

RISK RESILIENCE REPUTATION

Agile Strategy for Foreign Executives in China:

Avoid Personal Liabilities &
Navigate the Evolving Landscape



in partnership with





AGILE STRATEGY FOR FOREIGN EXECUTIVES IN CHINA

**Avoid Personal Liabilities &
Navigate the Evolving Landscape**

THE SPEAKER



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- Partner at Da Wo Law Firm Shanghai, in charge of Criminal Practice
- Member of Shanghai Bar Association for 10 years
- Legal Counsel of French Consulate General in Shanghai since 2017
- Specialize in White-collar and Corporate Crimes, Foreign Investment, International Commercial Law

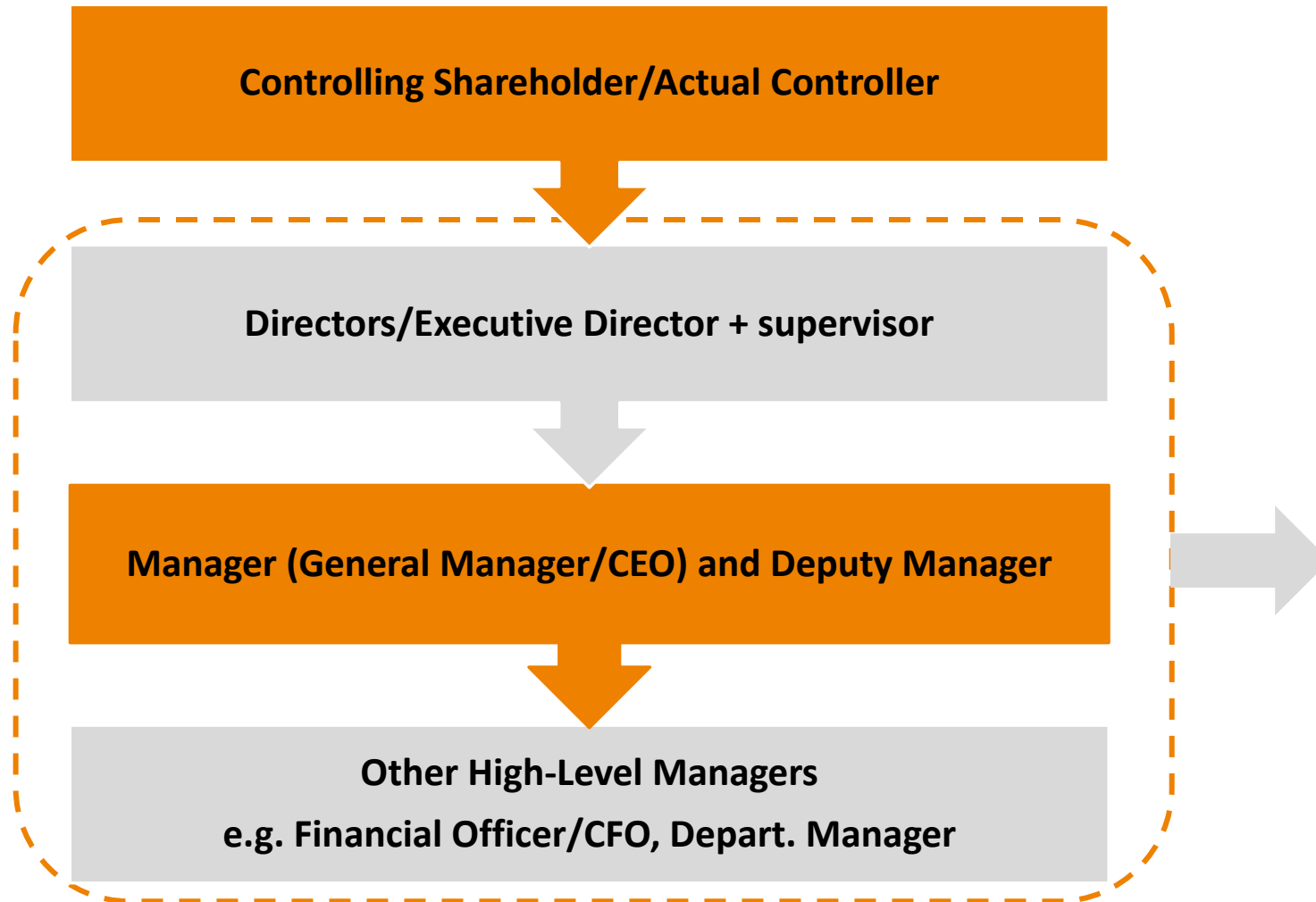
LEGAL FRAMEWORK

- Who is personally liable ?
- What are the liabilities ?
- How to avoid/mitigate such liabilities ?



I - Mapping “Executives” under Chinese Law

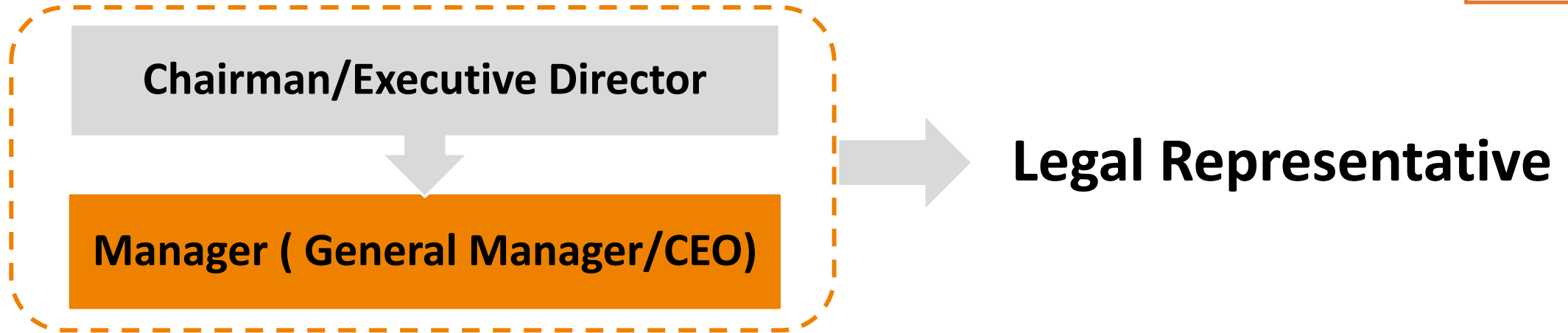
MAPPING “EXECUTIVES” UNDER CHINESE LAW



The determination of one's executive position is based on:

- 1) Articles of Association of the company/power of attorney, and**
- 2) Job description in the Employment Contract**

