### THE CCP ABSORBS CHINA'S PRIVATE SECTOR

### Capitalism with Party Characteristics

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#### **Executive Summary**

In 2020–2021, global markets were roiled by regulatory crackdowns on some of the best-known firms in the People's Republic of China (PRC): companies like Alibaba, Ant, Meituan, and Didi Chuxing. While foreign investors hoped for an end to the crackdowns, which had torched the value of US-listed PRC shares, instead, midway through 2021, Xi Jinping and the Chinese Communist Party (CCP) launched a massive structural undertaking to restore the party's political authority across the PRC's economic landscape.

Xi's crackdowns and market-value destruction at the beginning of this decade were not an aberration. Rather, they represented part of a "new stage" in the PRC's development defined by the assertion of party priorities across the domestic economy.

Xi Jinping and the CCP Politburo have announced to the world that the PRC has entered a "new stage" of development. The defining goals of this new stage are for the PRC to achieve "socialist modernization" and move from "standing up and getting rich to becoming strong." The prerequisites of this process are to downgrade the importance of GDP growth in economic planning in favor of "high-quality" and "people-centered" development, carry out painful structural reforms, and give a more prominent role to the party-state. Xi has said explicitly that the party must seek to avoid the fate of the Soviet Union—that development must lead to greater political unity, not disintegration. His strategy incorporates three key agendas:

• Offensive decoupling. Decreasing the PRC's dependency on the world while making the world increasingly dependent on the PRC.

- **Leverage.** Developing the PRC's self-sufficiency in high-tech sectors while amassing leverage over global resource flows, technology supply chains, and human talent.
- **Coercion.** Using the size of the PRC's economy—what Xi Jinping calls a "powerful gravitational field"—to exploit the economic vulnerabilities of others.

Crucially, this is a program not for eliminating private capital but harnessing it.

This report, based on the CCP's own documents, demonstrates how in Xi's vision of the PRC's economy, state objectives come first, technology is key, and national security underpins everything.

It argues that while the surface logic of each regulatory tightening varies, the common denominator is a reassertion of party-state authority over areas where the private sector has grown rapidly or is threatening Xi's vision of socialism. What this means is that Xi has launched a massive structural undertaking to restore the party's political authority across China's economic landscape, while preserving technology and capital flows necessary for Xi's ambition of making the PRC the world's dominant superpower. This story is being written according to strategic concepts that are mostly unfamiliar to observers who do not closely track the party's ongoing organizational transformation of capital markets and private enterprises, or the ideology and policies that underpin Xi's totalizing effort to politically restructure the economy.

Thus, understanding the PRC's economic and financial course now more than ever requires examining the ideological priorities of Beijing's top leadership, with Xi at the forefront.<sup>3</sup> Terms like "socialist modernization" and "red finance," for instance, may have little meaning outside the party-state, but they are organizing frameworks for official activity that flows downward from the party center through the capillaries of the PRC's Leninist political system.

This report unpacks these organizing frameworks and concludes that there is no meaningful way to analyze the PRC's private sector apart from CCP efforts to harness private capital for specific national goals as the party defines them—a list that includes defense, surveillance, propaganda, technological self-reliance, and supply chain leverage over the global economy. It builds its argument from the following evidence:

- Xi's plan to secure the party and its future is premised on a two-track approach to geostrategic "struggle" that aims to restore socialist coordination of the economy within the PRC while engaging in opportunistic cooperation and relentless, zero-sum struggle to obtain leverage and primacy over the West (section 1).
- The Party's mobilization and coordination of the private sector for competitive ends
  has relied on extralegal and otherwise opaque organizational mechanisms for forcing
  compliance that are largely invisible to foreign investors and corporate partners
  (section 2).

- The primary fulcrum of party control is its internal disciplinary apparatus—the Central Commission for Discipline Inspection (CCDI)—which is an intraparty organization for investigating and punishing violations of CCP norms, such as corruption and political disloyalty. The CCDI is complemented in this role by state security forces, including cyber authorities, and "softer" coordinating mechanisms such as local governments and the United Front system (section 3).
- Detailed case studies of corporations Alibaba and its strategic partner Ant Group illustrate that even the largest and most well-documented PRC companies have their own complex internal party organizations (section 4). These organizations are rarely disclosed in investor materials. Even companies whose ties to the party-state have elicited significant adverse press coverage, such as ByteDance, remain opaque from an organizational perspective (section 5). In both cases, the presence of party organizations corresponds with patterns of behavior in support of party-state interests that may cause serious hazards for investors and partners were they to be identified and addressed by foreign governments.

These findings paint a challenging picture for foreign investors, businesses, and governments. All will have to work cooperatively with party-controlled entities to maintain access to the PRC economy. This will entail growing risk as Washington and other capitals will react to CCP corporate control tactics and leverage through decoupling, sanctions, or other measures.

The methodology used in this report relies on a wide range of online and other publicly available sources. Many of these sources have been overlooked in public debates surrounding PRC companies and their internal structures of control; however, the accuracy of their information cannot otherwise be independently verified. A significant and growing literature on party-corporate relations is being produced in universities and other research institutions around the world. Such research has been valuable in documenting the ways in which distinctions between "state-owned" and "private" firms are increasingly blurred in the PRC economy as a result of Xi Jinping's imposition of new forms of CCP influence over private capital.<sup>4</sup> While debates concerning the nature and extent of party control over the corporate sector will continue, two important questions remain:

- The nature of CCP policy toward the private sector. Research on Xi's "state capitalist" system—a term that is disavowed by the party itself for failing to convey adherence to Xi's totalizing brand of socialism—views the goal of party control as more effective coordination of industrial policy. This industrial policy paradigm does not capture the nature of party control demonstrated in this report, which is to use private companies as platforms for pursuit of any of the party's myriad geostrategic policies, including propaganda, surveillance, espionage, national defense, and state-of-emergency resource mobilization.
- Organizational patterns of party governance within private firms. The sprawling and complex nature of transnational corporate structures makes party access and governance

within private firms opaque. This opacity, in turn, has given rise to theories about private conglomerates that type them as "mafia-like" vehicles for personal enrichment. The case studies in this report illustrate how Xi and the party have responded to manipulation of the private system by systematically neutralizing and removing personalistic corporate governance structures and replacing them with more controllable alternatives. As a result of these widening crackdowns across the private sector, financiers and entrepreneurs have been placed under new regulatory and extrajudicial burdens that reinforce the steady expansion of party organizations within the private sector.

• What lies ahead is uncertain. In the United States, the Biden administration has stated that drafting of outbound investment curbs targeting specific sectors is already underway. Some venture capital firms have already responded by splitting US and PRC operations or show signs of contemplating doing so in the future. Investment into the PRC has dropped sharply. At minimum, VCs, fund managers, corporations, and other investors will need to take into account that Xi's "rectified" and party-steered private sector means that firms are no longer private in any meaningful sense of the word. They are fused with the party-state and therefore are less innovative, less nimble, harder to price—and more suspect in foreign capitals. Markets are now in the position of needing to place new wagers on what it means that party leaders, as one critic within China put it, now want to "run the business." Such questions apply across the totality of the PRC economy. Among the troubling consequences for foreign investors is that the more businesses do to align with Beijing's priorities and avoid Xi's ire, the more they are likely to land in the crosshairs of Washington and other democratic capitals.

## 1. PARTY GOVERNANCE UNBOUND: FROM INTERNAL POLITICS TO ECONOMIC CONTROL

The regulatory crackdowns that have wracked many of the PRC's highest-flying firms and wrong-footed global investors are the logical extension of a political program that Xi Jinping has pursued since the beginning of his tenure.

Since Xi Jinping assumed the position of general secretary of the CCP at the 18th Party Congress in 2012, he has presided over a sustained tightening of the PRC's legal, economic, and security environment. Close examination of key CCP documents show that Xi foreshadowed this tightening early in his term with a series of speeches and statements on party ideology in international relations, business, law, and technology. However, the CCP's courtship of foreign investors obscured these authoritative pronouncements abroad.

#### 1.1 SECURING SOCIALISM, TRANSFORMING CAPITALISM

Under Xi's leadership, the party's endeavors to ensure "security" in the ideological and political security spheres have grown more explicit, emphatic, and expansive. The clearest publicly available exposition of his approach to ideological and geostrategic competition is laid out in

the text of a speech he delivered to the Central Committee on January 5, 2013, shortly after coming to power.

#### He told the Central Committee:

The eventual demise of capitalism and the ultimate victory of socialism will require a long historical process to reach completion. In the meantime, we must have a deep appreciation for capitalism's ability to self-correct, and a full, objective assessment of the real long-term advantages that the developed Western nations have in the economic, technological, and military spheres. Then we must diligently prepare for a long period of cooperation and struggle between these two social systems in each of these domains.

[S]ocialism must learn from the boons that capitalism has brought to civilization. We must face the reality that people will use the strengths of developed Western countries to denounce our country's socialist development. Here we must have a great strategic determination, resolutely rejecting all false arguments that we should abandon socialism. We must consciously correct the various ideas that do not accord with our current stage. Most importantly, we must concentrate our efforts on bettering our own affairs, continually broadening our comprehensive national power, improving the lives of our people, building a socialism that is superior to capitalism, and laying the foundation for a future where we will win the initiative and have the dominant position.<sup>12</sup>

In this speech—effectively his inauguration speech—Xi described a two-track strategy involving opportunistic cooperation and relentless struggle to obtain leverage and primacy over the West. Xi's strategic watershed also contained within it a second, more immediate line of thinking focusing specifically on the economy. Here, he called for the rolling back of capitalism within the PRC's economic planning and economy, warning that socialism's fragile nature ("socialism in our country is still in its infancy") meant that reform would require vigilant "struggle" against dangerous economic hybridity:

In the past, it was not possible to carry out full-scale Sovietization, and now it is not possible to carry out full-scale Westernization or other things. After the end of the Cold War, many developing countries were forced to adopt the Western model. As a result, partisan disputes, social turmoil, and people's displacement have occurred, and it has been difficult to stabilize until now. . . . The so-called "Chinese model" is the path of socialism with Chinese characteristics created by the Chinese people in their own struggle and practice. We firmly believe that with the continuous development of socialism with Chinese characteristics, our system will become more and more mature, the superiority of our socialist system will be further revealed, and our road will become wider and wider.

Xi's prescription for how to protect and develop socialism and prevent the PRC from the pitfalls of "Westernization" was simple and direct: to restore the party to its proper guiding role at every level of society. In the same speech, he diagnosed the causes of the collapse of the Soviet Union, enumerating them as negation of the party's ideology, dispersion of the party's organizational force, and loss of the party's control over the army.

The key meaning of this historical "lesson," Xi told the rest of the party, was that socialism would need to be developed further.<sup>13</sup> The PRC, in other words, would need to become more socialist in ways that would make a Soviet-style collapse impossible. This is why, in the years that followed this secret speech, Xi has championed "socialist values" and party building throughout the PRC's economy—including in its private sector.

Xi's program unfolded gradually. He spent the first five years of his tenure focused on internal politics—on securing and deepening his personal control over the party, and the party's control over society. He focused first on the military and internal security services, purging political rivals, appointing loyal replacements, and imposing tighter organizational supervision and discipline. Then he turned to the propaganda system and United Front—the interface between party and nonparty, the purpose of which is to shape the behavior of nonparty groups in line with party objectives—ensuring that the party's voice remained dominant and "new social classes" taking shape in the technology and services sectors were more directly absorbed into party structures. (For more about the United Front, see section 3.2.)

During this period, Xi's economic message emphasized that state-owned enterprises should be "the most reliable force for the party and country to rely on" and "an important force for victory in [the party's] struggle," while "party building" work must deepen inside private enterprise, and representatives of the United Front must play a more active role in the economy.<sup>15</sup>

The quest for absolute leadership extended not only to Xi's words but also to his thinking, with Xi Jinping Thought now officially written into both the CCP Constitution and Constitution of the People's Republic of China.<sup>16</sup>

In his 2017 Work Report to the 19th Party Congress, Xi declared that his political consolidation stage was approaching completion, and that socialism in the PRC was entering a "New Era" of political and ideological strength in which "party, government, army, society, and education—east and west, south and north, the party leads all."<sup>17</sup>

At that point, Xi turned his focus increasingly to the international stage, especially via economic coercion and Wolf Warrior diplomacy. At the 19th Party Congress, Xi announced the arrival of a "profound shift" in the distribution of world power, with "China moving closer to center stage and making greater contributions to mankind." A great struggle must be carried out," he said, in which the CCP must take on "various risks and tests at home and abroad" and "resolutely oppose all words and deeds weakening, distorting, and denying the party's leadership and our socialist system."

The shifts in the PRC's patterns of trade and foreign relations resulting from this assessment have since become the most visibly aggressive, volatile aspects of Xi's tenure. But they are

easier to understand when viewed as an ongoing test and demonstration of party strength and resiliency vis-à-vis Western capitals.

#### 1.2 XI'S CRACKDOWN ON PRIVATE CAPITAL AND FIRMS

As the PRC mobilized out from its early COVID-19 shutdown, Xi began to lay the regulatory foundations for the current crackdown on domestic Big Tech and capital markets. His April 2020 speech on the PRC's medium- and long-term development strategy made "offensive leverage" over supply chains the defining principle of party geoeconomics. The speech set up a contrast with the private tech economy and its associated risks by emphasizing that the "real economy" and state-owned enterprises must remain the "foundation" of the national economy. Then, in rapid succession:

- Alibaba's antitrust probe reportedly began three months later, in July 2020. In September, the State Council established trial measures for "diversified financial institutions" to re-register as financial holding companies.<sup>21</sup>
- Then came multiple warnings from the party center about preventing financial risk and taking a "zero tolerance" approach to corporate rule-breaking, followed by Jack Ma's fateful October 2020 speech publicly criticizing regulators and Xi's policies, and the early November suspension of Ant's IPO that followed.<sup>22</sup>
- In the aftermath, antitrust regulators and the People's Bank of China warned that "large technology companies" posed financial and competitive risks, and the Politburo declared in December 2020 that the party would "strengthen antimonopoly and prevent the disorderly expansion of capital." Conditions for Ant Group's "rectification" were announced later that month.

A critical inflection point came on July 6, 2021, when the General Office of the CCP Central Committee issued its "Opinion on Strictly Cracking Down on Illegal Securities Activities in Accordance with the Law." Pledging to combine regulation with law enforcement, the Opinion represented an extension of Xi's long-standing anticorruption and political discipline campaigns to the very heart of finance. It read:

Under the deepening background of profound changes in the economic and financial environment, and the constant deepening of reform and opening of capital markets, illegal behavior in capital markets is still relatively prominent, the investigation and handling of cases has become more difficult, and related law enforcement and judicial work faces a new situation and new challenges.<sup>24</sup>

The key message was that Beijing had opened a crackdown—personally led by Xi, guided by vice president and former anticorruption chief Wang Qishan, and enforced by political-legal discipline enforcer Chen Yixin—against independent concentrations of money and power

outside Xi's immediate circle.<sup>25</sup> The crackdown's "coordinating mechanism" included the Supreme People's Procuratorate, the Ministry of Public Security, and the China Securities Regulatory Commission, all subordinate to party leadership. Its scope is immense. According to the Opinion:

- The crackdown will "increase the intensity of investigation and punishment of major and important cases."
- By 2022, the campaign will have "significantly restored order" to capital markets.
- By 2025, the law-enforcement system encircling capital markets will be "more complete."

