# RECONCILING DUAL LOYALTIES: DIRECTOR DUTIES IN "STATE-INVESTED COMPANIES" UNDER CHINA'S 2023 COMPANY LAW

Ben Hines

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*Abstract:*

*The ratification of significant amendments to the Company Law of the People's Republic of China in December 2023 heralded comprehensive changes to China's corporate governance regime. Under this reform, directors' duties are outlined with greater clarity and specificity than before, and textually appear reminiscent of those imposed in various other jurisdictions. At the same time, questions arise as to the duties of directors in "State-Invested Companies". In practice, there is no doubt that under the Chinese system directors of such companies will generally owe and act upon duties—legal, political, or otherwise—to both company and state. The question, therefore, is not if but how the legal basis of these duties is reconciled under the 2023 law. This article posits that this reconciliation ought not be approached through western common law fiduciary principles alone. Rather, it posits that when read with an understanding of the Chinese legal-political context there are three potential sources in the law itself which may legally ground such dual obligations. The vague drafting of directors' duties provisions, the shareholder/director dynamic, and the ability for a State-Invested Company to arrange its articles of association such that these two interests may legally be conflated each provide a legal mechanism to import obligations to consider the interests of the state in addition to those of the company. Appropriately distilling these bases has important practical ramifications for investors in the Chinese market and their understanding of the potentially competing obligations acted upon by directors. It may also materially impact the exercise by these directors of their functions.*

*Keywords: Directors' Duties; Fiduciary Duties; State-Invested Companies; State-Owned Enterprises; Company Law; People's Republic of China; Articles of Association; Governance.*

## I. INTRODUCTION

When the Standing Committee of the 14th National People's Congress ratified a swathe of amendments to the Company Law of the People's Republic of China[1] (generally the "Company Law", or, as amended, the "2023 Company Law") on 29 December 2023,[2] exactly 30 years after the original Company Law was adopted,[3] it introduced some of the most significant and wide-ranging changes in decades to the legal regime governing corporations in China.[4] Despite the

[1] Gongsi Fa (公司法) [Company Law] (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 29, 1993, effective July 1, 1994; rev'd by the Standing Comm. Nat'l People's Cong., Dec. 25, 1999; rev'd by the Standing Comm. Nat'l People's Cong., Aug. 28, 2004; rev'd by the Standing Comm. Nat'l People's Cong., Oct. 27, 2005; rev'd by the Standing Comm. Nat'l People's Cong., Dec. 28, 2013; rev'd by the Standing Comm. Nat'l People's Cong., Oct. 26, 2018; rev'd by the Standing Comm. Nat'l People's Cong., Dec. 29, 2023) (Chinalawinfo) [hereinafter 2023 Company law].

[2] Shu Du et al., *Broad Reforms to China's Company Law Will Affect Most PRC Companies*, SKADDEN (Mar. 2024), https://www.skadden.com/insights/publications/2024/03/insights-special-edition/broad-reforms-to-chinas-company-law.

[3] Manuel Torres & Yingchun Lu, *Highlights of 2023 Revision to Company Law of China*, GARRIGUES (Jan. 30, 2024), https://www.garrigues.com/en_GB/new/highlights-2023-revision-company-law-china#:~:text=On%20December%2029%2C%202023%2C%20marking,of%20companies%2C%20liabilities%20of%20senior.

[4] In total, 16 provisions were removed and more than 70 were either inserted or substantially amended as compared to the Company Law as revised previously in 2018: *See* Gongsi Fa (公司法) [Company Law] (Dec. 29, 1993, effective July 1, 1994; rev'd by the Standing Comm. Nat'l People's Cong., Dec. 25, 1999; rev'd by the Standing Comm. Nat'l People's Cong., Aug. 28, 2004; rev'd by the Standing Comm. Nat'l People's Cong., Oct. 27, 2005; rev'd by the Standing Comm. Nat'l People's Cong.,

amendments still being in their infancy,[5] having only come into effect on 1 July 2024,[6] reactions from both practitioners and academics have been largely favorable, highlighting enhancements in the law's clarity, comprehensiveness, and structural cohesion.[7] Despite these apparent improvements, however, uncertainty remains in a number of key areas, including in the vitally important realm of directors' duties.

The 2023 Company Law appears to have been crafted to adapt to China's increasingly internationalized market environment and to stimulate both foreign and domestic investment in Chinese enterprises. To that extent, it makes sense that a considerable number of these amendments targeted areas such as enforcing capital contributions,[8] improving shareholder rights,[9] and enhancing corporate governance.[10] Such changes, in theory, provide greater certainty to investors and, at least to foreign investors, appear to align various elements of the Chinese law in this area with more familiar and longstanding legal regimes in other jurisdictions.

While much scholarly discussion has focused on the general implications of these reforms, particularly concerning the clarified duties of directors in China, scant attention has been paid to how the 2023 Company Law affects directors of State-Invested Companies (SICs), also referred to where applicable as State-Owned Enterprises (SOEs). Still less attention appears to have been placed, even before the most recent amendments, on the legal duties of these directors and how they may differ from those owed by directors in non-SICs. It appears clear that these directors in China, even those appointed as independent directors,[11] will at least in practice owe and act upon duties—legal, political, or otherwise—to both the company on whose board they serve and to the state.[12] After all, these companies are generally "owned", in whole or as a significant majority shareholder, by the state.[13] In practice, they are controlled by the State.[14] The directors are appointed, in one

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Dec. 28, 2013; rev'd by the Standing Comm. Nat'l People's Cong., Oct. 26, 2018) (Chinalawinfo) [hereinafter 2018 Company law].

[5] It is also worth noting here that in addition to the promulgation of the Company Law itself, the relevant Chinese authorities will continue to publish additional rules, regulations, and guidance documents to provide greater clarity on the law's effect in practice.

[6] 2023 Company Law, art. 266.

[7] *See* Shirley Sung & Reyna HU, *China's new company law: A summary of important changes for multinational orga nisations*, VISTRA (Sept. 3, 2024), https://www.vistra.com/insights/chinas-new-company-law-summary-important-changes-mu ltinational-organisations; Arendse Huld, *China's Revised Company Law in Effect from July 1, 2024: Key Details Here*, CHINA BRIEFING (Jul. 1, 2024), https://www.china-briefing.com/news/china-company-law-amendment-july-1-2024/; Du et al., *supra* note 2; Torres & Lu, *supra* note 3; Katharine Yin & Kate Tang, *Amendments to Company Law in China*, C LYDE & CO (Mar. 26, 2024), https://www.clydeco.com/en/insights/2024/03/amendments-to-company-law-in-china; Sarah Wong, *Explainer: How Will the Updated Company Law Help Corporate China?*, ASIAN LEGAL BUSINESS (Jul. 18, 202 4), https://www.legalbusinessonline.com/features/explainer-how-will-updated-company-law-help-corporate-china.

[8] *See* 2023 Company Law, arts. 47–56, 87–8, 98–9, 105, 225, 227–28, 266.

[9] *See id.* arts. 57, 71, 110, 187, 189, 190, 231.

[10] Huang Ling & Wu Ye, *Transformative Updates to China's Corporate Governance: A Comprehensive Overview of th e 2023 Amendment to PRC Company*, KING & WOOD MALLESONS (Feb. 29, 2024), https://www.kwm.com/us/en/insights /latest-thinking/transformative-updates-to-chinas-corporate-governance-a-comprehensive-overview-of-the-2023-amendment-to-p rc-company-law.html.