EXECUTIVE VS. LEGAL REPRESENTATIVE

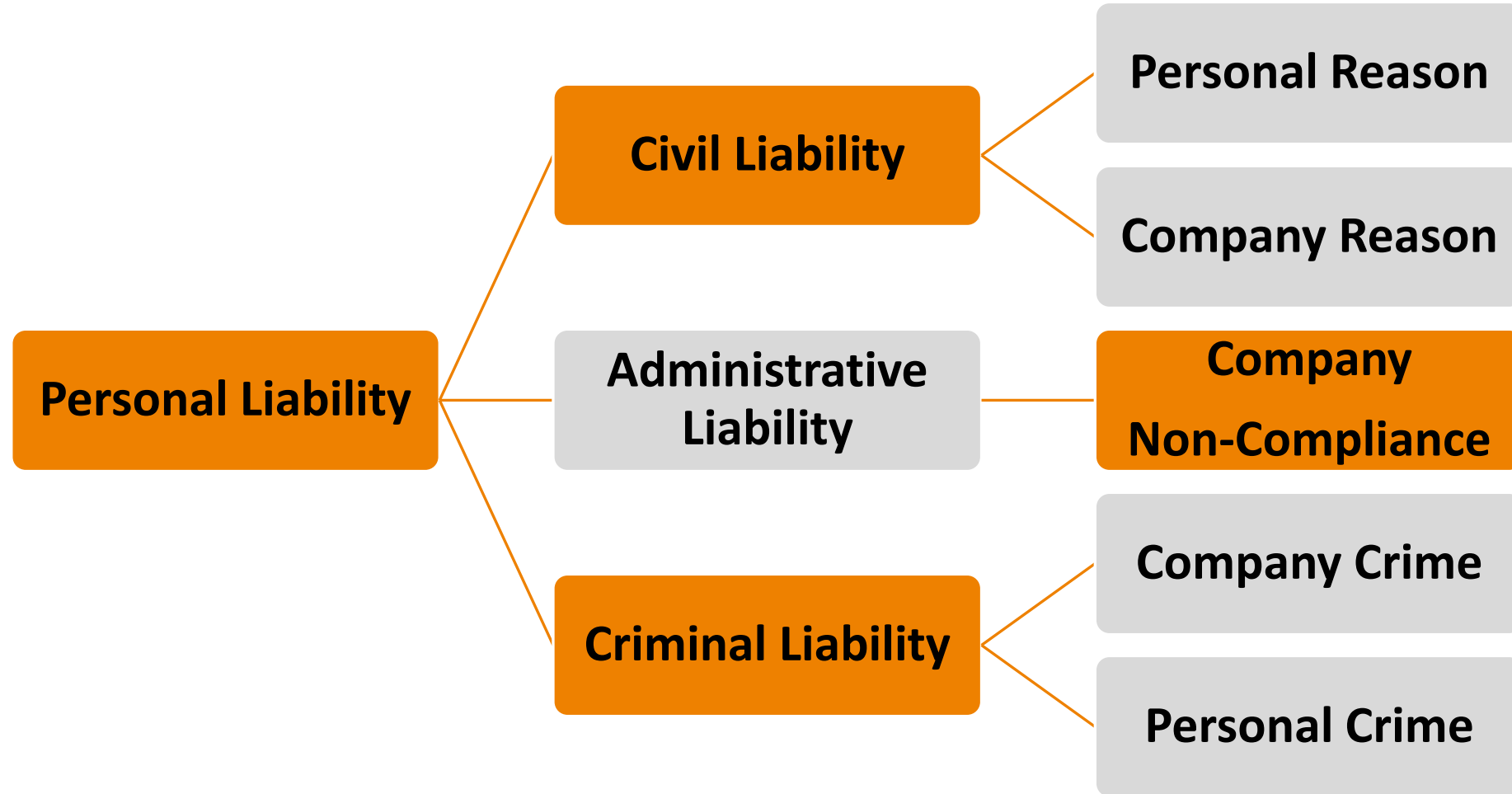


- Is Legal Rep. an executive ?
- Presumption of liability for Legal Rep. ?
- Is not being Legal Rep. a good way to avoid liability ?

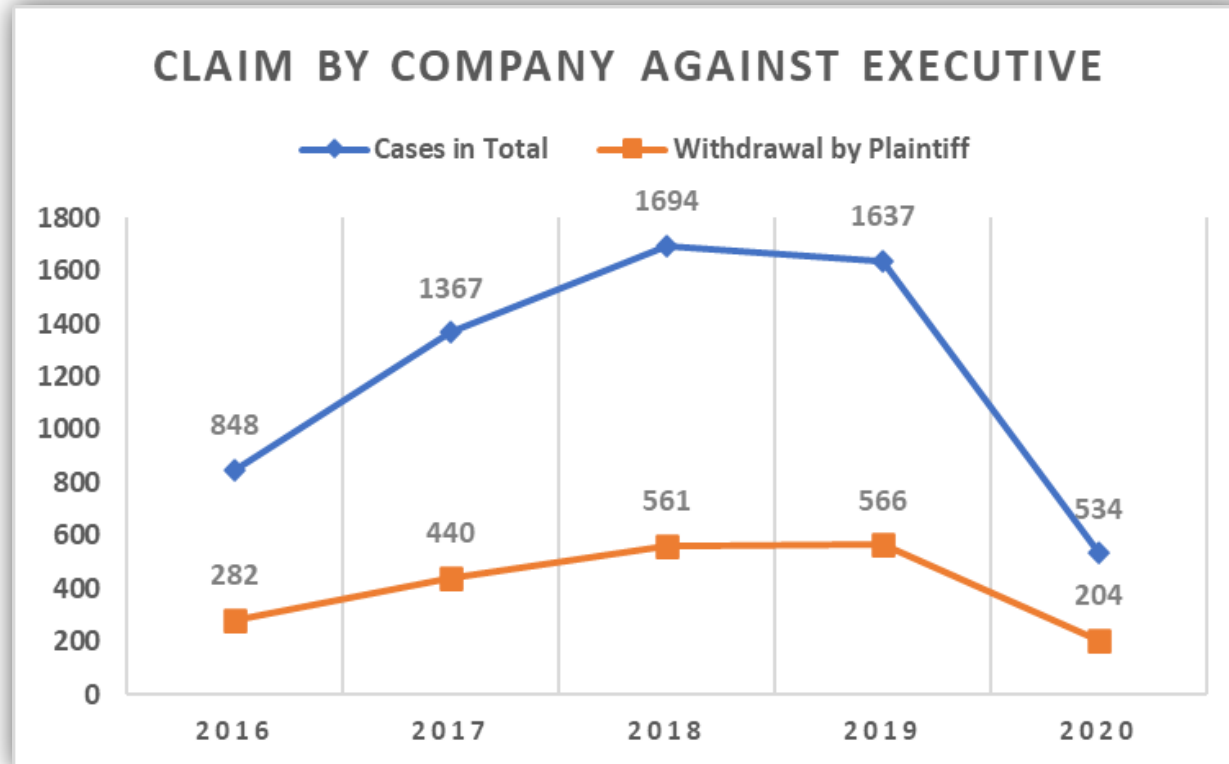


II - Executives' Personal Liability Overview

EXECUTIVES' PERSONAL LIABILITY OVERVIEW



CIVIL LIABILITY - PERSONAL REASON



- **Violation of Duty of Diligence & Duty of Loyalty by executives :**
 - Affiliated transactions
 - Misappropriation of funds
 - Disclosure of secrets
- **A growing trend of litigation against Executives from 2016-2018**
- **High Rate of withdrawal : 35%**

