CORPORATE GOVERNANCE

China

LEXOLOGY
Getting The Deal Through

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Corporate Governance

Consulting editors

Holly J.Gregory

Sidley Austin LLP

Quick reference guide enabling side-by-side comparison of local insights into corporate governance issues worldwide, including sources of rules and practice; responsible agencies and notable opinion formers; shareholder powers, decisions, meetings, voting, duties and liabilities; employee role in governance; corporate control issues; board structure and composition, duties, leadership, committees, meetings and evaluation; director and senior management remuneration; director protections; disclosure and transparency; hot topics, such as shareholder engagement, and sustainability, pay ratio and gender gap reporting; and other recent trends.

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Contributors

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Jan Holthuis
j.holthuis@burenlegal.com
Buren NV

Li Jiao
l.jiao@burenlegal.com
Buren NV

Amsterdam
WTC - Tower C level 14
Strawinskylaan 1441
1077 XX - Amsterdam
Telephone +31 (0)20 333 83 90
The Netherlands

Shanghai
Room 2505B, ICC-Tower
North Zhongshan Road 3000
200063 - Shanghai
Telephone +86 (21) 6173 03 88
China

SOURCES OF CORPORATE GOVERNANCE RULES AND PRACTICES

Primary sources of law, regulation and practice

What are the primary sources of law, regulation and practice relating to corporate governance? Is it mandatory for listed companies to comply with listing rules or do they apply on a 'comply or explain' basis?

The main pieces of legislation that regulate corporate governance in China are as follows:

- the Company Law and the judicial interpretations of the Company Law made by the Supreme People's Court of China, which are applicable to both private and public companies;
- the Minutes of the National Courts' Civil and Commercial Trial Work Conference which is, though not cited as law, still often referred to by the courts of all levels;
- the Foreign Investment Law (effective since 1 January 2020), applicable to foreign-invested companies, which has replaced and superseded the Wholly Foreign-Owned Enterprise Law,
- the Sino-foreign Equity Joint Venture Law and the Sino-foreign Cooperative Joint Venture Law and their respective implementation rules;
- the Securities Law, specific to the corporate governance of public companies;
- the Code of Corporate Governance for Listed Companies and related administrative measures, guidelines, rules and explanatory notes issued by the China Securities Regulatory Commission (CSRC),
- the Chinese stock exchanges (ie, Shanghai Stock Exchange and Shenzhen Stock Exchange) and other designated trading venues; and
- the rules and guidelines respectively issued by the China Banking and Insurance Regulatory Commission and CSRC, which apply to companies in the sectors of banking, insurance and securities.

China adopts a 'comply or explain' approach to enforcing corporate governance norms for listed companies.

Law stated - 13 October 2022

Responsible entities

What are the primary government agencies or other entities responsible for making such rules and enforcing them? Are there any well-known shareholder or business groups, or proxy advisory firms, whose views are often considered?

The National People's Congress and its Standing Committee are the main legislatures for the Company Law, the Foreign Investment Law and the Security Law, which are mainly enforced by the State Administration for Market Regulation, the Ministry of Commerce and the CSRC. For rules applicable to public companies, the CSRC, the Shanghai Stock Exchange and the Shenzhen Stock Exchange act as both legislators and enforcers. Other relevant rules applicable to the sectors of banking, insurance and securities are enacted and enforced by the China Banking and Insurance Regulatory Commission and CSRC respectively. Currently, there are no well-known shareholder groups or proxy advisory firms that exert material influence on the corporate governance-related issues of companies.

Law stated - 13 October 2022

THE RIGHTS AND EQUITABLE TREATMENT OF SHAREHOLDERS AND EMPLOYEES

Shareholder powers

What powers do shareholders have to appoint or remove directors or require the board to pursue a particular course of action? What shareholder vote is required to elect or remove directors?

There are two types of companies with limited liability in China:

1. limited liability companies (LLC), which only include private companies; and
2. companies limited by shares (CLS), which include both private and public companies.

For LLCs, shareholders are entitled to appoint and remove directors by law in accordance with the method as stipulated in the articles of association. However, an employee representative who serves on the board of directors of an LLC established by two or more state-owned enterprises and other state-owned investors or some other LLCs, is elected by the employees. As for CLSs, resolutions to appoint or remove directors shall be passed in a shareholders' general meeting by a simple majority of votes cast by shareholders present at the meeting. Under the Company Law, the shareholders' meeting is the highest decision-making body. A board of directors answers to shareholders at these meetings and must enforce resolutions carried at shareholders' meetings.

Law stated - 13 October 2022

Shareholder decisions

What decisions must be reserved to the shareholders? What matters are required to be subject to a non-binding shareholder vote?

The Company Law reserves decisions to the shareholders in both LLCs and CLSs on:

- the business direction and investment plans of the company;
- the appointment and dismissal of directors and supervisors and their remuneration;
- the resolutions on the increase or reduction of the registered capital of the company;
- the issuance of corporate bonds;
- the merger, division, dissolution, liquidation or change of company form;
- the amendment of the articles of association of the company;
- the review and approval of reports of the board of directors or supervisors, annual financial budget, accounting plan, profit distribution plan and loss recovery plan; and
- any other matters as provided in the articles of association.

The following additional rights are given to the shareholders:

- the approval, by resolution of a shareholder's meeting, of security provisions by the company for a shareholder or the de facto controller of the company;
- the approval of a director or senior manager entering a contract or trading with the company;
- the approval of a director or senior manager seeking business opportunities that belong to the company for themselves or any other person, or operating similar business themselves or for any other person to that of the company they work for; and

- the approval, in a listed company, of transactions by a two-thirds majority of the voting rights of the shareholders present in the meeting, if, within one year, the company purchases or sells major assets, or provides guarantees to third parties, and the transactional value exceeds 30 per cent of the company's total assets.

At present, there is no legal concept or practice of non-binding shareholding votes in China.

Law stated - 13 October 2022

Disproportionate voting rights

To what extent are disproportionate voting rights or limits on the exercise of voting rights allowed?

An LLC does not issue shares that shall be substituted for equity interests measured in terms of percentages.

In an LLC, the voting rights exercisable by a shareholder at a shareholders' meeting shall be based on the ratio of its capital contribution, unless otherwise provided in the articles of association of the company.

