

Arresting developments Part II: Understanding who is at risk under PRC law

The recent arrests, detentions¹, and travel bans imposed on top corporate executives have caused senior managers at other companies operating in China to question their own potential liability risk under PRC law. When would the activities of a company targeted for enforcement be attributed to its legal representatives, managers and officers? This article summarizes the potential liability of a company's legal representatives under PRC law to give some shape to the concerns keeping senior managers awake at night.

A legal representative's liability may be criminal, civil or administrative.

Criminal liability

Under PRC law, if a company is deemed to have committed a crime, "the person in charge who is directly responsible for the offence or other persons who are directly liable" should be personally liable for such crimes, unless otherwise provided under the relevant provisions of the Criminal Law.

The term "the person in charge who is directly responsible for the offence or other persons who are directly liable" is not defined under the Criminal Law. However, the Supreme People's Court ("**SPC**") has issued meeting minutes providing that

- "the person in charge who is directly responsible for the offence" refers to a person who takes the role of determining, approving, instructing, abetting or coordinating the criminal activities, normally including senior managers such as **the legal representative** [emphasis added];
- "other persons who are directly liable for the offence" refers to persons who take a relatively substantial role in the criminal activities, including both the managers or staff, whether or not an employee or a contractor. That being said, a person who acts upon the instruction of managers should generally not be personally liable.

¹ Discussed in last month's briefing, [Arresting Developments: Understanding Criminal Mandatory Measures Under PRC Law](#), by Wendy Wysong and Yu Bing

Accordingly, the legal representative is likely to be liable for the criminal activities of the company, especially if she or he is deemed to have taken the above roles during the criminal activities.

A legal representative's criminal liability for commercial bribery

A legal representative could be held criminally liable for having taken the role of "determining, approving, instructing, abetting or coordinating" the company's act of giving bribes to the following parties:

- employees of other companies (Article 164 of the Criminal Law);
- government entities (Article 391 of the Criminal Law); or
- government officials (Article 393 of the Criminal Law).

The criminal penalties to which the legal representative is subject include imprisonment (up to ten years under Article 164, three years under Article 391 and five years under Article 393), as well as criminal fines (Article 164), and confiscation of property (Articles 391 and 393).

Distinction between a crime committed by an employee and by the company

In accordance with an SPC interpretation of the Criminal Law, the following acts will be attributable to the relevant individual rather than the company:

- the company is set up as a vehicle to commit crimes; or
- the crime is committed in the name of the company without authorisation and the illegal gains are distributed among the individuals who carry out the crimes.

In comparison, the following acts should be attributed to the company:

- the crime is committed in the name of the company and the company receives the illegal gains; or
- the crime is committed in the name of the internal department or branch of the company and the internal department or branch receives the illegal gain.

Accordingly, one of the key elements in determining whether an individual is at risk for personal liability is who receives the illegal gain generated from the crime. In the context of commercial bribery, we have seen comments by a local prosecutor in Shanghai that if an employee pays commercial bribes to increase sales, the criminal liability should be attributed to the company despite the fact that the employee is motivated by a sales bonus. As a result, senior managers including the legal representatives may be potentially liable for such crimes.

Civil liability

To third parties. A company could be found liable for business operations conducted through the acts of its legal representatives under PRC civil law. Therefore, if an individual acts in her or his capacity as a company's legal representative or in the name of the company, it is the company, rather than the legal representative, who should be liable. However, if a legal representative actively participates in a tortious act with or through the

company (e.g., by issuing orders that constitute a tort toward a third party), she or he may also be held liable for the tort to the third party.

To the company. That being said, the company may still hold its legal representative liable for breaching her or his fiduciary duty to the company.

Administrative liability

When a company violates administrative laws or regulations, the person in charge who is directly responsible for the offence or other persons who are directly liable for the act could also be subject to penalties. Although not explicitly provided for under PRC law, in practice, a legal representative is often regarded as the "person in charge who is directly responsible" unless there is evidence showing that she or he did not know about and could not have known about the offence.

Conflict of interest

Given the distinction between individual and corporate liability, an inherent conflict may arise between the company and its legal representatives, managers, and employees. It is in the latter's interest to try to limit liability to the company by noting the corporate benefit gained by the improper conduct or referring to instructions coming from corporate leadership. On the other hand, the company may argue that the criminal activity was carried out against its policy and without its knowledge. Due to this conflict of interest, it may be inadvisable for the company and those who may be taken as the "person-in-charge who is directly responsible or other persons who are directly liable" (e.g. the legal representative or a senior manager) to share counsel. The company may recommend lawyers to its employees or legal representatives, understanding that the best interests of the parties may no longer align when under scrutiny by enforcement authorities.

For assistance relating to this topic, please contact one of our Clifford Chance contacts.

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