

**AIJA PRAAG 2014 – WS 6 LABOUR LAW**

**Who is not afraid to be a company director ?**

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The position of a director/managing director of a company has changed substantially during the past couple of years. Legislative changes, close monitoring by shareholders and the international economic and financial crisis have contributed to an increased attention towards management of companies. The expectations towards directors and managing directors have become much higher. Last but not least, also the media have developed a particular interest in company management, in particular, the remuneration of top management.

**Overview of topics:**

**A. Legal status of a company director**

- Status of a company director / managing director in the different jurisdictions: employee, self-employed, other
- Remuneration: fixed remuneration, stock options, termination packages
- Termination: is it possible to conclude agreements on termination of company directors, at what point in time, under which conditions ?

**B. Recent evolutions in the Board Room**

- Is there an obligation to include independent directors in the board ?
- Is there an obligation to have minimum female presence in the Board ?
- Is there an obligation to set up an audit committee, remuneration committee ?
- Is there any obligation to include certain stakeholders like f.ex. Trade unions in the board ?
- In general: which criteria are used to select and appoint company directors ?

**C. Director's Liability**

- Civil liability
- Criminal liability ?
- Can companies conclude agreements on director's liability ?

## **Questionnaire that was sent to national reporters**

### **1. The legal position/status of a director and/or managing director in the different jurisdictions ?**

- How to define the mandate of a director / managing director from a legal perspective? Distinctive factors between the mandate of director and the mandate of managing director;

#### **Answer:**

A mandate of a director, according to Chinese Corporate Law, mainly includes the right as follows:

- (1) Getting informed about necessary information of a company in order to fulfill the responsibilities of director;
- (2) Attending the meeting of board of directors and delivering its own opinions or advises;
- (3) Exerting its right of vote regarding the voting issues in the meeting of board of directors; and
- (4) According to the articles of association of a company, propose to call interim meetings of board of directors;
- (5) According to the articles of association of a company, propose to call interim shareholder's meetings;

A mandate of a managing director, according to Chinese Corporate Law, mainly includes the rights as follows:

- (1) Taking charge of the management of the production and business operations of the company, organizing the implementation of the resolutions of the board of directors;
- (2) Organizing the execution of the company's annual business plans and investment plans;

(3) Drafting plans on the establishment of the company's internal management departments;

(4) Drafting the company's basic management system;

(5) Formulating the company's specific rules and policies;

(6) Proposing to hire or dismiss the company's vice manager(s) and the financial officer;

(7) Deciding on the hiring or dismissal of the management personnel other than those who shall be decided by the board of directors; and

(8) Other powers granted by the board of directors.

- Terminology: difference between managing director and CEO...

**Answer:**

Under Chinese Corporate Law, managing director is appointed or dismissed by board of directors and his/her duties/powers are subject to the Chinese Corporate Law as well as the articles of association of the company; However, Chinese law remains silence on the definition of CEO. In practice, CEO performs his/her duties in accordance with the employment contract concluded between such CEO and the company rather than the Chinese Corporate Law.

- Distinction between aspects of employment law and aspects of company law :

- What is the contractual relation with the Company?

**Answer:**

As to the director's contractual relation with the company, though it is debatable on what kind of relationship between the director and the company, it is a common view that the director is regarded as the agent of the company and thus the contractual relation between the director and the company shall be agency contractual relation.

As to the managing director's contractual relation with the company, it is a common view that the relation between the managing director and the company is employment relationship and thus the contractual relation between them is employment contractual relation.

- Under what status does a director / managing director carry out his/her tasks: can a director and/or managing director carry out his/her duties as an employee?

**Answer:**

Normally, the director carry out his/her tasks as the agent of the company in accordance with the articles of association while the managing director as the employee of the company in accordance with both of the articles of association and the employment contract.

Unlike the managing director, the status of the director would not be regarded as the employee of company in China though this is arguable.

- Are there typical rights /obligations related to the mandate of director / managing director ?

**Answer:**

Please refer to the answer set out above.

- What are the rights in the event of termination/dismissal?

**Answer:**

Under Chinese Corporate Law, the shareholder's meeting has the discretionary right to dismiss a director and the law does not grant such dismissed director any right to challenge such decision.