[11] Liu Junhai (刘俊海), *Shangshi Gongsi Duli Dongshi Zhidu de Fansi he Chonggou - Kangmei Yaoye Anzhong Dudong Jue Liandai Peichang Zeren de Falv Sikao* (上市公司独立董事制度的反思和重构——康美药业案中独董巨额连带赔偿责任的法律思考) [*Reflection and Reconstruction of the Independent Director System of Listed Companies: Legal Consideration on the Huge Joint and Several Liability of the Independent Directors in Kangmei Pharmaceutical Case*], 3 FAXUE ZAZHI (法学杂志) [LAW SCIENCE MAGAZINE] 1, 10 (2022); Ma Kehui, *Analysis on New Regulations and Future Road of Independent Directors in China*, 16 TSINGHUA CHINA L. REV. 125, 137 (2023).

[12] Marcos Jaramillo, *Directors' Duties in China* , *in* RESEARCH HANDBOOK ON DIRECTORS' DUTIES 171–4 (Adolfo Paolini ed., 2014); Jiangyu Wang, *The Political Logic of Corporate Governance in China's State-owned Enterprises*, 47 CORNELL INT'L L.J. 631, 648 (2014).

[13] Zhengfei Lu & Jigao Zhu, *Tracing back to the source: Understanding the corporate governance of boards of directors in Chinese SOEs*, 13 CHINA J. ACCT. RSCH 129, 131–3 (2020).

[14] *Id.*

way or another, by the state.[15] The state also has a significant interest and intent to ensure that SICs work for the betterment of the Chinese state and people.

Insofar as the state is therefore both invested in these companies but at the same time is responsible for the implementation of the relevant legislative regimes and the operation of the court system, there is plainly a direct interplay between the legal and political systems in this space. The intentions of the Communist Party of China in enacting the Company Law will no doubt be considered by the courts in interpreting the very same Company Law. In the context of SICs this influence will only be stronger. With a growing emphasis on the rule of law in China,[16] this interplay is of increasing relevance and provides the mechanisms through which the political system shall exert influence in an increasingly international sphere where the wider world will hold expectations of legality.

To some extent, therefore, the practical reality of the Communist Party of China's involvement in the governance of SICs appears at first glance to moot a legal truth that owing and acting upon additional obligations to the state is inherent in the role of a director in an SIC.[17] No matter one's views on the appropriateness in either a governance or political sense of directors in SICs considering the interests of the state in a manner distinct from the interests of the specific SIC itself, it appears certain that this is what will occur in practice within the Chinese context.

With the growing ability of domestic and foreign investors to acquire interests in SICs,[18] and with the 2023 Company Law including increased protections for shareholders as well as budding mechanisms for shareholder remedies,[19] understanding the precise nature of the duties owed by the directors of SICs, to whom such duties are owed, and how they are likely to be fulfilled, is of growing importance and has continued to attract significant attention from domestic and international investors.[20] This is especially so where, importantly, the corporatization of SICs means that they, like other companies, are subject to the Company Law.[21]

Indeed, from the investors' perspective it is crucial that they be aware of the obligations on, and actions that are likely to be taken by, directors in the exercise of their functions, including in situations where the investor is either less likely in a practical sense to actively exercise shareholder rights[22] or less able to meaningfully do so owing to the makeup of the ownership of the relevant company.[23] This applies whether the investor has interests in a partially state-owned SIC or

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[15] *Id.* at 133.

[16] Naixin Hou, *Study on the Identity of Rule of Law China and Party Leadership*, 14 INT'L. J. EDUC. & HUMAN.'S. 74 (2024).

[17] This also therefore appears to be the result of the Chinese social context. As we will see, consideration of factors such as this context is an important element of the actual analysis of the relevant provisions of the relevant laws. This practical reality, where the assumption of Chinese society would be that this is a legitimate exercise of directors' authority, will thus be important to consider as one considers the ramifications and interpretations of the Company Law.

[18] Ian Hissey, *Investing in Chinese State-Owned Enterprises*, FACTSET (Dec. 17, 2019), https://insight.factset.com/investing-in-chinese-state-owned-enterprises; Nicholas Borst, *State-owned Enterprises and Investing in China*, SEAFARER FUNDS (Nov. 2019), https://www.seafarerfunds.com/documents/state-owned-enterprises-and-investing-in-china.pdf.

[19] *See* 2023 Company Law, arts. 57, 71, 110, 187, 189, 190, 231.

[20] Charlie Xiao-Chuan Weng & Andrew Godwin, *The Duty of Loyalty of Company Directors in China: Tracing Its Origins and Plugging the Gaps*, 49 U.W. AUSTL. L. REV. 46, 48 (August 2022).

[21] Wang, *supra* note 12, at 651.

[22] For example, being less able to attend shareholder meetings or less informed on how best to exercise such rights.

[23] For example, where the state is the majority shareholder or there are no shareholder meetings held.

where a company in which the investor has interests engages in economic interactions with partially or wholly state-owned entities. Conversely, from the state's perspective, whilst its decisions are unlikely to be challenged regarding the directors it appoints or removes, it may still be of use to understand the nature of the legal obligations its appointees owe and just how they may impact the furthering of the objectives outlined. Finally, from the perspective of the directors of SICs, there is utility in understanding the scope of their own role and the duties that they owe in the exercise of their functions, and in particular in ascertaining how to balance the interests of company and state in business decision-making.

This question is provided with further importance when the nature of the SICs themselves are considered. Particularly in the Chinese context, SICs are used by the government to pursue various important public social goals.[24] As a result, Chinese SICs rank among the largest and most economically influential corporations both domestically and globally.[25] To the extent therefore that boards play a central function in the governance and performance of these crucial SICs, the role is "no less important" than that of a board in other companies;[26] the decisions made by these directors, and the factors influencing them, may have significant ramifications. It might then be opined that understanding the duties of these directors is similarly "no less important" than understanding those of their non-SIC counterparts.

This paper is therefore concerned with an eminently practical question which will be of use to a variety of stakeholders, both domestic and foreign. It does not seek to provide some legal justification or political cover for a practice which is not ongoing or unlikely to otherwise be possible. Rather, it seeks to explain the precise interplay of the political state with the legal framework which governs this area and how it is applied in the Chinese business sphere, as opposed to simply describing that political governance rules will take precedence over the law,[27] as well as to provide greater clarity to all market participants in the process. This is an especially important approach in a context where the political and the legal interact, with the state being responsible for imposing the laws governing the companies it invests in and appoints directors to. In doing so, this paper also contributes to a growing focus in China on the rule of law and on the legal basis for the structures and activities undertaken, including those of the state.[28]

No doubt the National People's Congress did not intend to preclude the directors of SICs from considering the interests of the state in exercising their functions as a director. After all, the Chinese Communist Party Central Committee and the State Council released in August 2015 as part of its dangjian (党建) policies the Guidance on Deepening the Reform of SOEs, which outlined that "adhering to the CPC's leadership over SOEs is the political direction and principle when deepening the reform of SOEs".[29] At the same time, it appears that the 2023 Company Law does not under "Chapter 7 Special Provisions on the Organizational Structure of State-Invested

[24] Ming Du, *Chinese State-owned Enterprises and International Investment Law*, 53 GEO. J. INT'L. L. 627, 630 (2022).
[25] *See id.*
[26] ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, IMPLEMENTING THE OECD GUIDELINES ON CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES 64 (2020).
[27] *Cf.* Wang, *supra* note 12.
[28] Hou, *supra* note 16.
[29] Lu & Zhu, *supra* note 13, at 132.