In a CLS, the fundamental principle of 'one share, one vote' is adopted: one share of a shareholder represents one voting right at the shareholders' meeting. The company has no voting rights for the shares it holds. However, if a division of ordinary shares and preference shares is adopted in a CLS, preference shareholders are generally not entitled to attend a shareholders' general meeting, unlike ordinary shareholders, and therefore have no right to vote on matters raised during these meetings. However, preference shareholders are entitled to vote during a separate class of meetings on a few limited matters (eg, issuing new preference shares, the amendment of articles of association related to the preference shares, a single or accumulative reduction of the registered capital of the company exceeding 10 per cent, and the merger, division, liquidation or change of corporate form). In addition to preference shares, after considering the market demand, the Chinese government has introduced a special voting rights mechanism in the Shanghai Sci-Tech Innovation Board (STAR) called 'weighted voting rights'. This change was revealed in Announcement No. 2, 2019, of the China Securities Regulatory Commission Implementation Opinions on Setting up the Science and Technology Innovation Board and Launching the Pilot Program of the Registration System on the Shanghai Stock Exchange, which formally put forward a policy to allow 'enterprises with special equity structure and red-chip enterprises to be publicly traded'. In 2020, Shenzhen Stock Exchange introduced weighted voting rights in its listing rules of the Growth Enterprise Market board. In 2021, the establishment of the Beijing Stock Exchange and the corresponding listing rules affirmed the arrangement of 'weighted voting rights' with its own features. To be specific, this mechanism allows a company's shares to be split into two groups with different voting rights, usually termed 'A shares' and 'B shares'. 'A shares' provide the holder with equally up to 10 votes per share; however, they cannot be transferred at will (therefore they cannot be traded on open markets), and the shares' voting privileges must be waived if they are converted to ordinary voting shares. These are usually held by the founding team of a company. 'B shares' offer a single vote per share and can be circulated as normal in the market.

Law stated - 13 October 2022

Shareholders' meetings and voting

Are there any special requirements for shareholders to participate in general meetings of shareholders or to vote? Can shareholders act by written consent without a meeting? Are virtual meetings of shareholders permitted?

Shareholders legally registered in the shareholders' register are generally allowed to participate in general shareholders'

meetings. However, for a general meeting to decide on the matter of providing securities to a shareholder or the actual controlling party of the company, these shareholders or the shareholders controlled by the actual controlling party shall not participate in the general shareholders' meeting. Besides, where there are preference shareholders in a CLS, only under limited circumstances can preference shareholders participate in the general shareholders' meeting and vote. Besides physical meetings, for both LLCs and CLSs, shareholders are permitted to pass a resolution in writing without convening a physical shareholders' meeting as long as this resolution is approved unanimously and is signed and sealed by all the shareholders. If the company's articles of association permit, the shareholders' meeting can be held by telecommunication means. The Company Law is silent on the general requirements applicable to conducting a shareholders' meeting via telecommunication. It can be safely presumed that holding the shareholders' meeting by telecommunication is legal provided that the statutory requirement relating to running the meeting as well as the adoption of resolutions are adhered to, and relevant rules specified in the articles of association are followed.

Law stated - 13 October 2022

Shareholders and the board

Are shareholders able to require meetings of shareholders to be convened, resolutions and director nominations to be put to a shareholder vote against the wishes of the board, or the board to circulate statements by dissident shareholders?

To convene a meeting of shareholders, the following must be done:

- In a CLS, shareholders who alone or jointly hold 10 per cent or more of the company's shares for 90 consecutive days or more can convene and preside over a general meeting on their own initiative, if the board of directors and the board of supervisors have failed to fulfil their obligations to convene a general meeting.
- In an LLC, if the shareholders' meeting is not called by directors or supervisors, shareholders who represent 10 per cent or more of the voting rights can convene and preside over the meeting on their own initiative.
- A shareholder may also petition a court to revoke or nullify a general meeting if the procedure or content of the meeting violates any law, administrative regulation or the company's articles of association.

The Company Law does not provide specific rules on the nomination of directors. Pursuant to the Guidelines on Governance of Listed Companies, listed companies shall stipulate standardised and transparent procedures for the nomination and election of directors in their articles of association and ensure that the election of directors is transparent, fair and equitable. In practice, if a meeting of shareholders convenes, shareholders are able to make shareholder proposals, such as nominating a person to be a director, before the notice of invitation, which includes the programme and agenda of the meeting, is circulated to the shareholders. However, in a CLS, any shareholder that holds 3 per cent or more of the shares of the company can submit a written proposal to the board of directors at least 10 days in advance of a general meeting. The shareholders' meeting is the decision-making body in the company, while the board of directors executes the decision of the shareholders' meeting. There is no provision in Company Law that prohibits the shareholders from requiring the board to circulate statements by dissident shareholders, nor any provision supporting such practices.

Law stated - 13 October 2022

Controlling shareholders' duties

Do controlling shareholders owe duties to the company or to non-controlling shareholders? If so, can an enforcement action be brought against controlling shareholders for breach of these duties?

Under Chinese law, a company's controlling shareholder cannot abuse their controlling position, rights and pre-existing relationship with the company (including through manipulation of related-party transactions) to the detriment of the interests of the company and other non-controlling shareholders. Otherwise, this controlling shareholder shall be liable for the damages caused. As for the listed company, additional rules are regulated in the Code of Corporate Governance for Listed Companies in China. In accordance with article 63 of the Code, the controlling shareholders owe a duty of good faith towards the listed company and other shareholders thereof. In addition, the controlling shareholders should exercise their rights in strict compliance with laws and regulations. Any act that could infringe the company's interests or other shareholders' legal rights should be prohibited. The controlling shareholders are also forbidden to acquire additional profits by virtue of their controlling positions.

If the controlling shareholder infringes the lawful rights and interests of the company, causing the company to incur a loss, any shareholders of an LLC or CLS who alone or jointly hold at least 1 per cent of the company's shares for at least 180 days in succession have the right to request the supervisory board (or the supervisors, for an LLC without a supervisory board) to start legal proceedings in court regarding the infringement. If the supervisory board or the supervisors reject this request, fail to start legal proceedings within 30 days upon receipt of this request or in urgent circumstances where failure to promptly start legal proceedings could cause irreparable harm to the company's interests, the shareholders have the right, in the interests of the company, to directly start proceedings in a court in their own name against these controlling shareholders.