As to the termination of the managing director, though the board of directors has the right to dismiss the managing director in accordance with the Chinese Corporate Law, the managing director is entitle to make claims in case of the employment contract being terminated in accordance with the Chinese Employment Contract Law.

**2. What is the impact of corporate governance legislation or soft-law (such as corporate governance codes) for the position of a director / managing director ?**

- Distinction between listed and not listed companies

**Answer:**

The position as well the related functions/powers or the obligations of the director/managing director shall be subject to the articles of association of the company, which is the corporate governance legislation in China.

However, the position and the functions/powers or the obligations of the director/managing director of a listed company shall also be subject to the requirements/regulations of the China Securities Regulatory Commission in addition to the said articles of association.

### 3. **Liability of a company director / managing director?**

- Civil liability :
  - o contractual liability and liability on the basis of “tort”;
  - o liability towards the company and liability towards third parties;

#### **Answer:**

Under Chinese Corporate Law, the director/ managing director shall be liable for the losses/damages incurred by the company in the course of performing his/her company duties as a result of his/her violation of the laws, regulations or articles of association of the company.

In case where the company breaches the contract concluded with third parties or commit a tort resulting from the decisions made by the director / managing director out of negligence, the company needs first shoulder the liabilities against the third party and then may claim the losses from such director/managing director should it be justified.

- Criminal liability

#### **Answer:**

Chinese Criminal Law provides that where a company commits a crime, not only the company itself shall be fined but also the management personnel who is directly responsible for such crime shall be given criminal punishment as well.

- Noteworthy specific liabilities?

#### **Answer:**

See above

- Are there in your jurisdiction over the last few years more court cases involving company directors or managing directors ?

#### **Answer:**

There is indeed an increase of the court cases involving directors or managing directors particularly relating to the disputes arising from the director or managing director's violation of their non-competition obligations.

**4. Are there any recent changes in remuneration legislation / policies for company directors / managing directors ?**

- Fixed remuneration
- Variable compensation (bonus etc)
- Stock options
- Golden parachute

**Answer:**

Under Chinese Corporate Law, normally the amount of fixed remuneration and variable compensation of the director shall be decided by the shareholder's meeting while that of the managing director by the board of directors of the company.

However, the Chinese legislation/policies remain silence on the director/managing director's entitlement to the Stock options or Golden parachute.

**5. Has it occurred in your jurisdiction that management decisions were revised after being challenged by stakeholders (e.g. consumers) ?**

- [to the extent applicable] Can you give some examples?

**Answer:**

The most typical example in China is that: the management of Company A reached an acquisition agreement with Company B whereby Company A intends to receive the assets and labor from Company B, however, the employees of Company B refused to be transferred and make protest against such acquisition, which leads to that either both Parties canceled the transaction or revise the conditions offered to the employees.

- Was this protest spontaneous or organized by certain groups/institutions ?

**Answer:**

As the labor unions are not commonly established in the companies in China, such kind of protest is usually spontaneous.

**6. Has your jurisdiction issued specific legislation on female presence in the board of directors ?**

- If no, was this (n)ever a political topic ?
- If yes, which obligations apply under these laws ?

**Answer:**

No. To our knowledge, it has not become a political topic. However, we believe that more and more females will be present in the board of directors since China has attached great importance to the equality of employment opportunities between male and female.

A survey of Grant Thornton China shows that the female rate of the board of directors of listed companies in China is 21% while the global average is only 17%.

**7. Is there in your jurisdiction an obligation to have a minimum of independent and/or non-executive directors in the board?**

- Does this depend on the type of company?
- Does this depend on whether the company is listed or not ?

**Answer:**

This depends on whether the company is listed or not. There is no statutory obligation for the non-listed company to incorporate the independent/non-executive director into the board of directors.

However, for the listed company, the *<notification issued by China Securities Regulatory Commission regarding the regulation for a listed company to establish a independent director system>* issued by the competent authority stipulates that a listed company shall assume the responsibilities to establish an independent director system and the minimum of independent directors of the board of directors of a listed company may not below a third of the board members.

**8. Are there in your jurisdiction certain obligations that are different for private and for publicly owned companies and which are not yet covered by the above topics ?**

- Composition of Board of Directors?