The capital market crackdown has included high-profile targets who serve as focal points for national campaigns to restore party priorities across the fastest-growing areas of the economy.

At the time of its release, the 2021 Opinion was covered in media mainly for its clauses addressing overseas listings, which signaled changes in how foreign investors were able to access protected sectors of the PRC's economy through the variable-interest entity (VIE) business structure. Despite the media excitement, investors have always known that VIEs are legal fictions designed to allow Chinese companies to list overseas despite Chinese laws against foreign ownership of certain types of companies (especially tech and education). The party allows the use of these tenuous legal structures to import technology and capital if and when it suits the party's political and policy priorities. The relevant questions, therefore, involve deciphering those priorities. The party can be expected to continue allowing VIE use for any company that the party wants to allow to remain listed overseas. If and when Beijing wants to block a company from listing or remaining listed overseas, the VIE can be a convenient tool for bringing that about. The focus on VIEs therefore missed the point—it applied a lawyer's lens to what is in essence an extralegal problem.

But far more was at stake. In the party's language, imposing "order" on capital markets means taming the private sector so that Xi's version of the party remains dominant, dependency on foreign markets and investment is reduced, and more resources are steered toward strategically important technology, while keeping living standards stable. The inner logic is of systematically subordinating the private sector to an economic vision in which the party functions as the primary allocator of capital. This vision of "red finance" has been touted by the party committee of the People's Bank of China (PBOC), the country's central bank.<sup>27</sup>

A further signal of Chinese leadership intent was conveyed by *Qiushi*, the party's most important ideology and policy journal, in a lengthy excerpt from Xi's December 2021 speech at the Central Economic Work Conference titled: "Correctly Understanding and Handling Major Issues of Theory and Practice in Our Country's Development." The speech unambiguously signaled that Xi's campaign to tame the market economy was far from over. The thrust of its

message was that economic growth is important, but not as important as restraining and guiding capital and large institutions, and it included the following admonitions:

- **Common Prosperity.** "The inappropriate concentration of some wealth has brought risks and challenges to the healthy operation of the economy and society."
- Laws of capital. "Capital is all about chasing profits. . . . In recent years, due to inadequate awareness and omissions of supervision, capital's disorderly expansion appeared in some 'domains' of our country and was wantonly manipulative [in] seeking enormous profits. This therefore requires regulating capital's behavior, seeking advantages while avoiding disadvantages [through regulation], and not letting the 'predators of capital' run wild."
- Financial risk. "New risks continue to appear, 'black swan' and 'grey rhino' events are continuous . . . [for] several reasons. 29 One is the result of long-term accumulation. . . . Second is deficiencies in regulatory capacity and the [regulatory] system, serious failures of oversight concerning the issue of financial institution governance, unsuitable regulatory capacity and ability, and laxity in the management of local debt. . . . Third, the barbaric behavior of borrowers. Some large enterprises are blindly impulsive, engaging in irrational diversified expansion [and] excessively rely on financial leverage. Industrial capital is excessively entering the financial sector. Some shareholders and actual controllers operate and manage financial enterprises illegally and irregularly, and there is insider control, manipulation by major shareholders, financial fraud, and massive misappropriation of funds. Fourth is government-business collusion and corrupt practices. . . . Fifth is change in the economic cycle . . . [causing] the probability of local risk triggering systemic risk to increase."

Indeed, less than one year after Xi and the party announced their crackdown on private capital, a May 2022 state summit with Big Tech leaders demonstrated how deeply Beijing has integrated the country's most prominent private companies into national programs bearing Xi's stamp of approval. Though billed as a summit, the purpose of the meeting was to transmit policy, not pursue open dialogue. Wang Yang (then fourth-ranking Politburo member) and Liu He (Xi's former financial advisor) conveyed instructions from Xi Jinping concerning the development and governance of the digital economy.

Those assembled for this gathering were a combination of officials, policy advisors, and other Chinese People's Political Consultative Conference (CPPCC) representatives. (The CPPCC is the United Front's primary forum.) The Xinhua readout of this meeting did not mention that any leaders of the PRC's digital platform giants were present, but a Reuters scan of available CCTV footage shows that Baidu's Robin Li and Qihoo 360's Zhou Hongyi, both CPPCC members, were in attendance.<sup>30</sup>

According to the readout, the assembled officials were directed to study and understand Xi's important instructions, support national security, expand the PRC's digital economy, and better integrate digital companies into party-led economic policy.<sup>31</sup> Liu reportedly told the

group to strengthen the PRC, "fight the battle for key core technologies," promote investment in R&D and national projects, "properly handle the relationship between government and the market," and manage private sector data more securely.

Further signals indicate that these steps will not be reversed. On January 13, 2023, Ma Jianyang, the central bank's chief of financial markets, stated that rectification of Big Tech has ended "as a phase in a longer regulatory process"—because these firms have entered a new phase in which they will be permanently supervised by the party-state.<sup>32</sup>

#### 1.3 POLITICS DOMINATES ECONOMICS

It is increasingly clear that the era when investors and executives were led by Deng Xiaoping's supposed maxim "To get rich is glorious" is now over. In its place, Xi is superimposing the image of the "patriotic entrepreneur," which harks back to the Mao era. In leaving Deng behind, Xi is returning to that older model of redistribution, assaults on the rich, and a crusade to make the PRC strong through the mechanisms of Leninist control. In his words: "Socialism with Chinese characteristics is socialism, not any other 'ism'."

What Xi means by "redistribution," however, is very different from what Mao meant. Xi's Common Prosperity agenda (see section 2.3) is yet another bar in the cage being built around the private sector. Essentially, entrepreneurs are free to invest in profitable business lines, provided they invest where Xi points. This can be about social programs but also electric vehicles, microchips, blockchain, dual-use technologies, and any of the other sectors of the "real economy" prioritized by Xi as focus areas. The essential meaning of Common Prosperity is the politicization of the private economy. When it is convenient for Common Prosperity to mean private funding for social programs, then that's what it means. When it is convenient to mean support for Xi's science and technology projects, then that's what it means.

This is why, just after launching his capital market crackdown in late 2021, Xi gave an "important speech" mentioning "regulation" of capital twenty-six times. The essence of his remarks was highlighted in the first paragraph: "Regulating and guiding the development of capital under the conditions of a socialist market economy is not only a major economic issue, but also a political issue."<sup>33</sup>

These were Xi's most important passages:

- Sustaining Common Prosperity: "[We must] correctly handle the distribution of capital and interests. Adhere to the principle that development is for the people, depends on the people, and that the fruits of development are shared by the people. [We should] unswervingly follow the path of common prosperity for all people."
- Combating corporate power with antimonopoly: "[We must] strengthen supervision and law enforcement of antimonopoly and antiunfair competition, and crack down in

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accordance with the law on monopoly and unfair competition on acts such as abuse of market dominance."

- Guiding investment using party "traffic lights": "[We must] regulate and guide the development of capital. [We should] set up 'traffic lights,' improve the legal system for capital development, and form a system that has a complete structure with a clear logic and comprehensive rules."
- Separating profit from power, especially in tech: "[We must] strengthen anticorruption in the capital field, maintain high pressure on anticorruption, resolutely crack down on capital's profit-seeking conduct that relies on power, and focus on investigating and dealing with corrupt practices behind the disorderly expansion of capital and platform monopoly."
- Controlling capital and risk using party organizations: "Regulating and guiding the healthy development of capital is an important part of the party's leadership in economic work. Party committees (party groups) at all levels should unify their thoughts and actions into the decision making and deployment of the Party Central Committee, earnestly assume the main responsibility, improve their capital management skills, strengthen public communication of policies and guidance on expectations, and resolutely prevent the occurrence of systemic risks."

Lest there be ambiguity to Xi's message, the *People's Daily* published an explanatory commentary directly below the speech readout to distill its contents further.

The explanatory commentary told cadres:

It must be recognized that capital has a profit-seeking nature.... The more the market economy and capital develop, the more powerful laws and supervision are needed to maintain the effective operation of the market mechanism.<sup>34</sup>

With this Politburo study session and the *People's Daily* treatment of it, Xi is moving to ensure that there is no daylight between him, his Politburo colleagues, and the party's rank and file. Cadres at all levels have their instructions: "Unswervingly" uphold Common Prosperity, "traffic lights" for capital, antimonopoly enforcement, strict law enforcement, and party control over capital markets—all in the service of "educating and guiding the main body of capital to practice core socialist values."

### 1.4 A CASE STUDY IN XI'S "COMMON PROSPERITY": TENCENT'S POLITICAL INSURANCE RISK BLOWOUT

How much will shareholders have to pay to support Xi's Common Prosperity program? It's not going to be cheap. Just look at Tencent, where Pony Ma has recently paid what may rank as history's greatest political risk insurance premium.

Back in April 2021, Tencent announced an "investment" into "sustainable social value innovation" worth 50 billion renminbi, or some \$7.7 billion. The investment covers basic scientific research, education, rural area rejuvenation, carbon-neutral programs, food, environment, water, emergency response, technology for retirees, and digital technology for public services. All of these goals are tightly aligned with Beijing's national strategy and the personal preferences of Xi. 36

On the same day, Pony Ma also announced a major corporate restructuring of the company, merging Tencent's philanthropy platform and corporate social responsibility division into a new major business division under the corporate development group, which is one of six major business groups of Tencent. Organizationally, this means that politically correct philanthropy is now embedded inside a key business unit, on par with profit centers like WeChat Group, On-line Gaming, and Fintech.

Tencent's RMB 50 billion in philanthropy came on top of RMB 1.5 billion that the company put toward China's pandemic response and assorted millions for natural disasters such as flooding in Henan province.<sup>37</sup> And that doesn't account for the company's enormous investment in censorship and propaganda aimed at keeping its dominant social-media platform, WeChat, and its flagship gaming business on the right side of the political line.

Elsewhere in Tencent's entertainment portfolio, the company released what has become an ultrapopular television series, *You Are My Glory*, which doubles as an advertisement for the company's Honor of Kings online game.<sup>38</sup> The series features one of China's most famous actresses of Uyghur heritage, known as Dilireba. The plot involves the famous Uyghur actress falling in love with an underpaid Han Chinese space engineer who rejects a career in investment banking to stay true to his nation-building dreams.

And yet despite it all—the RMB 50 billion insurance premium, the patriotic TV series, the assorted emergency relief efforts, the social-media censorship—Tencent was still in the crosshairs.

On August 3, 2021, Xinhua subsidiary Economic Information Daily published a fiercely critical feature story on the negative effects of online gaming. The labeling of online games as "spiritual opium"—an unmistakably Marxist reference—led the share price of Tencent and other gaming companies to drop 10 percent.<sup>39</sup>

Tencent responded immediately by placing a cap on the amount of time teenagers can spend online. But Pony Ma believed more was necessary. Just one day after Xi's speech on Common Prosperity, Tencent announced it would pour another RMB 50 billion—another \$7.7 billion—into Xi's pet projects, namely rural rejuvenation, jobs for the disadvantaged, improving basic healthcare, and more equitable distribution of educational opportunities.<sup>40</sup>

Could it have been a coincidence? Not according to Tencent. The company's statement, made via its WeChat account, could not have been more explicit:

The new Tencent strategy is an enthusiastic response to the national strategy. The victory over poverty has laid the solid foundation for promoting common prosperity. The tenth meeting of the Central Commission for Finance and Economic Affairs states clearly the goal of achieving common prosperity through different stages; some people are allowed to get rich first and people who got rich first should help these who will get rich later.<sup>41</sup>

So over four months, Tencent pledged more money to party-backed philanthropy (RMB 100 billion, or \$15.4 billion) than it earned in profit across the whole first half of 2021 (some RMB 90.3 billion, or \$13.9 billion).<sup>42</sup>

The cost of sustaining profitable business lines—and staying out of jail—is rising fast. Even for Pony Ma, a famously politically sensitive operator, the price has doubled. Will it be enough?

The upshot: Politics will continue to trump economics in Xi's China, regardless of the costs. The private sector, in turn, will be given no alternative to the option of supporting the party's program or be targeted using tools of leverage and internal organizational co-optation.

# 2. XI'S BLUEPRINT FOR OPERATIONALIZING PARTY LEADERSHIP OF THE PRIVATE SECTOR

The previous section of this report elucidated the development of Xi's quest to mobilize private enterprise for his vision of the party's priorities. Increasingly, the party system has been exerting its power to press and incentivize the private sector to directly support political and policy objectives, such as centralized economic planning. This is clearly stated by top leaders and through authoritative party documents.<sup>43</sup>

Xi has taken the message of party control directly to China's private companies. He has explicitly tied their future success to their demonstrations of "patriotism"—a term the party uses interchangeably with "party loyalty." In a July 2020 speech to entrepreneurs, Xi was quoted as saying:

If entrepreneurs want to lead their enterprises to overcome current difficulties and move toward a more brilliant future, they must continuously improve themselves in patriotism . . . I hope everyone will improve their patriotism. Enterprise knows no borders, and entrepreneurs have a motherland. Excellent entrepreneurs must have a lofty sense of mission and a strong sense of responsibility for the country and the Chinese nation.<sup>44</sup>

The following subsections detail Beijing's leverage-based operationalization of Xi's patriotic program.

#### 2.1 FULCRUM ONE: INTEGRATING THE LAW WITH THE PARTY'S PRIORITIES

The party has multiple mechanisms for ensuring its leadership, including the formal legal system and a collection of nontransparent, extrajudicial instruments of power. Nevertheless, its emphasis on using laws and the legal system must not be understood as a commitment to independent regulatory institutions or Western conceptions of the rule of law.<sup>45</sup>

In contrast to the Western system of separation of powers, many decisions relating to the justice, police, and secret intelligence systems are made within a single CCP institution called the Central Political and Legal Affairs Commission.<sup>46</sup> Analysis of authoritative texts shows that the politicization of legal and regulatory institutions is intensifying and the powers of the Central Political and Legal Affairs Commission are embodied in the person of General Secretary Xi Jinping.<sup>47</sup>

In February 2018, for example, the president of the Supreme People's Court, Zhou Qiang, stated that the judiciary's overriding priority is to defend "the party's centralized and unified leadership, with Xi Jinping as the core leader." In January 2019, the Central Political and Legal Affairs Commission—which directs the courts, prosecutors, and police—issued a Work Directive that makes clear that all laws, regulations, and policies will be policed and adjudicated in accordance with the party's political priorities of the time. According to the directive, such work

- has the primary purpose of "upholding the absolute leadership of the party" (Article 6(1));
- is an important method by which the party "leads political units to lawfully perform dictatorship" (Article 6(3));
- requires that officials "strictly distinguish and correctly handle conflicts between ourselves and the enemy, and conflict among the people" (Article 6(6)); and
- requires that important matters are reported directly to the general secretary.

