



Chambers Global Practice Guides

Definitive global law guides offering
comparative analysis from top-ranked lawyers

Corporate Governance 2022

China: Law & Practice
Yunjian Hou
Global Law Office

practiceguides.chambers.com

Law and Practice

Contributed by:

Yunjian Hou

Global Law Office see p.16

CONTENTS

1. Introductory	p.3	4.8	Consequences and Enforcement of Breach of Directors' Duties	p.9	
1.1	Forms of Corporate/Business Organisations	p.3	4.9	Other Bases for Claims/Enforcement Against Directors/Officers	p.9
1.2	Sources of Corporate Governance Requirements	p.3	4.10	Approvals and Restrictions Concerning Payments to Directors/Officers	p.10
1.3	Corporate Governance Requirements for Companies With Publicly Traded Shares	p.3	4.11	Disclosure of Payments to Directors/Officers	p.10
2. Corporate Governance Context	p.4	5. Shareholders	p.10		
2.1	Key Corporate Governance Rules and Requirements	p.4	5.1	Relationship Between Companies and Shareholders	p.10
2.2	Environmental, Social and Governance (ESG) Considerations	p.4	5.2	Role of Shareholders in Company Management	p.11
3. Management of the Company	p.5	5.3	Shareholder Meetings	p.11	
3.1	Bodies or Functions Involved in Governance and Management	p.5	5.4	Shareholder Claims	p.12
3.2	Decisions Made by Particular Bodies	p.5	5.5	Disclosure by Shareholders in Publicly Traded Companies	p.12
3.3	Decision-Making Processes	p.6	6. Corporate Reporting and Other Disclosures	p.13	
4. Directors and Officers	p.6	6.1	Financial Reporting	p.13	
4.1	Board Structure	p.6	6.2	Disclosure of Corporate Governance Arrangements	p.13
4.2	Roles of Board Members	p.6	6.3	Companies Registry Filings	p.14
4.3	Board Composition Requirements/ Recommendations	p.7	7. Audit, Risk and Internal Controls	p.14	
4.4	Appointment and Removal of Directors/Officers	p.7	7.1	Appointment of External Auditors	p.14
4.5	Rules/Requirements Concerning Independence of Directors	p.8	7.2	Requirements for Directors Concerning Management Risk and Internal Controls	p.14
4.6	Legal Duties of Directors/Officers	p.8			
4.7	Responsibility/Accountability of Directors	p.9			

1. INTRODUCTORY

1.1 Forms of Corporate/Business Organisations

There are three principal forms of corporate/business organisation in China, namely:

- companies;
- partnership enterprises; and
- individual proprietorship enterprises.

Only companies have the status of legal persons, and shareholders shall bear liabilities for a company to the extent of their respective subscribed capital contribution/shares. However, if a shareholder abuses the independent legal person status of the company or the shareholder's limited liabilities to evades debts, thereby prejudicing the interests of the creditors of the company, the shareholder shall be jointly and severally liable for the debts of the company.

Companies are classified as limited liability companies and joint stock limited companies. Joint stock limited companies whose shares are listed and traded on a stock exchange are publicly traded companies. Currently, there are three stock exchanges in Mainland China, namely the Shanghai Stock Exchange (SSE), the Shenzhen Stock Exchange (SZSE), and the Beijing Stock Exchange (BSE), which launched trading on 15 November 2021.

1.2 Sources of Corporate Governance Requirements

The principal sources of corporate governance requirements for companies are the Company Law of the People's Republic of China (the "Company Law") and five judicial interpretations of the Company Law. In addition to the laws, judicial interpretations and regulations, the activities of a company and all participants are also governed by the articles of association of the company.

Publicly Traded Companies

Provisions on the supervision and administration of publicly traded companies are numerous and complex. As publicly traded companies are a type of joint stock limited company, the provisions of Chapter 4 of the Company Law, regarding joint stock limited companies, also applies to them. In addition, the organisation and activities of publicly traded companies are also regulated by the Securities Law of the People's Republic of China, the regulatory supervision rules of the China Securities Regulatory Commission (CSRC) and the relevant stock exchanges. The regulations relate to the issuing and trading of securities, corporate governance, disclosure, restructuring and other aspects. In short, publicly traded companies are subject to comprehensive and strict supervision because of their involvement in public interests.