In addition, according to article 95 of the Securities Law, when the interests of investors in a listed company are damaged due to actions of the company (eg, misrepresentation), the investors can file a securities civil compensation lawsuit or entrust an investor protection organisation to do so. However, the latter requires at least 50 investors to join in the request. If the issuer engages in fraudulent issuance, misrepresentation or other illegal acts committed at the direction of a controlling shareholder or the actual controller, the controlling shareholder or the actual controller will be directly civilly liable to the investors, in accordance with the law. Besides, if a resolution of the shareholders' meeting violates any law, administrative regulations or the company's articles of association, this resolution will be null and void. Non-controlling shareholders can request a court to confirm that the resolution is void. Moreover, non-controlling shareholders are entitled to directly initiate a lawsuit against the controlling shareholders before a court if his or her own interests be infringed by this controlling shareholder.

Law stated - 13 October 2022

Shareholder responsibility

Can shareholders ever be held responsible for the acts or omissions of the company?

Pursuant to article 20 of the Company Law, shareholders shall not abuse their shareholders' rights to cause damage to the company, or the interest of other shareholders or abuse independent legal person status of the company and limited liability of the shareholders to cause damage to the interests of the creditors of the company. Shareholders shall be held responsible for the acts or omissions of the company if the acts or omissions are considered the result of being abused by shareholders' rights and they cause the company or other shareholders to suffer damage. Shareholders of a company who abuse the independent legal person status of the company and limited liability of shareholders to evade debts and cause damage to the interests of the creditors of the company shall bear joint and several liability for the company's debt.

Law stated - 13 October 2022

Employees

What role do employees have in corporate governance?

Employees can participate in corporate governance through a unique system, namely the Employee's Representative Congress (ERC). It is stipulated under the Company Law that companies should adopt democratic management through the ERC or other forms. When considering important operational issues, such as restructuring, employees are encouraged to give their opinions. Employees' rights and benefits could also be protected by a company labour union organised under the Labour Union Law and the Company Law. It is through this built-in organisation that union activities may be carried out for employees, and under certain circumstances, collective contracts with the company may be arranged and signed. In an LLC jointly set up by two or more state-owned enterprises or other state-owned investors, the board of directors should include representatives of employees. However, for other companies (without the involvement of state-owned investors), employees' participation in the board is not mandatory. The representatives should be elected democratically through the ERC or other forms of a similar nature. Likewise, a representative of employees could also serve as a supervisor on the board of supervisors. The ratio of employee supervisors to all supervisors should be no less than 1:3. In listed companies, core employees may be offered equity incentives through which the core employees can become potential non-controlling shareholders.

Law stated - 13 October 2022

CORPORATE CONTROL

Anti-takeover devices

Are anti-takeover devices permitted?

Under Chinese law, there is no regulation restricting the use of any specific anti-takeover devices; however, the Measures for the Administration of Takeover of Listed Companies set out the basic anti-takeover rule, which is that controlling shareholders or actual controlling parties of a target company should not abuse the shareholders' rights to damage the legal rights and interests of the target company or any other shareholders. The directors, supervisors and senior managers of a target company have the duty of fidelity and diligence and shall treat equally all the buyers that intend to take over the company. The decision made and the measures taken by the board of directors of a target company for the takeover shall benefit the company and its shareholders, and it shall not erect any improper obstacles to the takeover by abusing its power, nor may it provide any means of financial aid to the purchaser by making use of the sources of the target company or damaging the legal rights and interests of the target company or its shareholders.

In practice, since the attempted Baoneng Group-Vanke hostile takeover in 2015, many listed companies (especially those with relatively scattered ownership structures) have revised their articles of association and added special anti-takeover clauses.

Among other details, these clauses define:

- what a 'hostile takeover' is;
- what process the enterprise is to follow when facing a hostile takeover;
- what golden parachutes (lucrative benefits employees receive if they are terminated) exist, which aim to make it more difficult for an acquirer to replace the company's management);
- what restrictions on directors' nomination rights exist, which aim to make it harder for an acquirer to organise a company's board of directors; and
- what the acquirer's disclosure obligations are.

Law stated - 13 October 2022

Issuance of new shares

May the board be permitted to issue new shares without shareholder approval? Do shareholders have pre-emptive rights to acquire newly issued shares?

Under the Company Law, only the shareholders' meeting in an LLC or the shareholders' general meeting in a CLS may adopt resolutions on the increase of registered capital or issuing new shares. In addition, a listed company shall submit an application and documents including the resolution of a shareholders' general meeting to the China Securities Regulatory Commission to issue new shares. For shareholders in an LLC, the Company Law explicitly stipulates that they have the pre-emptive right to subscribe to new capital in accordance with the ratio of capital contribution or another ratio as determined by all the shareholders. As for a CLS, the Company Law is silent on the pre-emptive rights of existing shareholders regarding the new shares. In judicial practice, for a CLS which has not listed or been classified as public company, the shareholders may create these pre-emptive rights for themselves in the articles of association by agreement, due to respecting the autonomy of the company.

Law stated - 13 October 2022

Restrictions on the transfer of fully paid shares

Are restrictions on the transfer of fully paid shares permitted and, if so, what restrictions are commonly adopted?

Restrictions on the transfer of fully paid shares in an LLC and a CLS are both permitted.

In an LLC, the transfer of equity interest to an external third party is usually subject to the prior approval of more than half of the other shareholders, and the other shareholders have a pre-emptive right to acquire this equity interest on similar terms. The articles of association of a company may include certain additional restrictive provisions on the transfer of equity interest, provided that these restrictions do not violate any mandatory rules of Chinese law.

In a CLS, shares held by incorporators shall not be transferred within one year from the date of incorporation of the company. Shares issued by the company before the share offering shall not be transferred within one year from the date on which the shares of the company are listed on a stock exchange.

Furthermore, the directors, supervisors and senior management personnel of a CLS shall not transfer more than 25 per cent of their shareholding in the company each year during their term of appointment or transfer their shares within one year from the date on which the shares of the company are listed on a stock exchange. The aforesaid persons shall not transfer their shares in the company within half a year after leaving their post.

In addition, the articles of association of a CLS may make restrictive provisions on the transfer of shares held by its directors, supervisors and senior management personnel.

Law stated - 13 October 2022

Compulsory repurchase rules

Are compulsory share repurchases allowed? Can they be made mandatory in certain circumstances?

The Company Law explicitly stipulates a few exceptional circumstances only under which a CLS can make a share buy-

back, which include the following:

- a reduction of its registered capital;
- a merger with another company that holds its shares;
- the use of its shares for carrying out an employee stock ownership plan or share incentive plan;
- a request from shareholders who object to a resolution of a shareholders' general meeting on a merger or division of the company to acquire their shares by the company;
- the use of its shares for conversion of convertible corporate bonds issued by a listed company; and
- the necessity that the share repurchase for a listed company maintains its company value and protects its shareholders' equity.