This directive empowers the full breadth of the PRC state security system to police all institutions—state and private—and individuals to ensure adherence to political instructions from the party center.

A case in point is the party's push to involve all sectors of the economy in defense development (see also section 2.4). This systemic push has been evident since the 2016 "Opinion on the Integrated Development of the Economy and National Defense" issued by the Party Central Committee, State Council, and Central Military Commission.<sup>49</sup> This directive set a policy framework for entities across the economy to do the following:

• Support military-civil fusion and create a foundation for "national defense construction"

- · Become more systemically integrated with national defense planning
- Coordinate with the military in development of advanced technologies, industrial products, and infrastructure
- Support formation of a national-defense-focused "military-civil science and technology collaboration innovation system"

The directive highlighted that the main "principle" of these measures would be to "strengthen state control and utilize the market, including guiding capital, technologies, and different forces [in society] to better serve the development of national defense."

In February 2018, the phrase "integrated national strategic system and capacity" was written into the "Decision of the CCP Central Committee on Deepening the Reform of Party and State Institutions." The phrase again appeared, and was ratified, at the Fifth Plenum of the 19th CCP Central Committee in October 2020. The key document to emerge from this event, the "Outline for the 14th Five-Year Plan for Economic and Social Development and Long-Range Objectives to 2035," sets the planning framework for both state and private corporate entities.

Although evidence of how such policies are implemented remains fragmentary, there is a strong pattern of cooperation between PRC technology companies and China's state-security and defense forces (see case studies of Alibaba and ByteDance in sections 4 and 5). The connection between guiding policies and firm behavior gives credence to the argument that party organizations within these companies adhere to their commitments to uphold CCP political priorities, as set out across key party-state documents that legalize the party's presence and role across the private sector:

- Party members in Chinese private companies are required to establish party
  organizations in all organizations with three or more full party members, according to
  the CCP Constitution.<sup>51</sup> The Constitution directs that party organizations "implement
  the party's principles and policies" and "exercise leadership" where they are present,
  including in all nonpublic-sector entities. Separately, the role of party leaders includes
  "guidance" of the nonpublic economy.
- The Party Constitution should be read in conjunction with Article 19 of the PRC Company Law, which requires: "In a company, an organization of the Communist Party of China shall be established to carry out the activities of the party in accordance with the charter of the Communist Party of China. The company shall provide the necessary conditions for the activities of the party organization."<sup>52</sup>
- In addition, companies are forbidden from "carrying out acts that endanger the national or social public interest" (Article 534).

Large, systemically important companies are therefore likely to have many party members. There is no public information to suggest that private companies are exempt from legal and extralegal obligations to develop and strengthen party organizations.

#### 2.2 FULCRUM TWO: LEVERAGING CYBERSECURITY FOR CONTROL

Consistent with that, the PRC legal system is imposing greater political control and securitization on economic entities.<sup>53</sup> Under the PRC's Cybersecurity Law, for example, all companies and individuals must comply with standards that make networks, data, and communication transparent to the Ministry of Public Security, the PRC's police.<sup>54</sup> Other research shows that the CCP is imposing requirements for "party building" provisions directly into corporate charters, including in some private companies.<sup>55</sup> The practical consequences are that private entities are required to comply with constant supervision and control exercised by party organs like the Political-Legal Commission and Central Commission on Cybersecurity and Informationization (publicly known as the Cyberspace Administration of China, or CAC).

The Cybersecurity Review Measures, released in 2022, established the Cybersecurity Review Office, under the CAC, and outlined the cybersecurity review process. The review process focuses on "national security" risks to "critical information infrastructure" as defined by the PRC Cybersecurity Law. As compliance burdens increase, investors and multinationals alike must now manage increased risk that comes with party data control across the entire private economy. The complete seconomy.

According to the Cybersecurity Law, critical information-infrastructure domains include but are not limited to public communication and information services, energy, transportation, water conservancy, finance, public services, e-government, "and other critical information infrastructure . . . whose destruction, loss of function, or data leakage could seriously harm national security, the 'nation's economy and people's livelihood,' and the public interest."58

According to Article 9 of the Cybersecurity Review Measures:

The cybersecurity review process focuses on assessing the potential national security risks brought about by procurement of network products and services, mainly considering the following factors:

- The risk that the use of products and services could bring about the illegal control of, interference with, or destruction of critical information infrastructure, as well as the theft, leak, or damage of important data;
- 2. The harm to critical information infrastructure business continuity from product and service supply disruptions;
- The security, openness, transparency, and diversity of sources of products and services; the reliability of supply channels, as well as the risk of supply disruptions due to political, diplomatic, and trade factors;

- 4. Product and service providers' compliance with national laws, regulations, and department rules;
- 5. Other factors that could harm critical information infrastructure security and national security.<sup>59</sup>

The measures state that the reviews will normally conclude within forty-five days and may require the company and its suppliers to make changes. Penalties for noncompliance are set out in the Cybersecurity Law and may include suspending use of certain systems, as well as fines.

Beijing's increasingly bold use of new regulators and regulatory regimes to reshape the PRC's capital markets and the underlying economic landscape has forced investors to take notice. For instance, in early July 2021, Beijing cited new data policies to investigate and drastically constrain the ability of ride-sharing company Didi Chuxing to operate just days after it listed on the New York Stock Exchange, triggering a post-IPO implosion at the firm. Suddenly, the PRC's newly built matrix of new data laws, policies, and regulators snapped clearly into focus.

The moves on Didi and the other tech players foreshadowed implementation of the Data Security Law passed by the National People's Congress on June 10, 2021, which took effect on September 1.

Notably, the Data Security Law is designed to have extraterritorial reach: It includes provisions for "investigation" of data-processing activities outside the PRC that may "harm the national security, public interest, or legal rights and interests of citizens and organizations" of the PRC.<sup>61</sup> The Data Security Law will impact business operations of PRC companies—and foreign companies—both inside and outside the PRC.

In addition, new revisions to the Counterespionage Law mean that this information control and absorption effort has been expanded to include foreign-facing firms within the PRC, including foreign-headquartered multinational corporations. Under the revised law, normal business practices—such as gathering intelligence on local markets, potential business partners, and competitors—could easily fall within the scope of espionage.

Under the new law, more forms of information and individual behavior are made hazardous:

• While the old law sought to protect "state secrets and intelligence" (Article 38.3), the new law adds an all-encompassing new category: "other documents, data, materials, or items related to national security or interests" (Article 4.3), which theoretically could mean anything.

- The old law focused on unmasking spies (Article 38.2). The new law targets not just spies but anyone "seeking to align with an espionage organization and its agents" (Article 4.2).
- The new law expands the list of potential perpetrators from "espionage organizations and its agents" to "agencies, organs, individuals, or other collaborators domestically or outside the PRC borders" (Article 4.4), again theoretically anyone working for anybody.

In short, while the old law had a somewhat circumscribed aim of protecting state secrets, the new law aims at prosecuting anyone deemed to be harming China's national interests.

The new law also asserts more power over communications networks and devices:

- Unlike the old law, which stated broadly that businesses and governmental agencies should cooperate with counterespionage investigations, the new law specifies that security forces have the right to demand assistance, in particular from telecommunication companies and internet service providers (Article 36).
- The law also increases the focus on cybersecurity with specific provisions that include a
  ban on discussing China's network vulnerabilities (Article 4.4). And it specifically grants
  security services the power to search phones and computers of anyone suspected of
  carrying out espionage, however expansively defined.

The new law signals more potential exit bans, and whistleblowers:

- The new law also includes a new subsection (Article 33) approving the use of exit bans, which have become an increasingly popular tool of Beijing's security forces, blocking both foreigners and Chinese alike from leaving China. (Since 2018, according to a new report by NGO Safeguard Defenders, no fewer than five new or amended laws provide for the use of exit bans, for a new total of at least fifteen laws.<sup>62</sup>)
- And finally, the amendments broaden the call for Chinese people to actively support
  counterespionage investigations, stipulating in Article 8: "All citizens and organizations
  shall support and assist counterespionage efforts in accordance with law."

Revisions to the law were preceded by issuance of new national security-related rules and legislation designed to restrict foreign access to what Beijing now considers sensitive data:

 March 31: The China Securities Regulatory Commission (CSRC) issues rules that mandate that "national security" be considered as a factor in the approval process on overseas IPOs.<sup>63</sup>

- **April 26:** Announcement of a significantly amended Counterespionage Law, which broadens the definition of espionage to include anything that involves national interests, to take effect on July 1. (See section 3.)
- May 4: The Ministry of Finance, the State-owned Assets Supervision and Administration
  Commission (SASAC), and the CSRC order state-owned enterprises and listed companies,
  when dealing with accounting firms, to "earnestly assume the main responsibility and
  confidentiality responsibility for information security."<sup>64</sup>

The enforcement blitz has been accompanied by the administrative removal of government information online, for example, blocking overseas IP access to official websites by multiple local governments, and censoring or removing online access to decisions from court cases (information important for assessing counterparty risk in China).

Xi's spring offensive against parts of the business community is not a signal that he is seeking accelerated decoupling from the West—at least not yet. Rather, Xi wants due diligence firms and consultancies cowed, accounting firms more closely scrutinized, and Western firms generally to change their behavior to conform with party expectations. The purpose of this campaign is not simply to deny information to foreign companies. It is to change the behavior of foreign firms and the Chinese employees and associates who deal with them. In short, political performance for Western and Western-facing firms and investors is becoming more important than ever. Firms will not only have to support Beijing's strategic development goals but accept more of Beijing's jurisdiction, both internally and externally.

#### 2.3 FULCRUM THREE: POLITICAL COMPLIANCE AND COMMON PROSPERITY

The party did not merely shake down billionaires and large firms to ensure political compliance. In Xi's view, now is the time for addressing inequality, driving a socialist morality campaign, and strengthening the state as a means of shoring up the party's political longevity as economic conditions become more testing.<sup>65</sup>

Media and markets have rightly picked up on Xi's new Common Prosperity drive and his call to "rationally regulate high incomes" while "encouraging high-income groups to give back more to society." What they missed, however, was the kicker.<sup>66</sup>

According to the readout from an August 17, 2021, meeting of the Central Commission of Finance and Economics, the party will henceforth "clean up and standardize unreasonable income, rectify income distribution order, and resolutely outlaw illegal income." This language does not fit neatly within Western frameworks of social safety nets and income redistribution. For students of Mao-era history, however, the significance of words like *clean up*, *rectify*, and *outlaw* are unmistakable.

This language foreshadows something far more muscular than mere adjustments to minimum wages, social security, and income-tax scales. According to Xinhua, the Xi-chaired group

called for strengthening "leadership of socialist core values." It called for expanding the role of the party-state in wealth redistribution, including on moral and philanthropic grounds. It used the term *tertiary redistribution*, which the party leadership has previously defined as "philanthropy and other social public interest endeavors." It also gave specific orders for the creation of a "foundational institutional arrangement" through which redistribution would be centrally coordinated.

All high-net-worth individuals and sizeable firms are on notice. Their value in the eyes of the party is defined by their ability to address what Xi called, in his July 1, 2021, speech at the Party's Centenary, "the problem of unbalanced and inadequate development and the people's urgent difficulties and worries." In practical terms, business leaders and corporations have to dig deep—very deep—to fund party social policies, lest their wealth be donated for them. This is the beginning of a tax raid, a regulatory crackdown, and a political campaign against actors and activities deemed outside Xi's norms of socialism with Chinese characteristics. 69

The current phase of Xi's "rectification" of private capitalism is intensifying a decade-long campaign to break key economic and technological dependencies on the US-led democratic world in anticipation of a new era of ideological and geostrategic "struggle."

#### 2.4 FULCRUM FOUR: MOBILIZING DEVELOPMENT FOR SECURITY

Through co-option and control, the resources of China's private enterprises are being used for political and policy objectives, including intelligence work, military-civil fusion, and foreign policy goals. Therefore, understanding the PRC's economic and financial course now more than ever requires examining how Beijing's top leadership, with Xi at the forefront, thinks about security.

Since the party's Fifth Plenum in October 2020, the watchwords of "security" and "financial security" have reverberated across the PRC's latest Five-Year Plan and speeches by Xi and his economic lieutenants. For instance, in a major policy document produced at that plenum, the Central Committee indicated the following intentions:

- Secure financial security by defending against systemic risk
- Strengthen centralized party leadership and political supervision over the entire economy and society
- Strengthen, optimize, and enlarge state capital and the state-owned sector<sup>70</sup>

These issues form the basis of economic thinking and policy in Xi's "New Era"—smoothing the economic cycle, controlling the movement and allocation of foreign capital, developing the PRC's "real" economy and commodity base, controlling global supply chains, and taming the private sector. The old model of rapid innovation in flashy consumer tech coupled with

nosebleed GDP growth rates is not so much in contradiction with this "bottom line" thinking as it is beside the point.

In March 2023, on the eve of the annual meetings of the National People's Congress and Chinese People's Political Consultative Conference, *Qiushi* issued a clarion call that Xi wants the PRC's entire economy to be recalibrated with the goal of accelerating preparation for war.<sup>71</sup> The piece, which borrowed liberally from remarks Xi first gave to military leaders in October 2022, also included barely camouflaged jabs at the United States:

At present, the world is once again standing at the crossroads of history. The Cold War mentality and power politics persist. Power politics and the law of the jungle are still prevailing. Our country's security situation is more unstable and uncertain. The world is not peaceful, and peace needs to be defended. In the face of wars that may be imposed on us, we must speak to enemies in a language they understand and use victory to win peace and respect. In the new era, the People's Army insists on using force to stop fighting, which means that it must always maintain a strategic awareness of possible war risks, be ready to fight at any time, fight based on existing conditions, not fight unprepared and unsure battles, effectively deter wars, and resolutely win war.

The essay, under the byline "Jun Zheng"—a pseudonym indicating the voice of the Central Military Commission—highlighted Beijing's more self-confident and urgent messaging around the PRC's military preparedness, encapsulated in the piece's exhortation to "dare to fight and dare to win." Significantly, it also called for an intensification of "military-civil fusion"—Xi's overarching signature policy requiring private companies and civilian institutions to serve the PRC's military modernization.