Companies", or elsewhere, exclude such directors from the duties placed on directors generally under the law or specifically enumerated in "Chapter 8 Qualifications and Obligations of Company Directors, Supervisors and Senior Managers". This includes, perhaps especially in the context of this paper's discussion of SICs, those which relate to prioritizing the interests of the company itself.[30]

This paper therefore seeks to ascertain how these two potentially competing duties, being duties to company and state, are reconciled under the 2023 Company Law, and assesses the extent to which this reconciliation has been realized. Rather than considering that the political governance mechanism exists separately to the legal governance mechanisms of the Company Law, it instead argues that this reconciliation may be understood through three potential lenses, one being found in the duties outlined in the Company Law directly, one derived from the governance structures and the interaction between decision-making bodies under the Company Law, and one given indirect force by the Company Law but grounded centrally in an SIC's articles of association.

In furtherance of these propositions, this paper is structured as follows. Part II outlines why the present enquiry cannot simply be approached by applying the general notions of fiduciary or directors' duties as understood in other jurisdictions, owing to not only the historical derivation of Chinese directors' duties in the civil law concept of "mandate" but also the cultural and sociopolitical context of China. Part III considers the relevant laws which codify the duties owed by directors and demonstrate that their vague drafting likely opens the gate for the justification of dual obligation to company and state. Part IV then depicts the interaction of shareholders and directors under the Company Law and the effect that this dynamic has on the duties of directors in SICs, explaining that if the shareholders instruct directors to consider the interests of the state, then they must do so. Part V then argues that, even if the Company Law does not itself directly ground a dual duty, the inclusion of such a duty in an SIC's articles of association will do so with similar force of law. Part VI concludes.

## II. THE DIFFICULTY APPLYING COMMON LAW FIDUCIARY PRINCIPLES

Whilst it may be so that China has seen "significant activity" in the realm of fiduciary and trust law,[31] it appears to very much remain the case that these developments, as with those in many other areas of the Chinese legal system, have continued along paths unique to the Chinese context rather than conforming neatly with international norms or principles.[32] They have also interacted with existing or prevailing legal concepts or approaches present in the Chinese civil law system.[33] The result of this is that in analyzing fiduciary, or fiduciary-like, duties owed by directors in China, one cannot simply transpose principles from Anglo-American or common law contexts.[34] The differences are further

[30] *See* 2023 Company Law, Chs. 7 & 8.
[31] Nicholas C Howson, *Fiduciary Principles in Chinese Law*, *in* The Oxford Handbook of Fiduciary Law 603–4 (Evan J. Criddle et al. eds., 2019).
[32] *Id.*
[33] *See* Jiangyu Wang, *Enforcing Fiduciary Duties as Tort Liability in Chinese Courts*, *in* Enforcement of Corporate and Securities Law: China and the World 185 (R. Huang & N. Howson eds., 2017).
[34] *Id*.; JIANGYU WANG, COMPANY LAW IN CHINA: REGULATION OF BUSINESS ORGANIZATIONS IN A SOCIALIST MARKET ECONOMY 201 (2014).

accentuated by the fact that whilst "the laws of fiduciary duties in common law countries have been mainly developed by judges through case law rather than by the lawmakers through written laws", in the case of China and the Company Law they "have to appear in the form of [written] legislations".[35]

The need to take a bespoke perspective when considering the Chinese law may seem intuitive, even as better-understood fiduciary principles from other contexts have played a not-insignificant role in shaping the development of directors' duties in China. However, it is crucial to recognize that common law principles, often derived through case law and precedent within a specific jurisdiction and social context, cannot be blindly applied to a civil law jurisdiction with a fundamentally different social milieu.[36] This distinction bears particular significance when considering the reconciliation of potentially competing duties owed by directors in the Chinese context. Conclusions drawn under common law jurisdictions regarding the viability or reconciliation of such dual obligations may not only fail to apply directly but might also be inapplicable by analogy.[37]

### A. Historical Derivation of "Mandate"

Leaving to one side briefly the apparent codification of directors' duties under the amendments to the Company Law made in October 2005 (the "2005 Company Law")[38] and as most recently amended in the 2023 Company Law,[39] it should be noted that it is by now well understood that early Chinese consideration of directors' duties was not exclusively based on the common law notion of the duty owed by a fiduciary to a beneficiary.[40] In fact, before the formal incorporation of specific duties into the Company Law, at least in some areas in Chinese legal academia there was what has been described as a "disdain" for these common law principles.[41]

Instead of embracing the concepts of directors' duties as understood in common law jurisdictions, early academic discussions in China center around the civil law application of the Roman Law concept of mandatum.[42] This "mandate" (weituo hetong 委托合同) described a relationship wherein one party acts under moral guidance to assist another in handling the principal's affairs based on instructions.[43] In this context, the mandatary would be indemnified by the mandator and was expected to exercise reasonable care as a "good manager"

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[35] WANG, *supra* note 34, at 186; Jiangyu Wang, *Enforcing Fiduciary Duties as Tort Liability in Chinese Courts*, *in* Enforcement of Corporate and Securities Law: China and the World 186 (R. Huang & N. Howson eds., 2017).

[36] Lynn A. Stout, *On the Export of U.S.–Style Corporate Fiduciary Duties to Other Cultures: Can a Transplant Take?, in* Global Markets, Domestic Institutions: Corporate Law and Governance in a New Era of Cross-Border Deals 46–76 (Curtis J. Milhaupt eds., 2003).

[37] Yuwa Wei, *Directors' Duties Under Chinese Law: A Comparative Review*, 1 U.N.E. L. J. 31, 36 (2006).

[38] Gongsi Fa (公司法) [Company Law] (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 29, 1993, effective July 1, 1994; rev'd by the Standing Comm. Nat'l People's Cong., Dec. 25, 1999; rev'd by the Standing Comm. Nat'l People's Cong., Aug. 28, 2004; rev'd by the Standing Comm. Nat'l People's Cong., Oct. 27, 2005) (Chinalawinfo) [hereinafter 2005 Company law].

[39] 2023 Company Law, Ch. 7.

[40] Howson, *supra* note 31, at 605.

[41] *Id.*

[42] LIU JUNHAI (刘俊海), XIANDAI GONGSI FA (现代公司法) [MODERN CORPORATION LAW] 506–7 (2nd ed. 2011).

[43] W. W. BUCKLAND & ARNOLD D. MCNAIR, ROMAN LAW AND COMMON LAW 268 (1952). As Wang Jiangyu outlines, this concept is explicitly replicated in the Company Law of the People's Republic of China in its art. 396: Wang, *supra* note 34, at 189.

