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**Liability of Foreign Directors
in a Chinese Company under Chinese Law**

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A foreign director in a Chinese company, must be aware of the legal obligations and consequences and the potential risks involved in (voluntary or involuntary) violations. This does not only include violations committed by the director, but also violations committed by the company. Even without any personal action or involvement (or inaction, as the case may be), the director may be held liable and may commit a crime.

To give an overview and understanding of the legal framework of a directors' liabilities under Chinese law, we have summarized the main provisions in this memorandum.

1. Chinese Data Protection laws

The protection of personal data has become increasingly important in the recent years, also in China. This includes not only the processing of personal data within China, but also cross-border transmission (or granting access via VPN or otherwise) of personal data. The Cybersecurity Law of the People's Republic of China and the attitude of the relevant agencies reflect the trend that China is restricting the outflow of personal information data to any third country.

Therefore, in view of China's legislative trend, it is recommended that cross-border operating companies take a cautious attitude when transferring employees' personal information

across the border. To be safe, the recommended approach is as follows:

- a) According to Article 37 of the Cybersecurity law of the People's Republic of China, personal information and important data collected and generated by an international operating company should be stored in **China only** and should also not be made available by remote access to the foreign HQs.
- b) According to Article 39 of the Cybersecurity Law of the People's Republic of China, if an internationally operating company wants to make personal information available to the HQs or to a third country, the management of the company must inform the Chinese employee first, ask for permission and ensure that it is authorised to do so.
- c) The enterprise should organize regular security assessments. If an enterprise intends to transfer employees' personal information out of the country, the enterprise should perform a security assessment on its own and keeping records for future reference.

2. Violation of Chinese Taxation laws

The China tax law stipulates criminal and administrative penalties for tax evasion, which is basically defined as “making a false tax declaration, failing to make any tax declaration, not paying or **underpaying the tax payable**.”

If a company commits tax evasion, a fine of 50% – **500%** of the tax payable can be imposed.¹ In addition, criminal penalties of up to seven years imprisonment can be imposed if the evaded tax amount exceeds certain thresholds.² In such case, the fines will be imposed on the company and the prison sentence will be imposed on the **company’s representative**.³ However, if the administrative fine is paid on time and the company is not a repeat offender, the criminal liability may be suspended.

However, the representative’s personal liability depends on whether he participated in the action of tax evasion or had knowledge thereof.

If the representative is a foreigner who signed the document in Chinese without knowing the actual meaning, and there is evidence to prove that he did not actively or deliberately participate, but was unaware of the tax evasion, he can use this in defence. However, it will be in the discretion of the court on whether to impose personal liability or not.

3. Violation of Chinese custom laws

The Chinese customs law stipulates penalties for the evasion of customs control, customs duties, and import or export of prohibited goods (“smuggling”).⁴ As for tax evasion, the

¹ Article 63 of the Law of the People's Republic of China concerning the Administration of Tax Collection:

Tax evasion means that a taxpayer forges, alters, conceals or, without authorization, destroys accounting books or vouchers for the accounts, or overstates expenses or omits or understates income in the accounting books, or, after being notified by the tax authorities to make a tax declaration, refuses to do so or makes a false tax declaration, or fails to pay or underpays the amount of tax payable. Where a taxpayer evades tax, the tax authorities shall pursue the payment of the amount of tax he fails to pay or underpays and the surcharge thereon, and he shall also be fined not less than 50 percent but not more than five times the amount of tax he fails to pay or underpays; if a crime is constituted, he shall be investigated for criminal responsibility in accordance with the law.

Where a withholding agent fails to pay, or underpays the tax which he withholds or collects by the means mentioned in the preceding paragraph, the tax authorities shall pursue the payment of amount of tax he fails to pay or underpays and the surcharge thereon, and he shall also be fined not less than 50 percent but not more than five times the amount of tax he fails to pay or underpays; if a crime is constituted, he shall be investigated for criminal responsibility in accordance with law.

² Article 201 of the Criminal Law of the People's Republic of China:

Where a taxpayer files false tax returns by cheating or concealment or fails to file tax returns, and the amount of evaded taxes is relatively large and accounts for more than 10 percent of payable taxes, he shall be sentenced to fixed-term imprisonment not more than three years or limited incarceration, and be fined;

or if the amount is huge and accounts for more than 30 percent of payable taxes, he shall be sentenced to fixed-term imprisonment not less than three years but not more than seven years, and be fined.

Where any withholding agent fails to pay or fails to pay in full the withheld or collected taxes by cheating or concealment, and the amount is relatively large, he shall be punished under the preceding paragraph.

Where either of the acts described in the preceding two paragraphs is committed many times without punishment, the amount shall be calculated on an accumulated basis.

Where any taxpayer who committed the act as described in paragraph 1 has made up the payable taxes and paid the late fine after the tax authority sent down the notice of tax recovery according to the law, and has been administratively punished, he shall not be subject to criminal liability, except one who has been criminally punished in five years for evading tax payment or has been, twice or more, administratively punished by the tax authorities.