The *Qiushi* essay was followed in March 2023 by three speeches in which Xi described a bleak geopolitical landscape, singled out the United States by name as the PRC's adversary, exhorted private businesses to serve the PRC's military and strategic aims, and called for a National Defense Education campaign to promote war-readiness. In them, Xi laid out a vision of self-sufficiency considerably farther-reaching than his previous discussions of the topic, saying that the PRC's march to modernization is contingent upon breaking technological dependency on other economies. According to an official Xinhua readout:

Xi Jinping pointed out that accelerating the realization of high-level technological self-reliance is the only way to promote high-quality development. In the fierce international competition, we need to open up new fields and new tracks for development, and shape new development momentum and new advantages. . . . Whether we can build a strong modern socialist country in an all-round way as scheduled depends on the self-reliance and self-improvement of science and technology.<sup>73</sup>

Xi appeared to be girding the PRC's industrial base for struggle and conflict. He said that he wanted to see the PRC end its reliance on grain imports and imports of manufactured goods,

and that it could not rely on the international market to protect it.<sup>74</sup> Crucially, his language contradicted media narratives about a more relaxed attitude toward the private sector.

In the coming period, the risks and challenges we face will only increase and become more severe. Only when all the people think in one place, work hard in one place, help each other in the same boat, unite as one, dare to fight, and be good at fighting, can they continue to win new and greater victories.<sup>75</sup>

To help the party to these "greater victories," Xi vowed that he would "correctly guide" private business to follow the state's direction and invest in projects that the state has prioritized. Notably, Xi also instructed private firms to promote his signature Common Prosperity program, directing entrepreneurs to pay workers well and donate generously to politically correct charities. Companies, he said, should aim to become "rich with responsibility, rich with righteousness, and rich with love." He blamed the United States and its allies as leading causes of the PRC's current problems: "Western countries—led by the United States—have implemented all-round containment, encirclement, and suppression against us, bringing unprecedentedly severe challenges to our country's development."

When Xi launched a series of convulsive campaigns against corruption, private enterprise, financial institutions, and the property and tech sectors—and then doubled down for almost three years on his signature Zero COVID policy (before he was forced uncharacteristically to reverse course)—many voices predicted that all these campaigns would be short lived. Yet they endured.

Now the PRC's private sector actors are envisioned by Xi as symbiotic components of the party-army necessary to achieving intertwined goals of self-reliance and national defense. Protecting the interests of investors is not Xi's priority. At the same time, Xi's commitment to the "real economy," including employment, and "eliminating financial risk" means he will proceed strategically and with care. He has no intention of ruining the macro economy or the financial system. Still, he is pioneering a new phase of Leninist development that has no antecedent.

#### 3. PARTY-ENTERPRISE FUSION

As described in the previous section, the party leverages laws, norms, and a variety of extra-judicial mechanisms to guide or control private companies, and it imposes costs on executives who fail to comply. The most direct lever of control is through party members and internal party organizations. Research has shown that the party has been systematically building the strength and influence of party committees since the Global Financial Crisis in 2008.<sup>79</sup> These structures are ubiquitous in large and technologically sophisticated companies and function like a parallel governance structure.

#### 3.1 RULES FOR PARTY MEMBERS AND NONMEMBERS

Party membership confers demanding political obligations. According to the Party Constitution, party members are required to "be ready to make any personal sacrifice" (Article 2) and prioritize "the interests of the party and the people . . . before all else" (Article 16).

The Party Constitution obliges CCP members to protect the party's secrets. New members take the following oath:

It is my will to join the Communist Party of China, uphold the Party's program, observe the provisions of the Party Constitution, fulfill the obligations of a Party member, carry out the Party's decisions, strictly observe Party discipline, protect Party secrets, be loyal to the Party, work hard, fight for communism for the rest of my life, always be prepared to sacrifice my all for the Party and the people, and never betray the Party.<sup>80</sup>

These are serious requirements, backed by the formidable enforcement apparatus discussed below, which can clash with and override other corporate obligations. The party's requirement for secrecy can potentially conflict with an employee's obligations to the enterprise.

The party exercises legal and extralegal mechanisms of control over nonparty members.

- The **State Security Law**, promulgated in 2015, requires that PRC citizens and organizations provide information, support, and other requested assistance to national security bodies, public security bodies, and the military, whose responsibilities include collecting information relevant to national security (Article 52).<sup>81</sup> State control over all network infrastructure and data is mandated by the law, as is the "safeguarding of national cyberspace sovereignty, security, and development interests." The law further states that China's development interests include "construction of autonomous innovation capabilities" and control over "strategic high-tech and core technologies in key fields" (Article 24).
- The Intelligence Law, which took effect in 2017, compels PRC entities to support China's intelligence services by turning over data collected in China or overseas, and to do so in secret.<sup>82</sup> The law states in Article 7 that "any organization or citizen shall support, assist and cooperate with the state intelligence work in accordance with the Law, and keep the secrets of the national intelligence work from becoming known to the public."
- The **Cybersecurity Law**, also effective from 2017, similarly compels companies and individuals to make networks, data, and communication within China available to the police and security services (Article 28).83 The law also institutionalizes the localization of all data concerning PRC entities and individuals (Article 37), helping to ensure that

no information stored in China, or sent cross-border to or from China, will be protected from Beijing's comprehensive security and surveillance framework.

 The Encryption Law, which took effect in 2020, requires that foreign companies seeking to use or sell encryption tools in China first get them approved by Beijing's State Cryptography Administration, a process that requires providing the government decryption keys, passwords, and access to all underlying data.<sup>84</sup>

These laws codify and reinforce an existing structure of extralegal obligations imposed by the party on the rest of society.

#### 3.2 THE UNITED FRONT

Recent policy documents show that the CCP's objective of exerting greater control over the private sector is now reaching individual corporations and their personnel. In practical terms, this means both party and nonparty members of organizations are subject to similar requirements of political performance. The party uses several mechanisms of control that sit outside its internal organizational system of members, cells, branches, and committees. One underappreciated mechanism is the United Front system.

United Front work is a methodology and strategic framework for exploiting the internal divisions of adversaries. The strategy involves forming tactical alliances with secondary adversaries in order to isolate, "struggle against," and crush a designated primary enemy. The Leninist tactic of United Front work was institutionalized in China in the form of a central internal party department, the United Front Work Department, and an outward-facing analogue, the Chinese People's Political Consultative Conference.

The United Front Work Department (UFWD) is one of the party's four core departments, reporting directly to the Central Committee. 85 In 2015, General Secretary Xi Jinping convened a Central United Front Work Conference at which he described the United Front as one of the party's "magic weapons," on par with "party building" and the People's Liberation Army. At this meeting he greatly elevated the status of United Front Work and signaled he would be intensifying its activities and extending its remit.

United Front work involves identifying and cultivating influential "representative nonparty individuals in order to form tactical alliances and exploit the internal divisions of adversaries." The work is conducted by the UFWD but also other agencies, such as the Ministry of State Security, state-owned enterprises, universities, and, increasingly, private companies. These agencies and actors can all have an international remit.

United Front organizations are usually overt but, as the use of the term "front" suggests, they are deceptive. They are designed to obscure the party's control of the organization and can provide cover for covert intelligence work.

Since the 2015 United Front Work Conference, the party has restructured the UFWD and added three new bureaus, in one of the most significant renovations of the party's bureaucracy since 1951. It added two new bureaus with responsibility for overseas work.<sup>88</sup> This expansion and reinvigoration has prompted analysts, journalists, and intelligence agencies to trace its influence into universities, business communities, and political circles in countries including New Zealand, Australia, Canada, and the United States.<sup>89</sup>

Much less well understood is the targeting of private companies, including multinational companies. In his 2015 speech, Xi designated employees of private companies as one of three new focuses for United Front work. In 2016, the UFWD established a new bureau dedicated to influencing "new social strata individuals"—a category covering urban professionals, including "technical and managerial personnel in foreign enterprises." 90

On September 15, 2020, the CCP Central Committee General Office issued a new document, titled "Opinion on Strengthening Private Economy United Front Work in the New Era," setting out a program for increasing the degree and scope of party leadership.<sup>91</sup>

The "Opinion on Strengthening Private Economy United Front Work in the New Era" contained the following actionable directives to party organizations and members:

- Strengthening "ideological and political construction" in the private sector
- Educating private sector leaders in Xi Jinping Thought and making party organizations within the private sector into "fighting fortresses"
- Strengthening ideological control over nonparty private sector personnel through propaganda and education
- Guiding the private sector to "establish a correct view of the country" and "be a model of patriotism"
- Extending United Front work to both investors and controllers of private enterprise
- Making the party a private sector "talent selection mechanism," with control over internal appointments and recruitment, in order to "grow a team of private economic professionals who unswervingly follow the party and devote themselves to development"
- Establishing permanent party mechanisms in the private sector for "political training" at all levels, integrating private companies into United Front organizations (e.g., the All-China Federation of Industry and Commerce), and absorbing more young people into the party

- Encouraging integration of the private sector into "major national strategies," including those related to foreign policy (e.g., the Belt and Road Initiative [BRI]) and national security
- Creating communication and "consultation" mechanisms to increase interaction between the private sector and government<sup>92</sup>

When issued by the party center, an "opinion" document is equivalent to a formal requirement for all subordinate party institutions. The Opinion makes clear that, as Xi has signaled earlier, politically correct behavior means elevating the interests of the party above economic performance.

It is likely that the new United Front directives anticipate the direction of party policy over private enterprise for the foreseeable future. In a little-observed CCP Central Committee and PRC State Council document released in May 2020, titled "Opinion on Perfection of the Socialist Market Mechanism in the New Era," China's top leadership laid out the following agenda:

Give full play to the party's core role of taking over the overall situation and leadership core role of coordinating all aspects, transform the institutional advantages of the party's leadership in economic work into governance effectiveness, strengthen the implementation of reforms and achieve results, and promote the continuous deepening of economic system reforms.<sup>93</sup>

This top-level framing document placed particular emphasis on strengthening legal control and supervision over market entities, including those of the private sector, through widespread use of party mechanisms: party committees and groups, discipline inspection committees, and the PRC Supervision Law.

Following release of these directives from the CCP Central Committee and the State Council, the CCP's UFWD issued a new document titled "United Front Work Regulations" in January 2021. An official explanation of the regulations published in *Qiushi* states that United Front work will prioritize the nonstate (private) economy, new social classes (a group that includes entrepreneurs and tech workers), and overseas groups including the Chinese diaspora.<sup>94</sup>

#### 3.3 EXTRAJUDICIAL COERCION

The enshrinement of political obligations in PRC law supports assertions by Western officials that PRC companies should be treated as appendages of the party-state. However, the most powerful mechanisms of party control are extrajudicial.

The party's principal instrument of extrajudicial power is the Central Commission for Discipline Inspection (CCDI), which is an intraparty organization for investigating and punishing violations of CCP norms, such as corruption and political disloyalty. The CCDI is one of the main tools by which the CCP leadership controls the behavior of its members, including those who are executives and employees of corporations. Discipline inspection committees

exist at all levels of party organization and are tasked with ensuring centralized control over the party's activities. CCDI investigations can include forced detention and torture. 96 Its impunity relative to other parts of the party system means that the CCDI is known for exercising control through fear. 97

The party's discipline machine has been routinely but mistakenly labeled as Xi's anticorruption apparatus. In fact, the CCDI is exactly what it says it is: the party's discipline enforcement corps, and through the CCDI the party imposes its control over private enterprise.<sup>98</sup>

Far from confining itself to cases of corruption, the CCDI has reverted to its original role of reshaping the PRC's political economy in line with the party's objectives as defined by Xi and Xi alone.

Since coming to power as party boss in 2012, Xi has consistently stressed the need to increase party "supervision" over the domestic economy and curb market excess. In 2017, he instructed the Politburo and all leading banking and financial regulators that they must "conscientiously take the safeguarding of financial security as a major matter in the governance of the country." Since then, Xi has pressed to take control of the PRC's economy, with the CCDI at the forefront.

In the period after the 19th Party Congress in October 2017, the CCDI purged several of the PRC's fastest growing and most debt-fueled companies. The corporate decapitations in this period flowed directly from Xi's instruction to manage financial risk as he worked to establish the credibility of his national deleveraging campaign. The CCDI has subsequently led the dismantlement of high-flying domestic players Baoshang Bank, Anbang Insurance, HNA Group, CEFC, and, more recently, debt-ridden property developer Evergrande. Top executives were detained, and assets were ingested by state entities, to be distributed (or not) according to the party's preferences. Foreign investors were mostly left searching for the creditors' queue.

By contrast, the courts and legal system have tended to play a more prominent role in smaller corporate insolvencies, most notably in the cases of technology companies Tsinghua Unigroup and Peking University Founder Group. Although poorly run, these were not overleveraged, elaborately financially engineered companies run by the nouveau riche and posing broad risk to the financial system. They were deliberate grafts from the state, and they made "real economy" products, such as semiconductors, that Xi wants and needs. Beijing has an incentive to encourage investors, domestic and foreign, to invest in these kinds of companies in the future. He wants the underlying tech assets to continue to be developed, just in a different guise.

The situation is reminiscent of another moment when the party believed that its political longevity was tied up with an uncertain economic future: the founding years of 1949–1956, when Mao Zedong and the party carried out their "socialist transformation" of private industry and commerce, wresting control of the PRC's urban economy while in the midst of a prolonged societal transformation. A series of recent meetings during the run-up to the 20th Party

Congress raises questions about whether Xi may be restoring the party's "Maoist" tradition of driving "forced" economic development through centrally directed political campaigns.

- The CCDI's 2017 Work Report explicitly targeted "the integration of political corruption and economic corruption [that] leads to the formation of interest groups which seriously endanger the political security of the party and the state."<sup>102</sup>
- On July 6, 2021, the General Office of the Party Central Committee issued the "Opinion on Cracking Down on Illegality in Capital Markets," which promised to "significantly restore order" to financial markets by 2022 and to ensure that the securities law enforcement system is "more complete" by 2025.<sup>103</sup>
- The 2021 Opinion was accompanied by a separate three-year plan for rectifying and purifying the real estate sector, issued by eight agencies including key national regulators and the Ministry of Public Security.<sup>104</sup>
- On September 9, 2021, the CCDI issued a new policy document saying that bribe givers will be prosecuted as well as bribe takers as part of the "deepening anticorruption struggle" to "break relationships of exchanging power for money."<sup>105</sup> Previously, it had been an idiosyncrasy of the PRC legal system to exempt businessmen who paid bribes from prosecution on the theory that they could be dangerous to too many people if ever incentivized to talk. The CCDI's new policy line seemed to complement new powers that the fearsome organization has been granted to expand its remit outside the party, including the ability to investigate families and nonparty bureaucrats.<sup>106</sup>
- On September 26, 2021, the PRC's sixth-ranked leader, Zhao Leji, convened a CCDI "mobilization meeting" for the financial sector. The mobilization meeting was widely reported in party media.<sup>107</sup> It announced anticorruption inspections of twenty-five institutions including the People's Bank of China, the China Securities Regulatory Commission (CSRC), the China Banking and Insurance Regulatory Commission (CBIRC), all the major state banks, sovereign wealth funds, stock exchanges, and select stateowned enterprises.<sup>108</sup>

A portentous CCDI article, published on the same weekend as Zhao's speech, carried a warning in its title: "Prevent Leaders and Cadres from Being Captured by Interest Groups." The article, reprinted in popular party newspapers, such as *China Youth On Line*, named specific corruption cases and detailed ways in which cadres can be captured

[through] power rent-seeking and collusion between insiders and outsiders to form interest groups, which lead to the party center's policies and deployment being cheapened and avoided through political-business collusion and secret dealings, and the party's principles and state system being infiltrated and eroded by quiet pay-to-play.