(shanliang guanli ren 善良管理人).[44] While this arrangement did not specifically constitute an agency relationship, it was not dissimilar to that of principal and agent. In the Chinese legal context, the term "mandate" has often been described as largely analogous to agency.[45] To that extent, the due diligence and care required was naturally in undertaking the specific tasks imposed, and in a manner imposed if relevant, rather than fulfilling a variety of obligations with comparatively wider discretions and functions which would later come to characterize common law fiduciary duties.[46]

The Chinese preference for this concept of mandate as opposed to an entire transposition of common law fiduciary duties was considered more appropriate for China's "national situation" (guoqing 国情), and more congruent with the "customs and traditions of the Chinese people".[47] The mandate principle grew, it would seem, from the civil law of the Republic of China as it existed prior to 1949.[48] The effect of this derivation, as well as an apparent "affiliation" between China's legal tradition and that of Japan,[49] was that a notion of mandate more similar to the law of contract and reflecting a specifically outlined relationship with ascertainable objectives, which was more familiar to the Chinese law, as opposed to being based in the less familiar equity or trusts.[50]

Perhaps then it is unsurprising that this perspective, which favored a mandate-based approach, was strongly supported by Chinese academics during the early development of the nation's corporations law.[51] And in 1993, when the first iteration of the Company Law was ratified (the "1993 Company Law"), fiduciary duties—or even a codified explication of their contents under another, or no, name—were notably absent.[52] The effect of this historical derivation in mandate rather than fiduciary duties in the common law sense is not a mere triviality of history. Even when provisions resembling Anglo-American fiduciary duties were introduced into the 2005 Company Law, this did not mean that they would necessarily take on the metes and bounds of those concepts as understood in other jurisdictions.[53] This was true first of their actual desired meaning when implemented into the laws themselves, but also of their likely interpretation and application in practice. Rather, it means that the contents of these duties must be understood through the appropriate lens.[54]

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[44] FREDERICK HENRY LAWSON, A COMMON LAWYER LOOKS AT THE CIVIL LAW 121 (1953); GUO MINGRUI ET AL., MINFA (民法) [CIVIL LAW] 508 (2nd ed. 2007).
[45] Wei, *supra* note 37, at 43, 51; WANG, *supra* note 34, at 189.
[46] J. A. C. THOMAS, TEXTBOOK OF ROMAN LAW 306–7 (1976).
[47] Wang Baoshu (王保树), *Gufen Youxian Gongsi de Dongshi he Dongshihui* (股份有限公司的董事和董事会) [*Directors and the Board of Directors at Companies Limited by Shares*], 1 HUANQIU FALÜ PINGLUN (环球法律评论) [GLOBAL LAW REVIEW] 5, 5 (1994).
[48] WANG, *supra* note 34, at 200.
[49] Howson, *supra* note 31, at 605.
[50] WANG, *supra* note 34, at 190.
[51] *See* Nicholas Calcina Howson, *The Doctrine That Dared Not Speak Its Name-Anglo-American Fiduciary Duties in China's 2005 Company Law and Case Law Intimations of Prior Convergence*, *in* TRANSFORMING CORPORATE GOVERNANCE IN EAST ASIA (Hideki Kanda et al. eds., 2008).
[52] Howson, *supra* note 31, at 607.
[53] WANG, *supra* note 34, at 201.
[54] Colin Hawes, *Interpreting the PRC Company Law through the Lens of Chinese Political and Corporate Culture*, 30 U.N.S.W. L. J. 813, 813 (2007).

### B. Fiduciary Law with Chinese Characteristics?

As outlined above, this historical aversion to common law fiduciary duties, it would appear, was no roadblock to the ultimate inclusion of duties "resembling common law fiduciary duties" in the Company Law.[55] With the introduction of the 2005 Company Law, the Chinese authorities for the first time included substantive provisions which outlined the duties owed by directors, and importantly "did so in a fashion clearly sourced in the Anglo-American (and not European continental civil law) tradition".[56] Despite this significant movement, however, criticism was levied repeatedly at the 2005 Company Law, and later the 2018 Company Law, that it merely listed the duties owed by directors, rather than providing the relevant standards or requirements thereof. It provided no "guidance or instruction to regulators or judges",[57] and did so in a civil law system which lacked the centuries of exposition of just what a duty of loyalty (zhongshi yiwu 忠实义务) or duty of diligence (qinmian yiwu 勤勉义务)—being concepts and terms by now well understood in common law jurisdictions—entailed. It also, despite approaching what might seem like fiduciary duties, did not include obligations such as that of "good faith" which could be found in other jurisdictions.[58] To the extent that this duty of good faith was absent, the duties placed on directors by the Chinese law could not be equated directly, in their scope or operation, to those in other contexts.[59] It also created ambiguity in interpreting whether directors' duties extended beyond a mere procedural compliance with specific provisions to encompass substantive loyalty and fairness toward the company in actions and intent. Such an absence would also mean that the judiciary was not provided clear benchmarks for the enforcement of duties which, again, did not have an extended history in China.

The inclusion of these fiduciary-like duties in the Company Law occurred, according to Nicholas C. Howson, alongside an ongoing process whereby administrative departments of the Chinese state had been enforcing some form of these duties on publicly held companies.[60] Additionally, this inclusion occurred in a context where, prior to its legal instantiation, the judiciary in China had also enforced something

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[55] WANG, *supra* note 34, at 197 n.6; *see also* Zhu Ciyun (朱慈蕴), *Lun Zhongguo Gongsi Fa Bentuhua yu Guojihua de Ronghe: Gaige Kaifang Yilai de Lishi Yange, Zuixin Fazhan yu Weilai Zouxiang*, (论中国公司法本土化与国际化的融合——改革开放以来的历史沿革、最新发展与未来走向) [*The Integration of Localization and Internationalization of China's Corporate Law: History, Development and Future since the Reform and Opening Up*], 2 DONGFANG FAXUE (东方法学) [ORIENTAL LAW] 91, 94–5 (2020).

[56] Howson, *supra* note 31, at 612.

[57] WANG, *supra* note 34, at 198 n.12.

[58] Howson, *supra* note 31, at 613. This is so notwithstanding the fact that a number of Chinese judges, including notably two from the PRC Supreme People's Court, have written extrajudicially to suggest that a requirement of good faith should be considered as falling under the duty of care to the company. *See* XI XIAOMING (奚晓明) & JIN JIANFENG (金剑锋), GONGSI SUSONG DE LILUN YU SHIWU WENTI YANJIU (公司诉讼的理论与实务问题研究) [CORPORATE LITIGATION: THEORY AND PRACTICE] 468–9 (2008).

[59] This is not to say necessarily that the nature of the duties of loyalty and diligence *would* differ, but that the broader, and at times more subjective, standards applicable in requiring good faith actions could not be imported. Given the brevity with which these duties were expressed in the 2005 Company Law and the 2018 Company Law, the more flexible requirement of good faith was unable to provide additional meaning owing to its omission. The 2023 Company Law goes some way to imposing obligations which begin to mirror those of good faith, in particular those relating to the purposes for which the powers or position of directors can be used. This addresses the issues of the absence of this duty to some extent. But it does not replicate the duty of good faith explicitly. To the extent that certain obligations imposed by the 2023 Company Law speak to the purpose of certain actions, or require them to be used in a manner analogous to "good faith", this article will consider them specifically in their direct operation and terms to examine how they impact the potential reconciliation of duties to the state and company. It still cannot be said that an explicit duty of good faith exists in the Chinese context, and it will not be appropriate to import Western notions of that duty even in the updated laws.

