receives a security interest in the VIE equity interests to secure the VIE's debts to the WFOE and the VIE's and its equity holders performance obligations under the arrange-



tracts provide a basis for including the VIE's results in the consolidated financial statements of the foreign firm. In 2000, Sina was the first U.S.-listed firm to use a VIE arrangement.<sup>88</sup> As of 2017, about 200 (or half) of China-based firms listed in the United States used VIEs.<sup>89</sup>

Alibaba operates its China-based businesses through a series of WFOEs, each with a corresponding VIE, including four VIEs "material" to its business: two for e-commerce, one for cloud computing, and one for digital media and entertainment.<sup>90</sup> These sectors are categorized as "Value-Added Telecommunications Services" (VATS) by China's Ministry of Industry and Information Technology (MIIT)<sup>91</sup> and are subject to restrictions on foreign investment, thus requiring the use of VIEs.<sup>92</sup> While Alibaba does not

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ments; and (5) enters into an exclusive technical services agreement with the WFOE that is designed to transfer substantially all of the profits from the VIE to the WFOE. *See generally* Guo, *supra* note 86.

<sup>88</sup> *See* Brandon Whitehill, *Buyer Beware: Chinese Companies and the VIE Structure*, COUNCIL OF INSTITUTIONAL INVESTORS 2 (Dec. 2017), [https://www.cii.org/files/publications/misc/12\\_07\\_17%20Chinese%20Companies%20and%20the%20VIE%20Structure.pdf](https://www.cii.org/files/publications/misc/12_07_17%20Chinese%20Companies%20and%20the%20VIE%20Structure.pdf); Christopher W. Betts, Client Memorandum, *Recent Developments in the Use of Variable Interest Entities*, SKADDEN, ARPS, SLATE, MEAGHER & FLOM (June 28, 2016), <https://www.skadden.com/insights/publications/2016/06/recent-developments-in-the-use-of-variable-interests>.

<sup>89</sup> *See* Whitehill, *supra* note 88, at 4; Justin Hopkins et al., *The Rise of U.S.-Listed VIEs from China: Balancing State Control and Access to Foreign Capital* 3 (Darden Bus. Sch., Working Paper No. 3119912, 2018).

<sup>90</sup> Alibaba's most important VIEs are Zhejiang Taobao Network Co., Ltd., Zhejiang Tmall Network Co., Ltd., Alibaba Cloud Computing Ltd., and Youku Information Technology (Beijing) Co., Ltd. *See* Alibaba Form 20-F (2020), *supra* note 19, at 123.

<sup>91</sup> *Id.* at 103.

<sup>92</sup> The digital media and entertainment sector—especially those involving audio-visual programming and culture—is largely off-limits to foreign investors. Most broadly, rules governing foreign investment prohibit involvement in online news, publishing, audio-visual programming, culture, and social media. *See* Waishang Touzi Zhunru Tebie Guanli Cuoshi (Fumian Qingdan) (2019 Nianban) (外商投资准入特别管理措施(负面清单)(2019年版)) [Special Administrative Measures on Access to Foreign Investment (Negative List) (2019 edition)] (promulgated by the National Development and Reform Commission, June 30, 2019, effective July 30, 2019) at items 34–40, <http://www.gov.cn/xinwen/2019-06/30/5404703/files/d0a86e1a90eb4e898e9a9ea6eb59703a.pdf> (China). In addition, any company with an Internet Content Provider (ICP) license (such as an Alibaba VIE) is subject to a number of rules issued by a series of Chinese regulators to monitor content for prohibited material. *See* Alibaba Form 20-F (2020), *supra* note 19, at 108 (referencing, among others, the MIIT, the News Office of China's State Council, the Ministry of Culture and Tourism, and the General Administration of Press and Publication as regulators of internet content).

E-commerce and cloud computing are nominally more open to foreign investors, but in practice are not. E-commerce requires various licenses or permissions related to the provision of "internet information services" that are difficult, if not impossible, for foreign companies to obtain. *See id.* at 44; *see also* US-CHINA BUS. COUNCIL, *Optimizing Connectivity: Updated Recommendations to Improve China's Information Technology Environment* 5 (2018), [https://www.uschina.org/sites/default/files/uscbc\\_ict\\_recommendations\\_en.pdf](https://www.uschina.org/sites/default/files/uscbc_ict_recommendations_en.pdf).

To provide cloud computing services in China, a company must obtain three different certifications: an Internet Data Center (IDC) license, an Internet Service Provider (ISP) license, and sometimes an Internet Content Provider (ICP) license. *See id.* at 4. Foreign companies may obtain these licenses if they have a partnership with a local firm and own no more than 50% of the partnership, but in practice getting such licenses has been difficult. *See* Yang Jie & Liza Lin, *Amazon Sells Hardware to Cloud Partner in China*, WALL ST. J. (Nov. 14, 2017), <https://www.wsj.com/articles/amazon-to-sell-its-china-cloud-computing-business-1510628802>.

reveal the exact holdings of each of these VIEs, the VIEs collectively hold various licenses that are critical to Alibaba's businesses and cannot be held solely by a WFOE, including a Value-Added Telecommunication Business Operation Permit (for online and mobile commerce business), a Network Culture Permit, and a License for Transmission of Audio-Visual Programs through Information Network.<sup>93</sup> Failure to comply with Chinese regulations around the ownership of these licenses would subject Alibaba to severe penalties "including being prohibited from continuing operations"—potentially of all of them.<sup>94</sup>

As is well understood, the problem for Alibaba and its foreign investors is that the VIE arrangement is legally fragile: its enforceability in China is, at best, uncertain. The reason is that Chinese contract law invalidates contracts that seek to achieve an illegal objective under the guise of otherwise legal acts.<sup>95</sup> In fact, Chinese government agencies have in the past indicated disapproval of VIE arrangements.<sup>96</sup> And in several cases government officials have barred their use, required them to be dismantled, or found them to be invalid.<sup>97</sup> Interestingly, in 1998 China forced the dismantling of an ar-

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<sup>93</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 46. The licenses for e-commerce businesses Taobao and Tmall (see *supra* note 25) are likely held by Zhejiang Taobao Network Co., Ltd. and Zhejiang Tmall Network Co., Ltd., respectively. Prior to a 2019 VIE restructuring (see *infra* note 104), licenses for Alibaba.com, 1688.com, and AliExpress were held by Hangzhou Alibaba Advertising Co., Ltd. See Alibaba Form 20-F (2019), *supra* note 34, at 115. Following the restructuring, it is unclear where these licenses are held. See Alibaba Form 20-F (2020), *supra* note 19, at 46, 71.

<sup>94</sup> See *id.* at 45, 128.

