

China Legal Briefing*291

11 November 2023



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I Mutual Recognition of Public Documents - the Apostille Convention Entered into Force in China on 7 November 2023

II Administrative Measures for Independent Directors of Listed Companies

III The Rules on the Issuance of Convertible Corporate Bonds to Specific Objects by Listed Companies for Purchase of Assets (Draft for Comments)

I. Mutual Recognition of Public Documents - the Apostille Convention has Entered into Force in China since 7 November 2023

On 8 March 2023, China acceded to the *Convention of 5 October 1961 Abolishing the Requirement of Legalisation for Foreign Public Documents* (hereinafter the “**Apostille Convention**”). The Apostille Convention is the international treaty with the widest scope of application and the largest number of contracting parties under the framework of the Hague Conference on Private International Law. It aims to simplify the procedures for the transnational circulation of public documents.

On 7 November 2023, the Convention entered into force in China, meaning the cumbersome double legalisation procedure between China and the convention-contracting member states will be abolished. Public documents sent between China and other contracting states will be legally recognised in the recipient country with a certificate (i.e., an Apostille) as provided for in the Convention.

It is important to note that the traditional consular authentication process remains in place between China and (i) states that are not signatories to the Apostille Convention; as well as (ii) member states that China does not officially recognise as sovereign entities.

The Apostille Convention will take effect for Canada on January 11, 2024, and for Rwanda on June 5, 2024. On these specific dates, the Convention will be officially applicable between these countries and China. Additionally, it is essential to note that the Convention does not cover the relationship between China and India.

In the past, Wenfei’s clients had to invest a significant amount of time and expense in the conventional legalisation procedure. However, with the enforcement of the Apostille Convention, international document processing for both businesses and individuals is expected to become significantly more efficient and economical.

II. Administrative Measures for Independent Directors of Listed Companies

On August 4, 2023, the China Securities Regulatory Commission (“**CSRC**”) issued the Administrative Measures for Independent Directors of Listed Companies (the “**Measures**”), which came into effect on September 4, 2023. This article intends to briefly introduce the revision to the Measures for Independent Directors.

(1) The definition of independent director is made clearer and the standards on its independence are made stricter.

- The new definition clarifies that an independent director shall be independent of a listed company and its major shareholders, as well as the company's actual controller, and shall not have a "direct or indirect interest" in the aforementioned controller. (**Article 2** of the Measures);
- Independent directors should annually conduct self-examination of independence and submit the results to the board of directors. The board of directors of a listed company shall annually conduct an assessment of the independence of the incumbent independent directors, issue a special opinion and disclose such opinion together with the annual report. Among many other scenarios, there are also two additional new situations in which one shall not be allowed to serve as an independent director (**Article 6** of the Measures);

(2) Improvement of the mechanism for selecting independent directors.

- Granting the investor protection agency the right to nominate independent directors. The investor protection agency may publicly request shareholders to entrust it to exercise the right to nominate independent directors (**Article 9** of the Measures);
- Establishing a system for recognizing the qualifications of independent directors. Prior to the election at the shareholders' meeting, the stock exchange shall examine the candidates for independent directors, judiciously determine whether they meet the qualifications for the position and have the right to raise objections. The listed company shall not submit an objected candidate to the shareholders' meeting for election (**Article 11** of the Measures);
- Clarifying the period for re-election of independent directors. In the event that the proportion of independent directors does not comply with the relevant regulations or there is a shortage of accounting professionals, the by-election shall be completed within 60 days (**Article 14** of the Measures).

(3) Refinement of the legal responsibilities of sole directors

In terms of supervision, management and legal responsibility, the Measures firstly clarify the treatment and punishment for violations thereof; secondly, it clarifies the standards for determining the responsibility of independent directors, and details the factors for determining the administrative responsibility of independent directors, including the degree of correlation between the performance of their duties and the relevant illegal and irregular behaviours, the characteristics of the director's status and external identity, the role they play in decision-making, the extent to which they know about it, and the attitude they take after knowing about it, etc.; Finally, the exemptions from administrative penalties are clarified, which to a certain extent clarifies the standard of "diligence"

of independent directors and embodies the principle of unity and interdependency of responsibilities and rights.