FIGURE 1 The PRC's central bank, the People's Bank of China (PBOC), one of the well-known, oft-cited economic regulators being increasingly eclipsed under Xi by the political-discipline cops at the CCDI



Source: Photo by Max12Max. Used under Creative Commons Attribution-Share Alike 4.0 International.

The article condemned private business owners who seek political power after financial power:

They "encircle-hunt" party members and leaders, engaging in power-for-money transactions and forming interest groups. Some leaders are encircled by criminals and become their prey. They then form interest groups with criminals. This ultimately becomes a vicious cycle. 110

In other words, the discipline enforcers have been working for years to identify and prepare to destroy networks where commercial and political interests most intimately intersect—a target zone that practically defines the PRC's private sector in recent decades.

The CCDI is also providing mobilization muscle behind Xi's crackdowns on sectors from property and tech to education and banking. It has played a key role in pushing aside tech founders (e.g., Jack Ma) and upending entire business sectors (e.g., private tutoring).<sup>111</sup>

Increasingly, the CCDI is overshadowing the governmental regulators that attract the focus of sell-side analysts: the PBOC, CSRC, and the CBIRC.

In January 2022, CCDI chief Zhao Leji linked the fight against "political gangs, small circles, and interest groups within the party" with "the control of corruption in the financial sector" and "the investigation and clean-up of political and commercial 'revolving doors.'" (Just three months later the new campaign had already begun to bite, with China Merchants Bank president Tian Huiyu—a former personal assistant of Vice President Wang Qishan—placed under investigation alongside other moves against senior bankers at China Construction Bank and Everbright Securities. (113)

The next month, CCDI inspection teams separately gave one-on-one feedback to the party committees in each of the twenty-five state-controlled financial institutions under investigation. These reports were not mere bureaucratic formalities. They named specific individuals; and they called for the elimination of their personal influence and networks from the financial system in the name of restoring "political ecology" and creating "capital markets with Chinese characteristics"—in other words, capital markets that are more responsive to imperatives coming from the party center. 115

The assessments highlighted corruption among officials who have left state-owned banks and financial regulators for positions in the private sector. But the assessments also made clear that the CCDI is not merely tackling isolated cases of personal malfeasance. To the contrary, it must be understood that the CCDI wants to ensure that institutions work harder to implement party policies—the vision of Xi Jinping.

The focus of Xi and his enforcers has transcended isolated instances of corruption and factional politics. The CCDI may indeed follow through on its promises to target the patronage networks and "interest groups" that lie at the nexus of economic, regulatory, and political power in the PRC, but under the guise of this anticorruption struggle the CCP is rewiring and reshaping the entire PRC economy. The cases of Alibaba and ByteDance illustrate two ways in which this is happening.

#### 4. ALIBABA: A CASE STUDY FOR PARTY-PRIVATE FUSION

We are in the dark about who really controls party structures in most companies. Open-source information often doesn't reveal the organizational hierarchy for party committees in companies, which is significant because internal party rules give a firm's superior party organization the final word on key matters such as leadership appointments. Alibaba and "strategic partner" Ant Group exemplify the lengths to which the party goes to obscure these arrangements.

On March 28, 2023, during the same week that its founder Jack Ma returned to China, Alibaba Group announced it would become a holding company over six businesses, each with its own

board. Alibaba acknowledged that the reshuffle could signal the breakup of the country's biggest e-commerce firm.

In a letter to employees, Alibaba CEO Daniel Zhang called the breakup the "most significant revolution in Alibaba's twenty-four-year history."<sup>116</sup> Zhang explained that turning Alibaba's \$220 billion empire into a holding company could allow each of the new businesses the chance to individually raise funds and explore their own IPOs. "When children grow up, they have to go out and face the market independently," Zhang said. "The Alibaba Group is more like a big base to support them." In a Q&A with investors, CFO Xu Hong noted that after each business is listed, "Alibaba will further evaluate their strategic importance to the entire group to decide whether to maintain control or give up control."<sup>117</sup>

Foreign and PRC media hailed Alibaba's move—and Ma's return—as fresh signs that authorities in the PRC are reining in their yearslong campaign against Big Tech as they seek to boost economic growth and make peace with the entrepreneurial class that they have targeted.

Market consensus is correct that the breakup is good news—for shareholders and for Alibaba—in that it offers perhaps the only way forward for a conglomerate and an industry that the party-state simply didn't trust for political, data-security, and national security reasons. It was those concerns that prompted Beijing's highly disruptive, three-year "rectification campaign" of Big Tech in the first place, starting in 2020. As such, a key element of Daniel Zhang's "revolution" that has generally been ignored by analysts and media alike is that while money can still be made, Alibaba's newly spun-off companies will be operating in a very different, more highly regulated environment than the one they left behind in 2020. Moreover, even prior to the breakup, the parent company had already been ingested into the party through a complex, decade-spanning process of internal party-building that has eluded analysts due to its intentionally secretive nature, but which this section now describes.

Big Tech rectification may have been declared "basically completed" in January 2023, but private firms will still need to closely align themselves with the interests of the party-state, which is committed to ensuring that they pose no threat to its rule.

Alibaba's absorption and breakup should also be seen as a window into the pressures faced by larger Chinese firms with private roots. Similar fates could be awaiting other PRC tech giants, such as Tencent. That is the prism through which Alibaba's reorganization should be viewed. Breaking up conglomerates into smaller parts helps soothe the ruling Communist Party's fear of alternative power centers in China—especially big, powerful firms with charismatic leaders, financial clout, and profit incentives often at odds with the party's priorities. And smaller companies make it easier for the party-state and its security apparatus to assert control over all the sensitive data that tech firms accumulate.

#### 4.1 ANT GROUP'S STORY TO INVESTORS

The prospectus that Ant Group provided to international investors on October 27, 2020, said that Jack Ma directly controls 56 percent of group shares through two personal investment

vehicles, and indirectly controls 33 percent of the shares through his stake in Alibaba Group.<sup>118</sup> Its 750 pages detail a raft of laws and listing rules and a vast range of investment risks, except the ones that may matter most.

The prospectus did not warn that the richest, most famous, and most successful entrepreneur in Chinese history could disappear, or that the world's biggest IPO could be pulled without warning. It failed to mention that the Hong Kong and Shanghai stock exchanges, the securities regulator, the banking regulator, the competition regulator, and even Ma himself are all subject to the ultimate authority of the CCP. It further did not indicate that the CCP is an organization that operates above the law and is increasingly open about its desire to cut private enterprise down to size.

The Ant Group prospectus does not mention the CCP anywhere in the main body of the document. Investors must plough through the appendices to find the first and only mention of the CCP, at Appendix VI, roughly 620 pages in—and there it is mentioned only in the title of a guidance document related to mobile payments platforms.<sup>119</sup>

To be fair to the teams of lawyers and bankers who compiled the Ant Group prospectus, the CCP is not an easy subject to talk about. The party still has a strong tradition as an underground organization. There is no publicly available central register of party members or party units. There is no transparent guide to party decisions, policies, or campaigns, except to the extent that the party chooses to reveal them. There are very few useful secondary sources except those published by the party itself. And those closest to the party—its members—have sworn to protect its secrets and put its interests first. Increasingly, party members are being required to live up to their commitments, as Jack Ma has discovered.

Neither state-owned nor private, Alibaba is a hybrid entity that is effectively state-controlled. In Alibaba's true governance structure, the CCP is not only taken into account by decision makers but appears to be deeply integrated into decision-making structures, from the group-wide executive level down to individual business divisions. This is not about micromanaging decisions about technology or commerciality. It is about controlling strategic decisions and helping to shape the way lesser decisions are made all the way down.

Jack Ma may be allowed to continue as the group's dominant shareholder. Or he may not. But true control of strategic decision making may have long since passed from his hands to a party committee system led by the company's party secretary, a former public security official named Shao Xiaofeng. The co-option of Alibaba Group by the CCP, as we shall see, has had material, and not just ideological, implications.

#### 4.2 ALIBABA'S INTERNAL PARTY SECRETARY SYSTEM

Shao is not entirely unknown to close watchers of the PRC's corporate scene. A 2014 piece in the *Wall Street Journal* described Shao as an "old friend" of Ma and noted, presciently: "It isn't clear whether he still leads the company's internal Communist Party apparatus, an important position at major Chinese companies that helps executives coordinate with the organization

that dominates politics in China."<sup>120</sup> Most of the occasional references to Shao in the Western press have identified him by the corporate titles he has held at various times, including chief risk officer and head of Alibaba Pictures. According to the 2021 Hurun China Professional Managers List, Shao was the fifth-wealthiest executive in the PRC and the second-wealthiest at Alibaba, behind only Ant Group executive chairman Eric Jing. (Jack Ma formally retired as executive chairman in 2019.)<sup>121</sup>

Viewed through Chinese-language sources, however, a crisper image of Shao emerges, one showing an improbable rise through the party-state ranks to the pinnacle of Alibaba leadership, and largely hidden from public view. A 2004 biography of Shao, appearing on the Hangzhou People's Government website, identifies him as the leader of the Hangzhou Public Security First Criminal Investigation Brigade. The biography states that Shao's brigade had been recognized as a "national political and legal system 'strike hard' [campaign] advanced collective." It describes his party branch as a "Hangzhou City advanced grassroots party organization."

In addition to being the hometown of Jack Ma and Alibaba Group, Hangzhou is also the capital of Zhejiang province, where Xi Jinping was party secretary from 2002 to 2007, just as Shao was reaching the pinnacle of his public security career.

Shao joined Alibaba in 2005 as head of cybersecurity and rose swiftly thereafter. In 2006, he became Jack Ma's special assistant. In 2007, the same year Xi was elevated to the Politburo Standing Committee as heir to the top job, Shao became vice president of Taobao, Alibaba's flagship e-commerce site. Shao was promoted to president of Alipay one year later. In 2010, he became group secretary general.<sup>123</sup>

Most of what we know about Shao's role across the Alibaba Group comes from a seemingly obscure essay that Shao penned for what appears at first glance to be a marginal party publication, the online magazine *Mishu Gongzuo* (translation: *Secretarial Work*).<sup>124</sup> In fact, this magazine is published by the center of power in the PRC, the General Office of the Central Committee, and the essay itself was republished on the website of the Secretarial Bureau of the General Office.

Shao's self-described job responsibilities are remarkably extensive. He describes an idiosyncratic role of "secretary general" that evolved from being an advisor to Jack Ma to something far larger: an "omnipotent" role where "wherever needed" he will "go and participate." He also holds a smorgasbord of other "important group positions" and states that "party committee secretary" of Alibaba is one of the most important among these.

Online sources confirm he continued to hold the post of secretary of the Alibaba Group party committee as recently as November 2019. Shao's role as secretary general has, by his telling, evolved into something akin to a combined chairman and chief executive in the context of a Western public company. He is responsible for Alibaba's strategic decisions, business direction, and risk assessment and response.

Shao also presents himself as the convenor of the company's highest governing body, the Alibaba Partnership, which appoints a majority of Alibaba Group board directors. Shao further notes that his leadership of the partnership organization gives him control and oversight over the firm's entire strategic direction, mission, and culture. He therefore represents the extension of CCP authority into the apex of Alibaba Group's visible corporate structure.

While it is always possible that Shao may overstate his personal importance, the display of his highly personalized article on the website of one of the party's most powerful organs provides an indication of his status and position within the party apparatus. A brief tagline at the bottom of the essay confirms Shao's formal position within the Chinese Communist Party as Alibaba Group party committee secretary, in addition to his Alibaba-specific secretary general role.

The implication of Shao's essay is that he holds unrivalled decision-making power at Alibaba. In retrospect, its publication in early 2018 foreshadowed a formal transition of power from Jack Ma to the party committee system, of which Shao was (and still is) the leader. Soon after publication of Shao's essay, in September 2018, Ma announced his retirement as executive chairman.

Shao's article is the most important publicly available source for illuminating internal mechanisms of party control that are emerging within Alibaba Group and across the PRC tech sector more broadly. The position and prominence given to Shao's essay signals that the party intends for his innovative approach to what he himself calls "party building" to serve as a model for cadres to follow in other large, systemically important companies.

Shao shows himself to be pioneering a new kind of party organization that is managerially competent, adaptable, and organically entwined with company governance and management. He describes Alibaba as a corporate pioneer in introducing competition between party branches to secure the most outstanding talent. Shao also crows that party members rank among the company's best employees at triple the rate of nonparty employees, and that the majority of key management positions are held by party members.

Shao's 2018 article also contains what is probably the most explicit and authoritative account of how Alibaba aligns its business strategy with the party's political and policy aims:

If an enterprise wants to become great, [its] development must be in keeping with the national interest and the people's interest. Alibaba, as a multinational enterprise, must learn from the country's major government plans and policies, and maintain a high degree of consistency with the spirit of the party center, and actively participate in the national strategy. For example, for several years we have actively participated in "One Belt, One Road," economic globalization, targeted poverty alleviation, and rural revitalization strategies. How to link together enterprise development and the country's major government plans and policies is also what the group secretary general needs to promote in the process of enterprise decision making.

Shao does not appear on Alibaba Group's leadership page, which lists the company's current board of directors and senior management.<sup>128</sup>

When Jack Ma was first spotted in Hangzhou on March 27, 2023, in a Toyota Coaster minibus, Shao was there sitting behind Ma and CEO Daniel Zhang and talking animatedly with Ma.<sup>129</sup> Significantly, censors have allowed this photograph to be circulated online along with wall-to-wall media coverage. It seems that the message, bolstered by a recent laudatory piece in the financial media on Shao's career and his reported \$2.4 billion net worth, is that Jack Ma is physically back in China but the party remains in charge.<sup>130</sup>

Amid Ant's separation from Alibaba, there has been a shift in the advertised corporate role of Shao Xiaofeng, even as Alibaba's main market-facing documents remain mum on Shao's outsize role in the company's Communist Party structure.

In Alibaba's 2021 annual report, Shao was identified as one of the thirty-three members of the Alibaba partnership and a senior vice president of Ant. In the 2022 edition, Shao, 56, is again identified as an Alibaba partner, while his corporate title has shifted to senior vice president of Alibaba.<sup>131</sup>

#### 4.3 AN INTERNAL PARTY LABYRINTH

Analysis of party control structures shows they often bear no relation to the corporate structures visible on a company's public "org chart." They can also differ greatly between a company and its subsidiaries. The problem is that Alibaba's visible structure of ownership, control, and management is enmeshed with party structures that are not designed to be transparent or accountable to investors. There is no official map to show how the organization works.