³ Article 31 of the Criminal Law of the People's Republic of China.

⁴ Article 82 of the Customs Law of the People's Republic of China:

Any of the following acts of evasion of customs control, customs duties, and state import and export prohibited or restricted control in violation of this law and other related laws and administrative regulations shall constitute an act of smuggling.

(1) to transport, carry or send by post into or out of the territory goods or articles the importation or exportation of which is prohibited or restricted by the state or goods or articles for which duties are payable according to the law.

(2) to sell within the territory, without customs permission and without payment of the payable duties or without producing relevant licenses, beyond goods, goods

customs law stipulates administrative and criminal penalties.

The administrative penalties are:

- a) Fines in the amount of up to RMB 50,000 for smuggling prohibited goods, or up to three times the equivalent value or tax payable for smuggling prohibited goods.
- b) Confiscating of smuggled goods and gains derived therefrom.
- c) Confiscating or demolishing of items (incl. means of transport) that are specifically or repeatedly used to facilitate smuggling.

The criminal penalties are imprisonment for 10 years or more, which will be imposed on the representative of the company (see above).

4. Handling of Chinese ‘State Secrets’

Companies and individuals dealing with state secrets⁵ or other highly sensitive data that may endanger national safety must be extra vigilant. Submitting abroad any plans and **drawings of high-end technical developments** that **may** be deemed as state secret or intelligence that may endanger national safety may violate the laws on guarding of state secrets and punishable with up to ten years of imprisonment, detention, public surveillance or deprivation of political rights.⁶

5. Changes in Chinese Foreign Investment laws

Since the implementation of the NEW Foreign Investment Law of the People's Republic of China on **01 January 2020**, many Chinese foreign joint ventures will need to adjust their governance structure. They need to focus on the analysis of the organization, distribution of power, constitution

listed for specific duty reduction or exemption and other goods, articles or inward foreign means of transport under customs control; or
 (3) *to commit other acts by evading customs control that constitute smuggling. Where any one of the acts listed in the preceding paragraph does not constitute a crime, the Customs Department shall confiscate the smuggled goods, articles and illegal gains and a fine may be imposed. The Customs Department shall confiscate the goods or articles that are specially or repeatedly used for shielding smuggling and the means of transport that are specially or repeatedly used for smuggling. Specially made equipment used for concealing smuggled goods or articles shall be ordered to be demolished or confiscated.*
Anyone who commits any of the acts listed in the first paragraph, which constitutes a crime, shall be investigated for criminal responsibility in accordance with the law.

⁵ Article 9 of the Law of the People's Republic of China on Guarding State Secrets:

The following matters related to national security and any interests that may harm the country's security and interests in its political, economic, national defence, diplomatic and other fields after being leaked shall be determined as state secrets:

- (1) *Secret matters in major national affairs decisions.*
- (2) *Secret matters in national defence construction and armed forces activities.*

- (3) *Secret matters in diplomatic and foreign affairs activities, and secret matters under the obligation of keeping confident.*
- (4) *Secret matters in national economic and social development.*
- (5) *Secret matters in science and technology.*
- (6) *Maintaining national security activities and tracing secret matters in criminal crimes.*
- (7) *Other secret matters determined by the State Secrecy Administration Department.*

The secret matters of a political party that meet the provisions of the preceding paragraph are state secrets.

⁶ Article 111 of the Criminal Law of the People's Republic of China:

Whoever steals, spies into, buys or unlawfully supplies State secrets or intelligence for an organ, organization or individual outside the territory of China shall be sentenced to fixed-term imprisonment of not less than five years but not more than ten years; if the circumstances are especially serious, he shall be sentenced to fixed-term imprisonment of not less than ten years or life imprisonment; if the circumstances are minor, he shall be sentenced to fixed-term imprisonment of not more than five years, criminal detention, public surveillance or deprivation of political rights.

development and rules of procedure, and make corresponding adjustments, to adapt to the legal environment in the new era as soon as possible, which is more conducive to the future development of enterprises.

Joint venture companies need to complete the compliance transformation of the corporate governance structure within five years. They should further pay close attention to the promulgation of the supporting management regulations and specific rules of the Foreign Investment Law of the People's Republic of China by the Ministry of Commerce and relevant departments. In addition, its impact on the enterprise should be timely assessed.

Starting from January 1, 2025, the market supervision and administration departments shall not handle any registration matters applied for by existing foreign-invested enterprises that have not adjusted their governance

structure in accordance with the Foreign Investment Law and will make the relevant circumstances known to the public.

Furthermore, if a foreign investor or a foreign-invested company violates the provisions of the Foreign Investment Law and fails to submit investment information in accordance with the requirements, the competent administration department may order it to make corrections within a specified time limit; if no corrections have been made within the time limit, a fine between RMB 100,000 and RMB 500,000 may be imposed.

We do recommend a field audit in your Chinese company to address all important issues in order to avoid taking unnecessary risk and ensure a smooth operation.

*We hope that the information provided in this brochure was helpful for you.
If you have any further questions, please do not hesitate to contact us.*

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