<sup>95</sup> A contract in China is invalid when "there is an attempt to conceal illegal goals under the disguise of legitimate forms." See Lin & Mehaffy, *supra* note 8, at 447, citing *Zhonghua Renmin Gongheguo Hetong Fa* (中华人民共和国合同法) [Contract Law of the People's Republic of China] (enacted by the National People's Congress, Mar. 15, 1999, effective Oct. 1, 1999) art. 51 (iii), (v), <https://www.wipo.int/edocs/lexdocs/laws/en/cn/cn137en.pdf> (China). Because Alibaba uses VIEs to obtain permits and other licenses to do business in sectors forbidden to foreign entities pursuant to Article 28 of the Foreign Investment Law of the People's Republic of China, their contracts fall under this Article 52 provision. As one U.S. lawyer with expertise in Chinese law puts it, "[t]o the extent a VIE contract structure is designed to circumvent the requirements of Chinese law, such contracts are void. Not voidable, void. It is as if they did not exist." See Hopkins et al., *supra* note 89, at 11. See also Steve Dickinson, *China's New Foreign Investment Law does NOT Resuscitate VIEs*, CHINA L. BLOG (Apr. 10, 2019), <https://www.chinalawblog.com/2019/04/chinas-new-foreign-investment-law-does-not-resuscitate-vies.html> (observing that China "understands that the only reason VIEs exist is to evade the clear requirements of Chinese law . . . and has firmly concluded this behavior is wrong and . . . will not be tolerated . . .").

<sup>96</sup> See Guo, *supra* note 86, at 580–84. Tellingly, China-based Fangda law firm, which was asked to provide an opinion on the legality of the VIE structure in Alibaba's registration statement, opined that the individual contracts did not violate Chinese law but did not opine that the contracts, when taken together, complied with Chinese law. See Alibaba Grp. Holding Ltd., Registration Statement (Form F-1), 40–41, 74 (May 6, 2014) [hereinafter Alibaba Form F-1 (2014)].

<sup>97</sup> See Whitehill, *supra* note 88, at 8 (describing the case of Baosheng Steel in 2011); Charles Comey et al., Client Alert, *China VIEs: Recent Developments and Observations*, MORRISON & FOERSTER 2–3 (Aug. 15, 2013), <http://media.mofo.com/files/uploads/Images/130716-Variable-Interest-Entities-China.pdf> (describing a ruling invalidating the VIE structure of Gigamedia by the Shanghai Sub-Commission of China International Economic and Trade Ar-

rangement similar to the VIE arrangement, the “China-China-Foreign” (CCF) structure, generating large shareholder losses.<sup>98</sup>

However, at present China lets most VIEs operate without officially endorsing or prohibiting them, retaining discretion to treat some or all of them as illegal in the future.<sup>99</sup> Nothing prevents China from invalidating one or more of Alibaba’s VIE structures and eliminating its foreign investors’ economic interest in the VIE.<sup>100</sup> For this reason, Alibaba’s prospectus warns:

*[T]here are very few precedents and little formal guidance as how contractual arrangements in the context of a variable interest entity should be interpreted or enforced under PRC law, and as a result it may be difficult to predict how an arbitration panel or court would view such contractual arrangements.*<sup>101</sup>

But our interest here is not in the risk that Chinese officials will decide on their own to take such steps. Rather, our interest is in the possibility that Ma can exploit the legal fragility of Alibaba’s VIE arrangements to exert control over Alibaba. To this we now turn.

### B. Ma’s Ability to Exploit the VIEs’ Legal Fragility

After Alibaba’s initial public offering in 2014, Ma directly controlled the VIEs as owner of 80–90% of each VIE’s equity; Simon Xie, Alibaba’s cofounder, owned the remainder.<sup>102</sup> In 2019, Alibaba announced it was restructuring its VIEs so that by the end of 2019 all material VIEs would be controlled through various layers of China-registered entities by “selected

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bitration Commission because it was designed “to enable the WFOE, which did not have online operation qualifications, to participate in the operation of online games in the PRC to obtain financial returns therefrom”).

<sup>98</sup> See Samuel F. Ziegler, *China’s Variable Interest Entity Problem: How Americans Have Illegally Invested Billions in China and How to Fix it*, 84 GEO. WASH. L. REV. 539, 552–53 (2016).

<sup>99</sup> See Paul Gillis & Michelle René Lowry, *Son of Enron: Investors Weigh the Risks of Chinese Variable Interest Entities*, 26 J. APPLIED CORP. FIN. 61 (2014). In 2015, a draft proposal was issued by the State Council that would have “legalized” VIEs like Alibaba’s, but revised rules proposed in 2018 omitted that solution. See Gillis & Oqvist, *supra* note 81, at 8. China’s recently enacted Foreign Investment Law, effective January 1, 2020, does not indicate one way or the other whether VIEs are legal. See Paul D. McKenzie et al., Client Alert, *China’s Foreign Investment Law: Are You Ready for It?*, MORRISON & FOERSTER (Jan. 3, 2020), <https://www.mofo.com/resources/insights/200102-chinas-investment-foreign-law.html> (noting that the current law likely deferred the issue, and that an “open-ended definition of foreign investment leaves ample room for the State Council to regulate VIEs in the future”).

<sup>100</sup> Even if China deems a VIE to be legal, it can interpret its tax rules to subject payments flowing from the VIE to the foreign-domiciled and listed entity (ListCo) via the WFOE to a series of taxes that, collectively, would eat up over 50% of the payments. See Whitehill, *supra* note 88, at 11 (describing the various types of taxes that might be imposed along the way as the cash moves from the VIE to ListCo). China can also use capital controls to stop payments to ListCo. See Hopkins et al., *supra* note 89, at 12.

<sup>101</sup> See Alibaba Grp. Holding Ltd., Amendment No. 7 to Alibaba Form F-1 (2014) (Sept. 15, 2014) at 51.

<sup>102</sup> See Alibaba Form 20-F (2017), *supra* note 52, at 112.

members” of the Alibaba Partnership or Alibaba’s management who are Chinese nationals.<sup>103</sup> In July 2020, Alibaba revealed the identities of ten individuals controlling the VIEs.<sup>104</sup> All but one (Fan Jiang) are partners<sup>105</sup>: one of those nine individuals (Angel Ying Zhao) is an Ant Group executive, and the others are Alibaba executives.<sup>106</sup>

As we have seen, Ma’s position as controller of Ant Group enables him to dominate not only partners who are Ant Group executives, but also any member of the Alibaba Partnership, including Alibaba executives, via Ma’s control of the Partnership Committee.<sup>107</sup> Ma can also dominate any Alibaba executive who is not a partner. Thus, Ma dominates all those controlling the VIEs.<sup>108</sup>

In fact, Ma could exploit the legal fragility of the VIE arrangements to impose his will on Alibaba, even if he did not effectively control the board. For example, he could have the VIEs threaten not to honor contracts with their associated WFOEs, which would cripple Alibaba’s business. Alibaba would not cause the WFOEs to sue in such a case for fear that the VIE arrangements would be declared illegal and therefore void.<sup>109</sup> Even if Alibaba’s board was otherwise independent of Ma, it might well bend to his wishes.<sup>110</sup>

<sup>103</sup> See Alibaba Form 20-F (2019), *supra* note 34, at 39, 117.