CIVIL LIABILITY - COMPANY REASON

Examples	Personal liabilities	Executives Potentially liable
<p>Ongoing court proceeding against a foreign invested company</p>	<ul style="list-style-type: none"> • Restriction on travel abroad 	<p>Legal representative, person in charge</p>
<p>Failure to execute a court decision</p>	<ul style="list-style-type: none"> • Restriction on luxury consumption • Restriction on travel abroad • Fines • Judicial detention 	<p>Legal representative, person in charge, person directly responsible for impact on performance of the obligation</p>

ADMINISTRATIVE LIABILITY - REGULATION AXIS



- Industry-specific laws and regulations are being updated frequently
- A growing number of industries are being regulated
- Increasing focus on personal liability by the authority

ADMINISTRATIVE LIABILITY - CONSEQUENCES

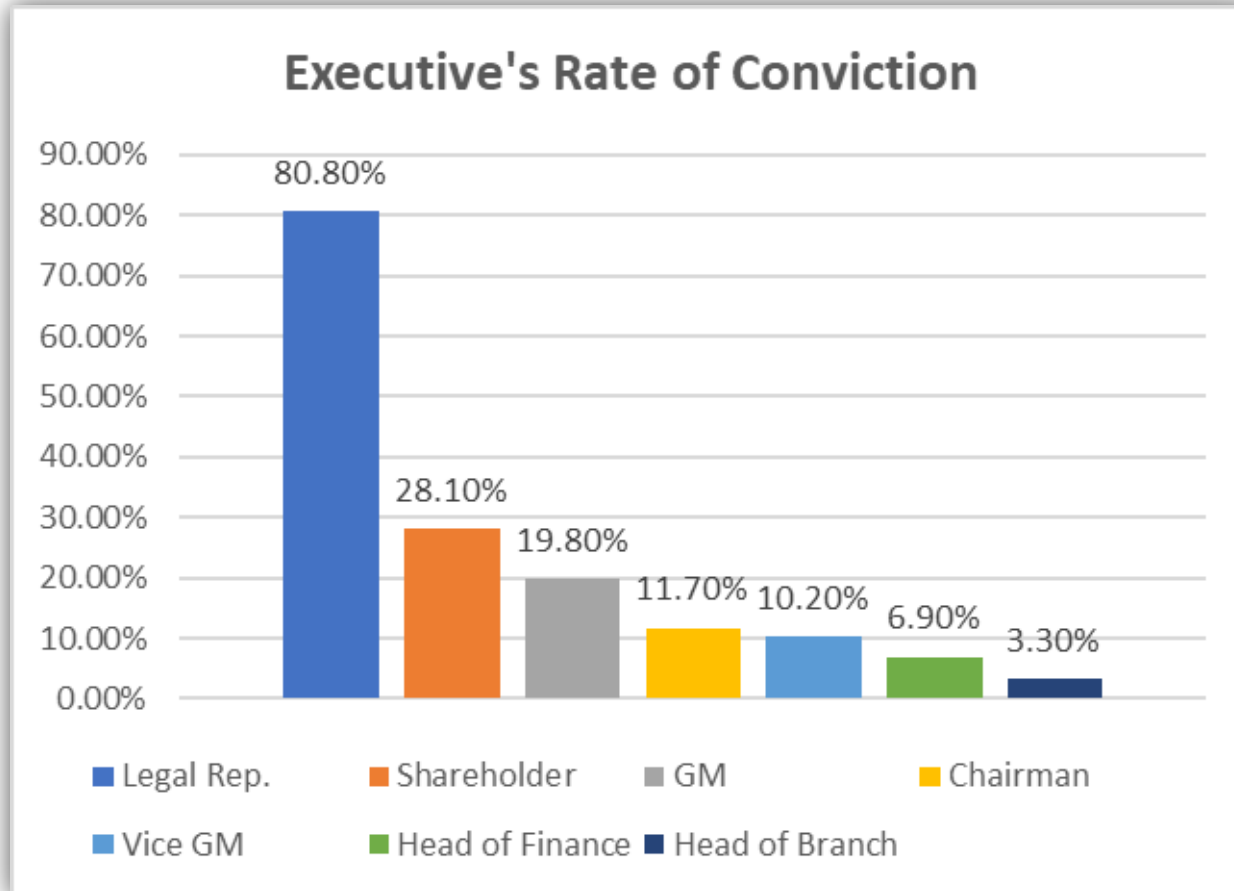
- Fines or administrative detention may be imposed on legal rep. or the person in charge
- The executive's future career prospects may be affected:
 - ◆ No director/supervisor/manager position in other companies for 3 years if he/she is personally liable in case involving revocation of business licenses
 - ◆ No future position as person in charge in certain industry, e.g. food industry
 - ◆ "Clean record" is needed for holding a management position in a listed company

CRIMINAL LIABILITY - COMPANY CRIME

“Dual-penalty” Principle :

- ◆ Monetary penalties on the company
- ◆ Criminal penalties on the person directly in charge/directly responsible
 - Detention, imprisonment or even death penalty
 - Fine or confiscation of property
 - Deportation may be applicable for foreign executives
 - Enforcement measures during investigation process

CRIMINAL LIABILITY - LESSONS FROM 2019



Source: www.itslaw.com

- Legal Rep. is highly likely to be convicted in case of company crimes.
- The chance of GM and Chairman being charged is quite high.
- Financial manager is more likely to be charged than other depart. managers.

CRIMINAL LIABILITY - WHITE-COLLAR CRIME

- ◆ Embezzlement
- ◆ Misappropriation of funds
- ◆ Commercial bribery (offering or taking)
- ◆ Illegal fundraising
- ◆ Making illegal profits for relatives and friends
- ◆ Contraband
- ◆



III - Strategy for Avoiding and Mitigating Personal Liabilities

PREVENTIVE MEASURES

For executives of top management/holding level

- Keep updated on laws and regulations specific to the company's industry, design and implement proper compliance policies
- Review and update regularly the organization structure and the chain of responsibilities of the company
- Define and keep documentation of detailed powers and responsibilities of other executives and key employees, such as power of attorneys, board resolutions, internal regulations and employment contracts
- Prepare contingency plan to ensure continuity of operations in the event that local management is under investigation

PREVENTIVE MEASURES

For other executives

- Understand your position as an executive from a legal perspective; look deep into your responsibility both as an employee and as part of the corporate management structure
- Be aware of laws and regulations specific to your industry, follow company compliance policies
- Keep written records of any objections throughout the decision making process in case non-compliant behavior is identified
- Remain diligent and loyal to the company, be careful with any situation that may present a conflict of interest



Questions & Answers



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Directors & Officers Liability

Agile Strategy for Foreign Executives in China



IN PARTNERSHIP WITH





WHO ARE WE?