[60] Howson, *supra* note 31, at 613.

approaching fiduciary duties, even in the absence of a specific legal basis for doing so.[61] The effect of implementing amendments to the Company Law to impose what seemed like fiduciary duties, in a context where notions of mandate and fiduciary law had long competed for supremacy, was that the dual concepts appeared to each gain separate yet inextricable sway over the development of the Chinese law. Notionally, the duties were codified using terminology familiar to common law jurisdictions; however, the contextual understanding of what constitutes loyalty, diligence, or care remained deeply rooted in the historical civil law understanding of mandate and agency, as well as the broader social milieu of Chinese society.[62]

As Wang Jiangyu noted, it may be erroneous to assume that the two principles of mandate and fiduciaries are equivalent. However, ongoing developments in Chinese civil law have implied that "the two doctrines can co-exist in China's corporate law".[63] That is, whether one examines the obligations owed by directors through either lens, in most situations, they lead to similar outcomes.[64] While this may hold true in many cases, as Wang identifies, it does not establish a universal rule that the two principles are co-extensive.[65]

Once this codification was complete, concerns arose regarding how Chinese courts would interpret these terms, given their removal from the "great longevity" of common law courts in the Anglo-American tradition and their unfamiliarity with common law reasoning.[66] Indeed, it was foreseen that owing to a lack of "common law tradition that draws on a rich body of cases in respect of a fiduciary duty" in China,[67] "eventually we will have a doctrine of fiduciary duties that are full of Chinese characteristics".[68] This was so even where courts had, intermittently and inconsistently, applied fiduciary requirements to directors in the past, especially as now the seemingly discretionary decision to do so had to be grounded in the specifically applicable terms of the Company Law.

This idea of "fiduciary duties with Chinese characteristics", or fiduciary duties adapted and appropriate to Chinese circumstances rather than the western contexts in which they were initially derived elsewhere, in itself is not necessarily undesirable. It does, however, mean that in the short term it remains to be seen just how these Chinese contextual influences will manifest in interpreting the 2023 Company Law and the obligations it places on directors, especially in situations where their decision-making cannot be removed from socially-grounded value judgements.[69] Again this appears only ever the more likely when the context of SICs is considered, given the unique intersection between these companies and the state, and the socialist nature of China's market

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[61] *Id*. at 610.
[62] Wang, *supra* note 34, at 190.
[63] *Id.* at 200.
[64] *Id.* n.21.
[65] *Id.*
[66] *Id.* at 201.
[67] Nicholas Calcina Howson, *Twenty-Five Years On—The Establishment and Application of Corporate Fiduciary Duties in PRC Law*, THE OXFORD HANDBOOK OF FIDUCIARY LAW (Evan J. Criddle et al. eds., 2019); *see also* Weng & Godwin, *supra* note 20, at 66.
[68] Wang, *supra* note 34, at 202. This term appears reminiscent of the phrase "Socialism with Chinese characteristics" (中国特色社会主义), and refers to the fact that the nature of the fiduciary duties that will arise and apply in the Chinese legal system will naturally reflect and adapt to the underlying Chinese circumstances.
[69] Wang, *supra* note 34, at 191.

economy.[70]

The growing emphasis of the state to allow for opening up of investment into China's international economy may on one hand lend itself to judicial interpretations which reflect the understandings of the wider international sphere. At the same time, in circumstances relating to SICs it may be so that the clear desire of the state to retain the necessary control whilst also opening up investment to the outside world may see these political priorities reconciled by the judiciary to give effect to the intent of the state. Changes to the economic climate in China may prompt clear political mandates for the scope of fiduciary duties to inform corporate and economic behavior. The changes to the wider political climate in the Company Law realm and priorities in this area will no doubt play a role. These influences will also stem from and be be unique to the Chinese context, imbuing further these bespoke "Chinese characteristics".

In considering questions such as those raised in this paper, it is crucial to remember that the derivation of western-style fiduciary principles in the Chinese context through entrenched notions of mandate and agency rather than trust and beneficiaries has left the 2023 Company Law in a position where it may be so that the wording of the relevant provisions refers to terms understood in other jurisdictions as fiduciary or having specific content, but one cannot simply transpose the connotations and ramifications of these concepts elsewhere into the Chinese law.[71] Whilst a general understanding of these terms can serve as a useful starting point, it is vital to recognize that the Chinese interpretation will differ and must be considered within its specific context.[72] These ramifications necessitate a contextual reading of the relevant provisions that situates the director essentially as an agent who must comply with the mandate imposed upon them.

## III. TEXTUALLY GROUNDED LEGAL OBLIGATIONS

In seeking to understand how the dual loyalties this paper considers might be legally reconciled under relevant Chinese laws, it is prudent to turn first to the laws themselves.[73] As will become clear, the legal sources which impose obligations on companies and directors of relevance to this paper have been drafted with vague terms and considerable breadth of scope.[74] This drafting allows for provisions that may conceivably import considerations permitting directors to act in the interests of both the company and the state, or either. It would seemingly provide a legal basis or justification for considering the latter where intuitions surrounding directors' duties might imply otherwise. In the Chinese context, particularly concerning SICs, this enabling interpretation would appear all the more likely.[75]

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[70] *See* YUKYUNG YEO, VARIETIES OF STATE REGULATION: HOW CHINA REGULATES ITS SOCIALIST MARKET ECONOMY (2020).
[71] WANG, *supra* note 34, at 201.
[72] *Id.* at 196.
[73] In fact, it is likely that these laws, or the legal structures that they create, are at present almost exclusively the relevant sources of analysis. Even leaving aside the fact that in the Chinese civil law system the decisions of the judiciary are not technically binding precedent, and that there have been no guiding cases disseminated by the state, it remains the case that the new provisions, and in particular the parts most relevant to this paper, do not appear to have seen meaningful judicial or academic engagement. Nonetheless, we will consider the interaction between these laws and other sources of obligation, such as those within the Communist Party of China or other publications made by the state.
[74] Michael Aldrich & Ke Chen, *The People's Republic of China, in* DIRECTORS' LIABILITY: A WORLDWIDE REVIEW 185–195 (Alexander Loos ed., 2nd ed. 2010).
[75] See *supra* text accompanying note 19.

### A. Vague Drafting and Wide Interpretation

It has been observed elsewhere that "an abstract and vague drafting style is a common characteristic of Chinese legislation",[76] and that the effect of this style is that the judicial interpretation, or otherwise the implementation of the law in practice, may be that which will favor the prevailing social or political climate.[77] This approach appears to have been similarly employed in the drafting of the Company Law. In the context of SICs, the prevailing social or political climate suggests that the governing state would hope to encourage or require directors to consider its interests.[78] In fact, the state has repeatedly made it clear that it believes directors of SICs ought to prioritize these considerations.

The claim that a director acting in accordance with laws, and complying with the obligations a company owes under the law, is acting in the best interests of that company appears uncontroversial.[79] Ensuring that the company avoids sanctions and remains a going concern necessitates legal compliance. This is especially critical where non-compliance would expose the company and its directors to legal liability.[80] It is so even where, in the absence of that legal requirement to act or operate in a certain way, it may have been in the company's interests to act or operate in a different manner.[81] Thus, in a situation where it can be argued that the terms of the law, in this case the Company Law, require specific factors to be considered, then directors will in theory have to undertake this consideration.

This section outlines that under the vague provisions of the 2023 Company Law regarding how companies must operate, it might be argued by either a director or the state that considering the good of the state is just as necessary as considering the good of the company. It also notes that, in most circumstances, the specific duties placed on directors in the law will not preclude this consideration of the state. Thus, even if such considerations are not explicitly mandated, directors who are subject to supervening obligations to the state will likely seek to invoke these provisions as a legal basis.

#### 1. General Provisions Applying to Companies

In other jurisdictions and contexts, the "best interests of the company" has generally been accepted at the most basic level to be focused on the company alone.[82] Even then, there appears growing acceptance that the company and its directors may take into account external factors and even external stakeholders, such as Environmental, Social, and Governance (ESG) or Corporate Social Governance (CSG)

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[76] Charlie Xiao-Chuan Weng, *A Promising Path or Dead End? A Director's Duty of Care in China*, 45 U.N.S.W. L. J. 1288, 1288 (2022).