The most complete picture of the company's party organization that we have identified comes from a photograph of an Alibaba Group internal party organization chart posted online in October 2018.<sup>132</sup> The article in which the photograph appeared describes the first national meeting on party building for internet companies, held in Shenzhen in September 2018, in response to guidance from Xi Jinping.<sup>133</sup> Reflecting its importance, the conference was organized by the two most important agencies for party-building and cyber policy, the Party Central Committee's Organization Department and the Cyberspace Administration of China.

The photograph shows that the party's control system extends downward from the group level into Taobao, Alibaba Cloud, and other subsidiaries. Based on this photograph, and on recent media announcements pointing to the creation of a new party organization in Alibaba (Beijing) Software Services, it is possible to visualize how Alibaba's multiple internal party control structures are organized.

Alibaba (Beijing) Software Services is a standard subsidiary of the Alibaba Group, notable because the launch of its new party committee was reported publicly by Beijing's government. While corporate ownership structures place Alibaba (Beijing) Software Services firmly

under the Hangzhou-based Alibaba Group, party control structures pull it in another direction: up to Beijing's Zhongguancun Chaoyang Party work committee. The Hangzhou-based Alibaba Group party committee appears to have a branch in Beijing, but it has an unclear relationship to party structures in Alibaba (Beijing) Software Services. It is rather the Zhongguancun Chaoyang Party work committee that has control over appointments to Alibaba (Beijing) Software Services' leadership, its disciplinary work, and evaluations of its performance.

The divergence of corporate control structures from party structures requires dividing the responsibilities of executives who are both party officials and Alibaba managers. What this signifies in practice is difficult to say. At the very least, it once again underscores how little foreign investors can possibly know about how major PRC tech companies are actually governed.

Alibaba's internal party organizations have grown even faster in recent years than its business. The company was established in Hangzhou in 1999 and its first CCP branch was founded one year later. A party branch is the lowest level of party organization, and usually has between three and fifty members. By the early 2010s, Alibaba employees included more than two thousand party members, and the party branch was upgraded to a party committee. A party committee is the highest level of party organization for a corporation and usually has more than one hundred members. As of 2018, party membership within Alibaba had grown to seven thousand members across more than two hundred party branches and three party committees, according to Shao's article in *Mishu Gongzuo*. Since Shao's essay, two more party committees have been revealed in open sources, bringing the total to at least five.

According to the website of the Chinese Federation of Internet Societies, Alibaba's party members now number more than sixteen thousand. 142

#### 4.4 ANT GROUP'S ELUSIVE PARTY STRUCTURES

Ant's governance and party structures overlap to some extent with those of Alibaba, but the precise relationship between them is unclear. For example:

- Ant Group nonexecutive directors include Alibaba co-founder Joseph Tsai, Alibaba CTO
  Cheng Li, and Alibaba deputy chief personnel officer and special assistant to the CEO
  on international affairs Jiang Fang.<sup>143</sup>
- Alibaba executive Wang Qiang was described in a 2021 report as both head of public affairs at Alibaba and deputy secretary of Ant's Beijing party committee.<sup>144</sup>
- In 2018, Alibaba and Ant held a major joint party member conference for the ninetyeighth anniversary of the party's founding. 145

Alibaba Group party secretary Shao Xiaofeng has described the Ant Group party committee as "parallel" to Alibaba Group's. 146

Analysis of reports on Ant's party committee and its branches indicates that it is involved in government affairs and integrity and compliance work. The Ant party committee's deputy secretary, Xu Hao, was previously the company's deputy CEO for government affairs, according to a 2019 Hangzhou Government article. But Ant's website indicates that Xu no longer sits on the company's executive team. No other past or present members of the company's top party committee are known.

A January 2021 report described Wang Qiang, head of public affairs at Alibaba (and previously head of the strategic development department), as deputy secretary of Ant's Beijing party committee. Ant's chief compliance officer in 2018 was listed as a Beijing party branch secretary. In 2018, Ant established an Integrity and Compliance Hall within its office as part of a campaign by the party committee to promote "honesty" in response to newly revised party regulations.

Government affairs, integrity and compliance, and human resources together form a common set of outward-facing responsibilities for tech company party committees. As a comparison, Huawei's party committee doubles as the company's ethics and compliance committee. Like Huawei and Alibaba, Ant Group can be described as a state-controlled hybrid entity.

In contrast with Alibaba, Ant appears to have no "secretary general." Rather, the party organization overlaps with key personnel and bodies within the company's corporate structures.

But the picture remains, at best, incomplete and fundamentally opaque. Were Ant Group to list publicly, as was planned until the last-minute suspension of its IPO last year, investors would lack essential information about who calls the shots and how.

## 4.5 DOING THE PARTY'S WORK

From its inception, Alibaba Group has maintained a dual corporate identity: as a remarkably innovative commercial enterprise with strong appeal for consumers, businesses, and investors, and as a partner to the CCP in digitally transforming the economy and key institutions of social management. Alibaba needs the party-state's support to defend and extend its official and implicit licenses to operate, particularly in "gray" areas that have traditionally been dominated by the state, such as the financial system and the intersection between technology and societal control. This coexistence means that the political system wraps around and extends inside Alibaba, while the company actively supports the political system, including in the following ways:

#### Financial Infrastructure

Alibaba affiliate Ant Group has been revealed as a co-developer of China's central bank digital currency project, the E-CNY.<sup>153</sup>

A strategic agreement between the People's Bank of China and Ant was also announced in April 2023, focusing on building an E-CNY digital platform using Ant's OceanBase database

and mobile platform as a service (mPaaS) technology.<sup>154</sup> Ant-owned MYbank is already one of the institutions authorized by the People's Bank of China to pilot the E-CNY.<sup>155</sup>

Ant was one of forty-four financial companies involved in the establishment of the China National Clearing Center's operating company for transactions involving online payment services and banks.<sup>156</sup> The company, NetsUnion Clearing Corporation, is 9.61 percent owned by Alipay and supervised by the PBOC.<sup>157</sup>

## **Judicial and Credit Systems**

Alibaba is a "technology partner" to China's Supreme People's Court (SPC), using credit history data from its Sesame Credit program to help the SPC enforce court judgments. This partnership has existed since 2015.

According to Alibaba Group, its SPC partnership has resulted in identification of 730,000 debtors, leading to 50,000 settlements. 158

### **Smart Cities and Governance**

Alibaba has formed strategic partnerships with more than thirty provincial-level governments throughout China for digital government projects covering 442 cities, 1,000 service areas, and 900 million people.<sup>159</sup>

Alibaba's "City Brain" platform for municipal government big data analysis and resource allocation is used in cities throughout China and has been designated a "national Al open innovation platform" by the Ministry of Science and Technology. 160

The Ministry of Science and Technology selected Alibaba in 2017 as part of a "national team" charged with developing various types of artificial intelligence, with Alibaba to focus on smart cities and cloud computing.<sup>161</sup>

#### **Tax Services**

Alipay's facial recognition technology is used by national and provincial tax authorities to digitize tax payment and fight tax evasion. Alipay is reportedly the technology solution partner behind the country's most widely used e-tax app. The State Taxation Administration uses Alipay's facial recognition technology to help it verify taxpayer identity remotely.

## **Rural Development**

Alibaba announced a Thousand Counties and Ten Thousand Villages rural strategy in 2014, promising to invest RMB 10 billion to build a network of service centers and boost e-commerce in the countryside.

## **Public Security Work**

Alibaba Cloud Intelligence's Yiduoyun cloud computing platform for government digital transformation is certified by the country's Ministry of Public Security.<sup>164</sup>

In 2016, Alibaba began a "special investigation and exchange" with Changsha (Hunan province) public security criminal investigators. The focus of the discussions was "new types of crimes on telecommunications networks." Cooperation between Alibaba and Changsha law enforcement authorities has since expanded into Alibaba Cloud-provided big data platforms for public security tasks, including predictive policing. 166

# Intelligence and Law Enforcement

Also in 2016, Alibaba Cloud became a strategic partner of Global Tone Communication Technology Co. Ltd. (GTCOM), a state-owned enterprise subsidiary supervised by the CCP Central Propaganda Department. GTCOM's main activities are development of hardware and software translation tools and collection of bulk data in more than sixty-five languages. Collected data is processed into products and services for government and corporate clients. According to research published by the Australian Strategic Policy Institute, GTCOM openly contributes to state security and intelligence data collection.

# Xinjiang

In 2014, Jack Ma and his team visited Xinjiang and signed a strategic partnership agreement with the provincial government. The agreement, reported by official state media, included provisions for the purchase of Alibaba's cloud computing and big data technology for public security, counterterrorism, and governance use, all with the stated aim of building a "digital interconnected Xinjiang." <sup>170</sup>

## Propaganda

"Xuexi Qiangguo" is a Chinese Communist Party propaganda platform whose name literally means "Study [Xi Jinping] to make China strong." The platform's app, often mandatory for party members and government employees, was created by Alibaba, according to Reuters.<sup>171</sup> A well-known technology website in China suggests the app is based on Alibaba's social media app DingTalk.<sup>172</sup>

Alibaba Cloud's website has disclosed a RMB 60 million contract to provide cybersecurity and cloud computing services to run the Xuexi Qiangguo app.<sup>173</sup>

## Military-Civil Fusion

According to a December 2018 article published on the National Military-Civil Fusion Public Platform, administered by the Ministry of Industry and Information Technology, Alibaba products and technologies have been used in the research, production, and repair of weapons and equipment for the People's Liberation Army (PLA).<sup>174</sup>

This article reflected a series of military-civil and defense-related projects involving Alibaba announced around that time. In May 2018, Alibaba Cloud was named as a partner in building a "high-level security" cloud platform for defense and government customers, in cooperation with a subsidiary of defense electronics conglomerate China Electronics Technology Group Corp. 175 In December 2018, Alibaba's R&D wing, DAMO Academy, was listed as a participant in Hangzhou Government plans to implement and accelerate military-civil fusion in the artificial intelligence industry. 176

These cases indicate that Alibaba is required to invest in often unprofitable projects to advance the party's political agenda; serve as an extension of integral government functions; assist the party's intelligence, political security, and social control functions; and contribute to Beijing's military-civil fusion strategy.

#### 4.6 BEYOND ALIBABA

Jack Ma's continued withdrawal from his businesses (he stepped down as Alibaba chairman in 2019) deepens the trend of China's Big Tech founders, once the public face of an economic boom, being forced into the shadows. Ma's control over Alibaba and Ant has been questionable for years; by contrast, Shao Xiaofeng has become the visible leader of both businesses as party secretary of Alibaba and executive vice president of Ant Group. While Alibaba's corporate structure continues to shift, the party ligaments that tie together its disparate enterprises persist.

This story is bigger than the big tech entrepreneurs: It is about the nature of governance and control of private enterprise itself. The assault on Jack Ma's empire may best be explained only in light of a longer-term, centrally directed shift toward imposing hidden but powerful structures of Communist Party control inside private enterprise, at the expense of the visible structures of corporate control, including those reflected in securities filings. The power of the party's internal systems of committees and cells is reinforced by external levers, both legal (through mechanisms of the state) and extralegal (through the party's own mechanisms, which sit outside the legal system).

By asserting itself inside Chinese tech firms, the party makes it even harder to convince governments around the world that these companies are not tools of the state. This will increase political and regulatory costs on Chinese firms and accelerate decoupling.

# 5. BYTEDANCE AND TIKTOK: HOW A PRC ENTERPRISE SEEKS PLAUSIBLE DENIABILITY

Alibaba is not an anomaly. ByteDance, once described as the "world's most valuable startup," is a very similar company in terms of its hidden party structures and track record of CCP policy support.<sup>177</sup>

If ByteDance was once a private enterprise controlled by its founder, it is no longer. Owing to a Chinese Communist Party program of co-option, infiltration, and legal and extralegal coercion, ByteDance, like Alibaba, should rightly be understood as a "hybrid" party-private entity.

TikTok's claims that it is about entertainment, not politics, are untenable.<sup>178</sup> Last year, a third of adult users got their news from it, while one in six American teens say they are on the platform "almost constantly."<sup>179</sup> Clearly the potential for Beijing to exploit TikTok for global surveillance is huge; however, the most significant risk posed by TikTok is its unprecedented potential for censoring and proactively shaping public opinion overseas, in the United States and in other countries around the world.

In 2017, ByteDance launched TikTok and acquired the US company Musical.ly. At the same time, Beijing launched a six-year regulatory campaign to build party control systems inside ByteDance and accelerated the integration of senior corporate leaders into its "public opinion guidance" regime. Over this same period, Beijing has blocked the TikTok app inside China while enabling it to flourish outside China, to the point that it is now one of the most sophisticated and powerful social media platforms in the world.

In May 2021, during a Politburo "Study Session," Xi Jinping instructed his colleagues to use "external discourse mechanisms" in order to "target different regions, different countries, and different groups of audiences" with "precise communication methods" in order to "make friends, unite and win the majority, and constantly expand our circle of friends who know China and are China-friendly."<sup>180</sup>

Xi did not name TikTok in the official meeting readout, published by Xinhua. Subsequently, however, the *People's Daily* (Overseas Edition) elaborated on Xi's message in an article (republished by Xinhua) that called for China to "allow short video platforms to become 'megaphones' for telling Chinese stories well and spreading Chinese voices well." The article mentioned TikTok specifically as the representative example of short video platforms.

Answering basic questions about how the app works, how it is controlled, and who controls it is not straightforward. Ownership aside, what is clearer are Beijing's capabilities and intent relating to the deployment of targeted propaganda designed to shape global discourses overseas, the identification of short video platforms as a key arena for exploitation, and ByteDance's responsiveness in directly aiding party propaganda, surveillance, and repression, as discussed below.

## 5.1 OPACITY AND OBFUSCATION

Media reporting has emphasized the opacity of TikTok's algorithm, even to some of TikTok's own employees. This opacity extends to its corporate organization. Answering basic questions about how the app works, how it is controlled, and who controls it is not straightforward. ByteDance's company website contains just the bare bones, shorn of details about the company's founder, corporate structure, partners, and sizeable investment into Al.