GET TO KNOW US





We are a group of international insurance brokerage companies.

We specialize in advising and servicing clients professionally.

With trust, care and integrity we protect our client`s best interests.

Insuring 30,000+ lives insured worldwide

Fully licensed insurance broker in Mainland China, Hong Kong and Singapore.

We advise groups and individuals on:

Medical Insurance, Life Insurance, Liability Insurance, Property & Casualty Insurance

WHAT
WE BELIEVE
IN

Care

Experience

Integrity

Service

Innovation



We've got an International Presence

- 1 Headquartered in Hong Kong
- 2 Founded in 1997
- 3 Presence in 6 cities
- 4 A team of 130 persons from 17 nationalities
- 5 Multilingual service including Mandarin, English, French, Italian, Spanish, German, Portuguese...



MEET OUR STRATEGIC PARTNER



Established on 1st
August 2008 in Beijing



4 main business
segments

Sales agent, Insurance broker,
Insurance assessment – fraud
detection, Internet insurance



5Bn CNY premium in
2018



Cover 26 provinces and municipalities



Presence in 140 advanced cities



50,000 sales personnel



As our local partner, Datong Group has a well-established presence in China and we benefit from it.

Our Insurance Partners we chose to work with





CONTEXT

Senior managers and legal representative are exposed to various risks

Adherence to regulatory compliance, labor dispute, litigation with clients/ suppliers etc.

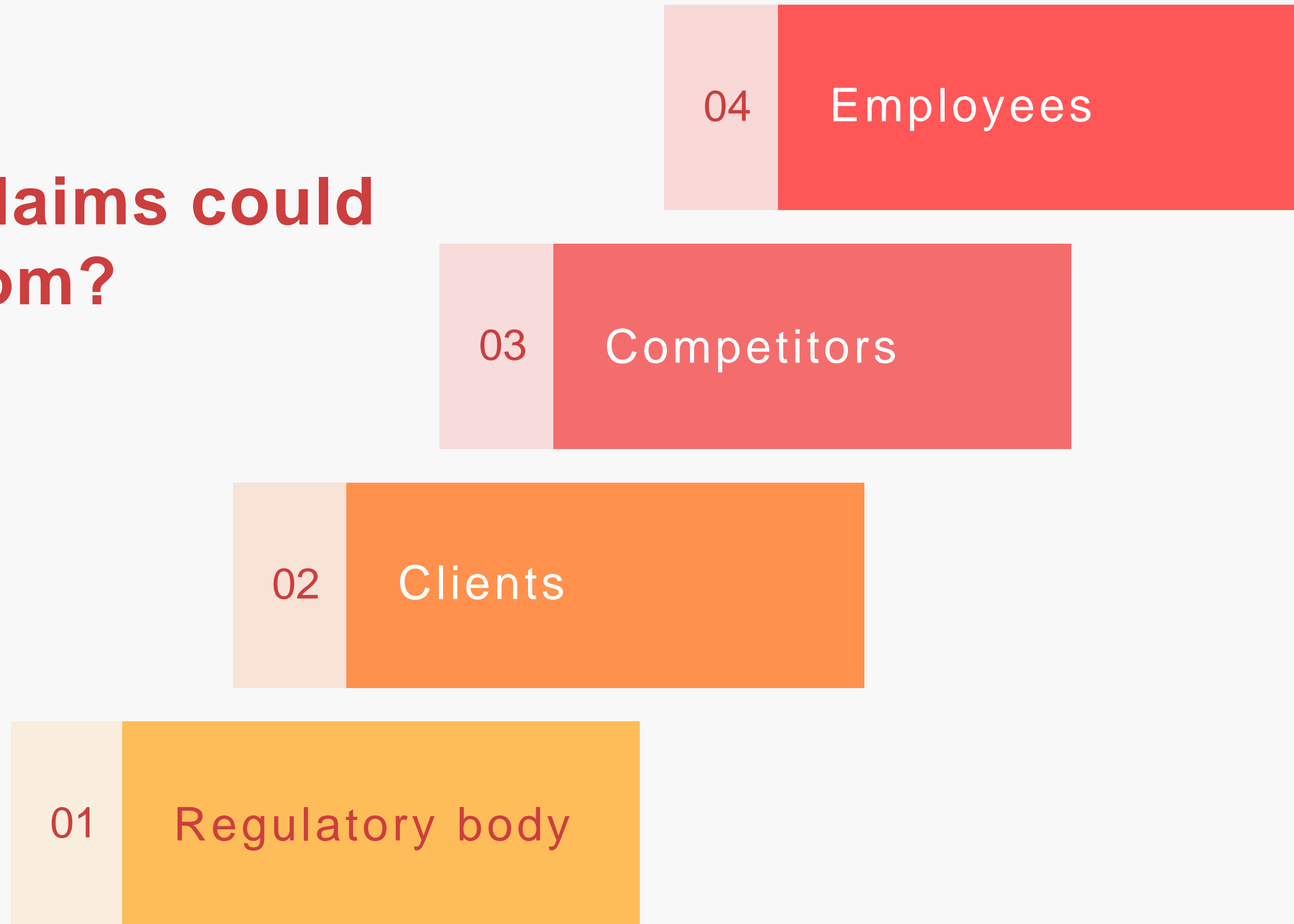
Plaintiffs are more willing to engage in legal proceedings

The number of claims made against directors are increasing.

Personal assets can be involved

Should their direct responsibility be put in evidence, directors may be condemned to pay fines from their own funds.

Where claims could come from?





The number of claims against executives doubled in 20 years



Increased regulator and prosecutor resources feed into activist shareholder lawsuits



Top cause of D&O claims is non-compliance with laws and regulations, followed by negligence and maladministration



**Why More
Companies
Consider Getting
D&O Coverage?**



Increase in the number of Class Actions lawsuit



Growing concern about the reputation damages



Skyrocketing legal defense costs with slow to resolve and more complex cases



The largest cases have reached a Billion Dollar in settlement



WHAT IS A DIRECTORS & OFFICER POLICY?