1.3 Corporate Governance Requirements for Companies With Publicly Traded Shares

Corporate governance requirements for companies with publicly traded shares include the following:

- the company shall establish and improve the systems of shareholder meetings, boards of directors, boards of supervisors, independent directors, board secretaries, and special committees in accordance with the law;
- the company shall be encouraged to appoint officers in an open and transparent manner;
- the company shall establish fair and transparent standards and procedures for evaluating the performance of directors, supervisors and officers;
- the company shall establish a mechanism linking remuneration with the company's performance and individual performance;
- the company shall be strictly independent from its controlling shareholder and actual controller in terms of personnel, assets, finan-

- cial affairs, institutions, business, accounting, and assumption of responsibilities and risks;
- decision-making procedures and information disclosure obligations shall be strictly performed in connection with affiliated transactions in accordance with relevant provisions;
 - the company shall establish and implement a management system of information disclosure – it shall make public disclosures on documents such as periodic reports, interim reports, prospectuses, offering prospectuses, listing announcements, acquisition reports, etc; and
 - internal control and risk management systems shall be established.

Corporate governance requirements for companies with publicly traded shares are mainly stipulated in the Code of Corporate Governance of Publicly traded companies. Some requirements are mandatory, while some are voluntary. However, certain provisions seem to be voluntary but in fact have become quasi-mandatory, because companies may be confronted with unnecessary complications if they have not strictly complied with them in the IPO procedure.

2. CORPORATE GOVERNANCE CONTEXT

2.1 Key Corporate Governance Rules and Requirements

Over and above those issues addressed below, there are some other key or typical corporate governance rules and requirements for companies. The requirements are mainly on controlling shareholders and actual controllers of companies, especially those of publicly traded companies, as provided by laws and regulations. For example, the controlling shareholder and the actual controller of a company shall not harm the interests of the company by taking advantage of their associated relationship. Controlling

shareholders of publicly traded companies shall not set pre-approval processes for the personnel election results of shareholder meeting or the personnel appointment resolutions of the board of directors, and shall not disturb the regular decision-making procedures in ways that violate the laws, regulations and articles of associations of companies.

2.2 Environmental, Social and Governance (ESG) Considerations

The current supervision regulations have not imposed compulsory requirements on publicly traded companies to disclose ESG reports but do encourage them to make voluntary disclosure. However, the disclosure of certain special ESG issues is mandatory.

Environmental Issues Reporting

With respect to reporting on environmental issues, a publicly traded company shall disclose, in its annual report, any administrative penalties on it due to environmental issues during the reporting period. A company or its major subsidiary that is a key pollutant discharging entity, as established by the environmental protection department, shall also disclose major environmental information, including:

- pollutant discharge information;
- construction and operation of pollution prevention and control facilities;
- environmental impact assessments of construction projects; and
- other environmental protection administrative licensing.

Companies are encouraged to voluntarily disclose the measures that have been taken to reduce carbon emissions and the effect of such measures during the reporting period.

Social Issues Reporting

With respect to reporting on social issues, companies listed on the SSE or the SZSE, companies listed both onshore and offshore, and financial companies shall disclose a corporate social responsibility report (“CSR Report”) at the same time when disclosing annual reports. Other publicly traded companies are encouraged to disclose a CSR Report. The contents of a CSR Report shall include the construction and implementation of social responsibility systems concerning protection of workers, environmental pollution, quality of commodities, and relationships with relevant communities. In addition, publicly traded companies are encouraged to disclose the active fulfilment of their social responsibilities in consideration of their particular industrial characteristics, such as consolidation and expansion of achievements in poverty alleviation and rural revitalisation.

Governance Issues Reporting

With respect to reporting on governance issues, please see **6.2 Disclosure of Corporate Governance Arrangements** for specific disclosure requirements.

3. MANAGEMENT OF THE COMPANY

3.1 Bodies or Functions Involved in Governance and Management

In China, the principal bodies involved in the governance and management of a company include the shareholder meeting, the board of directors, the board of supervisors, and the manager. The shareholder meeting is the key organ of authority, responsible for making decisions on fundamental issues and electing the main members of the board of directors and the board of supervisors. The board of directors is the executive organ, and the manager is the auxiliary executive organ. The manager is appointed by the board of

directors. The board of directors is responsible for making decisions on day-to-day operation and management, and the manager assists the board of directors in the execution of the company business. The board of supervisors is the supervisory organ, responsible for supervising the execution of business and the company’s financial status.