[77] *See* Jianlong Liu, *Judicial Interpretation in China*, *in* The Indian Yearbook of Comparative Law 2018 213–229 (Mahendra Pal Singh & Niraj Kumar eds., 2019).

[78] See *supra* text accompanying note 30.

[79] Norwood P. Beveridge, *Does the Corporate Director Have a Duty Always to Obey the Law*, 45 DEPAUL L. REV. 729, 729 (1996).

[80] *Id.* at 730.

[81] As a hypothetical example, a law might require that a company must abide by a limit on carbon emissions, or that it must not act to harm a certain natural habitat. Even if it would otherwise be in the interests of the company to do either of these things, given the requirements in law that they not, it would hardly be considered as not acting in the interests of the company, or as acting against them, to abide by the requirements of the law.

[82] Meaning that the best interests of the company are the best interests of the company alone.

considerations, in deciding what is the best course of action for the company.[83] In a similar vein, art. 19 of the 2023 Company Law requires, inter alia, that a company conducting business activities shall abide by laws and regulations, abide by social and business ethics, and accept government supervision.[84] Further, art. 20 requires that a company engaging in business activities "fully consider" the interests of employees and customers, but perhaps more importantly also those of "other stakeholders" and "social public interests".[85] This emphasis on social considerations is mirrored in art. 86 of the Civil Code of the People's Republic of China (the "Civil Code"),[86] which requires any "for-profit legal person" to "assume social responsibilities" when engaging in operational activities.[87] Article 17 of the Law of the People's Republic of China on the State Owned Assets of Enterprises[88] also mirrors these obligations. This was described by the Chinese Securities Regulatory Commission (the "CSRC") as meaning that "instead of maximizing shareholders' interest alone, companies now take a more holistic view".[89] These obligations extend not only to companies, but naturally to the directors responsible for their operation.[90]

One may readily imagine that a director in an SIC acting in the interests of the state could rely on such provisions, claiming that furthering state interests is necessary to adhere to social ethics within the Chinese context, representing the giving of "full consideration" to the state as an "other stakeholder", or reflecting "social public interests". After all, whilst this paper does not wage into the debate as to whether the interests of the state are always synonymous with those of society or the people, in the Chinese context, considering the two as significantly overlapping appears to be accepted legally and socio-politically.[91] This would appear to fall naturally, in that context, within the "holistic" approach described by the CSRC.

The vagueness of the drafting utilized, whereby these terms are left undefined and are inherently ambiguous or abstract,[92] as well as the inherent width of the terms employed and their potentially subjective content, allows for the importation of various concepts as required. Given the nature of SICs, it seems likely that these terms would be considered to extend to the interests of the same state which appoints the directors and monitors their performance. After all, it would not be unthinkable to hear rhetoric which claimed that an action for the betterment of the state was an action taken for the public good and with consideration of the social impacts of a decision. When the consideration of these factors, even in their vague state, is mandated by law, a director acting for the interests of the state would claim they were

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[83] *See* Susan N. Gary, *Best Interests in the Long Term: Fiduciary Duties and ESG Integration*, 90 U. COLO. L. REV. 731 (2019); *Best interests duty*, AUSTRALIAN INSTITUTE OF COMPANY DIRECTORS (Aug. 1, 2022), https://www.aicd.com.au/company-policies/corporate-social-responsibility/examples/best-interests-duty.html.

[84] 2023 Company Law, art. 19.

[85] *Id.* art. 20.

[86] Min Fadian (民法典) [Civil Code] (promulgated by the Nat'l People's Cong., May 28, 2020, effective Jan. 1, 2021) (Chinalawinfo).

[87] *Id.* art. 86.

[88] Qiye Guoyou Zichan Fa (企业国有资产法) [Law on State-Owned Assets of Enterprises] (promulgated by the Standing Comm. Nat'l People's Cong., Oct. 28, 2008, effective May 1, 2009) (Chinalawinfo).

[89] ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, CORPORATE GOVERNANCE OF LISTED COMPANIES IN CHINA: SELF-ASSESSMENT BY THE CHINA SECURITIES REGULATORY COMMISSION 95 (OECD, 2011).

[90] Jaramillo, *supra* note 12, at 165.

[91] *E.g.*, David Cottam, *Do party interests always represent national interests?*, CHINA DAILY (Mar. 18, 2024), https://www.chinadailyhk.com/hk/article/381547.

[92] Indeed many such terms might be considered as importing value judgments on the part of the director.

following the legal requirements of the Company Law, as they are required to do by art. 179.[93] On the other hand, it may be that the state, in instructing and reviewing the performance of the directors of SICs, indicates that it ought be considered as such.

This paper has already commented on the overlaps at play between the legal sphere and the political and economic spheres in the Chinese context. Noting that Chinese courts have held generally that decisions of directors must not harm state interests, it seems likely that the judiciary would not oppose an interpretation of the relevant provisions as described above if it were proposed by the director of an SIC who had taken the state interest actively into account.

Overall, therefore, the provisions which ground obligations placed on companies would appear to be drafted in sufficiently vague terms and with a wide enough ambit that even if they were not read as encouraging the consideration of state interests in directors' decision-making, they could or indeed would likely be pointed to by any director whose decision to do so was challenged as justifying their consideration.

### 2. Specific Provisions Applying to Directors

The amendments included in the 2023 Company Law provided a level of clarity surrounding directors' duties which had been lacking in previous iterations of the law. Whilst the 2005 Company Law was the first to explicitly impose duties of diligence and loyalty on directors, it still did so in an ambiguous, notional, and underdeveloped manner.[94] Even with the further explanation within the 2023 Company Law, there remains significant scope for interpretation, both in a purely legal sense and in practical application. This flexibility perhaps permits the consideration of state interests in SICs, where a fully independent notion of the board's role might otherwise not. The central provision in the 2023 Company Law which appears to impose common law style fiduciary duties, or at least something approaching these duties, is art. 180, which provides, in greater detail than previous iterations of the law:[95]

"Directors, supervisors, and senior managers have a duty of loyalty to the company, shall take measures to avoid conflicts between their own interests and those of the company, and shall not use their powers to seek improper benefits.

Directors, supervisors, and senior managers have a duty of diligence to the company, and when performing their duties, they should exercise the reasonable care normally expected of managers in the best interests of the company."

This provision therefore incorporates in explicit terms what is understood in company law elsewhere to be the duty of loyalty and the duty of diligence. It also imposes a requirement that reasonable care be exercised "in the best interests of the company".[96] In the SIC context, these requirements are additionally mirrored in art. 26 of the Law of the

[93] 2023 Company Law, art. 179.
[94] Wei, *supra* note 37, at 42.
[95] 2023 Company Law, art. 180.
[96] *Id.*

People's Republic of China on the State-Owned Assets of Enterprises.[97] As the terms of art. 180 indicate, the duty of loyalty focuses on ensuring that directors do not act in their own self-interest when it conflicts with that of the company.[98] The duty of diligence, meanwhile, addresses issues of managerial shirking and ensures that directors exercise care and discretion in their functions.[99] The issue of exercising care in the interests of the company appears to some extent to incorporate elements of both duties but, for the first time, expressly provides that the obligations owed by directors in China are centrally to the company rather than to shareholders specifically or some other group.[100] It is useful therefore to turn to each duty and consider how they interact with the potential obligations of directors in SICs.