<sup>104</sup> See Alibaba Form 20-F (2020), *supra* note 19, at 124 (“For our major variable interest entities, these individuals are Daniel Yong Zhang, Jessie Junfang Zheng, Xiaofeng Shao, Judy Wenhong Tong and Angel Ying Zhao (with respect to each of Zhejiang Taobao Network Co., Ltd., Zhejiang Tmall Network Co., Ltd. and Alibaba Cloud Computing Ltd.), and Sophie Minzhi Wu, Trudy Shan Dai, Jeff Jianfeng Zhang, Fan Jiang and Winnie Jia Wen (with respect to Youku Information Technology (Beijing) Co., Ltd.).”).

<sup>105</sup> See *id.* at 179.

<sup>106</sup> See *id.* at 175, 179.

<sup>107</sup> See *supra* Part II.

<sup>108</sup> Ma can also use his various sources of leverage over Alibaba’s directors, including his control of the director-nominating Partnership Committee, to ensure that any changes in the VIE arrangements preserve or increase Ma’s VIE-based leverage against Alibaba’s directors, discussed next.

<sup>109</sup> This appears to have happened at Nasdaq-listed GigaMedia. The executive of one of its VIEs, T2CN, seized the VIE’s business license and financial documents, paralyzing the business, after discovering that GigaMedia’s stockholders wanted to remove him. GigaMedia did not risk litigating the contractual arrangements between the T2CN and the paired WFOE, which might have been invalidated by a court, and instead settled with the executive, selling its ownership in the WFOE. See Whitehill, *supra* note 88, at 9. As one commentator noted, “[i]t is telling that the company would rather settle with a manager who effectively took the company assets hostage than take the chance of having a court declare the entire operation illegal.” See Ziegler, *supra* note 98, at 550. See also Paul Gillis, *Testimony Before the U.S.-China Security and Economic Commission*, CHINA ACCOUNTING BLOG (Jan. 26, 2017), <https://www.chinaaccountingblog.com/gillis-january-26-testimony.pdf> (“Attempts to enforce [VIE] . . . arrangements have generally failed since China’s Supreme Court and arbitrators have held that VIE contracts are not enforceable under Chinese law because they attempt an illegal work around the foreign investment restrictions.”).

<sup>110</sup> A threat to disrupt a VIE-WFOE contract would be credible only if Ma expected to gain more from imposing his will on Alibaba than the permanent loss, if any, in the value of his equity that he expected would result from the disruption. Of course, to the extent the disruption caused the short-term stock price to fall below its long-term value, Ma could buy

Alternatively, Ma could use the threat of unfavorable Chinese regulatory action as an opportunity or pretext to renegotiate terms of Alibaba's VIEs with their WFOE counterparties. As others have pointed out, Ma arguably followed this playbook when he unilaterally moved Alipay (now operated by Ant Group) from pre-IPO Alibaba, where its value had been shared with Alibaba investors Yahoo and SoftBank, to a firm he controlled.<sup>111</sup>

At that time, Alipay was held by one of Alibaba's VIEs, Zhejiang Alibaba, which was 80% owned by Ma,<sup>112</sup> and worth around \$5 billion.<sup>113</sup> In 2010, the People's Bank of China (PBOC) indicated that online payment services like Alipay needed to obtain a license, and such a license would be granted only to Chinese-owned and domiciled entities.<sup>114</sup> In 2011, the PBOC asked Alipay by fax if it had a VIE arrangement with any foreign investor, which may or may not have meant that Alipay's application would be denied if there were such an arrangement.<sup>115</sup> Ma then decided to terminate the VIE arrangement with Alibaba, transferring Alipay to himself and the other co-owner of the VIE.<sup>116</sup> Major Alibaba shareholders Yahoo and SoftBank claimed they had not been notified.<sup>117</sup> The parties settled the dispute by agreeing that Alipay (now Ant Group) would provide Alibaba with a profit-sharing or equity interest.<sup>118</sup> According to one estimate, the settlement reduced the value of Yahoo's stake in Alipay by over 60%.<sup>119</sup> In early 2020, Ant Group traded on secondary markets at a value exceeding \$200 billion.<sup>120</sup>

The risk of Ma exploiting the VIEs' legal fragility is heightened for Alibaba's investors given how Ma arranged for disputes between Alibaba's WFOEs and VIEs to be resolved. Ordinarily, Chinese businesses and their foreign counterparties contract for dispute resolution via arbitration rather than via Chinese courts, as arbitration is thought to be more efficient and fair.<sup>121</sup> And while Chinese courts cannot be expected to enforce judgments

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additional stock at the temporarily depressed price and thereby profit directly from the disruption itself.

<sup>111</sup> See, e.g., Whitehill, *supra* note 88, at 9.

<sup>112</sup> See Wei Shen, *Deconstructing the Myth of the Alipay Drama—Repoliticizing Foreign Investment in the Telecommunications Sector in China*, 36 TELECOMM. POL'Y 929, 933 (2012).

<sup>113</sup> See Gillis & Oqvist, *supra* note 81, at 6.

<sup>114</sup> See Shen, *supra* note 112, at 933.

<sup>115</sup> See *id.*

<sup>116</sup> See *id.*

<sup>117</sup> See Evelyn M. Rusli, *Yahoo and Alibaba Resolve Dispute Over Alipay*, N.Y. TIMES (July 29, 2011), <https://dealbook.nytimes.com/2011/07/29/yahoo-and-alibaba-resolve-alipay-dispute/>.

<sup>118</sup> See *id.*

<sup>119</sup> See Whitehill, *supra* note 88, at 9 (reporting that the seizure of Alipay devalued Yahoo's stake in Alipay by over 60%).

<sup>120</sup> See Julie Zhu et al., *Exclusive: China's Ant aims for \$200 billion price tag in private share sales—sources*, REUTERS (Jan. 17, 2020), <https://www.reuters.com/article/us-ant-financial-valuation-exclusive/exclusive-chinas-ant-aims-for-200-billion-price-tag-in-private-share-sales-sources-idUSKBN1ZG1C6>.

<sup>121</sup> See generally Jerome A. Cohen, *Settling International Business Disputes with China: Then and Now*, 47 CORNELL INT'L L.J. 555 (2014) (concluding that arbitration in China is

from U.S. courts,<sup>122</sup> they will enforce arbitration rulings pursuant to the New York Convention.<sup>123</sup> But Ma did not arrange for contracts between Alibaba and the VIEs to be arbitrated. Rather, the disputes are to be resolved by a “people’s court.” And not just any people’s court: a people’s court of Hangzhou City, Ma’s hometown and where Alibaba is based.<sup>124</sup>

We do not claim that Ma plans to use the VIEs to transfer value to himself, only that he can. Should Ma wish to get his way with Alibaba, the VIEs provide another channel beyond his domination of the board.<sup>125</sup>

Figure 3 depicts both of Ma’s channels of control: via Alibaba’s board and via the VIEs.