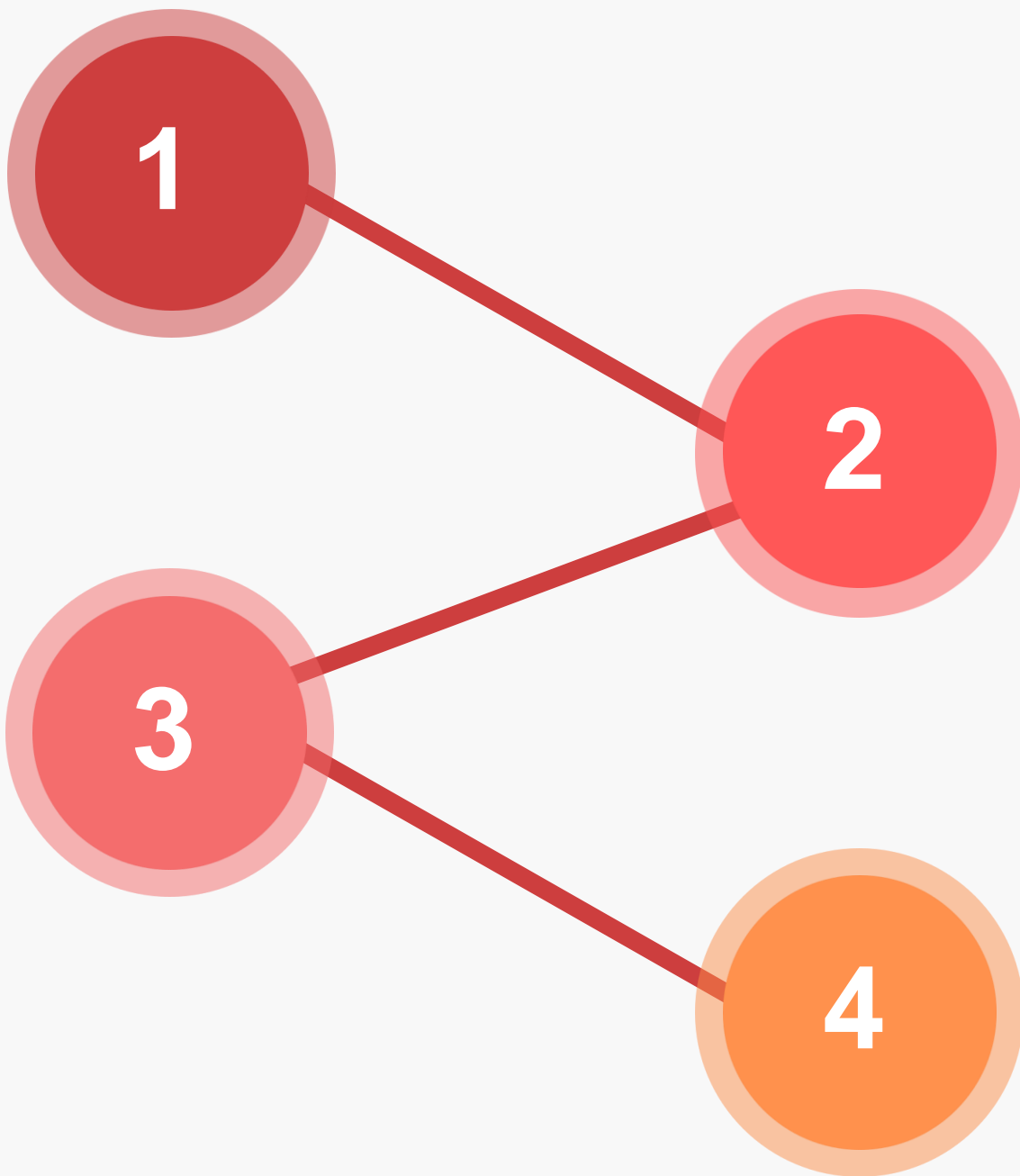


- This policy provides corporate and **personal protection** for directors, officers and management against financial loss arising from the potential exposures associated with managing or supervising the company (whether private or listed), and legal representation expenses regarding regulatory investigations.
- This policy cover directors & officers when they are sued personally due to wrongful acts.
- Directors & Officer's liability insurance applies to anyone who serves as a director or an officer of a for-profit business or non-profit organization. Directors & Officer include CEO, COO, CFO, HRD etc. It usually covers **a group of people**.

COVERAGE HIGHLIGHTS

Defense costs, legal representation expenses, damages, judgements, settlements, bail bond costs, crisis costs, deprivation of asset costs, prosecution costs, public relations expenses

Tax contributions where the parent company has become insolvent and there's personal liability of an insured



Costs arising from extradition proceedings

Losses incurred against Insured Person for civil fines and penalties








MORE SPECIFICALLY **D&O INSURANCE CAN:**

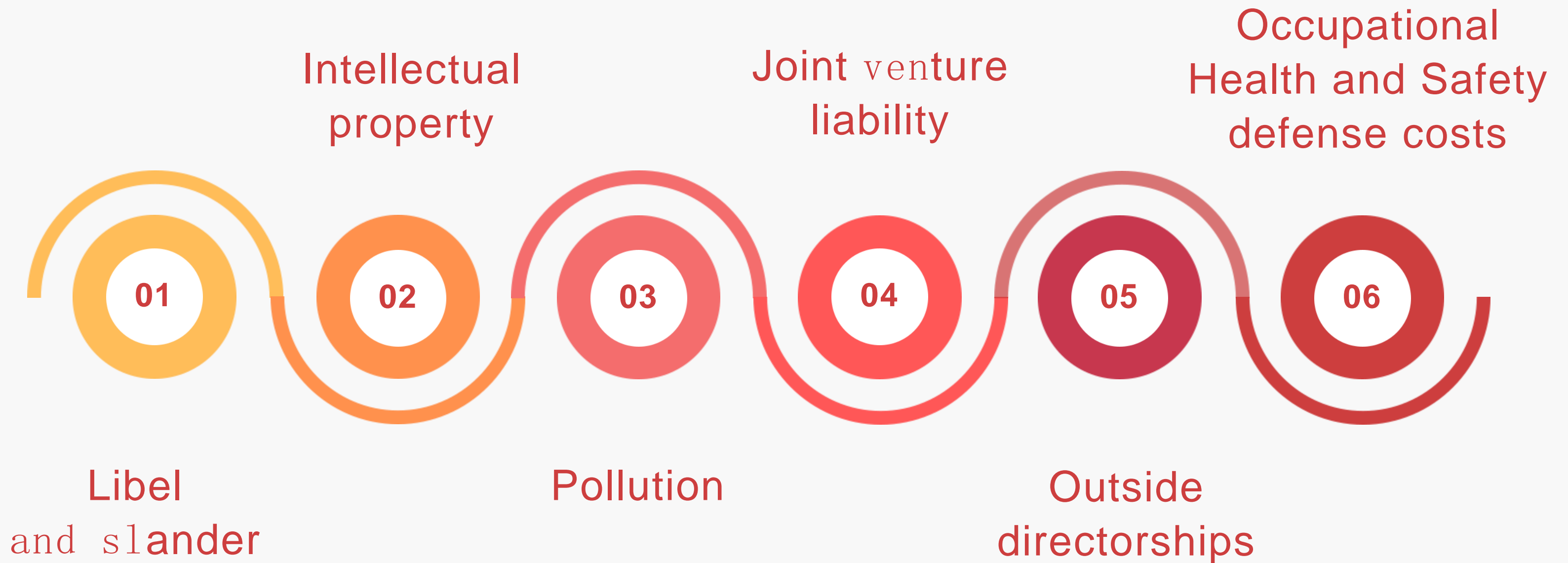
- Cover litigation brought by stakeholders against directors and officers where there has been an allegation of a breach of duty or breach of law
- Respond to litigation arising out of a broad range of business activities including IPO or other debt or equity initiatives, M&A, financial reporting & other statutory obligations and corporate failures
- Provide umbrella cover to all the directors and officers of the holding company and all subsidiary companies. The insurance can also extend to joint venture or associated company board positions.