3.2 Decisions Made by Particular Bodies

Decisions of the Board of Directors

The board of directors is responsible for making decisions on day-to-day operation and management, and shall decide on the following matters:

- determining the company’s business plans and investment programmes;
- determining the establishment of the company’s internal management departments;
- formulating the company’s basic management system; and
- deciding on the hiring or dismissal of the manager and their remuneration.

In addition to its decision-making power over operation, management and personnel matters, the board of directors shall also have the right to formulate plans in respect of the company’s annual budget and final accounts, dividends distribution, loss recovery, increase/decrease of registered capital, issuance of bonds, merger, division, dissolution, or change of the company form, provided that all such plans shall be subject to the review and approval of the shareholder meeting.

Decisions of the Shareholder Meeting

The shareholder meeting is responsible for making decisions on fundamental issues, among which the two most important are:

- electing and replacing directors and supervisors, and determining their remuneration; and

- amending the articles of association of the company.

In addition, the shareholder meeting shall also have the right to review and approve the plans formulated by the board of directors, such as plans for the company's annual budget and final accounts, dividends distribution, loss recovery, etc. If a publicly traded company purchases or sells significant assets, or guarantees an amount exceeding 30% of the company's total assets within one year, such actions must be authorised by resolutions of the shareholder meeting.

In addition, a publicly traded company shall state principles of authorisation by the shareholder meeting to the board of directors in its articles of association, and the contents of the authorisation shall be clear and detailed. The shareholder meeting shall not authorise the statutory functions or powers to the board of directors.

3.3 Decision-Making Processes

The shareholder meeting or the board of directors shall make decisions by convening meetings to review and vote on relevant matters and form a resolution. However, if shareholders unanimously agree in writing (all shareholders sign and seal on the resolution documents), it is possible not to convene a shareholder meeting.

Normally, meetings of the board of directors shall be convened and presided over by the chairman of the board. When the board of directors votes on a resolution, each director shall have one vote. Furthermore, the board of directors of a joint stock limited company shall convene at least two meetings a year, which must be notified to all directors and supervisors ten days in advance. Shareholders representing more than a tenth of voting rights, or more than a third of the board of directors or supervisors may propose to convene an interim meeting of the board of directors. The chairman shall convene and pre-

side over the meeting within ten days of receipt of such proposal. No meeting of the board of directors can be held unless more than half of the directors are present. When the board of directors makes a resolution, it shall be adopted by more than half of all the directors.

With respect to the shareholder meeting, please see **5.3 Shareholder Meetings** for its decision-making processes.

4. DIRECTORS AND OFFICERS

4.1 Board Structure

The board of directors in a limited liability company shall consist of three to 13 members, while a smaller limited liability company or a limited liability company with fewer shareholders may have an executive director, but without the board of directors. The board of directors in a joint stock limited company shall consist of five to 19 members. A publicly traded company shall have independent directors and board secretaries. The board of directors shall establish an audit committee, and may establish special committees of strategy, nomination, remuneration and assessment.

4.2 Roles of Board Members

The board of directors shall be presided over by a chair, and may have one or more vice-chairs. The chair shall be responsible for presiding over shareholder meetings, convening and presiding over meetings of the board of directors and inspecting the implementation of resolutions of the board. A vice-chair assists the chair in their work. If the chair cannot or does not carry out their duties, such duties shall be carried out by the vice-chair; if the vice-chair cannot or does not carry out their duties, the duties shall be carried out by a director jointly elected by more than half of the directors.

Members of the board of directors in wholly state-owned companies shall include representatives of the employees, and the Company Law allows employees to take positions of members of the board of directors in other limited liability companies and joint stock limited companies, although this is not very common in practice.

A publicly traded company shall have independent directors and board secretaries. Independent directors shall be responsible for supervising the directors and officers, and shall report their work to the shareholder meeting annually. The board secretary shall be responsible for the preparation for shareholder meetings and meetings of the board of directors, custody of documents, management of shareholders' materials, disclosure of information, investor relations and other matters.