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preferable to judicial proceedings but still leaves much to be desired); Shahla Ali & Hui Huang, *Financial Dispute Resolution in China: Arbitration or Court Litigation?*, 28 *ARB. INT’L* 77 (2012), <https://academic.oup.com/arbitration/article-abstract/28/1/77/229998>.

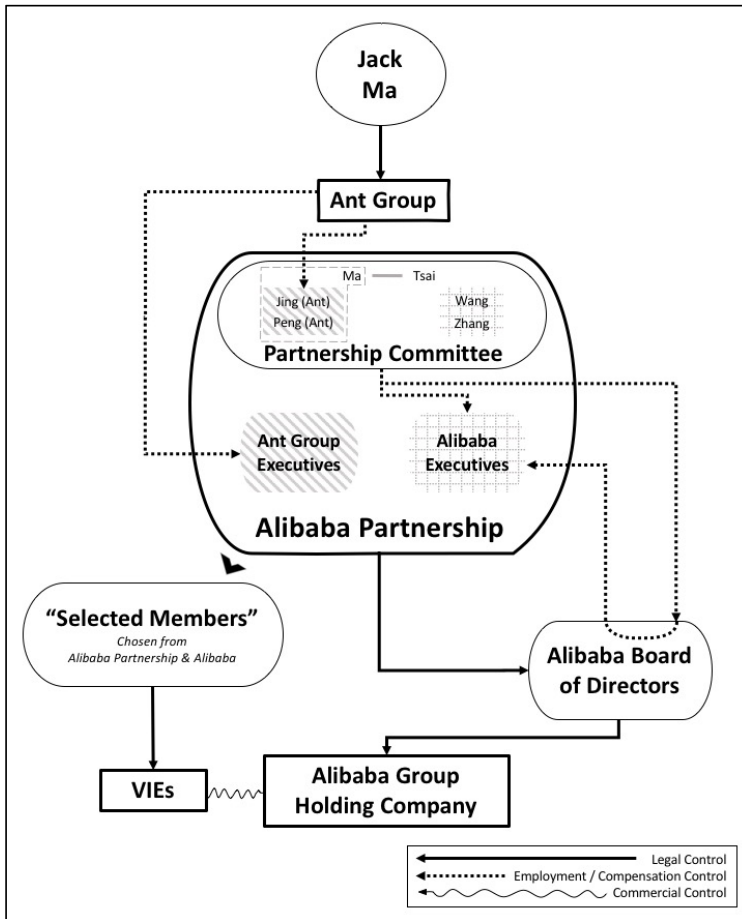
<sup>122</sup> See *infra* note 124.

<sup>123</sup> See Zuigao Renmin Fayuan Guanyu Zhixing Woguo Jiaru “Chengren ji Zhixing Waiguo Zhongcai Caijue Gongyue” de Tongzhi (最高人民法院关于执行我国加入《承认及执行外国仲裁裁决公约》的通知) [Notice of the Supreme People’s Court on Implementing the Convention on the Recognition and Enforcement of Foreign Arbitral Awards Acceded to by China] (issued by the Supreme People’s Court, Apr. 10, 1987, effective Apr. 10, 1987), Judicial Interpretation No. 5 [1987] of the Supreme People’s Court, <http://en.pkulaw.cn/display.aspx?cgid=B96476088a462bafdbf&lib=law>; see also Weixia Gu, *Arbitration in China*, in *INT’L COM. ARB. IN ASIA* 77, 85 (Tom Ginsburg & Shahla Ali eds., Juris Publishing 3d ed. 2013).

<sup>124</sup> See Exhibits 10.10, 10.11, 10.12, 10.13, and 10.14 to Alibaba Form F-1 (2014), *supra* note 96 (requiring disputes to “be brought before the competent people’s court of Hangzhou City for adjudication”).

<sup>125</sup> Naturally, the VIEs provide a pre-carved channel for value-shifting. Alibaba relies heavily on Alipay, owned by Ma-controlled Ant Group, for payment processing, through contractual arrangements that are currently “on preferential terms.” See Alibaba Form 20-F (2020), *supra* note 19, at 29. Alibaba reports that approximately 70% of the GMV on its Chinese retail marketplaces was settled through Alipay. See *id.* at 27. Alibaba thus highlights the risks associated with disruption of this relationship, including the loss of these preferential terms and the potential losses from Alipay pursuing opportunities that Alibaba might otherwise exploit. See *id.* at 29–30. As with the VIEs, Ma can use his control over Alipay both for extracting value and for exerting pressure on Alibaba’s board to benefit him in other ways.

FIGURE 3: ALIBABA—MA’S CONTROL VIA BOARD AND VIA VIEs



#### IV. CONSTRAINTS ON MA

As we have seen, Ma effectively controls Alibaba through a web of employment, commercial, and contractual arrangements. This Part explores the external constraints on Ma’s use of his power.

Section A explains that the securities law and corporate law applicable to Alibaba and Ma, primarily U.S. securities law and Cayman corporate law, cannot easily be enforced against Alibaba and Ma, as Ma and Alibaba and the bulk of their assets are located in mainland China, which neither extradites defendants nor enforces foreign judgments. Section B briefly describes other potential constraints on Ma, including fear of running afoul of the Chinese Communist Party (CCP) and Chinese government, which can do with Alibaba and Ma whatever they like.

### A. Securities Law and Corporate Law

Since its IPO in 2014, Alibaba has been subject to U.S. securities law and Cayman corporate law. Since its secondary listing in Hong Kong in 2019, it has also been subject to Hong Kong securities law. But none of these laws can provide much of a constraint on Ma's ability to, along with other insiders (hereinafter, Ma-controlled insiders), expropriate most of the firm's assets.<sup>126</sup>

The main problem is that every person or thing required to enforce U.S., Cayman, or Hong Kong law—Ma, Ma's assets, Alibaba's records, and Alibaba's assets—is behind China's "Great Legal Wall" and out of reach both for private plaintiffs and for public prosecutors in the United States.<sup>127</sup> China cannot be expected to extradite defendants, enforce foreign judgments, allow foreigners to file claims in its courts, or even permit litigation-critical information to be shared with foreign authorities or plaintiffs' lawyers.<sup>128</sup> Below, we explain how enforceable law can prevent insider expropriation, and then why corporate law and securities law are not effectively enforceable against Ma.