MORE SPECIFICALLY

D&O INSURANCE CAN:

-  1 Cover all the current, past and future directors and officers on an unnamed basis
-  2 Pay legal defense costs, including the advancement of defense costs as well as settlements and judgments awarded by the court for indemnified claims
-  3 Cover employment related claims brought against the company
-  4 Cover securities claims brought against the company
-  5 Be structured to comply with the insurance laws of other jurisdictions.

COVERAGE EXTENSIONS



WHAT ARE THE MOST COMMON D&O RISK SCENARIOS?

Common risk scenarios include failure to comply with regulation or laws, reporting errors or misrepresentation.

1



Conflicts of interest
e.g. Positions on outside boards

2



Wrongful termination,
sexual harassment or
discrimination

3



Initial public offerings

4







Misrepresentations

Common D&O risk scenarios

- Employment practices and HR issues
- Shareholder actions
- Reporting errors
- Inaccurate or inadequate disclosure (for example, in company accounts)
- Misrepresentation in a prospectus
- Decisions exceeding the authority granted to a company officer
- Failure to comply with regulations or laws
- Corporate manslaughter
- Insolvencies
- Creditor claims
- Mergers and acquisitions
- Divestitures
- Competitor claims
- Claims made by the company, itself

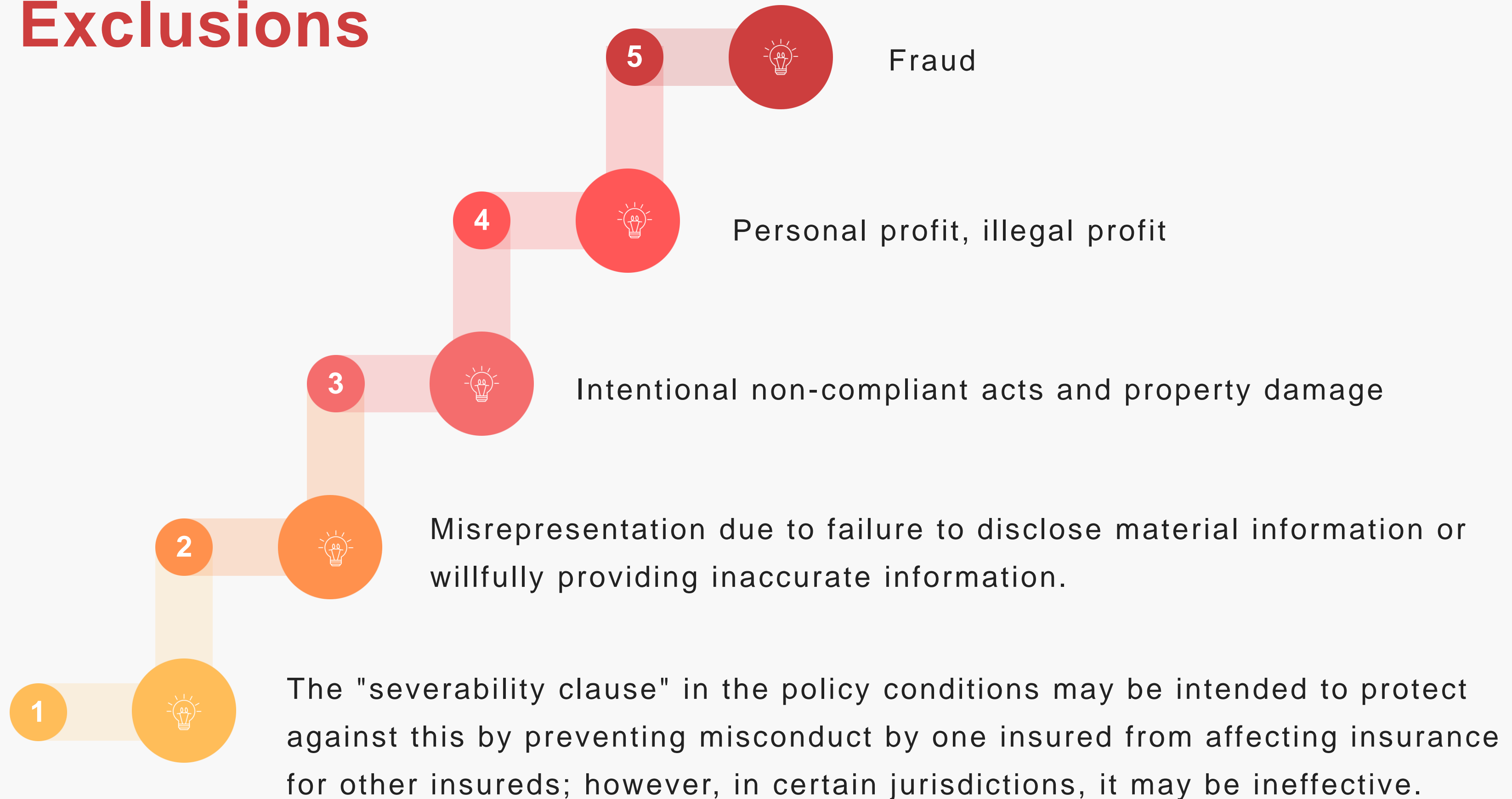
EMERGING RISKS

-  1 Environmental pollution/climate change related
-  2 Cyber incident – data protection
-  3 Shareholder activism
-  4 Public outcry resulting in government investigation

WHAT IS NOT COVERED?