Leaked internal advice from TikTok about public relations talking points encapsulates the company's evasive self-presentation. The document instructs TikTok spokespersons to "downplay the parent company ByteDance, downplay the China association, downplay Al." The memo directs spokespersons to say, "There's a lot of misinformation about TikTok right now. The reality is that the TikTok app isn't even available in China." 185

This opacity and obfuscation are now compounded by what appears to be a concerted campaign to airbrush away what little material was available online. Excavating four years of archived snapshots of ByteDance's company website reveals layers of disappearing information. Pages that once recounted Communist Party activities inside ByteDance have been deleted from the website of the Beijing Internet Association (an industry association charged with guiding the party-building work of internet companies in Beijing). Pages 187

When TikTok Inc. and ByteDance Ltd. sued the Trump administration in August 2020 for banning the TikTok app, they stressed in court papers that the company is and has always been a wholly private entity: "The TikTok application began as a product of private-sector entrepreneurship. . . . No foreign government, or person controlled by or acting on behalf of a foreign government, owns any significant interest or any other affirmative or negative rights or powers in ByteDance." 188

This claim is misleading. A longer-term, centrally directed shift toward imposing hidden but powerful structures of Communist Party control inside ByteDance has developed at the expense of more transparent structures of corporate control. The power of the party's internal systems of committees and cells used to wield control over the enterprise is reinforced by external levers, both legal (through mechanisms of the state) and extralegal (through the party's own mechanisms, which sit outside the legal system).

As TikTok continues to be scrutinized overseas for its links to the CCP—which it flatly denies—the company has also downplayed its ties to parent company ByteDance.

- Hiring "global" leadership. Since 2020, TikTok has had three CEOs from outside the PRC. Kevin Mayer, a former Disney executive, was brought on as TikTok CEO in May 2020, reporting to Zhang Yiming, before resigning after just four months.<sup>189</sup> Vanessa Pappas then became interim CEO, until Shouzi Chew's appointment in April 2021.<sup>190</sup>
- No headquarters. TikTok engages in what has been called "Singapore-washing" to deflect the increased scrutiny facing companies from the PRC. 191 Leaders have asserted that TikTok is not headquartered in the PRC but is a "distributed" company with offices all around the world and a significant presence in Singapore. 192 In addition to native Singaporean TikTok CEO Shouzi Chew, multiple ByteDance executives are now at least partially based there, including founder and former CEO Zhang Yiming, CEO Liang Rubo, CFO Julie Gao, and TikTok's global R&D head Zhu Wenjia. 193

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• Changes to company name. ByteDance renamed several subsidiaries from "ByteDance" to "Douyin" in May 2022. 194 TikTok CEO Shouzi Chew explained in a June 30, 2022, letter to the US Congress that "multiple corporate entities share the 'ByteDance' name, [therefore] several PRC-based ByteDance entities were renamed earlier this year to keep the names of businesses and entities more consistent. Beijing ByteDance Technology Co. Ltd. is now called Beijing Douyin Information Service Limited." 195 Observers have read this as another move to distance TikTok from its PRC operations. 196

## ByteDance Is the Parent Company of TikTok and Douyin

According to a legal petition that TikTok Inc. and ByteDance Ltd. filed on November 10, 2020, ByteDance Ltd. (Cayman), owns TikTok Ltd. (Cayman), which wholly owns TikTok LLC, a Delaware limited liability company.<sup>197</sup> TikTok LLC holds "all of the outstanding shares of capital stock of TikTok Inc."<sup>198</sup> An archived version of ByteDance's website that shows a corporate structure last updated on June 30, 2020, confirms this chain of ownership.<sup>199</sup>

Douyin and other PRC operations are likely held through a Hong Kong subsidiary, Douyin Group (Hong Kong) Ltd.<sup>200</sup> In January 2023, *Hong Kong Economic Journal* reported that Douyin Co. Ltd. is an entity that ByteDance established in Mainland China under the variable-interest entity (VIE) structure for business operations.<sup>201</sup>

# ByteDance Is Headquartered in the PRC

While the parent company that owns TikTok is incorporated in the Cayman Islands, ByteDance declared in November 2020 that its headquarters were in the PRC. ByteDance referred to itself as a "Chinese-headquartered company" multiple times in its appeal against the US official Divestment Order and action by the Committee on Foreign Investment in the United States (CFIUS):

[TikTok Inc. and ByteDance Ltd.] did not submit the Musical.ly transaction to CFIUS for review in 2017 because ByteDance was a Chinese-headquartered company and Musical.ly was also a Chinese-headquartered company. . . . It is necessarily the case that whatever national security risks posed by the Musical.ly app and its Chinese ownership at the time of the acquisition were not enlarged or changed by the acquisition of the Musical.ly company by another China-headquartered company, ByteDance.<sup>202</sup>

## ByteDance Co-founder Liang Rubo Leads TikTok

Liang Rubo is CEO and chairperson of the global ByteDance corporate group. ByteDance Ltd. (Cayman) currently lists Liang as one of its five directors on the Cayman Islands company registry. <sup>203</sup> Both TikTok CEO Shouzi Chew and Douyin Group CEO Kelly Zhang report to Liang, at least nominally. On November 2, 2021, Liang announced the company's organizational restructuring (in a letter published on Sina). <sup>204</sup> Liang stated that the individuals in charge of each of the six business units would report to him, including TikTok CEO Shouzi Chew and Douyin Group CEO Kelly Zhang. <sup>205</sup>

Liang Rubo is a visible link between the Cayman company's board and ByteDance's PRC operations. He occupies various management positions in the company's PRC-based subsidiaries, despite claims that the Cayman board is divorced from PRC operations.<sup>206</sup>

## Interchangeability of TikTok and ByteDance Employees and Cloud Infrastructure

A simple search on LinkedIn shows at least 4,400 people who list "ByteDance" and "TikTok" in a single profile. A significant number of profiles list ByteDance and TikTok interchangeably, including prominent TikTok leaders such as Blake Chandlee, "President, Global Business Solutions at ByteDance/TikTok." Solutions at ByteDance/TikTok."

This echoes reporting by *Forbes* that TikTok employees had ByteDance listed on their paychecks and tax returns, and by CNBC as well as *Forbes* reporter Emily Baker-White that TikTok email aliases are simultaneously ByteDance email aliases.<sup>209</sup> It points to the fungibility of ByteDance and TikTok as employer.

The cloud infrastructures for both TikTok and other ByteDance products appear to be administered by the same team. A role titled "Tech Lead (Database Administrator), Cloud Infrastructure" manages database services within ByteDance, providing "online storage service support for all types of products in ByteDance (TikTok, Douyin, [Today's Headlines], etc)."<sup>210</sup> This role may be akin to a PRC-based "Master Admin" that *BuzzFeed* reporting refers to, who reportedly has access to US user data.<sup>211</sup>

The ties that bind TikTok to ByteDance, coupled with the presence of robust party control, raise the likelihood of Communist Party influence over TikTok.

## The Party-State's Stake in Beijing Douyin

Beijing Douyin Information Service Limited, renamed from Beijing ByteDance Technology Co., Ltd. was established in March 2012 at the company's founding. The party-state formally registered a 1 percent stake in Beijing Douyin Information Service Limited in April 2021. The largest beneficial owners of this 1 percent stake are the State-owned Assets Supervision and Administration Commission (SASAC, which oversees state enterprises), China Media Group, and the Cyberspace Administration of China.

The company's own statements imply that the government stake was required by regulators. Responding to direct questioning in a letter to US senators about whether the Chinese government owns a stake in TikTok, CEO Shouzi Chew clarified:

Beijing Douyin Information Service Limited is a separately held subsidiary of ByteDance Ltd. Beijing Douyin Information Service Limited does not have any direct or indirect ownership interest in or control over any TikTok entity. The Chinese state-owned enterprise's acquisition of 1% of Beijing Douyin Information Service Limited was necessary for the purpose of obtaining a news license in China for several China-based content applications, such as Douyin and [Today's Headlines].<sup>215</sup>

The party-state's acquisition of "golden shares" in private tech companies gives it direct and open insider access to corporate decision making, and influence through board seats and veto rights. <sup>216</sup> This institutionalization of party alignment can limit or eliminate the need for subsequent state intervention.

In the case of ByteDance, the Cyberspace Administration of China (CAC)—China's internet regulator and the external "nameplate" and office of the CCP Central Cybersecurity and Informatization Commission—appointed an official, Wu Shugang, to the board of Beijing Douyin Information Service Limited at the time of the "golden share" acquisition.<sup>217</sup>

A *Financial Times* review of the company charter provides details about Wu's powers within the company: Wu reportedly gets a say over business strategy and investment plans, mergers and acquisitions, profit allocation, and a vote on the group's top three executives and remuneration packages. Wu can control the content on ByteDance's media platforms in the PRC, such as Douyin and Today's Headlines through his right to appoint the group's editor-in-chief and the chair of a "content safety committee." 218

Wu gained notoriety a decade ago from his June 2012 Weibo post: "I only have one wish—that one day I can cut off the dog head of traitors [i.e., liberal voices in the PRC]. Let the Chinese traitors preaching so-called 'human rights and freedom' go to hell!!"<sup>219</sup>

Later, Wu became party secretary of the Communist Youth League for organs directly under the Ministry of Education.<sup>220</sup>

Before joining ByteDance, Wu worked in the Local Guidance Office of the CAC's Online Commentary Work Bureau. He visited internet companies to give lectures to party members about instructions from Xi Jinping and events such as the 19th Party Congress, particularly in relation to online public opinion and discourse power on the main "battlefield" of the internet.<sup>221</sup>

# Communist Party Organization Members within ByteDance

In a 2022 hearing, US Senator Josh Hawley questioned TikTok COO Vanessa Pappas about whether employees were affiliated with the CCP. Pappas responded that she "wouldn't be able to tell [Hawley] the political affiliation of any individual," but that among TikTok's "US and Singapore leadership, there are no CCP members. . . . Everyone who makes a strategic decision at this platform is not a member of the CCP."

According to a party newspaper, *Study Times*, ByteDance established its first party branch in October 2014, followed by a party committee in April 2017 with branches within Review and Operations, Public Affairs, and Technical Support.<sup>223</sup>

In 2020, the Cyberspace Administration of Beijing Municipality (Beijing CAC) mobilized ByteDance to establish a "public opinion research and evaluation small group" as well as an "internet content security committee," with party members serving as content "gatekeepers"

and overseeing editing, auditing, technology, products, marketing, commercialization, and other operational areas across the company.<sup>224</sup>

The Beijing CAC also prescribed integrating the party organization with company management by creating a "triple-hatted position incorporating the roles of party secretary, editor-inchief, and vice president."<sup>225</sup>

# Chief Editor and Party Secretary Zhang Fuping

Zhang Fuping joined ByteDance as deputy chief editor of Today's Headlines in 2016 and rose to chief editor the following year.<sup>226</sup> Zhang Fuping is not listed as the company's party secretary on either the Chinese or English versions of ByteDance's website. Nor does the company identify him as the business's top-ranked official for political matters. Nevertheless, following a content crackdown on the company in March 2018, he started making public appearances as not just ByteDance chief editor but also as party secretary.<sup>227</sup> Zhang was appointed a board member of the Beijing Douyin Information Service Ltd. in April 2021 alongside the CAC's Wu Shugang.<sup>228</sup>

Zhang also serves as executive vice president at the Beijing Communication Industry Association, of which Beijing Douyin Information Service is a member.<sup>229</sup> It is worth noting that the association "uses Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era as an operational guide."<sup>230</sup>

### 5.2 THE MILITARY-PROPAGANDA NEXUS

ByteDance claims that the company "does not produce, operate or disseminate any products or services related to surveillance." However, the ByteDance platform Douyin, TikTok's analogue in China, serves Beijing's security and repression systems in direct and explicit ways.

Through its network of subsidiaries, ByteDance cooperates with military organs on propaganda work. In November 2017, the People's Armed Police, a paramilitary organization that reports to the Xi-led Central Military Commission, signed a cooperation agreement with Today's Headlines. Chief editor Zhang Fuping was pictured at a signing ceremony with the director of the Political Work Department in the People's Armed Police, Yan Xiaodong. A year and a half later, the People's Armed Police announced their forces would be joining Douyin to "spread the positive energy of the People's Armed Police."

ByteDance also engages in formal cooperation with the Ministry of Public Security (MPS), supporting the MPS to influence and guide public opinion and to provide propaganda that portrays the MPS as being in service to citizens.

Built from the CCP's analogues of Stalin's secret police, the MPS combines traditional police roles with the prosecution of political dissent.<sup>234</sup> It is tasked with investigating ideological crimes (including elastic interpretations of inciting the subversion of state power) alongside ordinary crimes recognized and prosecuted in liberal democracies.

ByteDance is not merely a passive host for public security accounts on its Today's Headlines and Douyin platforms. The company offers expert guidance and big data analysis to assist the MPS in its dissemination of propaganda.

In April 2019, the MPS Information and Propaganda Bureau signed a strategic cooperation framework agreement with ByteDance, as the Australian Strategic Policy Institute first reported. According to a social media account run by the Public Security Bureau of Yangshan County, Guangdong:

[T]he strategic cooperation agreement aims to maximise [Today's Headlines'] and Douyin's specialised technology and platform advantages in big data analysis, accuracy of push notifications, and creative strategy. The cooperation agreement would . . . elevate public security propaganda in its capacity to influence, guide, and gain public trust . . . creating positive public opinion as an environment for the development and progress of public security work in the new era.<sup>235</sup>

ByteDance's collaboration with the MPS extends to Xinjiang, where it plays a role in disseminating party propaganda. According to a report by the Australian Strategic Policy Institute, Xinjiang local authorities received guidance to use Douyin to broadcast a sanitized depiction of state poverty alleviation policies in Hotan, a region of Xinjiang with roughly a dozen suspected detention centers for Uyghur Muslims and other minorities.<sup>236</sup>

ByteDance has also been involved in party-state efforts to whitewash the internment of Uyghurs in Xinjiang, where the United Nations has found that the CCP's repression of minority ethnic groups may amount to "crimes against humanity," the most serious allegation the body is able to make, absent an International Criminal Court investigation.<sup>237</sup>

## 5.3 BYTEDANCE OPERATIONAL TIES TO THE PROPAGANDA SYSTEM

ByteDance and key company executives are members of media associations established to ensure compliance with party norms. Institutional ties include the following:

- Kelly Zhang, CEO of Douyin Group, is vice president of the China Netcasting Services
   Association, of which Beijing ByteDance Network Technology is a member.<sup>238</sup> Nie Chenxi,
   former deputy chief of the Central Propaganda Department and a member of the 19th
   CCP Central Committee, is president of the association.<sup>239</sup> The CCP Central Committee's
   Propaganda Department controls the National Radio and Television Administration (NRTA),
   which supervises the China Netcasting Services Association.<sup>240</sup> As the largest professional
   association in the industry, China Netcasting Services Association publishes mandatory
   standards for online short video platforms.<sup>241</sup>
- Party secretary and chief editor Zhang Fuping serves as executive vice president at the Beijing Communication Industry Association, of which Beijing Douyin Information Service is a member.<sup>242</sup> The association "uses Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era as an operational guide."<sup>243</sup>

- ByteDance is a member of the People's Daily Smart Media Research Institute. One key purpose of the institute is to explore how to use AI in media operations, including "using mainstream values to control the algorithm, so as to comprehensively improve capacity to guide public opinion."<sup>244</sup>
- Beijing Douyin Information Service is an executive corporate member of the Internet Society of China (ISC). One of ISC's goals is to "participate in the formulation of global internet policies, norms and standards, improve the global internet governance system, and maintain cyberspace order."<sup>245</sup>

Outside of institutional ties, a notable number of employees have worked for party propaganda outfits before joining TikTok and ByteDance. In August 2022, *Forbes* reported that its analysis of public LinkedIn profiles showed "300 current employees at TikTok and its parent company ByteDance previously worked for Chinese state media." ByteDance and TikTok did not challenge the report's findings.