#### 1. The Role of Enforceable Corporate Law and Securities Law in Constraining Ma

Absent external constraints, Ma and Ma-controlled insiders could use their control over Alibaba to massively expropriate public investors via tunneling transactions.<sup>129</sup> Cayman corporate law and U.S. and Hong Kong securities law could in theory play complementary roles in deterring Ma-

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<sup>126</sup> Even if securities law and corporate law were completely enforceable, investors in Alibaba could not mitigate two other types of risk. The first is *business risk*: the firm's business may not succeed due to managerial incompetence, market developments, or regulatory shifts. The second is *dissipation risk*: Ma may deliberately seek nonpecuniary psychic benefits at the expense of shareholder value. Such dissipation is largely unpreventable: there is usually no legal constraint on a controller's ability to make value-destroying decisions absent a clear *financial* conflict of interest.

<sup>127</sup> See Jesse M. Fried & Ehud Kamar, *China and the Rise of Law-Proof Insiders* 7–8 (Eur. Corp. Governance Inst., Working Paper No. 557, 2020) (explaining why American investors and authorities cannot rely on securities or corporate law to prevent massive value extraction by insiders of China-based, U.S.-listed firms).

<sup>128</sup> *Id.*

<sup>129</sup> The tunneling transactions could take place before the end of Alibaba's life as a public company. Such midstream tunneling transactions could include value-shifting asset transactions between Alibaba and Ma-controlled insiders or related parties, or value-shifting securities transactions involving Ma-controlled insiders, public investors, and Alibaba. See generally Luca Enriques, *Related Party Transactions: Policy Options and Real-World Challenges (With a Critique of the European Commission Proposal)*, 16 EUR. BUS. ORG. L. REV. 1 (2015) (describing tunneling transactions); Jesse M. Fried & Holger Spamann, *Cheap-Stock Tunneling around Preemptive Rights*, 137 J. FIN. ECON. 353 (2020) (explaining how equity issuances by controlled firms can be used to dilute minority shareholders). At the end of Alibaba's life as a public company, there could also be endgame tunneling: a freeze-out at a low price determined by Ma-controlled insiders. For example, the insiders can cause Alibaba to merge with a shell corporation owned by the insiders in consideration for cash.



controlled insiders from tunneling. When enforceable, they can make tunneling impossible or too costly to be worthwhile.

The fundamental purpose of corporate law, including Cayman corporate law, is to prevent tunneling. To this end, corporate law prohibits transactions that benefit insiders at public investors' expense by imposing fiduciary duties on insiders, which public investors and their attorneys enforce via private litigation.

U.S. and Hong Kong securities law requires listed firms to publicly disclose accurate information about their financial condition and certain insider transactions.<sup>130</sup> This disclosure serves two primary purposes. First, it provides public investors with information about firm value to facilitate trading in the firm's shares. Second, it alerts public investors to violations of corporate law and thereby enables them to enforce their corporate-law rights. Without disclosure it would be difficult for investors to use these rights against tunneling. Securities law is enforced by public investors and their attorneys as well as by the government.

## 2. The Difficulty of Enforcing Cayman Corporate Law and U.S. Securities Law Against Ma in the United States

Corporate law and securities law deter violations only if insiders believe they will be subject to punishment for violating these laws. The law provides for two main types of penalties: imprisonment and monetary damages.<sup>131</sup> As the likelihood of punishment declines, so does deterrence.<sup>132</sup>

As we explain in more detail below, Ma can largely escape these penalties. Chinese law shields China-based insiders like Ma from extradition and blocks the seizure of their personal assets (as well as their firm's assets) in China.<sup>133</sup> In short, China surrounds its residents and firms by a "Great Legal

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<sup>130</sup> See, e.g., Alexander F. Cohen et al., *Financial Statement Requirements in US Securities Offerings: What You Need To Know*, LATHAM & WATKINS LLP & KPMG LLP 1, 6–7 (Jan. 2020), <https://www.lw.com/thoughtLeadership/us-financial-statements-guide-2018> (describing the variety of financial statement requirements of U.S. federal securities laws, including both those "necessary to understand an issuer's financial condition [and] changes in financial condition," as well as "related-party transactions"); *The MOFO Guide to Compliance for Hong Kong Listed Companies*, MORRISON & FOERSTER 1, 22 (Sept. 1, 2013), <https://media2.mofo.com/documents/130617-the-mofo-guide-to-compliance-for-hk-companies.pdf> (noting that Hong Kong's Listing Rules impose disclosure obligations on issuers, including the announcement of financial information as well as certain "connected transactions," i.e., insider transactions).

<sup>131</sup> The enforcement of corporate law and securities law against an insider can also impose considerable collateral costs, even if in the end the insider avoids both jail and financial penalties. A defendant in protracted civil or criminal litigation bears the risk of an adverse outcome until the litigation ends. The defendant also loses time, energy, and money in the process. See Fried and Kamar, *supra* note 127, at 9.

<sup>132</sup> See generally Gary S. Becker, *Crime and Punishment: An Economic Approach*, 76 J. POL. ECON. 169 (1968).

<sup>133</sup> See Fried and Kamar, *supra* note 127, at 11. It also prevents depositions and the sharing of litigation-critical documents. *Id.* The domiciling of Alibaba in the Cayman Islands also creates procedural hurdles to private litigations. *Id.* at 32.

Wall” that is all but impossible to scale for authorities or investors suing in the United States.<sup>134</sup>

*a. No Extradition to the United States*

Corporate insiders can be imprisoned for violating U.S. securities law,<sup>135</sup> embezzlement,<sup>136</sup> fraud,<sup>137</sup> perjury in corporate or securities litigation,<sup>138</sup> or contempt of court.<sup>139</sup> Arrest warrants have been issued against insiders of China-based, U.S.-listed firms for such infractions.<sup>140</sup>

But Ma and other China-based insiders need not fear imprisonment. China lacks an extradition treaty with the United States.<sup>141</sup> To our knowl-

<sup>134</sup> Investor litigation would be expected to originate in the United States, the only jurisdiction where attorneys representing public investors can easily bring class-action corporate or securities suits and corporate derivative suits; investor litigation will not arise in the Cayman Islands. See Fried and Kamar, *supra* note 127, at 30 (explaining that there has never been a case in the Cayman Islands against insiders of a public company because of unfavorable procedural rules). U.S. authorities would also bring cases in U.S. courts. Below, we discuss the effects of Alibaba’s Hong Kong listing and explain why it does not expose Ma-controlled insiders to more risk of enforcement if they remain in mainland China.

<sup>135</sup> Any willful violation of the substantive provisions of the securities law, including registration and fraud provisions, is a criminal offense. See 15 U.S.C. § 78ff.

<sup>136</sup> See, e.g., DEL. CODE ANN. tit. 11, § 841(b) (West 2021) (“A person is guilty of theft if the person, in any capacity, legally receives, takes, exercises control over or obtains property of another which is the subject of theft, and fraudulently converts same to the person’s own use.”); depending on the value of the stolen property, imprisonment may be for a term of not less than two and up to 25 years, see tit. 11 § 4205(b). See also NEV. REV. STAT. ANN. § 205.300 (West 2021) (“[A]ny agent . . . of any person, corporation, association or partnership . . . who uses or appropriates the money, property or effects . . . is guilty of embezzlement and shall be punished in the manner prescribed by law for the stealing or larceny of property of the kind and name of the money, goods, property or effects so taken, converted, stolen, used or appropriated.”).