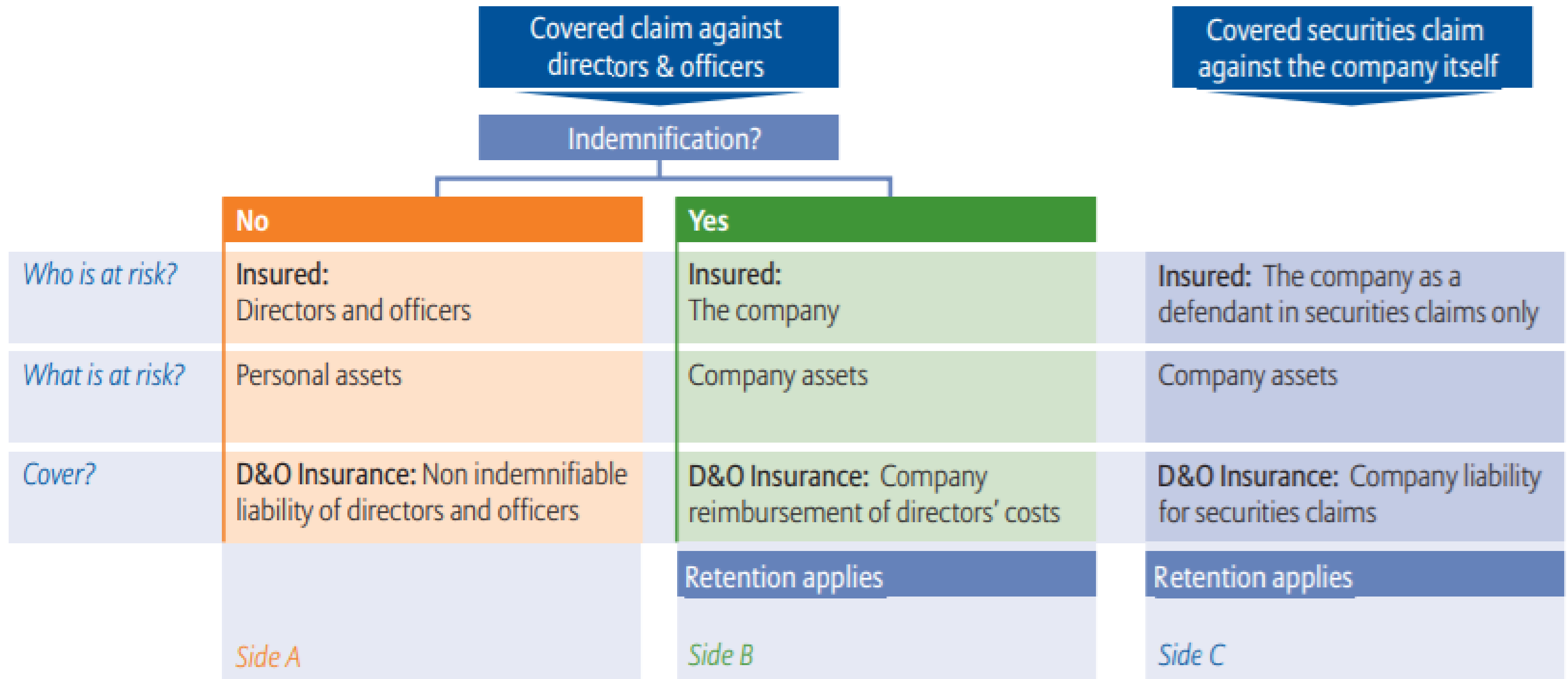
- Intentional fraudulent actions, dishonest act, misconduct
- Personal Gain
- Discrimination
- Wrongful termination
- Breach of contract
- The antitrust or competition exclusion
- Legal action taken before the policy started
- Claims made to a previous policy or paid by another insurance company

Exclusions



D&O insurance structure

HOW DOES IT WORK?





D&O INSURANCE STRUCTURE

The structure of a D&O insurance policy depends on which of three insuring agreements are purchased (ABC policies are generally chosen, as these are standard form policies for publicly listed companies; for private or non-profit companies, only AB policies would be used).

Cover	Description	Who is the insured?	What is at risk?
Side A	Protects assets of individual directors and officers for claims where the company is not legally or financially able to fund indemnification	Individual officer	His/her personal assets
Side B	Reimburses public or private company to the extent that it grants indemnification and advances legal fees on behalf of directors/officers	Company	Its corporate assets
Side C	Extends cover for public company (the entity, not individuals) for securities claims only	Company	Its corporate assets

- Directors and officers are confronted with an increasing peril that their company may not be able to reimburse them for loss. An extra layer of defense to personal funds can be secured by purchasing Side A cover, which ensures directors and officers only (not the company) when indemnification is unavailable.
- Often not enough coverage is bought for the risk, so a major trend is for more Side A cover to be purchased in order for an individual officer to protect personal assets. D&O cover has become a regular cover for large multinational companies, but all sizes of organizations – public, private or non-profit – have potential exposures.
- There is increasing demand for SME D&O cover, though penetration is still low due to lack of awareness and education. D&O products are perceived to be expensive, but actually are quite affordable. For example, a small firm with a \$100m turnover can obtain no-frills D&O cover with very low limits for less than \$1,000 per year.

HOW D&O WORKS : EXCESS LAYER STRUCTURE

Larger sized programs with limits **over \$30m** are usually too large for one insurer and require a group of insurers to share the risks. In this setup, the lead insurer is usually more experienced and able to handle wordings, advise on international insurance program (see below) setup and settle claims.

The lead carries the “primary layer” up to, for example, \$30m, and would pay claims up to that amount. When that limit is reached, it “erodes” and the next layer kicks in, up to a certain amount, and so on. The lead insurer carries most of the claims and generally pays defense costs and creates policy wording, so is most at risk. Hence, premiums are much higher.

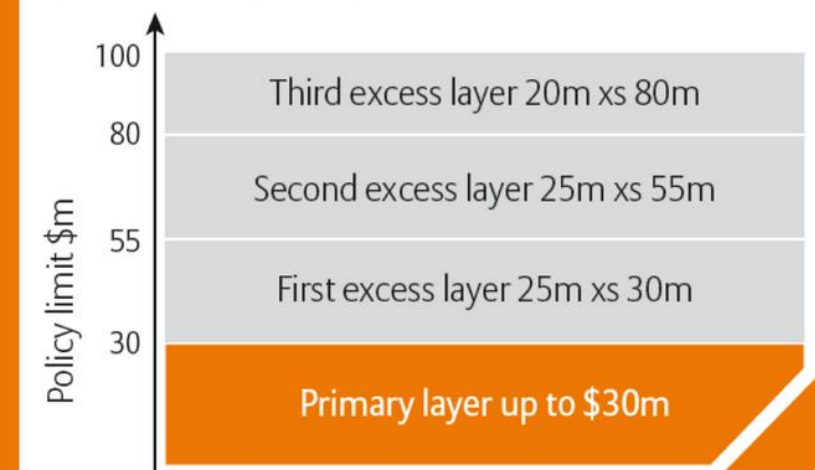
Another way of risk sharing is through proportional coinsurance, where insurers split the premium proportionally depending on their risk share. Claims would be settled likewise. More difficult scenarios with mixtures of proportional and non-proportional elements also exist.

Each insurer will be **re-insured** to cover risk beyond their insurance capacity.