In conclusion, the formal introduction of the Measures aims to promote the improvement of the independent director system and the systematization of the rules in various aspects, including emphasizing the independence of independent directors, giving full play to the role of independent directors, protecting the interests of small and medium-sized investors, and standardizing the governance of listed companies. It is a commonly shared goal that the Measures will have a positive and far-reaching impact on corporate governance and the efficient and high-quality development of the capital market.

III. The Rules on the Issuance of Convertible Corporate Bonds to Specific Objects by Listed Companies for Purchase of Assets (Draft for Comments)

On September 15, 2023, the China Securities Regulatory Commission (the “CSRC”) released *the Rules on the Issuance of Convertible Corporate Bonds to Specific Objects by Listed Companies for Purchase of Assets (Draft for Comments)* (the “Rules”). **Directional convertible bonds** as specified under the Rules are bonds issued by companies to specific parties. Bondholders can choose to convert the bonds into company stocks at the specified time and price, becoming shareholders of the company to receive dividends. Alternatively, they can choose to hold the bonds and receive principal and interest payments at the agreed-upon time and interest rate. The "equity nature" (shares) and "debt nature" (bonds) may provide market players with a more flexible mechanism in a transaction and are conducive to improving the vitality and efficiency of the mergers, acquisitions and restructuring activities in the market.

In this article, we will briefly introduce the key points of the Rules.

- **Conditions of Issuance**

A listed company issuing directional convertible bonds shall meet the same conditions for the public issuance of corporate bonds and for the issuance of new shares to specific objects (except that the converted shares are derived from repurchase). Meanwhile, listed companies that use directional convertible bonds as payment instruments to carry out restructuring shall also comply with the relevant provisions of *the Administrative Measures for the Material Asset Restructuring of Listed Companies* (the “Measures”).

- **Pricing Mechanism**

In consideration that both directed convertible loans and shares may be payment instruments, it is clarified in the Rules that the initial conversion price of the

directed convertible bonds shall not be less than 80% of one of the average trading prices of the company's shares in 20 trading days, 60 trading days or 120 trading days prior to the announcement date of the board resolution to issue the directional convertible bonds.

- **Lock-Up Period**

A sales restriction period of the directional convertible bonds is implemented to safeguard the interests of both listed companies and SME investors. Additionally, the Rules specify that directional convertible bonds within the lock-up period may be converted into stocks, and stocks after the conversion shall continue to be locked up until the expiration of the aforesaid lock-up period; and the lock-up period before and after the conversion shall be calculated together.

- **Investor Suitability**

The Rules clarify that if an investor who obtains directional convertible bonds does not meet the suitability requirements for stock investors in the relevant securities market, the directional convertible bonds held can be converted into shares, but after the conversion, they can only be sold out and cannot be used to buy in corresponding stocks. Investors who acquire directional convertible bonds shall comply with the stock exchange's investor suitability management requirements for directional convertible bonds.

- **Calculation of Interests**

When calculating the number and proportion of interests in a listed company owned by the relevant investor, the Rules clarify that the directional convertible bonds issued by the listed company held by the investor shall be taken into consideration. The directional convertible bonds held are to be aggregated with other non-equity interests of the investors in the same listed company. The proportion of its shareholding shall be compared with the proportion of its shareholding converted from non-equity securities under the aggregated calculation, whichever is the higher.

In conclusion, the Rules are expected to deepen the market-oriented reform of mergers, acquisitions and restructuring. The aim is to support listed companies to carry out restructuring by using the convertible corporate bonds issued to specific targets and used as the payment instrument.

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