Law stated - 13 October 2022

Dissenters' rights

Do shareholders have appraisal rights?

Appraisal rights for dissident shareholders in an LLC are set out in article 74 of the Company Law, which provides a non-exhaustive list of circumstances under which shareholders who cast an opposing vote to a resolution passed at the shareholders' meeting may request the company to buy back the equity interest held by them based on a reasonable price, where:

- the company has not made a profit distribution to the shareholders for five consecutive years even though the company has been profitable for those five consecutive years and satisfies profit distribution requirements stipulated by law;
- there has been a merger, division and transfer of main assets of the company; or
- the business terms of the company have expired or the company has been dissolved for reasons stipulated in the articles of association, and a resolution is passed by a shareholders' meeting to amend the articles of association for the subsistence of the company.

Where the shareholders fail to conclude an agreement for the acquisition of equity interests within 60 days from the date of the resolution at the shareholders' meeting, the shareholders may file a lawsuit with a people's court within 90 days from the date of the resolution of the shareholders' meeting. As for the dissident shareholders in a CLS, the Company Law is silent on their appraisal rights. Except that the resolution of a shareholders' general meeting on a merger or division is objected to by the shareholders, dissident shareholders may also request the company to acquire their shares at a fair value.

Law stated - 13 October 2022

RESPONSIBILITIES OF THE BOARD (SUPERVISORY)

Board structure

Is the predominant board structure for listed companies best categorised as one-tier or two-tier?

The Company Law requires listed companies to adopt a two-tier board system structure, consisting of a board of directors managing the company and a supervisory board supervising the management.

Law stated - 13 October 2022

Board's legal responsibilities

What are the board's primary legal responsibilities?

The board of directors are responsible to the shareholders' general meeting for carrying out the following duties:

- to convene shareholders' meetings and report to the board of shareholders;
- to execute the resolutions passed by the board of shareholders;
- to decide on the business plans and investment schemes of the company;
- to formulate the annual financial budget and financial accounting plan of the company;
- to formulate the profit distribution plan and loss recovery plan of the company;
- to formulate the plan for the increase or reduction of registered capital and issuing corporate bonds;
- to formulate the plan for a merger, division, dissolution or change of company structure;
- to decide on the set-up of internal management organisation of the company;
- to decide on the appointment or dismissal of company managers and their remuneration, and decide on the appointment or dismissal of deputy managers and the finance controller of the company based on the nomination by the managers; and
- to formulate the basic management system of the company.

Duties of a board of supervisors include the following:

- to inspect the company finances;
- to supervise the performance of duties by directors and senior management personnel and propose to remove a director or a member of the senior management who violates the provision of the laws and administrative regulations and the articles of association of the company or the resolutions of the board of shareholders;
- to require a director or a member of the senior management who acts against the interests of the company to make corrections;
- to propose to convene an ad hoc shareholders' meeting, and convene and chair a shareholders' meeting when the board of directors fails to convene and chair a shareholders' meeting in accordance with the provisions of the Company Law;
- to make proposals at shareholders' meetings; and
- to file a lawsuit against a director or a member of the senior management in accordance with the provisions of article 151 of the Company Law.

Law stated - 13 October 2022

Board obligees

Whom does the board represent and to whom do directors owe legal duties?

A board of directors has the executive rights of the company and a board of supervisors has the right to inspect the company finances and supervise the performance of duties by directors and senior management personnel. The board of directors and the board of supervisors are independent of each other, but both boards owe legal duties to the shareholders and the company. Directors and senior managers must not be members of the board of supervisors.

Law stated - 13 October 2022

Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed? Is there a business judgment rule?

Pursuant to the Company Law, if a director or a member of the senior management violates his or her fiduciary duties owed to the company, violates the provisions of laws and administrative regulations or the articles of association of the company or manipulates a related-party transaction causing losses to the company, any shareholder of an LLC or a CLS who alone or jointly hold at least 1 per cent of the company's shares for at least 180 days in succession have the right to request the supervisory board (or the supervisors, for an LLC without a supervisory board) to start legal proceedings in court in respect of the infringement. If the supervisory board or the supervisors fail to start legal proceedings within 30 days of the date of receiving the request or, in urgent circumstances, where failure to promptly start legal proceedings could cause irreparable harm to the company's interests, the shareholders have the right, in the interests of the company, to directly start proceedings in a court in their own name. According to article 94 of the Securities Law, if an issuer's directors, supervisors or senior management personnel violate laws, administrative regulations or provisions in a company's articles of association during the performance of their corporate duties, causing the company to suffer losses, an investor protection organisation holding shares in the company may file a lawsuit with a People's Court in its own name in the interest of the company. In these cases, the shareholding ratio and shareholding period are not subject to the restrictions stipulated in the Company Law of the People's Republic of China. Article 95 of the Securities Law further stipulates that an investor protection organisation that is entrusted by more than 50 investors may participate in the lawsuit and register with a People's Court as a representative for the rights holders who are confirmed by a securities registration and settlement organisation, unless the investors state they do not want to participate in the lawsuit. The Company Law has not introduced the business judgement rule from common law systems.

Law stated - 13 October 2022

Care and prudence

Do the duties of directors include a care or prudence element?

As stipulated by article 147 of the Company Law, the board of directors and supervisors owe a duty of loyalty and diligence to the company. In addition, pursuant to the Guidelines on Governance of Listed Companies, directors in listed companies shall perform their duties loyally, diligently and prudently, and perform the undertakings.

Law stated - 13 October 2022

Board member duties

To what extent do the duties of individual members of the board differ?

Generally, in Chinese practice the duties of individual members of the board do not differ from each other irrespective of the difference in skill or experience. In most companies in China, directors have the same duties following the provisions of the Company Law and the articles of association. If the board members also serve as officers in charge of a specific aspect of the management of the company, the duties of these board members in this sense will differ. However, for listed companies, the Guidelines on Governance of Listed Companies stipulate that the professional structure of the board of directors must be reasonable. Members of the board of directors must possess the requisite knowledge, skills and quality for the performance of their duties. Furthermore, diversity in the members of the board of

directors is encouraged. Pursuant to the Guidelines on Governance of Listed Companies, the board of directors of a listed company must set up an audit committee and may establish the relevant specialised committees, such as a strategic committee, nomination committee, remuneration and appraisal committee, based on the company's needs. All members of a specialised committee must be directors. The convener of the audit committee must be an accounting professional.