4.3 Board Composition Requirements/ Recommendations

The board of directors shall consist of directors, whose terms of office shall be specified by the articles of association of the company, provided that each term of office shall not exceed three years. Upon expiration of a director's term of office, a director can serve another term if re-elected.

A person may not serve as a director of a company in any of the following circumstances:

- they are without civil capacity or have limited civil capacity;
- they have been sentenced to criminal penalties for corruption, bribery, embezzlement or misappropriation of property or for sabotaging the socialist market economy order, and less than five years has elapsed since the expiration of the period of execution;
- they have been deprived of their political rights for committing a crime and less than

five years has elapsed since the expiration of the period of execution;

- they have served as a director or manager of an enterprise that has been declared bankrupt and bear personal responsibility, and less than three years has elapsed since the date of completion of the bankruptcy liquidation;
- they have served as the legal representative of an enterprise whose business licence has been revoked due to a violation of law and bear personal responsibility, and less than three years has elapsed since the date of the revocation of business licence; and
- they have a large amount of debt, which is due but has not been repaid.

In addition to those listed in **4.1 Board Structure** and **4.2 Roles of Board Members**, members of the board of directors shall have the knowledge, skills and qualities that are necessary for the performance of their duties. Furthermore, diversity of members of the board of directors is encouraged.

4.4 Appointment and Removal of Directors/Officers

The method of appointing the chair and vice-chair of the board of directors in a limited liability company shall be stipulated in the articles of association of the company. In practice, the chair and vice-chair can be elected or recommended by the shareholder meeting or the board of directors. The chair and vice-chair of the board of directors in a joint stock limited company are elected by more than half of all the directors on the board of directors.

The representatives of the employees shall be democratically elected by the employees through the employees' congress, the employees' meeting or in other ways. The directors that are not the representatives of the employees shall be appointed and removed by the shareholder meeting.

The manager shall be appointed and removed by the board of directors. The appointment and removal of the deputy manager and chief financial officer shall be recommended by the manager and decided by the board of directors. The appointment and removal of other officers shall be decided by the manager.

4.5 Rules/Requirements Concerning Independence of Directors

The rules and requirements concerning the independence of directors are mainly applicable to publicly traded companies. According to the regulatory supervision rules, publicly traded companies shall establish rules for independent directors. At least a third of members of the board of directors in a publicly traded company shall be independent directors. Independent directors shall constitute a majority of the members of the audit committee, the nomination committee and the remuneration and assessment committee, and shall act as the convener therein. Independent directors must have independence, which means they shall perform their duties and responsibilities independently, without interference from the major shareholders, the actual controller, or other entities or individuals that are interested parties of the publicly traded company.

Independent Director Requirements

In principle, an individual may concurrently hold the position of independent director in no more than five publicly traded companies. The following persons may not hold the position of independent director:

- those who hold a position in the publicly traded company or one of its subsidiaries, or where their immediate family members or persons with whom they have major social relations do so;
- natural person shareholders who directly or indirectly hold more than 1% of the issued

shares of the publicly traded company or who rank in the top ten shareholders of the publicly traded company, and their immediate family members;

- those who hold a position in entities that directly or indirectly hold more than 5% of the issued shares of the publicly traded company or that rank in the top five shareholders of the publicly traded company, and their immediate family members;
- those to whom any of the circumstances in the three pullet points above have applied in the last year; and
- those who provide financial, legal, consulting or other services to the publicly traded company or its subsidiaries.

A person holding the position of independent director shall meet the following basic conditions:

- qualified to hold the position of a director of a publicly traded company;
- possessing a basic knowledge of operation of publicly traded companies;
- familiar with relevant laws, administrative regulations, rules and regulations of publicly traded companies; and
- having more than five years of working experience in law, economics or another field giving them the experience necessary for performing the duties of an independent director.

4.6 Legal Duties of Directors/Officers

The principal legal duties of directors and officers of a company are their duties of loyalty and diligence to the company. The duty of loyalty requires that directors and officers shall not take advantage of their position to pursue illegitimate interests, among which some important restrictions are that:

- directors and officers shall not enter into contracts or engage in transactions with the

company they are serving in violation of the articles of association or without the consent of shareholder meetings;

- without consent of shareholder meetings, directors and officers shall not seek business opportunities that would have belonged to the company for themselves or others by taking advantage of their position; and
- without consent of shareholder meetings, directors and officers shall not engage in business that is similar to the company's, for themselves or others.