<sup>137</sup> See 18 U.S.C. § 1343.

<sup>138</sup> See 18 U.S.C. §§ 401–403; FED. R. CRIM. P. 42; See also CHARLES DOYLE, CONG. RSCH. SERV., RL34303, OBSTRUCTION OF JUSTICE: AN OVERVIEW OF SOME OF THE FEDERAL STATUTES THAT PROHIBIT INTERFERENCE WITH JUDICIAL, EXECUTIVE, OR LEGISLATIVE ACTIVITIES 65 (2014).

<sup>139</sup> See *id.* at 30. While imprisonment is uncommon, a number of U.S. insiders have been jailed for criminal violations in connection with their governance of firms. See *Timeline: A History of Insider Trading*, N.Y. TIMES (Dec. 6, 2016), <https://www.nytimes.com/interactive/2016/12/06/business/dealbook/insider-trading-timeline.html> (reporting that Enron’s CEOs Jeffrey Skilling and Kenneth Lay were both sentenced to prison for their participation in the Enron accounting fraud, although Lay died before entering jail); 7 of the *Biggest Corporate Scandals*, CNN MONEY (Oct. 14, 2015), <https://money.cnn.com/gallery/news/2015/10/14/biggest-corporate-scandals/2.html> (reporting that WorldCom’s CEO Bernard Ebbers went to prison on fraud and conspiracy charges).

<sup>140</sup> For example, in *Deutsch v. ZST Digital Networks, Inc.*, No. 8014-VCL, 2018 WL 3005822, at \*1 (Del. Ch. June 14, 2018), the Delaware Court of Chancery issued an arrest warrant for two Chinese executives who for several years had not complied with court orders in a shareholder suit. See Vince Sullivan, *Chancery Issues Arrest Warrants for Chinese Tech Execs*, LAW360 (Jan. 7, 2019), <https://www.law360.com/articles/1115940/chancery-issues-arrest-warrants-for-chinese-tech-execs>.

<sup>141</sup> See, e.g., *Rogers v. State*, 40 So. 3d 888, 889 (Fla. Dist. Ct. App. 5 Dist. 2010) (noting that the Department of Justice, Office of International Affairs produced information to the court and confirmed that “there was no extradition treaty between China and the United States”).

edge, no Chinese national has ever been extradited to the United States for violation of U.S. securities law or U.S. judicial orders in corporate matters. As long as insiders remain in China, they cannot be taken to the United States for trial and possible imprisonment.

They are now likely safe also in Hong Kong. Although the United States had an extradition treaty with Hong Kong,<sup>142</sup> it was suspended in August 2020.<sup>143</sup> Even before the treaty was suspended, China had successfully pressured Hong Kong not to extradite a fugitive to the United States pursuant to the treaty.<sup>144</sup>

### *b. No Enforcement of U.S. Judgments*

Nor can the U.S. legal system impose financial penalties on China-based insiders, either directly or by seizing firm assets. Thus, neither U.S. investors nor U.S. authorities seeking to enforce U.S. judgments can seize Alibaba's or Ma's assets in China.

U.S. investors asserting corporate claims or securities claims in the United States cannot expect to recover from insider assets or firm assets located in China. China does not have an enforcement treaty with the United States.<sup>145</sup> While a Chinese court can still choose to enforce a U.S. judgment,

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<sup>142</sup> See Agreement with Hong Kong for the Surrender of Fugitive Offenders, U.S.–H.K., Dec. 20, 1996, S. Treaty Doc. No. 105–3.

<sup>143</sup> See The President's Executive Order on Hong Kong Normalization, Exec. Order No. 13,936, 85 Fed. Reg. 43,413 (July 14, 2020), <https://www.govinfo.gov/content/pkg/FR-2020-07-17/pdf/2020-15646.pdf>. The suspension occurred as a part of a broader U.S. response to Beijing's imposition of the National Security Law in Hong Kong. See Press Statement, Morgan Ortagus, Spokesperson, U.S. Department of State, *Suspension or Termination of Three Bilateral Agreements With Hong Kong* (Aug. 19, 2020), <https://www.state.gov/suspension-or-termination-of-three-bilateral-agreements-with-hong-kong/>. The United States was one of several nations that suspended the agreement, in addition to Canada, New Zealand, Australia, Britain, Finland, and Ireland; France decided not to ratify a pending extradition agreement. See Reuters Staff, *Ireland suspends extradition treaty with Hong Kong*, REUTERS (Oct. 23, 2020), <https://www.reuters.com/article/uk-hongkong-security-ireland/ireland-suspends-extradition-treaty-with-hong-kong-idUKKBN2781XA>; Shannon Tiezzi, *US Becomes Latest Country to Suspend Extradition Treaty with Hong Kong*, DIPLOMAT (Aug. 20, 2020), <https://thediplomat.com/2020/08/us-becomes-latest-country-to-suspend-extradition-treaty-with-hong-kong/>.

<sup>144</sup> See Venus Wu, *China Leaned on Hong Kong Not to Hand Fugitive to U.S.*, STATE DEPARTMENT SAYS, REUTERS (May 30, 2018), <https://www.reuters.com/article/us-hongkong-extradition/china-leaned-on-hong-kong-not-to-hand-fugitive-to-u-s-state-department-says-idUSKCN1IIV1HV>.

<sup>145</sup> See Song Jianli, *Recognition and Enforcement of Foreign Judgments in China: Challenges and Developments*, CHINA INT'L COMM. CT. (Aug. 30, 2018), [http://cicc.court.gov.cn/html/1/219/199/203/1048.html#\\_ftnref23](http://cicc.court.gov.cn/html/1/219/199/203/1048.html#_ftnref23). Even if there were such a treaty, a U.S. judgment would not be enforced if it were considered to “violate the basic principles of the laws of China and the sovereignty, security, and public interest of China.” Zhonghua Renmin Gongheguo Minshi Susong Fa (中华人民共和国民事诉讼法) [Civil Procedure Law of the People's Republic of China] (promulgated by the Standing Comm. Nat'l People's Cong., June 27, 2017, effective July 1, 2017) art. 282, <http://cicc.court.gov.cn/html/1/219/199/200/644.html>; King Fung (Dicky) Tsang, *Chinese Bilateral Judgment Enforcement Treaties*, 40 LOY. L.A. INT'L & COMP. L. REV. 1, 5 (2017).