Law stated - 13 October 2022

Delegation of board responsibilities

To what extent can the board delegate responsibilities to management, a board committee or board members, or other persons?

Pursuant to the Company Law, the board of directors may delegate management responsibilities to managers on the following matters:

- the management of the production and business operations of the company and organising and implementing resolutions passed by the board of directors;
- the organisation and implementation the annual business plan and investment scheme of the company;
- the draft of plans for setting up the internal management organisation of the company;
- the draft of the basic management system of the company;
- the formulation of company rules and policies;
- the recommendation, appointment or dismissal of management staff other than those positions that are to be decided by the board of directors; and
- other duties and rights granted by the board of directors.

In addition, the board of directors in a listed company may authorise certain matters to the specialised committees. Meanwhile, it is stipulated by the Guidelines on Governance of Listed Companies that major matters of a listed company shall be decided collectively by the board of directors, and the board of directors shall not authorise the chairman or the general manager to exercise powers vested statutorily in the board of directors.

Law stated - 13 October 2022

Non-executive and independent directors

Is there a minimum number of 'non-executive' or 'independent' directors required by law, regulation or listing requirement? If so, what is the definition of 'non-executive' and 'independent' directors and how do their responsibilities differ from executive directors?

Under Chinese law, there is no legal concept of the non-executive director. As for independent directors, Chinese law requires that a listed company must establish an independent director system and at least a third of board members must be independent directors, including at least one accounting professional.

The term 'independent director of a listed company' under Chinese law is defined as a director who does not hold any position in the company other than director and who has no relationship with the listed company engaging him or her or its principal shareholders that could hinder his or her making independent and objective judgements.

In addition to the functions and powers granted directors under the Company Law and other relevant laws and regulations, listed companies should grant independent directors the following special functions and powers:

- to approve major related-party transactions (referring to transactions that the listed company intends to conclude with the related party and whose total value exceeds 3 million yuan or 5 per cent of the company's net assets audited recently) before being submitted to the board of directors for discussion. Before the independent director makes his or her judgement, an intermediary agency can be employed to produce an independent financial advisory report, which will serve as the basis for his or her judgement;
- to put forward the proposal to the board of directors relating to the appointment or removal of the accounting firm;
- to propose to the board of directors the calling of an interim shareholders' meeting;
- to propose to call a meeting of the board of directors;
- to appoint the external auditing or consulting organisation independently; and
- to solicit the proxies before the convening of the shareholders' meeting.

Apart from the above duties, the independent director shall provide an independent opinion on the following matters to the board of directors or to the shareholders' meeting:

- the nomination, appointment or replacement of directors;
- the appointment or dismissal of senior managers;
- the remuneration for directors and senior managers;
- the existing or new loans borrowed from the listed company by, or other funds transfer made by, the company's shareholders, actual controllers or affiliated enterprises that exceeds 3 million yuan or 5 per cent of the company's net assets audited recently, and whether the company has taken effective measures to collect the amount due;
- the events that the independent director considers to be detrimental to the interests of minority shareholders; and
- other matters stipulated by the articles of association.

Law stated - 13 October 2022

Board size and composition

How is the size of the board determined? Are there minimum and maximum numbers of seats on the board? Who is authorised to make appointments to fill vacancies on the board or newly created directorships? Are there criteria that individual directors or the board as a whole must fulfil? Are there any disclosure requirements relating to board composition?

Under the Company Law, an LLC must have a board of directors with between three and 13 members. An LLC with relatively few shareholders or of a relatively small size can have one executive director instead of a board of directors. For an LLC established with investment from two or more state-owned enterprises or two or more other types of state-owned investors, the members of its board of directors must include employee representatives of the company. Article 51 of the Company Law stipulates that a supervisory board of an LLC must be comprised of at least three members. LLCs with relatively fewer shareholders, or of a relatively smaller scale, may appoint one or two supervisors instead of establishing a supervisory board. A CLS must have a board of directors that is to be composed of five to 19 members. Article 117 of the Company Law stipulates that an LLC's supervisory board must comprise no less than three members.

The composition of directors or supervisors is regulated in the articles of association. Filling vacancies on the board or among newly created directors or supervisors shall be decided at the shareholders' meeting and will entail the amendment to the articles of association of the company.

The Company Law does not set out the criteria a director or a supervisor should meet; however, it provides a negative list and any person that falls under this list cannot be a director or a supervisor:

- a person who has no civil capacity (under the age of 18 or unable to account for his or her own conduct) or limited civil capacity (under the age of 18 or unable to fully account for his or her own conduct);
- a person who has been convicted for corruption, bribery, conversion of property or disruption to the order of socialist market economy and a five-year period has not elapsed since the expiry of the execution period, or a person who has been stripped of political rights for being convicted of a crime and a five-year period has not elapsed since the expiry of the execution period;
- a person who acted as a director, factory manager, manager in a company that has been declared bankrupt or liquidated and who is personally accountable for the bankruptcy or liquidation of the company, and a three-year period has not elapsed since the completion of bankruptcy or liquidation of this company;
- a person who has acted as a legal representative of a company that has had its business licence revoked or has been ordered to close down for a breach of law and who is personally accountable, and a three-year period has not elapsed since the revocation of the business licence of such company; and
- a person who is unable to repay a relatively large amount of personal debts.

At the incorporation of a company, the information of the identities of each member of the board of directors and supervisors must be registered with the commercial registry and any changes regarding the board members must also be registered with the commercial registry. The names of board members of a company can be found in the nationwide company registration search system, the National Enterprise Credit Information Publicity System.

Law stated - 13 October 2022

Board leadership

Is there any law, regulation, listing requirement or practice that requires the separation of the functions of board chair and CEO? If flexibility on board leadership is allowed, what is generally recognised as best practice and what is the common practice?

The Company Law does not require the separation of functions between a board's chair and the chief executive or president. For LLCs, especially relatively small ones, it is not uncommon that a person performs the dual roles of the board chair and CEO. For a CLS, the separation of the board chair and CEO roles is widely deemed as a more reasonable approach to avoid conflicts of interest.

Law stated - 13 October 2022

Board committees

What board committees are mandatory? What board committees are allowed? Are there mandatory requirements for committee composition?