The duty of diligence requires that directors and officers shall perform their duties with reasonable care in the best interests of the company, including:

- timely understanding the operation and management of the company's business;
- diligently exercising the powers granted by the company to ensure that the commercial activities of the company comply with the requirements of laws, administrative regulations and various economic policies; and
- ensuring the commercial activities do not go beyond the scope of business stipulated in the business licence.

4.7 Responsibility/Accountability of Directors

The board of directors is responsible for the shareholder meeting, and the directors owe duties of loyalty and diligence to the company. Directors are required to take into account the overall interests of the company and the interests of all shareholders when discharging their duties. In publicly traded companies, the directors shall pay special attention to the interests of the minority shareholders, as well as other interested parties, such as creditors, employees, clients, suppliers and communities, etc.

4.8 Consequences and Enforcement of Breach of Directors' Duties

If directors or officers breach their duties and thereby cause losses to the company, any income arising from the breach shall belong to the company and the directors or officers shall be liable to compensate the company. In such a situation, the company may file a lawsuit with the people's court. Shareholders holding equities of a limited liability company, or shareholders individually or collectively holding more than 1% of shares of a joint stock limited company for more than 180 consecutive days may request the board of supervisors in writing to file a lawsuit with the people's court. If the board of supervisors does not file a lawsuit, a shareholder satisfying the aforesaid conditions has the right to file a lawsuit with the people's court in their own name directly, in the interests of the company. In an emergency, instead of requesting the board of supervisors to file suit, the shareholder may do so directly. If directors or officers breach their duties and thereby cause losses to shareholders, the directors or officers shall be responsible to compensate the shareholders, who may file a lawsuit with the people's court.

Directors and officers of publicly traded companies may also be subject to administrative punishment from the CSRC due to false statements, breach of promises, insider trading and manipulation of the market, and shall be responsible to compensate the investors who have suffered losses as a result of such conduct.

4.9 Other Bases for Claims/ Enforcement Against Directors/Officers

There are other bases for claims or enforcement against directors or officers for breaches of corporate governance requirements; for example, directors shall be responsible for resolutions of the board of directors. If a resolution of the board of directors violates laws, administrative regulations, the articles of association of the com-

pany or resolutions of shareholder meetings, the shareholders may petition the people's court to invalidate or revoke the resolutions. If the company suffers serious losses as a result thereof, the directors who participated in the adoption of such resolutions are responsible for compensation. However, the liability of a director or officer can be limited. If a director can prove that they expressed an objection to such resolutions in the vote, and their objection was recorded in the minutes of the meeting on that resolution, then such director can be exempted from liability.

4.10 Approvals and Restrictions Concerning Payments to Directors/Officers

According to the Company Law, remuneration, fees or benefits payable to directors are decided by the shareholder meeting. Payments to the manager are decided by the board of directors, and payments to the deputy manager and chief financial officer are decided by the board of directors upon proposals by the manager.

In a publicly traded company, when the board of directors or the remuneration and assessment committee is evaluating the performance of a director or is discussing their compensation, the director shall not participate in such evaluation or discussion. The remuneration distribution plan for officers shall be approved by the board of directors, explained at shareholder meetings and fully disclosed.

Publicly traded companies shall provide appropriate allowances to independent directors. The proposed standard of such allowances shall be formulated by the board of directors, then reviewed and approved by the shareholder meeting, and disclosed in the annual report of the company. In addition to the above mentioned allowances, independent directors shall not accept additional, undisclosed benefits from the publicly traded company, its major share-

holders or entities/individuals that are interested parties of the company.

4.11 Disclosure of Payments to Directors/Officers

A joint stock limited company shall regularly make public disclosures in relation to the remuneration, fees or benefits payable to directors and officers. A publicly traded company shall disclose the appointments, changes of shareholding and annual remuneration of its directors and officers in its annual report, including but not limited to:

- decision-making procedures, the basis of determination and the actual payment of the remuneration;
- the total amount of pre-tax remuneration received from the company and the aggregates of all the directors and officers; and
- whether or not the directors and officers receive remuneration from affiliated parties of the company.