The Convention on Choice of Court Agreements, June 30, 2005, 44 I.L.M. 1294 [hereinafter Hague Convention], signed by China in 2017, does not avail either. While the Convention

China generally does not enforce U.S. judgments.<sup>146</sup> Attempts to enforce a foreign judgment that has not been recognized by a Chinese court can be punished as a violation of Chinese judicial sovereignty.<sup>147</sup>

U.S. authorities can bring securities claims against a China-based firm and its China-based insiders and obtain judgments. But these judgments are unlikely to be enforced in China, even though U.S. authorities have enforcement tools not available to investors. The United States and China have agreed to mutual legal assistance in criminal matters, including in forfeiture proceedings.<sup>148</sup> But China can refuse assistance on a number of grounds, including that the requested assistance would “prejudice the sovereignty, security, public order, important public policy or other essential interests” of China.<sup>149</sup> Such refusal is routine.<sup>150</sup> To our knowledge, U.S. authorities have never used this agreement successfully.

### 3. Effect of Alibaba’s Hong Kong Listing

Because Alibaba is listed on the Hong Kong Stock Exchange, it and Ma-controlled insiders subject themselves to the listing rules of that exchange and to enforcement by the Hong Kong Securities and Futures Commission (SFC) and Hong Kong investors.<sup>151</sup> But a Hong Kong listing does not constrain China-based insiders of China-based firms.

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enables a party with a court judgment in one signatory country to enforce the judgment in another, the Convention has not been ratified by either the United States or China. More importantly, the Convention applies only if the parties’ contract “. . . designates, for the purpose of deciding disputes which have arisen or may arise in connection with a particular legal relationship, the courts of one Contracting State or one or more specific courts of one Contracting State to the exclusion of the jurisdiction of any other courts.” See Hague Convention, art. 3(a). Because U.S. investors and U.S. authorities will not have entered into such a contract with Alibaba and its insiders, even a fully-ratified Convention would not help.

<sup>146</sup> See Donald Clarke, *The Bonding Effect in Chinese Cross-Listed Companies: Is It Real?*, in ENFORCEMENT OF CORPORATE AND SECURITIES LAW: CHINA AND THE WORLD 88, 94 (Robin Hui Huang & Nicholas Calcina Howson eds., 2017).

<sup>147</sup> See ISDA & KING & WOOD MALLESONS, CHINA’S DERIVATIVES MARKET AND JUDICIAL TRENDS 1, 19 (2018), <https://www.isda.org/a/9pREE/Chinese-Derivatives-Market-and-Legal-Trends.pdf> (reporting a case in which KPMG was fined for receiving the assets of a Chinese company according to a BVI court’s judgment that had been recognized by Chinese courts, thereby demonstrating “that a foreign bankruptcy or similar order must be first recognized by a Chinese court before the administrator or receiver may exercise its powers against the relevant assets in China”).

<sup>148</sup> See Agreement on Mutual Legal Assistance in Criminal Matters, U.S.-China, June 19, 2000, T.I.A.S. 13,102.

<sup>149</sup> See *id.*

<sup>150</sup> See John Hill, *DC Circ. Won’t Let 3 Chinese Banks Duck US Subpoenas*, LAW360 (Aug. 6, 2019), <https://www.law360.com/articles/1185604/dc-circ-won-t-let-3-chinese-banks-duck-us-subpoenas> (reporting that the U.S. Department of Justice did not bother to use this agreement to get records from Chinese banks in connection with an investigation into evasion of North Korean sanctions because cooperation from China under this agreement has been “poor”).

<sup>151</sup> See Alibaba Grp. Holding Ltd., Supplement to Prospectus (Nov. 13, 2019) at S–29 (“Upon the Listing, we will be subject to Hong Kong and NYSE listing and regulatory requirements concurrently.”).

Hong Kong does not allow for contingent fees or class actions, and has a loser-pay default rule.<sup>152</sup> Consequently, private litigation is rare and the enforcement of corporate law and securities law is left to public authorities.<sup>153</sup> But Hong Kong, like the United States, is on the other side of the Great Legal Wall of China. Its authorities lack investigation and enforcement jurisdiction in China and must rely on Chinese cooperation.<sup>154</sup> There is no extradition treaty between Hong Kong and China,<sup>155</sup> and Chinese courts are not obligated to enforce Hong Kong judgments.<sup>156</sup> Insiders can thus avoid enforcement by staying in China.<sup>157</sup>

### B. Other Potential External Constraints on Ma

While corporate law and securities law cannot easily be enforced against Ma and other Ma-controlled insiders, he may still be subject to other external constraints. For one thing, Ma may wish to preserve his reputation

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<sup>152</sup> See David C. Donald & Paul W. H. Cheuk, *Hong Kong's Public Enforcement Model of Investor Protection*, 4 *ASIAN J.L.S.* 349, 352 (2017).

<sup>153</sup> See *id.* at 372–73 (“[A]ll judicial actions taken against false and misleading securities prospectuses or to punish violations of rules against insider dealing or market manipulation have been commenced by a public body,” primarily the SFC.).

<sup>154</sup> See Andrei Filip et al., *Cross-Listing and Corporate Malfeasance: Evidence from P-Chip Firms*, 63 *J. CORP. FIN.* 101232, 1, 2 (2020).

<sup>155</sup> Although the Hong Kong legislature proposed the *Fugitive Offenders and Mutual Legal Assistance in Criminal Matters Legislation (Amendment) Bill 2019*, which would have established a mechanism for transfers of fugitives between Hong Kong and Mainland China, the bill was withdrawn after months of protests. See James Pomfret & Claire Jim, *Hong Kong Leader Pulls Extradition Bill, But Too Little Too Late, Say Some*, *REUTERS* (Sept. 3, 2019), <https://www.reuters.com/article/us-hongkong-protests/hong-kong-leader-pulls-extradition-bill-but-too-little-too-late-say-some-idUSKCN1VP05B>.

<sup>156</sup> In January 2019, China and Hong Kong entered into an arrangement regarding reciprocal recognition and enforcement of judgments in civil and commercial matters, although the arrangement is not yet effective. See Mun Yeow, *Hong Kong: Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters*, *MONDAQ: CLYDE & CO.* (Apr. 4, 2019), <http://www.mondaq.com/hongkong/x/794838/Contract+Law/Arrangement+and+Reciprocal+Recognition+and+Enforcement+of+Judgments+in+Civil+and+Commercial+Matters>. Even if the arrangement becomes effective, it excludes cases brought by the Securities and Futures Commission (SFC). See Gareth Thomas et al., *A Significant Step Towards Simpler Judicial Procedures and Reduced Re-litigation: Hong Kong and the Mainland Sign a Broader Arrangement to Recognize and Enforce Judgments in Civil and Commercial Matters*, *HERBERT SMITH FREEHILLS* (Jan. 25, 2019) <https://hsfnotes.com/asiadisputes/2019/01/25/a-significant-step-towards-simpler-judicial-procedures-and-reduced-re-litigation-hong-kong-and-the-mainland-sign-a-broader-arrangement-to-recognise-and-enforce-judgments-in-civil-and-commercial-matte/>. Exclusion of the SFC means that the treaty is likely to have little effect because, as we explained, public shareholders do not typically bring claims in Hong Kong. Even if shareholders bring such an action and get a judgment in Hong Kong, a Chinese court can refuse to enforce the treaty on grounds that enforcement would be “manifestly contrary to the basic legal principles of Mainland law or the social and policy interests of the Mainland.” See Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters by the Courts of the Mainland and of the Hong Kong Special Administrative Region, Section E, 22(g) (2019) [https://www.doj.gov.hk/en/mainland\\_and\\_macao/pdf/Doc6\\_481354e.pdf](https://www.doj.gov.hk/en/mainland_and_macao/pdf/Doc6_481354e.pdf).