Pursuant to the Guidelines on Governance of Listed Companies, the board of directors of a listed company must set up an audit committee and may establish the relevant specialised committees, such as a strategic committee, nomination committee and a remuneration and appraisal committee, as required. The audit committee should supervise and evaluate external and internal audit work and internal control, propose the appointment or replacement of external audit firms, examine the company's financial information and disclosure this information. The key duties of the strategic committee are to study the company's long-term development strategies and major investment decisions and

make recommendations thereto. The key duties of the nomination committee should include studying the selection standards and procedures for directors and senior management personnel and making recommendation thereto, shortlisting qualified candidates and reviewing candidates for the aforesaid positions. The remuneration and appraisal committee should study the appraisal standards for directors and senior management personnel, conduct appraisal and make recommendations thereto, and study and examine remuneration policies and schemes for directors and senior management personnel. Members of the special committees should be composed of directors. Moreover, independent directors should constitute the majority of the members of the audit committee, the nomination committee and the remuneration and appraisal committee and act as the convener. The convener of the audit committee must be an accounting professional.

Law stated - 13 October 2022

Board meetings

Is a minimum or set number of board meetings per year required by law, regulation or listing requirement?

There is no minimum requirement on the number of meetings an LLC's board of directors must hold each year, but its board of supervisors must convene at least one meeting per year. The Company Law requires a CLS to convene at least two meetings of its board of directors every year, and at least one meeting of its board of supervisors every six months. The Guidelines on Governance of Listed Companies, which apply to listed companies, only states that a board of directors must convene meetings on a regular basis, while the Guidelines for Articles of Association of Listed Companies states that the board of directors shall hold meetings no less than twice a year, which is consistent with the Company Law.

Law stated - 13 October 2022

Board practices

Is disclosure of board practices required by law, regulation or listing requirement?

The board practices of an LLC and a CLS are mainly set out in the Company Law and the articles of association. Companies are only allowed to set up their own rules of board practices in the articles of association when the Company Law does not stipulate otherwise. Article 48 of the Company Law states that board minutes should be made for each board meeting, which shall be signed by all the directors present at the meeting. Resolutions should be passed through voting by all the directors present, with each director having one vote. Nevertheless, disclosing the articles of association to the public is not obligatory. Authorised natural persons or qualified lawyers may retrieve companies' files from local counterparts of the State Administration for Market Regulation from which the articles of association could be acquired.

Listed companies, however, are subject to more rigorous regulations. Listed companies should disclose regularly through publishing their regular reports (ie, annual reports, semi-annual reports and quarterly reports). An annual report should include, among other things, the reports of the board of directors, the committee structures and the number of board meetings where resolutions and attendance would be covered. In addition, listed companies should also formulate a system to manage information disclosure. The Measures of Disclosure provide a wide range of the items that this system should embrace. These include, inter alia, the duties of reporting, deliberating and disclosing for the directors, the board of directors, the supervisors, the board of supervisors and senior managers. With regard to the board of directors' procedural rules, article 29 of the Guidelines on Governance of Listed Companies specifies that the rules of procedure for the board should be formulated and be incorporated into a company's articles of association. Board meetings should be conducted strictly according to the rules of procedure.

Law stated - 13 October 2022

Board and director evaluations

Is there any law, regulation, listing requirement or practice that requires evaluation of the board, its committees or individual directors? How regularly are such evaluations conducted and by whom? What do companies disclose in relation to such evaluations?

There is no mandatory requirement or practice that requires the evaluation of the board in LLCs or CLSs. They may implement their own evaluation mechanism in the articles of association. In listed companies, the Guidelines on Governance of Listed Companies require fair and transparent standards and procedures to be implemented in assessing the performance and fulfilment of the duties of the directors, supervisors and senior executives. Performance assessment should be organised by the board of directors or the remuneration and appraisal committee or, alternatively, other independent (external) firms. Self-assessment, mutual assessment or other methods are introduced in the Guidelines to assess the fulfilment of duties. Each assessment result and remuneration should be reported to the shareholders' general meeting and be disclosed.

Law stated - 13 October 2022

REMUNERATION

Remuneration of directors

How is remuneration of directors determined? Is there any law, regulation, listing requirement or practice that affects the remuneration of directors, the length of directors' service contracts, loans to directors or other transactions or compensatory arrangements between the company and any director?

It is specifically stated under article 37 of the Company Law that the shareholders' meeting should exercise a number of powers. These powers are inherent and, therefore, cannot be derogated or circumvented by the articles of association or other shareholders' agreements. One of these powers is to appoint and remove directors, as well as to decide their salaries and compensation. Article 45 of the Company Law provides certain autonomy to companies when it comes to the tenure of directors, requiring the tenure to be set forth in the articles of association, but subject to a three-year maximum. Upon re-election or reappointment, they may continue to serve as directors in the company. For listed companies, a contract should be formed between the company and the director specifying their rights and obligations, the tenure of the director, the liabilities when the statutory or contractual obligations are breached and the compensation when the contract is terminated prematurely. The principle of fairness should be applied when considering the amount of compensation, while keeping the company's lawful interests unharmed and any behaviour amounting to the transmission of interests barred. As in LLCs and CLSs, according to the Guidelines on Governance of Listed Companies, the remuneration of directors should be decided by shareholders' meetings. Board committees, such as remuneration and appraisal committees, may also be set up to study and review directors' remuneration schemes. It is, however, not mandatory under the Guidelines to have such a committee in place. The board of directors should report the directors' performance, the assessment results and remuneration to shareholders' meetings, which should eventually be disclosed by the company. It is expressly prohibited under the Company Law to provide loans to directors, either directly or indirectly through subsidiaries.

Law stated - 13 October 2022

Remuneration of senior management

How is the remuneration of the most senior management determined? Is there any law, regulation, listing requirement or practice that affects the remuneration of senior managers, loans to senior managers or other transactions or compensatory arrangements between the company and senior managers?

In LLCs or CLSs, the board of directors should hire or dismiss the manager, the vice-manager and the finance manager, as well as decide their salaries and compensation. Usually, the articles of association will provide further details regarding the factors that may affect the remuneration of senior managers.

It is expressly prohibited under the Company Law to provide loans to senior managers either directly or indirectly through subsidiaries.

The picture is very different where listed companies are involved. A few regulations on managers' remuneration echo those for directors:

- the remuneration and appraisal committee, if set up, would be responsible for studying and reviewing senior managers' remuneration;
- the principle of fairness to be applied when considering the amount of compensation, without prejudice to the company's lawful interests; and
- a comprehensive evaluation mechanism for performance and remuneration must be in place, based on which performance appraisal could be conducted when determining senior managers' remuneration and other bonuses.