5. SHAREHOLDERS

5.1 Relationship Between Companies and Shareholders

Shareholders mainly have the following rights with regard the company.

- The right to income:
 - (a) dividend claims;
 - (b) residual claims;
 - (c) pre-emptive rights for new shares;
 - (d) dissenting shareholders' right to request repurchase of shares; and
 - (e) pre-emptive rights for shares sold by other shareholders in limited liability companies.
- Voting rights and related rights:
 - (a) voting rights;
 - (b) rights to attend shareholder meetings;

- (c) rights to propose to convene interim shareholder meetings and meetings of the board of directors;
 - (d) rights to convene and preside over shareholder meetings; and
 - (e) rights of proposal.
- The right to know and other rights.

The shareholders' principal obligation to the company is to invest capital. In addition, the shareholders (i) shall exercise the shareholders' rights in accordance with laws, administrative regulations, and the articles of association of the company; and (ii) shall not to abuse their rights to damage the interests of the company or other shareholders. Moreover, the shareholders shall not abuse the independent legal person status of the company and limited liabilities of shareholders to damage the interests of the company's creditors.

5.2 Role of Shareholders in Company Management

Ownership of companies is somewhat separated from management rights. The managers are responsible for the operation and management of the company, while as owners of the company, shareholders normally do not directly participate in the daily operation and management of the company. Their management in a company is indirect; ie, they shall, in accordance with the procedures provided by laws and the articles of association of the company, exercise their rights in a collective manner by participating in shareholder meetings and voting on proposals. The shareholders may make decisions on fundamental issues and elect the main members of the board of directors by exercising their voting rights and thereby control the company.

5.3 Shareholder Meetings

The shareholder meetings of a limited liability company are divided into regular meetings and interim meetings. Regular meetings shall

be convened in accordance with the articles of association of the company. Interim meetings shall be convened upon proposal by the shareholders representing more than a tenth of voting rights, more than a third of directors or the board of supervisors. Generally, shareholder meetings are convened by the board of directors and presided over by the chairman of the board. If there is no special provision in the articles of association of the company, all the shareholders shall be notified 15 days before a shareholder meeting is held and the shareholders shall exercise their voting rights in proportion to capital contribution at the meeting. According to the Company Law, resolutions on amendment of the articles of association, increase/decrease of registered capital, merger, division, dissolution, or change of the company form shall be approved by shareholders representing more than two thirds of voting rights.

Shareholder meetings of a joint stock limited company shall be held once a year. An interim shareholder meeting shall be held within two months under any of the following circumstances:

- the number of directors is less than two thirds of the number required by the Company Law or the articles of association of the company;
- the company's uncovered losses amounted to a third of its paid-up capital;
- shareholders individually or collectively holding more than 10% of the company's shares make a request;
- the board of directors deems it necessary; and
- the board of supervisors proposes to hold it.

A meeting hall shall be set up for the shareholder meeting, and the meeting shall be held by way of combining an on-site meeting and network voting. All the shareholders shall be notified of the time, the place and the agenda of the shareholder

er meeting 20 days in advance of a regular meeting or 15 days in advance of an interim meeting. For a publicly traded company where a single shareholder and any persons acting in concert with them hold more than 30% of the shares, the cumulative voting system shall be adopted in the election of directors and supervisors at the shareholder meeting; ie, each share shall have the same number of voting rights as the number of directors or supervisors to be elected, and the voting rights held by shareholders may be exercised cumulatively.

5.4 Shareholder Claims

Normal claims of shareholders against the company are asserted in situations where shareholders' rights have been infringed. The common claims include:

- requesting the company to distribute dividends;
- requesting confirmation of the non-existence, invalidity or revocation of the resolution of the shareholder meeting or the board of directors; and
- requesting the inspection or copying of certain documents or materials of the company.

In addition, investors of a publicly traded company who have suffered losses in securities trading due to the company's false statement have the right to sue the company for compensation.

The base of a claim for shareholders against the directors is the directors' breach of their duties of loyalty and diligence, which has led to damage to the interests of the shareholders or the company. The shareholder may claim damages against the directors in their own name for the company's interests. Investors in a publicly traded company, who have suffered losses in securities trading due to the company's false statement, the directors' breach of promises, insider

trading or manipulation of the market, have the right to sue the directors for compensation.