Turning first to the duty of loyalty. In addition to explicitly referring to the duty in art. 180, the 2023 Company Law then goes on to outline a list of prohibited conduct in art. 181, which appears to largely correspond to the requirements of such a duty as provided for in the first paragraph of art. 180:[101]

"Directors, supervisors, and senior managers shall not engage in the following conduct:

(1) Misappropriating company property and misappropriating company funds;

(2) Store company funds in an account opened in his or her own name or in the name of another individual;

(3) Taking advantage of one's position to bribe or accept other illegal income;

(4) Accept commissions from others' transactions with the company and keep them as your own;

(5) Unauthorized disclosure of company secrets;

(6) Other behaviors that violate the duty of loyalty to the company."

The duty of loyalty is seemingly given further content, or is at the least augmented by, additional provisions which deal specifically with, and at times prohibit, related party transactions,[102] improper use of the position for gains for themselves or others,[103] and competing with the company.[104] Further provisions imparting legal obligations akin to a duty of loyalty may be found in the Civil Code, which in substance reflect those in the 2023 Company Law.[105] It would therefore appear that, despite a lack of binding case law precedent on the matter noting the civil law context[106] and the recency of these amendments, the revisions in the 2023 Company Law go a significant way to making clear the obligations of the duty of loyalty and capture the common law notions of both the no-conflict rule and the no-profit rule.

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[97] Zhonghua Renmin Gongheguo Qiye Guoyou Zichan Fa (中华人民共和国企业国有资产法) [Law of the People's Republic of China on the State-Owned Assets of Enterprises] (promulgated by the Standing Comm. Nat'l People's Cong., Oct. 28, 2008, effective May 1, 2009), art. 26 (Chinalawinfo).

[98] Weng & Godwin, *supra* note 20, at 47.

[99] *Id.*

[100] The effect of this additional inclusion is that many of the analyses regarding previous iterations of the company law and its interaction with the state do not fully address the strength of the potential textual arguments for preventing consideration of state interests under the 2023 Company Law. Whilst this paper argues these are not fatal to the proposition that state interests can be considered, it is still and important element of the new law to address.

[101] 2023 Company Law, art. 181.

[102] *Id.* art. 182.

[103] *Id.* art. 183.

[104] *Id.* art. 184.

[105] Civil Code, arts. 83, 84, 86.

[106] In the United Kingdom context, see *Aberdeen Railway Co v. Blaikie Bros* (1854)1 Macq 461. *See also Boardman v. Phipps* [1967] 2 AC 46.

Nonetheless, the contents of the duty of loyalty under the 2023 Company Law do not appear to, on their face, prohibit the consideration of the interests of the state by directors in decision-making. Considering the interests of the state does not expressly fall under the provisions which give content to the duty, does not represent a director placing their own interests above the company,[107] nor does it involve the director profiting from their role. As outlined above, it is also not necessarily inconsistent with working to holistically benefit the company, especially in the context of the Chinese state and to ensure the company remains a going concern. It appears unlikely that a Chinese court would consider the duty of loyalty breached if the interests of the state were considered, and there does not appear to be any case law indicating otherwise. Given the implementation of this duty in the Chinese context, and noting the other sources of obligations to the national or state interest, it would not readily be assumed that this loyalty would be to the exclusion of the state.

We might then turn to consider the contents of the duty of diligence in the second paragraph of art. 180.[108] The first issue that arises is that the law does not provide any content or additional meaning to the phrase "diligence", in the same way that it had failed to fully codify the meaning of terms in previous iterations of the Company Law.[109] Indeed, the relevant provisions[110] have been described by Weng Xiaochuan as "too coarse for the judiciary to apply" and "requiring further explanatory legislation".[111]

Despite these lingering issues surrounding certainty, it appears that the work of the courts and state agencies such as the CSRC have overseen some development of guidance for this principle to be applied in practice, both through publications and through actual decision-making.[112] This is particularly useful, as despite China's civil law system, the Supreme People's Court has developed the guiding case system, leading "judges… becoming more inclined to apply precedents to apply vague statutes".[113] The CSRC's issuance of the Code of Corporate Governance for Listed Companies stipulates, for example, that the duty of care and diligence involves investing appropriate time and energy in the role, possessing the requisite competence, and complying with legal obligations.[114] Similarly, the CSRC's Guidance for Articles of Association of Listed Companies 2019[115] speaks of fiduciary and diligence obligations in similar terms.[116] The Shanghai

[107] Though there may be an argument, in certain situations where acting in such a manner was to ensure personal progression, that this was occurring.
[108] 2023 Company Law, art. 180.
[109] Wei, *supra* note 37, at 49–50.
[110] Whilst the analysis was made in relation to their previous iteration, for present purposes the analysis remains applicable.
[111] Weng, *supra* note 76, at 1297; Charlie Xiao-Chuan Weng, *Assessing the Applicability of the Business Judgment Rule and the "Defensive" Business Judgment Rule in the Chinese Judiciary: A Perspective on Takeover Dispute Adjudication*, 34 FORDHAM INT'L. L. J. 124, 144 (2010).
[112] Weng, *supra* note 76, at 1290.
[113] *Id*. at 1292.
[114] Zhongguo Shangshi Gongsi Zhili Zhunze (中国上市公司治理准则) [Code of Corporate Governance for Listed Companies in China] (promulgated by China Sec. Regul. Comm'n, Jan. 7, 2002, effective Jan. 7, 2002; rev'd by China Sec. Regul. Comm'n, Sep. 30, 2018), arts. 22, 25, 26, 29, 30 (Chinalawinfo).
[115] Shangshi Gongsi Zhangcheng Zhiyin (上市公司章程指引) [Guidance for Constitutions of Listed Companies] (promulgated by China Sec. Regul. Comm'n, Dec. 16, 1997, effective Dec. 16, 1997; rev'd by China Sec. Regul. Comm'n, June 16, 2006; rev'd by China Sec. Regul. Comm'n, May 28, 2014; rev'd by China Sec. Regul. Comm'n, Oct. 20, 2014; rev'd by China Sec. Regul. Comm'n, Sept. 30, 2016; rev'd by China Sec. Regul. Comm'n, Apr. 17, 2019) (Chinalawinfo) [hereinafter 2019 Guidance].
[116] *Id.* art. 136.

and Shenzhen Stock Exchanges have also imposed additional requirements, largely reflecting a requirement of actually undertaking the requisite functions. Interesting, the Shanghai Stock Exchange Listing Rules elaborate on "directors' loyalty duty and diligence duty", referring to "performing other fiduciary duty and due diligence duty as set forth in the Company Law or acknowledged by the public".[117] Overall, as Weng Xiaochuan describes, "after examining the existing laws and rules on the obligation of diligence, it seems that most of the explanations of the duty revolve around the obligation of diligence. This suggests that Chinese statutes are more concerned with how diligently directors are working rather than whether they are exercising necessary and reasonable care and utilising skills in the course of fulfilling their duty".[118]

It therefore appears that the duty of diligence as specified deals with, in crude terms, the willingness and ability of directors to actually act as directors. It speaks to effort and application, more than it speaks to the content of the work undertaken. This paper will not delve into the ripe debate as to the exact requirements of this duty or the relevant standards to apply,[119] but still this conceptual distinction is important. It would be hard to argue, unless the duty of diligence is conflated with the duty of care to the interests of the company to which we will turn,[120] that acting to consider the interests of the state was not carrying out their role with sufficient effort or diligence, if they were otherwise performing their duty with the required time and effort.