Upon being approved by the board of directors, the remuneration distribution plan for senior managers must then be explained in a shareholders' general meeting and be disclosed sufficiently.

Law stated - 13 October 2022

Say-on-pay

Do shareholders have an advisory or other vote regarding remuneration of directors and senior management? How frequently may they vote?

One of the statutory powers of the shareholders' meetings is to elect and change the directors and supervisors, as well as to decide their salaries and compensation. The shareholders' meeting could be a regular or an interim one. Regular meetings should be held in a timely fashion according to the articles of association. Where an interim meeting is proposed by shareholders representing 10 per cent of the voting rights or more, by directors representing a third of the voting rights or more or by the board of supervisors or supervisors (when no board of supervisors is in place), an interim meeting should be held. In a listed company, the remuneration of directors and supervisors would be decided at the general meeting of shareholders.

Law stated - 13 October 2022

DIRECTOR PROTECTIONS

D&O liability insurance

Is directors' and officers' liability insurance permitted or common practice? Can the company pay the premiums?

Directors' and officers' liability insurance was first brought to China in 2002 following the promulgation of the Guidelines on Governance of Listed Companies. Article 24 of the Guidelines on Governance of Listed Companies allows listed companies to purchase liability insurance for directors on the premise that the shareholders' general meeting gives prior approval. The coverage of this liability insurance should be set out in the contract of employment or services, expressly excluding the liabilities arising out of a breach of laws, regulations or the articles of association.

Law stated - 13 October 2022

Indemnification of directors and officers

Are there any constraints on the company indemnifying directors and officers in respect of liabilities incurred in their professional capacity? If not, are such indemnities common?

Under the current legal framework in China, no specific law or regulation has directly touched upon these indemnities and constraints on them. Nonetheless, according to the Company Law, the director, executive director or general manager of a company may also be the legal representative of the company. When a company's legal representative engages in civil activities in conformity with the law and the articles of association for and on behalf of the company, all the legal consequences arising therefrom should be borne by the company. If, while performing his or her duties, the legal representative causes harm or damage to third parties, the company should assume the liability. After the company indemnifies the third parties, it may seek to recoup from the legal representative who has caused or contributed to this harm or damage.

In short, if the company's director or executive director is also the legal representative, or if this officer is the general manager who also holds the position of a legal representative, then the aforementioned provisions apply.

Law stated - 13 October 2022

Advancement of expenses to directors and officers

To what extent may companies advance expenses to directors and officers in connection with litigation or other proceedings against them or in which they will be a witness?

This is not applicable.

Law stated - 13 October 2022

Exculpation of directors and officers

To what extent may companies or shareholders preclude or limit the liability of directors and officers?

The Company Law greatly limits the circumstances in which directors' and officers' obligations might be precluded or limited. In non-listed companies, the director should be responsible for resolutions of the board of directors. When any of these resolutions is in violation of laws, regulations, the articles of association or resolutions made by shareholders' general meetings, causing serious damage to the company, the directors taking part in the resolutions should be held

liable for the company's damages. The liability may only be exempted if the directors raised objections to these resolutions at the board meeting, and these objections were recorded in the minutes. The same provision is laid down in article 23 of the Guidelines on Governance of Listed Companies, governing directors' liabilities and exculpation in listed companies.

Law stated - 13 October 2022

DISCLOSURE AND TRANSPARENCY

Corporate charter and by-laws

Are the corporate charter and by-laws of companies publicly available? If so, where?

In China, the articles of association embody the functions and features of the corporate charter and by-laws in combination. Parts of the company information that have been registered with a local branch of the State Administration for Market Regulation (SAMR) are publicly available. However, the articles of association, in their entirety, are generally not available to the public. Qualified Chinese lawyers may acquire the articles of association through a local branch of the SAMR if certain conditions are met (eg, when they are authorised by the company itself, or in the course of a civil proceeding, by exercising their statutory power of inquiry to retrieve all the company's files, including articles of association, from the local branch of the SAMR).

Investors are able to check articles of association through the websites of the China Securities Regulatory Commission , Shanghai Stock Exchange and the Juchao Information Network .

Law stated - 13 October 2022

Company information

What information must companies publicly disclose? How often must disclosure be made?

The following information must be disclosed constantly by SAMR and other government departments to the public regarding non-listed companies according to the administrative regulations:

- the company's registered general information;
- the registered movable assets;
- the pledges on equity;
- the administrative punishments;
- the information on granting, altering or renewing administrative permits; and
- other information that must be disclosed in accordance with the law.

In addition, companies must submit their annual reports for the previous year to the online credit disclosure system which will be disclosed to the public. This submitted information must include:

- the company's postal address, postcode, telephone number and email;
- the company's commencement, discontinuation or liquidation;
- the company's investments in other enterprises;
- the amounts, time and forms of capital contributions, subscribed and paid-up, where the enterprise is a limited liability company or a company limited by shares;
- the shareholders' equity transfer;
- the company's website and the name, website and other information on online shops engaging in online

business; and

- the number of employees, total assets, total liabilities, guarantees provided externally, total owners' equities, gross operating income, prime operating income, total profits, net margin and total tax payment.

All of the above items shall be disclosed to the public with the exception of the last item, which companies may opt to disclose to the public. For listed companies, the Measures of Disclosure set forth the main documents that should be disclosed: stock prospectuses, bond prospectuses, the listing memorandum, periodic reports (annual reports, half-yearly reports and quarterly reports) and interim reports. In summary, any information that would affect investors' decisions must be disclosed. Effective from 2019, the Securities Law expanded the scope of significant events that should be disclosed in the reports. For stock listed companies, major events now include significant changes in a company's assets, significant guarantees or related transactions and the inability of the chairperson or manager to perform his or her duties. Article 81 stipulates that a bond-listed company should make interim reports on significant matters affecting the trading price of bonds. In particular, the second paragraph lists 10 specific matters, including significant changes in the company's shareholding structure or production and operation status and changes in the bonds' credit ratings.

Law stated - 13 October 2022

HOT TOPICS

Shareholder-nominated directors

Do shareholders have the ability to nominate directors and have them included in shareholder meeting materials that are prepared and distributed at the company's expense?

This is not applicable.