5.5 Disclosure by Shareholders in Publicly Traded Companies

According to the regulatory supervision rules, a shareholder or actual controller of a publicly traded company shall inform the board of directors and co-operate with the company in performing information disclosure obligations under any of the following circumstances:

- a relatively significant change in the control of the company, or the shareholding of shareholders who hold more than 5% of the company's shares, or the actual controller;
- a relatively significant change in the situation of engagement in business identical or similar to the company that is taken by the company's actual controller and other enterprises controlled by the actual controller;
- the controlling shareholder was prohibited from transferring their shares by a court's ruling or judgment;
- more than 5% of the company's shares held by any shareholder are pledged, frozen, judicially auctioned, kept in custody, established in trust, or their voting rights are restricted, or there is a risk of being forced to transfer ownership; and
- a plan to significantly restructure assets or business of the publicly traded company.

Where the controlling shareholder or actual controller of a publicly traded company plays an important role in the occurrence or progress of a significant event which may have a great influence on the trading prices of the company's securities and derivatives, the controlling shareholder or actual controller shall inform the company of the relevant situation in writing in a timely manner, and co-operate with the company in performing information disclosure obligations, including the cause, current status and possi-

ble impact of the disclosed event. In addition, when a publicly traded company's controlling shareholder or actual controller makes a public promise, such a promise shall be disclosed.

6. CORPORATE REPORTING AND OTHER DISCLOSURES

6.1 Financial Reporting

Companies are subject to annual and interim financial reporting requirements. According to the regulatory supervision rules, an annual report shall record the key accounting data and financial indicators, and the full text of the financial statement and the audit report. An interim report shall record the key accounting data and financial indicators, and the financial statement. An annual report shall be prepared and disclosed within four months from the end of each fiscal year, and an interim report shall be prepared and disclosed within two months from the end of the first half of each fiscal year.

6.2 Disclosure of Corporate Governance Arrangements

There are some requirements for companies to disclose their corporate governance arrangements in the interim report and annual report. In the interim report, a publicly traded company shall disclose its corporate governance arrangements, including:

- the annual shareholder meeting and interim shareholder meetings held during the reporting period;
- the removal of directors, supervisors and officers, as well as the reasons for doing so, during the reporting period;
- whether the dividends distribution plan and the plan for conversion of capital reserve fund to share capital (i) comply with the articles of association and provisions for review proce-

- dure, and (ii) have adequately protected the legitimate interests of the minority investors, and (iii) whether the independent directors have issued opinions; and
- the implementation of an equity incentive plan, employees' stock holding plan or other incentive measures for employees during the reporting period.

Publicly Traded Companies

In the annual report, in addition to the arrangements mentioned above, a publicly traded company shall also disclose:

- the measures that the controlling shareholder and actual controller take to guarantee the independence of the company;
- the situation of engagement in business identical or similar to the company that is taken by the controlling shareholder, actual controller and other enterprises controlled by them;
- the implementation of and changes to the arrangements on difference in voting rights during the reporting period;
- basic information on and annual remuneration of directors, supervisors and officers;
- meetings of the board of directors held during the reporting period and the performance of each director;
- the membership of the special committees under the board of directors, and meetings of special committees held during the reporting period;
- opinions of the board of supervisors on supervision matters during the reporting period;
- employees of the company's parent company and its main subsidiaries;
- the construction and implementation of the internal control system during the reporting period; and
- management of its subsidiaries during the reporting period.

6.3 Companies Registry Filings

The specific documents a company is required to file with the companies registry and their format may differ depending on the type of company in question. Generally, a company is required to submit the following documents to apply for registration of establishment:

- application for registration of company establishment;
- the articles of association of the company signed by all the shareholders/promoters;
- legal person qualification certificates or identity certificates of the shareholders/promoters;
- appointment documents of legal representatives, directors, supervisors and officers, and their identity certificates;
- minutes of the shareholder meeting/inaugural meeting;
- certificate of the domicile of the company; and
- certificate of capital verification (only required by a joint stock limited company).

If a joint stock limited company established by public offering issues shares to the public, it shall also submit the approval documents of the CSRC to the companies registry.