#### 5.4 PARTY INSTRUCTION AND SUPERVISION

Beijing's cyber authorities mobilize and monitor internet companies such as ByteDance in times of crisis, such as during COVID-19 and the protests against the government's Zero COVID restrictions. Examples include the following:

In February 2020, as the party mobilized against COVID-19, the CAC placed ByteDance (among other internet companies) under "special supervision" to ensure support for "a good internet environment for winning the battle of COVID prevention and control."<sup>247</sup>

ByteDance was responsive to party calls from the Wuhan Internet Industry Party Committee—and from Xi Jinping himself—to crack down on COVID misinformation, antigovernment sentiment, foreign reporting, and other "harmful information," as defined by the party. By late February 2020, ByteDance had set up channels on Douyin, Today's Headlines, and its other apps for "broadcasting positive energy" and information about the government's epidemic control efforts.<sup>248</sup>

More recently, on December 1, 2022, after antilockdown protests across major cities in China, the CAC instructed tech companies such as ByteDance to "expand censorship of protests," pay attention to content about antigovernment protests, and restrict information about how to use VPNs to circumvent state internet controls. At an internal meeting, the CAC instructed ByteDance to increase staffing of censorship teams, according to insiders who spoke to the Wall Street Journal.<sup>249</sup>

#### 5.5 SURVEILLANCE TECH PARTNERS

As described previously (see section 5.2), ByteDance whitewashes Ministry of Public Security work in Xinjiang and broadcasts sanitized depictions of the region. In business operations

and research, ByteDance has cooperated with companies identified as part of the military-industrial-surveillance complex enabling repression in Xinjiang:

## Leon Technology

On the US Entity List since 2019 for ties to repression in Xinjiang. ByteDance cooperates with Leon Tech in data centers.<sup>250</sup>

#### SenseTime

On the US Entity List since 2019 for alleged ties to repression in Xinjiang. Sanctioned by Washington again in 2021 for ties to Beijing's military-industrial complex. ByteDance used facial recognition technology developed by SenseTime.<sup>251</sup>

# Dawning Information Industry, a.k.a. Sugon

A subsidiary of the Chinese Academy of Sciences sanctioned for ties to Beijing's military-industrial complex and enabling repression in Xinjiang. ByteDance was a major client of Sugon cloud services. Sugon also makes data centers for ByteDance.<sup>252</sup>

## *iFlytek*

On the US Entity List since 2019 for enabling repression in Xinjiang.<sup>253</sup> ByteDance uses iFlytek for voice synthesis technology and music on Douyin and for office collaboration products on Feishu.<sup>254</sup>

## Megvii

Sanctioned by Washington in 2019 and 2021, as noted above. ByteDance collaborated with Megvii on computer vision research.<sup>255</sup>

#### 5.6 SERVING THE MINISTRY OF PUBLIC SECURITY

ByteDance's flagship China products—Douyin and Today's Headlines—serve as resources for surveillance, particularly for China's Ministry of Public Security (MPS).

In 2015, the MPS announced a raft of internet measures, including cybersecurity bureaus for major websites and major internet enterprises. The cybersecurity bureaus target cybercrime, including the party-defined offence of spreading rumors.<sup>256</sup>

In September 2018, ByteDance party secretary Zhang Fuping announced Douyin's integration with the MPS Network Security and Protection Bureau. The cybersecurity bureaus, together with Douyin and Douyin users, would collaborate to clean up cyberspace and promote the constructive environment of platform governance.<sup>257</sup>

The strategic cooperation agreement between ByteDance and the MPS signed in April 2019 includes a clause for Douyin to cooperate with public security organs and jointly plan "offline

activities."<sup>258</sup> The agreement is vague on the meaning of cooperation and joint planning. But ByteDance's 2019 CSR report documented the company's efforts in establishing an "integrated linkage mechanism [joining] behavior recognition, online confrontation, and cooperation with public security agencies to crack down on behavior offline."<sup>259</sup>

There is evidence of arrests made on the basis of ByteDance cooperation with the security services. ByteDance claims that it has aided in solving police cases, some involving hundreds of arrests, facilitated by an in-house official police cybersecurity team. According to ByteDance's 2022 Anti-Fraud Report, as reported by state media, between January 2021 and March 2022, Douyin helped public security organs capture 140 fraud-related criminal gangs, arrest 576 suspects, and solve more than 800 cases.<sup>260</sup>

#### 5.7 A POLITICAL INTERFERENCE BELLWETHER

ByteDance is a PRC company, and ByteDance is subject to all the influence, guidance, and de facto control to which the Chinese Communist Party now subjects all PRC technology companies. CCP and PRC state agencies (together, the party-state) have extended their ties into ByteDance to the point that the company can no longer be accurately described as a private enterprise.

While TikTok is a household name, its analogue in China, Douyin, is not. TikTok claims to be its own insulated entity; however, research indicates that TikTok and Douyin share personnel and technological resources, have parallel management structures, and permit data sharing with each other. Review of Chinese-language sources indicates that ByteDance founder Zhang Yiming hasn't just relinquished his role as CEO but has also given up all his shares in Douyin, after years of party pressure. This recalls Jack Ma, who gave up his role at Alibaba before giving away his Ant Group shares. This opacity and obfuscation are now compounded by what appears to be a concerted campaign to airbrush what little material was available online recounting Communist Party activities inside ByteDance.

ByteDance does not publicize that its editor-in-chief, Zhang Fuping, is also its Communist Party secretary. His guidance is clear: "Transmit the correct political direction, public opinion guidance, and value orientation into every business and product line." <sup>262</sup> Chief editor and party secretary Zhang Fuping was pictured at a 2017 signing ceremony with the director of the Political Work Department of the People's Armed Police, the CCP's domestic paramilitary force. According to a 2019 announcement, Douyin would help to "spread the positive energy of the People's Armed Police." <sup>263</sup>

ByteDance says it "does not produce, operate, or disseminate any products or services related to surveillance." But Douyin, TikTok's analogue in China, directly aids party propaganda and repression, and its top leaders are "double hatted" in official propaganda organizations. That ByteDance has a party secretary who is also "chief editor" is just one strand of a web of personnel connections designed to integrate ByteDance into the state propaganda system. The biggest risks, however, involve TikTok's unprecedented potential for shaping narratives and curating overseas political landscapes. ByteDance has a demonstrated record of

adopting norms in service of party propaganda. TikTok, in turn, has faced increasing scrutiny in democratic capitals for several years, dating most significantly to the Trump administration's August 2020 attempt to ban the app altogether.

The party's leverage over TikTok gives it vast potential to sway elections, corrode people's faith in self-government, and undermine the will of open societies to compete against China's authoritarian model globally. Beijing could use these platforms' big data on overseas public opinion to establish an internal early-warning system and generate highly effective targeted propaganda, aided by Al.

US intelligence agencies have signaled clear concerns with China's data cultivation, influence, and interference activities. The US National Intelligence Council, a formal panel of intelligence officers and independent scholars, provides an assessment:

Beijing will be able to exploit Chinese companies' expansion of telecommunications infrastructures and digital services, these enterprises' growing presence in the daily lives of populations worldwide, and Beijing's rising and global economic and political influence. Beijing has demonstrated its willingness to enlist the aid of Chinese commercial enterprises to help surveil and censor regime enemies abroad.<sup>265</sup>

Also toward the end of 2022, key US national security officials intensified their warnings about TikTok. In November, FBI chief Chris Wray stated that the FBI has "a number of concerns" regarding TikTok as a "national security threat":

They include the possibility that the Chinese government could use it to control data collection on millions of users or control the recommendation algorithm which could be used for influence operations if they so chose, or to control software on millions of devices which gives it the opportunity to potentially technically compromise personal devices.<sup>266</sup>

On December 3, Director of National Intelligence Avril Haines addressed TikTok at the Reagan National Defense Forum:

It is extraordinary the degree to which China, in particular . . . [is] developing just frameworks for collecting foreign data and pulling it in and their capacity to then turn that around and use it to target audiences for information campaigns or for other things, but also to have it for the future so that they can use it for a variety of means that they're interested in.<sup>267</sup>

On December 16, CIA Director William Burns echoed such concerns:

I think it's a genuine concern, I think, for the U.S. government, in the sense that, because the parent company of TikTok is a Chinese company, the Chinese government is able to insist upon extracting the private data of a lot of TikTok users in this country, and also to shape the content of what goes on to TikTok as well to suit the interests of the Chinese leadership. . . . What I would underscore, though, is that it's genuinely troubling to see what the Chinese government could do to manipulate TikTok.<sup>268</sup>

TikTok poses risks that may impact not only the data privacy of individual users but also social cohesion, democratic functioning, and the national security interests of democratic nations including the United States.

The Biden administration faces a difficult test over TikTok. The app has been under review by CFIUS for more than three years and clearly raises national security concerns that Biden said he would address in his 2021 Executive Order on "Protecting Americans' Sensitive Data from Foreign Adversaries." However, CFIUS is reportedly buffeted by disagreements between economic and national security officials. Congressional efforts to ban TikTok are still in their infancy. Fundamental questions remain about the viability of legislating a ban; for example, could a majority of a Republican-led House and a Democratic-led Senate come together to do this at all?

Given the company's potential value—and related regulatory hazards—in the event of an IPO, TikTok is perhaps the central bellwether for investment and regulatory dynamics involving China, the tech market, and dataflows. So much about the party's organizational structures, and legal and extralegal mechanisms for influencing, coercing, and controlling nominally privately owned technology companies like parent company ByteDance only amplifies those risks further.

# 6. THE NEW CHINA RULES: MANAGING THE INHERENT RISKS OF HYBRID CORPORATE STRUCTURES

The profiles of Alibaba and ByteDance as private companies can be misleading for investors and partners due to internal structures of party governance and numerous state linkages, particularly in highly sensitive areas of military, surveillance, propaganda, and data. These case studies illustrate the way many of the PRC's private companies have nonprivate dimensions that are difficult to assess. Their governance and operational structures are shrouded from regulators, investors, and the public generally. Their PR, management, and legal counsels generate information asymmetries—regulatory reporting, statements to media, and management of investor relations—that make it difficult for foreign investors and governments to accurately assess their operations. US regulators, for example, cannot effectively determine how to apply a range of new laws intended to protect national security from risks posed by foreign adversaries, including the People's Republic of China. These risks potentially include the following:

 Exploitation of vulnerabilities in information and communications technology and services (ICTS)<sup>271</sup>

- Illegal use of US capital markets and investment by military-industrial and surveillance companies<sup>272</sup>
- Theft and abuse of sensitive individual data through connected apps<sup>273</sup>
- Cyberattacks against critical infrastructure and industrial control systems<sup>274</sup>
- Backlash against investors who invest in PRC companies later discovered to pose national security and personal data risks

The party's assimilation of China's best-known Big Tech firms may be best explained only in light of a longer-term, centrally directed shift toward imposing hidden but powerful structures of CCP control inside private enterprise, at the expense of the visible structures of corporate control, including those reflected in securities filings. The power of the party's internal systems of committees and cells is reinforced by external levers, both legal (through mechanisms of the state) and extralegal (through the party's own mechanisms, which sit outside the legal system).

The result has been a new type of corporate organization that is so poorly understood as to lack a recognized name. Neither state-owned nor private, companies like Alibaba are hybrid entities that are effectively state-controlled. In these companies' true governance structure, the CCP is not only taken into account by decision makers but appears to be deeply integrated into decision-making structures, from the executive level down to individual business divisions. This is not about micromanaging decisions about technology or commerciality. It is about controlling strategic decisions and helping to shape the way lesser decisions are made, all the way down.

In the case of Alibaba's Jack Ma and ByteDance's Zhang Yiming, both may be allowed to continue as dominant shareholders. Or they may not. But true control of strategic decision making may have long since passed to figures like former public security official Shao Xiaofeng and elusive, state-adjacent figures with ambiguous roles like Zhang Fuping.

The implications for foreign counterparties include the following:

• Corporate absorption by the party could cut both ways for long-term profitability. Clearly the assertion of internal and external mechanisms of political control exposes new risks to capital and threatens innovation as companies are pressed to diversify beyond their core competencies. Political forces of regulation have already been responsible for stunning slides in market capitalization and mediocre post-Zero COVID recoveries. But the party's insertion of itself inside companies may also provide a form of domestic political insurance—dulling competitive instincts, yet also putting a floor under long-term survival. The ultimate question is, At what net cost to profitability?

- There are also factors beyond the domestic. The spectacle of the party's public
  humiliation of figures like Jack Ma has overshadowed a set of international dynamics
  worth closely tracking; for example, the direction of Chinese politics at home is driving
  China's deepening friction with the United States and other nations—and this, in turn,
  will impose mounting political, regulatory, and reputational costs on Chinese firms and
  their foreign investors and partners.
- The risks include being cut off from foreign technology and intellectual property, being shut out of key foreign markets, and being excluded from global capital markets. These risks are likely to increase as PRC corporate links to the CCP deepen, and as those links become more visible to policymakers, shareholders, and activists in the United States and elsewhere.
- While it's still early days, the cases of Alibaba/Ant and ByteDance may point to the
  center of a wider political campaign that risks deepening into a full mobilization of
  private capital in support of Xi's increasingly ambitious military and geopolitical aims.
   With the party poised to coordinate the economy in this manner, investors will need to
  navigate a fluid new political order in what has been the most dynamic and profitable
  segment of China's economy.

PRC corporate partnerships with government, particularly when they serve as extensions of government functions, can of course be good for business. But navigating complexities is becoming harder not only at home but also abroad as burgeoning tech multinationals manage significant business lines, commercial and technology partnerships, stakes in other tech firms, and other interests. The PRC's private sector long faced no international reputational or political tax for links to the CCP. On the contrary, its firms' status as a new breed of national champion boosted their standing overseas. But this has begun to change—and could shift dramatically as Beijing's relations with the world grow more rivalrous.

The more that PRC private firms are seen to be run by the party, the less they will be able to benefit from their former image as the innovative champions of China's nonstate economy, and the more their operations will face regulatory barriers and other costs overseas. These changes in the investment environment are not being driven only by US-China rivalry. Other countries have their own disputes and sources of friction with Beijing, and all are attuned to the spectacle of Jack Ma, the party crackdown on big tech, the PR-augmented opacity of ByteDance, and the fast-shifting landscape of corporate control in Xi Jinping's China.

#### **NOTES**

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