Law stated - 13 October 2022

Shareholder engagement

Do companies engage with shareholders? If so, who typically participates in the company's engagement efforts and when does engagement typically occur?

There are a significant number of small and medium-sized private investors in China, making up a large proportion of total investors. Listed companies' engagement with these private investors and shareholders is mainly led by companies' investor relations teams. On 7 May 2022, the Shanghai Stock Exchange revised the No. 1 Self-regulatory Guidelines for Listed Companies, comprehensively obliging the companies to appoint the secretary of the board of directors as the person in charge of relations with the investors, building all kinds of platforms to inform the investors and use the interactive platform designed by Shanghai Stock Exchange, etc. In summary, listed companies should develop companies' investors relations management mechanisms through which the investors can engage with the company effectively and be well informed. The secretary of the board of directors shall be held responsible for detailed work. The

China Securities Regulatory Commission (CSRC) also posted new guidance in 2022, expanding contents disclosed to the investors and setting up all kinds of channels to facilitate communication. Generally, the obligations of the listed companies with respect to engagement with the investors involve not only the company and its senior management (directors, supervisors and senior managers), but also the secretary of the board. The guidance does not stipulate specifically when to engage with the investors, leaving it to the discretion of both parties, but the company should

actively engage with the investors in accordance with the principles set in the guidance.

Law stated - 13 October 2022

Sustainability disclosure

Are companies required to provide disclosure with respect to corporate social responsibility matters?

Generally, the methodology towards disclosing environment-related information is to combine mandatory disclosure with voluntary disclosure. The Company Law stipulates expressly that companies shall bear social responsibility, but it does not mention requirement of disclosure. According to the Environment Protection Law and other environmentally related laws, companies that discharge pollutants must disclose to the public the names of their major pollutants, discharge methods, discharge concentration and total volume of discharged pollutants and any discharge beyond the approved quota, as well as information relating to construction and operation of pollution-preventing facilities. Listed companies are subject to more demands of the disclosure of performing environmental protection duties. Apart from the environmental information (including the information of serious pollution in the course of major asset transactions), a listed company should also disclose information pertaining to poverty alleviation and other social responsibilities in accordance with the Guidelines on Governance of Listed Companies, which since its implementation in 2018, has established the basic framework for information disclosure of ESG (Environment, Social, Governance). Further requirements are established in documents released by China Securities Regulatory Commission (CSRC).

In addition to compulsory disclosures, the voluntary disclosure includes but is not limited to:

- the purpose and philosophy of the company in fulfilling its social responsibility;
- the protection of the rights and interests of shareholders and creditors
- the protection of the rights and interests of employees
- the protection of the rights and interests of suppliers, customers and consumers
- the environmental protection and sustainable development the company is involved in; and
- the public relations and social public welfare the company is engaged in.

What is distinct under Chinese law is that the efforts to revive the rural areas and reduce poverty is encouraged to be disclosed.

Law stated - 13 October 2022

CEO pay ratio disclosure

Are companies required to disclose the ‘pay ratio’ between the CEO’s annual total compensation and the annual total compensation of other workers?

This is not applicable.

Law stated - 13 October 2022

Gender pay gap disclosure

Are companies required to disclose 'gender pay gap' information? If so, how is the gender pay gap measured?

This is not applicable.

Law stated - 13 October 2022

UPDATE AND TRENDS

Recent developments

Identify any new developments in corporate governance over the past year. Identify any significant trends in the issues that have been the focus of shareholder interest or activism over the past year.

The release of the draft revision of the Company Law by Standing Committee of the National People's Congress on 24 December 2021, makes significant amendments to the Company Law in many respects, including corporate governance. For shareholders, classified shares are introduced in the law. By diversifying the types of shares, the company enjoys more autonomy. The authorised capital system is also introduced in, empowering the company to be provided with more flexibility about shares issuance. For the board of directors, the role has been clarified and attached with more importance when the board of directors is defined as an executive body and shareholders are entitled to determine the powers of the board of directors in the articles of association. Besides, the cap of board size is cancelled, leaving more room for the company to decide. The one-tier board structure in which supervisors can be omitted is also permitted under the draft revision of the Company Law. The organisation structure of some companies is simplified because it is feasible for companies with a smaller size not to set the board of directors. Employee directors are considered to be more common as the position no longer relates to whether the company is state-owned or not. The draft revision of the Company Law also strengthens the liabilities of the controlling shareholders, the directors, the supervisors and the senior managers. For example, the duty of loyalty and the duty of diligence are given more precise and extensive definition in its articles. By expanding the scope of connected persons, obliging the parties to report and avoid voting, the regulation of connected transactions is thus enhanced. Last but not least, social responsibilities of the company and the disclosure reports related are now given more encouragement. Currently, the collection of public comments in relation to this draft is over, but the possibility of further amendments cannot be ruled out. More shall be revealed when the formal revision of the Company Law becomes available.

Establishment of Beijing Stock Exchange

Differentiated from the Shanghai Stock Exchange and Shenzhen Stock Exchange, the Beijing Stock Exchange was set up in 2021 to support enterprises of a small and medium size but with bright prospects, especially for small and smart technology innovation companies. It designs its own regulations of corporate governance in the listing rules. Its listing rules include a whole chapter on regulations about how the shareholders' meeting, the board of directors and the board of supervisors' function, which is consistent with the basic requirements of listed company regulations. However, because listed companies in Beijing Stock Exchange are mainly small and medium-sized companies, the standard of information disclosure is more detailed. It raises the requirement of disclosure with respect to unusual stock fluctuations, rumour clarifications, share pledges, judicial freezes, litigation, arbitration and other matters.

Law stated - 13 October 2022

Jurisdictions

Australia	Kalus Kenny Intelex
Belgium	White & Case LLP
Brazil	Loeser e Hadad Advogados
China	Buren NV
France	Aramis Law Firm
Germany	POELLATH
India	Chadha & Co
Italy	Ughi e Nunziante
Japan	Anderson Mōri & Tomotsune
Kenya	Robson Harris Advocates LLP
Luxembourg	Bonn & Schmitt
Malaysia	SKRINE
Malta	GVZH Advocates
Mexico	Chevez Ruiz Zamarripa
Netherlands	Buren NV
Nigeria	Streamsowers & Köhn
North Macedonia	Polenak Law Firm
South Korea	Lee & Ko
Switzerland	BianchiSchwald LLC
Thailand	Chandler MHM Limited
Turkey	Gün + Partners
USA	Sidley Austin LLP