Members of the public may apply to the companies registry to inquire about the registered matters of the company; and the companies registry shall provide a response to such an inquiry.

7. AUDIT, RISK AND INTERNAL CONTROLS

7.1 Appointment of External Auditors

A company shall prepare a financial statement upon the end of each fiscal year, which shall be audited by an accounting firm in accordance with laws. According to the articles of association of

the company, the decision to hire or dismiss the accounting firm that undertakes the company's auditing business shall be taken by the shareholder meeting or the board of directors. When the shareholder meeting or the board of directors votes on the dismissal of the accounting firm, the accounting firm shall be allowed to state its opinions. The board of directors of a publicly traded company shall establish an audit committee to supervise and evaluate the external auditing work, and to propose hiring or replacing the external auditing institution.

7.2 Requirements for Directors Concerning Management Risk and Internal Controls

Large and Medium-Sized Companies

There are some requirements for directors in connection with the management of risk and internal controls in large and medium-sized companies; the key ones are set out below:

- The board of directors shall be responsible for the establishment and implementation of internal controls. The board of supervisors shall supervise the establishment and implementation of internal controls by the board of directors. Managers shall be responsible for organising and leading day-to-day operation of the company's internal controls. A company shall establish a special department or designate an internal department to be specifically responsible for organising and co-ordinating the establishment and implementation of internal controls and daily work.
- A company shall establish an audit committee under the board of directors. The audit committee shall be responsible for examining the company's internal controls, supervising effective implementation and self-evaluation of internal controls, and co-ordinating the audit of internal controls and other related matters.

- The internal audit institution shall supervise and inspect the effectiveness of the internal controls, and shall have the right to report – directly to the board of directors and its audit committee and the board of supervisors – any major defect of internal controls discovered during the supervision and inspection.

Publicly Traded Companies

There are some specific requirements for directors in connection with the management of risk and internal controls in publicly traded companies; these mainly include the following:

- A publicly traded company shall establish internal control and risk management systems, and establish a special department or designate an internal department to be responsible for inspecting and supervising the important operations of the company, the management of subordinate companies, the disclosure of financial information and the compliance with laws and regulations.
- A publicly traded company shall regularly disclose the construction and implementation of its internal control system, as well as the audit opinions of accounting firms on the effectiveness of the internal controls.

Global Law Office (GLO) was one of the first leading law firms in the PRC to take an international perspective on its business, fully embracing the outside world. With more than 600 lawyers practising in the Beijing, Shanghai, Shenzhen and Chengdu offices, the firm continues to set the pace as one of the most innovative and progressive legal practices in China. Over the last 40 years, GLO has helped set the agenda for change through precedents, includ-

ing working on the first foreign general offer targeting Chinese companies on the Hong Kong Stock Exchange, the first state-owned red chip company listed in Hong Kong acquiring the controlling interest in an A-share company listed in China by means of a reverse takeover, and the first reverse merger case in which a red chip Hong Kong-listed public company span off part of its China business to list on a share market.

AUTHOR



Yunjian Hou is a partner at Global Law Office (Beijing) and specialises in disputes resolution (including litigation, arbitration, and alternative disputes resolution) and corporate work. Mr Hou has extensive practical experience in handling complex dispute resolution cases, and he has helped his clients to achieve unexpected outcomes in many significant cases, safeguarding their interests. In addition, Mr Hou has also provided long-term legal services for many major corporates, and has participated in a series of bankruptcy liquidation and reorganisation cases that have had significant domestic influence.

Global Law Office

15 & 20/F Tower 1, China Central Place
No.81 Jianguo Road
Chaoyang District, Beijing
100025, China

Tel: +86 10 6584 6688
Fax: +86 10 6584 6666
Email: global@glo.com.cn
Web: www.glo.com.cn/en



环球律师事务所
GLOBAL LAW OFFICE



Chambers Global Practice Guides

Chambers Global Practice Guides bring you up-to-date, expert legal commentary on the main practice areas from around the globe.

Focusing on the practical legal issues affecting businesses, the guides enable readers to compare legislation and procedure and read trend forecasts from legal experts from across key jurisdictions.

To find out more information about how we select contributors, email Katie.Burrington@chambers.com

practiceguides.chambers.com