**Answer:**

For a public owned company such as wholly state-owned company, the members of the board of directors shall be appointed by the state-owned assets supervision and administration institution, but of whom the representatives of the employees shall be elected through the assembly of the representatives of the employees of the company. Further, the chairman and deputy chairmen shall be designated by the state-owned assets supervision and administration institution from the members of the board of directors.

- Compensation for Directors?

**Answer:**

Unlike the private company as mentioned above, the compensation to be paid to the director of wholly state-owned company shall be subject to the decision of the state-owned assets supervision and administration institution.

- Obligation to have certain stakeholders represented in the Board?

**Answer:**

According to Chinese Corporate Law, (a) the members of the board of directors of the wholly state-owned company shall include representatives of the employees of the company and (b) the members of the board of directors of a limited company invested by at least two state-owned company or at least two other state-owned investment entities shall include representatives of the employees of the company.

However, the private company has no obligation to include representatives of employees in its board of directors.

**9. Position of directors/ managing directors in the event of disposal and/or merger of the company?**

- Is it typical to have wording on the position of the management in transfer agreements? If yes, which topics would usually be covered ?

**Answer:**

It is really an issue on case by case basis.

- Is it common to have wording on discharge for the services performed prior to the disposal/merger?

- **Answer:**

- It is really an issue on case by case basis.

- Is it common to have contractual limitations of liability towards the acquirer?

**Answer: Yes.**



- Is it common for the sale agreement to provide restrictive covenants on the part of directors / managing directors? If yes, what type of restrictive covenants ?

**Answer:**

It is really an issue on case by case basis.

**10.Are there in your jurisdiction minimum requirements to become a company director ?**

- Does a director need to prove certain knowledge on company business ?
- Does he need to have certain degrees ?

**Answer:**

In this respect, Chinese Corporate Law set out several circumstances that prohibit one person from becoming a director:

(1) Being without civil capacity or with only limited civil capacity;

(2) Having been sentenced to any criminal penalty due to an offence of corruption, bribery, encroachment of property, misappropriation of property or disrupting the economic order of the socialist market and 5 years have not elapsed since the completion date of the execution of the penalty; or he has ever been deprived of his political rights due to any crime and 3 years have not elapsed since the completion date of the execution of the penalty;

(3) He/she was a former director, factory director or manager of a company or enterprise which was bankrupt and liquidated, whereby he/she was personally liable for the bankruptcy of such company or enterprise, and three years have not elapsed since the date of completion of the bankruptcy and liquidation of the company or enterprise;

(4) He/she was the legal representative of a company or enterprise, but the business license of this company or enterprise was revoked and this company or enterprise was ordered to close due to a violation of the law, whereby he/she is personally liable for the revocation, and three years have not elapsed since the date of the revocation of the business license thereof;

(5) He/she has a relatively large amount of debt which is due but has not been paid.

Certain financial industries such as securities requires that a eligible director should have at least 3 years working experience engaging in finance industry/securities industry /accounting industry or 5 year working experience in other business industries and a college degree or above is also required for the post.

For an independent director, the requirement is stricter, besides the compulsory requirement concerning the working experience and degree; an independent director should also meet the conditions that set forth for a director by the listed company. in practice, an independent director are usually selected from accountants, lawyers and

authorities who have rich enterprise management experience and is required to participate training programme organized by China Securities Regulatory Commission which have the final decision whether a person is eligible for the position of independent director.

**11.Does a company director has specific obligations with regard to:**

- Non-compete obligations
- The obligation to reveal so-called "corporate opportunities" towards the company

**Answer:**

Yes, Chinese Corporate Law prohibits the director from committing the following acts:

- (1) Conclude a contract or carry out transactions with the company in breach of the company's articles of association or without the consent of the shareholder' meeting or shareholder's general meeting.
- (2) Without the consent of the shareholder's meeting or shareholder's general meeting, utilize the advantages of his or her position to obtain for himself or herself or others commercial opportunities rightly belonging to the company or, for himself or herself or for the benefit of another, engage in business identical to the business of the company in which he or she serves;
- (3) Accept for himself or herself commissions for transactions between other parties and the company; and
- (4) Disclose company secrets without authorization.