<sup>157</sup> See Filip et al., *supra* note 154, at 2. Not surprisingly, China-based firms listed in Hong Kong engage in more misbehavior than Hong-Kong based firms listed in Hong Kong. See *id.*

(at least in the West),<sup>158</sup> or travel or conduct business in the United States or other countries that will enforce U.S. judgments or effect extradition. Some insiders might wish to protect assets outside of China that are not easily moveable and are vulnerable to seizure. In addition, Alibaba has legally-reachable non-Chinese nationals serving as directors or officers.<sup>159</sup> As long as they remain in office, Ma may refrain from wrongdoing to avoid jeopardizing them.

Another potential external constraint on Ma is the Chinese Communist Party (CCP). While so far China has turned a blind eye to massive expropriation of U.S. investors by Chinese residents,<sup>160</sup> it may wish to prevent expropriation in the future, especially at a highly visible firm.<sup>161</sup> In addition to its ability to destroy Alibaba by invalidating key business licenses and staging intrusive regulatory investigations,<sup>162</sup> the CCP could take various steps against Ma personally, including finding criminal charges that could be used to seize his assets and imprison him.<sup>163</sup> Of course, the CCP may not mind if

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<sup>158</sup> Massive expropriation of U.S. investors may not harm China-based insiders' reputations at home, as Chinese residents often do not pay attention to legal action in the United States against China-based insiders, even if such information is not blocked by Chinese censors. Cf. Yawen Li, *The Shell Game: Reverse Merger Companies and the Regulatory Efforts to Curb Reverse Merger Frauds*, 15 N.Y.U. J.L. & BUS. 153, 175 ("Because of the informational barrier created by distance, language and culture, such companies' poor performance in the U.S. stock market or even legal actions against them in the United States often do not reach domestic investors.").

<sup>159</sup> For example, Alibaba's President (Michael Evans) and several members of its board are non-Chinese nationals. See Alibaba Form 20-F (2020), *supra* note 19, at 170. Of course, these people could be replaced by Jack Ma and other Chinese nationals who ultimately control Alibaba. See Fried & Kamar, *supra* note 127.

<sup>160</sup> China has never prosecuted Chinese nationals for acts related to foreign-listed, China-based companies, even when there were clear violations of Chinese criminal law. See Gillis, *supra* note 109, at 9.

<sup>161</sup> See Tamar Groswald Ozery, *Illiberal Governance and the Rise of Corporations: An Oxymoron or China's Greatest Triumph?*, 42(4) U. PA. J. INT'L L. (forthcoming 2021) (explaining how the Chinese Communist Party's pervasive control over Chinese firms gives it sufficient carrots and sticks to induce most Chinese nationals to act according to its wishes, potentially providing protection to domestic and foreign investors in China-based foreign-listed firms). Cf. Tamar Groswald Ozery, *The Politicization of Corporate Governance—A Viable Alternative*, AM. J. COMP. L. (forthcoming 2021) (explaining how politicized corporate governance in China provides functional substitutes for traditional corporate governance mechanisms); Jake Laband, *Fact Sheet: Communist Party Groups in Foreign Companies in China*, CHINA BUS. REV. (May 31, 2018), <https://www.chinabusinessreview.com/fact-sheet-communist-party-groups-in-foreign-companies-in-china/> (discussing China's plans to put CCP organizations in Chinese private firms as well as in foreign-owned firms operating in China).

<sup>162</sup> See *supra* Part IV; see also Lingling Wei, *China Eyes Shrinking Jack Ma's Business Empire*, WALL ST. J. (Dec. 29, 2020), <https://www.wsj.com/articles/china-eyes-shrinking-jack-mas-business-empire-11609260092>.

<sup>163</sup> Even criticizing the CCP can land you in jail. Consider the case of Ren Zhiqiang, an influential businessman and the former head of a state-owned real estate group, who was ousted and prosecuted following his criticism of the President's handling of the pandemic. See Chun Han Wong, *Chinese Tycoon Kicked Out of Communist Party, Faces Prosecution After Criticizing Xi*, WALL ST. J. (July 23, 2020), [https://www.wsj.com/articles/chinese-tycoon-kicked-out-of-communist-party-faces-prosecution-after-criticizing-xi-11595526273?mod=article\\_inline](https://www.wsj.com/articles/chinese-tycoon-kicked-out-of-communist-party-faces-prosecution-after-criticizing-xi-11595526273?mod=article_inline). He was then sentenced to eighteen years imprisonment for corruption, abuse of power, and other alleged crimes. See Chun Han Wong, *China Sentences Xi Critic Ren Zhiqi-*

Ma expropriates foreign investors, in which case this constraint will not apply.

### CONCLUSION

Although Alibaba is one of the world's most valuable companies, its governance arrangements do not appear to be fully understood by investors, analysts, or academics. Analyzing these arrangements, we have shown that Jack Ma effectively controls Alibaba even though he owns less than 5% of its stock, and that this control will persist even if his equity stake drops.

Ma's control can persist because it is based entirely on his control of a completely different firm: privately-held Ant Group. Control of Ant Group enables Ma to dominate Ant Group executives who, along with Ma, make up a majority of the powerful Partnership Committee of the Alibaba Partnership. Control of the Committee, in turn, provides effective control of the Partnership, which appoints a majority of the directors on Alibaba's board. Domination of Ant Group executives also enables Ma to effectively control Alibaba's key VIE-held assets, giving him holdup power over Alibaba that is independent from his influence over the board.

Alibaba is a useful case study of how a single entrepreneur can control a firm not through equity, but rather through a mixture of employment, contractual, and commercial arrangements. We do not know how Ma will wield his power in the future or whether public investors will be harmed. But control matters, and it is important to understand who controls Alibaba.

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*ang to 18 Years in Prison*, WALL ST. J. (Sept. 22, 2020), <https://www.wsj.com/articles/china-sentences-xi-critic-ren-zhiqiang-to-18-years-in-prison-11600755598>. Few details were released about the evidence for such crimes. See Chris Buckley, *China's 'Big Cannon' Blasted Xi. Now He's Been Jailed for 18 years*, N.Y. TIMES (Sept. 22, 2020), <https://www.nytimes.com/2020/09/22/world/asia/china-ren-zhiqiang-tycoon.html>.