An example excess layer structure

- Total cover of \$100m
- Panel led by Insurer A
- Insurer A pays initial losses up to \$30m
- Further losses covered by Insurer B, etc.
- Insurer A carries the most costs and claims and therefore receives a larger, non-proportional share of the premium

Excess layer structure
(limit \$100m) non proportional



Proportional coinsurance (limit \$100m)

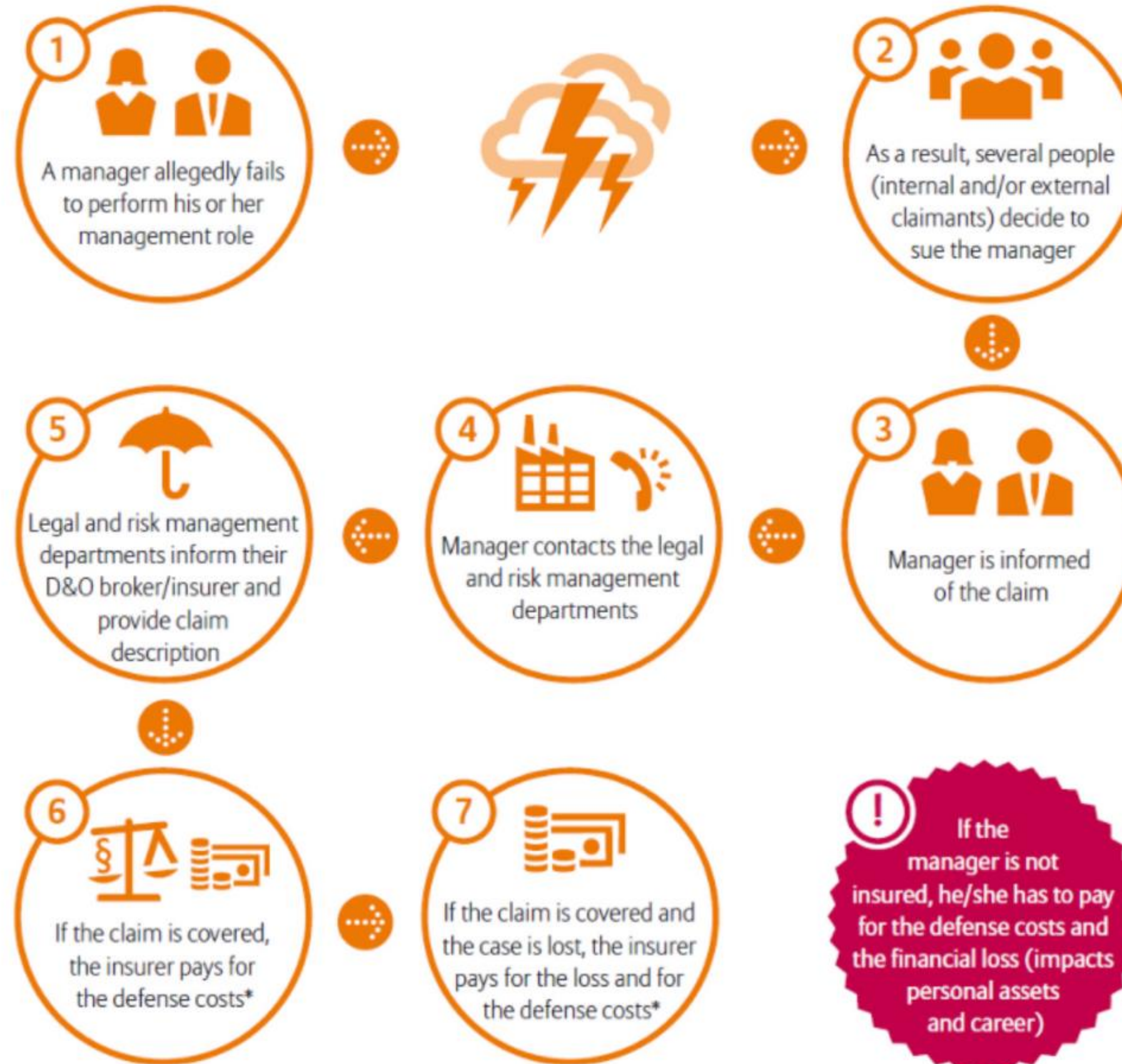


International Programs

Larger clients with subsidiaries in other countries need an **international insurance solution** to protect directors and officers in all markets. Some markets require the company to take out insurance from a locally admitted insurer.

Other more progressive markets allow a **master policy** to be issued in another country that covers **local exposures**. Cover is typically provided by a combination of locally admitted policies and a global master policy, which provides additional cover to harmonize the protection globally (unless standalone local policies are required).

HOW DOES D&O WORKS IN PRACTICE?



What a D&O claim mean?

A specimen D & O claim definition may read:

Claim means:

1. A written demand for monetary damages, nonmonetary damages or injunctive relief; or
2. A civil proceeding commenced by service of a complaint or similar pleading; or
3. A criminal proceeding commenced by a return of an indictment; or
4. An administrative or regulatory proceeding commenced by the filing of a formal, written notice of charges, notice of violations, notice of investigation, cease and desist or similar action; or
5. An arbitration proceeding seeking monetary damages; or
6. A written request to toll or waive a statute of limitations relating to a potential civil or administrative proceeding; against any **Insured** for a **Wrongful Act**, including any appeal there from.

EXAMPLE OF D&O CLAIMS

PROVIDED BY DNO INSURERS

Claim 1

Insured: CEO

Misconduct: alleged breach of fiduciary duty.

Claim for compensation: civil action

Loss: defense costs, settlement amount

The defense cost is more than 5 million yuan, and the settlement amount is more than 6 million yuan

Non listed company, headquartered in China with overseas branches. Risk could still happen from overseas but settled in China.

Claim 2

Insured: several directors

Misconduct: alleged inaction

Claims: regulatory investigation

Loss: Legal defense fees

No penalty was imposed after the investigation. The legal defense fee however exceeded 1 million yuan after removing the deductible.

Directors (supervisors) and senior executives are also faced with the risk of regulatory investigation!

Claim 3

Insured: overseas subsidiary

Misconduct: alleged employment misconduct

Claim for compensation: civil action

Loss: settlement amount, lawyer's fee

In the end, the two sides reached a settlement of more than 110,000 USD, including severance payment, mental damage compensation and lawyer's fees. After deducting severance payment and deductible, the total amount of settlement and lawyer's fee exceeds 60,000 USD.



HOW MUCH COVERAGE DO I NEED?

The limit of liability is available for the payment of legal defense costs, settlements and court awarded judgements, which would be otherwise payable by a company or its executive.

It is payable after the retention (deductible) has been settled by the policyholder. The amount depends on the scope of its operations, but also the type and number of stakeholders affected by the actions of directors and the risk inherent to the business.

D&O claims can be very long (2-3 years), and defense fee can consume most of the benefits hence it is important to forecast the right amount.

The coverage will also depend on the company revenue

1. small companies with a few million \$ will usually insure \$1-2M,
2. larger private companies could go from \$5-10M and listed companies up to \$50M

WHAT INFORMATION ARE REQUIRED TO GET A PROPOSAL

- Description of the company (name, address, activity, number of employees)
- Constitution articles of the company
- Last two years financial report
- Ownership structure
- Whether the company is listed or not?
- Indemnity limit and deductibles desired
- Name and qualification of the directors
- Loss history and any foreseen claims



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**ANY
QUESTIONS
?
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