Nonetheless, the term "diligence" must be read with the explicitly referenced interests of the company and the duty to act with reasonable care in the "best interests" thereof.[121] With the inclusion of this phrase in the 2023 Company Law, we begin to be provided with some direction as to how these powers must be exercised. Unfortunately, it does not appear that the term "best interests of the company" (gongsi de zuida liyi 公司的最大利益) in the context of the relevant provisions has received judicial consideration in China to date, or any official interpretation for that matter. That said, even where this was not made explicit in previous iterations of the Company Law, courts saw fit to interpret their application to mean that "when the powers of directors are exercised, they should be for the best interests of the corporation"[122] or "the best interests of the firm".[123] As these extracts show, the cases generally considered the term in its plain meaning, but even then did not

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[117] Shanghai Zhengquan Jiaoyisuo Gupiao Shangshi Guize (上海证券交易所股票上市规则) [Rules Governing the Listing of Stocks on Shanghai Stock Exchange] (promulgated by Shanghai Stock Exch., Jan. 1, 1998, effective Jan. 1, 1998; rev'd by Shanghai Stock Exch., Apr. 28, 2000; rev'd by Shanghai Stock Exch., June 8, 2001; rev'd by Shanghai Stock Exch., Feb. 25, 2002; rev'd by Shanghai Stock Exch., May 18, 2006; rev'd by Shanghai Stock Exch., Nov. 29, 2004; rev'd by Shanghai Stock Exch., May 18, 2006; rev'd by Shanghai Stock Exch., Sept. 4, 2008; rev'd by Shanghai Stock Exch., July 7, 2012; rev'd by Shanghai Stock Exch., Dec. 27, 2013; rev'd by Shanghai Stock Exch., Oct. 17, 2014; rev'd by Shanghai Stock Exch., Apr. 20, 2018; rev'd by Shanghai Stock Exch., June 15, 2018; rev'd by Shanghai Stock Exch., Nov. 16, 2018; rev'd by Shanghai Stock Exch., Apr. 30, 2019), § 3.1.5 (Chinalawinfo).

[118] Weng, *supra* note 76, at 1303.

[119] Such a debate presently appears to be evoking significant discussion in the literature, also owing to the vagueness of drafting for the relevant provisions. Nonetheless, this paper explores moreso the substantive content of the provisions rather than the legal standards applicable to their breach. That said, the latter will no doubt have an effect in practice in the judicial determination of matters even in the areas this paper contends with.

[120] And in any event, this latter duty would still exist and require analysis even if they were not so conflated.

[121] 2023 Company Law, art.180.

[122] Shanghai Fumi Wenhuachuanbo Youxiangongsi Su Zuo Chunju Sunhai Gongsi Liyi Zerenjiufen Yi An Ershen Minshi Panjue Shu (上海福米文化传播有限公司诉左春举损害公司利益责任纠纷一案二审民事判决书) [Shanghai Fumi Art Co Ltd v. Zuo Chunju , Huang Feng], (2017)沪 01 民终 10301 号 (Shanghai First Interm. People's Ct. 2017).

[123] Shanghai Yachang Yishu Yinshua Youxian Gongsi Yu Daihu Sunhai Gongsi Liyi Zerenjiufen Ershen Minshi Panjue Shu (上海雅昌艺术印刷有限公司与戴虎损害公司利益责任纠纷二审民事判决书) [Shanghai Yachang Art Co Ltd v. Dai Hu], (2019)沪 02 民终 11313 号 (Shanghai Second Interm. People's Ct. 2019).

provide substantial exposition as to what this entails. They were also considered in the context of non-SICs, where the interests of the company are comparatively more clear-cut, especially vis-à-vis separation at times from the interests of the state itself. The requirements of this provision, explicitly referring to the interests of the company, would still however prima facie appear the largest barrier a director would face in acting in the interests of the state.

Nonetheless, again the vague drafting of the provision might provide some comfort for directors seeking to consider the state. As Wei Yuwa argues, the requirement must be interpreted in accordance with the nature of the relationship between directors and the company itself.[124] Thus, given that this specific fiduciary-like duty is not explained in great detail or provided content by the Company Law, and does not come with the centuries of common law development found in other jurisdictions, means even more so than might otherwise be the case it will likely take on specific characteristics unique to the Chinese context. This means incorporating considerations of the idea of mandate, insofar as in civil law jurisdictions such as China it is "generally understood that the relationship between a company and its directors resembles the relationship between a principle and an agent".[125] In the context of SICs, the director acts as the agent, while the state serves as the principal. How, then, does a director under a mandate consider what is in the best interests of their state-invested company?

It is noteworthy that even with this explicitly included provision, it remains uncertain just what is required to fulfil this duty to the company, what it means to act in its interests, what those interests are, and even to what extent these interests can be balanced with other interests,[126] especially if there may be indirect benefits in doing so.[127] It has been described that in practice the "influence goes both ways", and that SICs which act in the interests of the state are often able to influence state policymaking or government priorities in ways which benefit them.[128] Would then acting in a way which benefits the state in order to gain greater influence, even if there were short term detriment to the company, be in the company's best interests?

Even in the literature, this is vaguely described as a duty targeted at the "maximization of the company's interests" with little further exposition.[129] This absence of further guidance in the Company Law "will inevitably cause confusion in practice," potentially granting

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[124] *See* Wei, *supra* note 37, at 42.

[125] *Id. See also* Zhou Hao (周昊), *Gongsi Dongshi De Chengxin Yiwu Lungang* (公司董事的诚信义务论纲) [*Directors' Duty of Good Faith*] *in* Minshang Falü Pinglun (民商法律评论) [CIVIL LAW AND COMMERCIAL LAW FORUM] 434, 437 (Jiang Ping (江平) & Yang Zhenshan (杨振山) eds., 2004); Weng & Godwin, *supra* note 20, at 66; Nicholas Calcina Howson, *Twenty-Five Years On—The Establishment and Application of Corporate Fiduciary Duties in PRC Law in* THE OXFORD HANDBOOK OF FIDUCIARY LAW 6 (Evan Criddle et al. eds., 2018).

[126] Wei, *supra* note 37, at 43.

[127] For example, there may be reputational benefits from considering social good in corporate activities. This might be raised as justification for a company investing in ESG securities which have lower financial returns than their non-screened alternatives. The same logic might be applied to considering state interests, which may result in indirect benefits to the company, even where already an SIC.

[128] Dong Zhang & Owen Freestone, *China's unfinished state-owned enterprise reforms*, AUSTRALIAN GOVERNMENT (Nov. 19, 2013), https://treasury.gov.au/publication/economic-roundup-issue-2-2013-2/economic-roundup-issue-2-2013/chinas-unfinished-state-owned-enterprise-reforms

[129] ZHU JINGWEN (朱景文) (eds.), ZHONGGUO TESE SHEHUIZHUYI FALÜ TIXI: JIEGOU, YUANZE YU ZHIDU CHANSHI (中国特色社会主义法律体系——结构、原则与制度阐释) [CHINA'S LEGAL SYSTEM: AN INTERPRETATION OF ITS STRUCTURE, PRINCIPLES, AND INSTITUTIONS] 119, 162 (2023).

directors significant latitude in this context of uncertainty.[130] Other sources of legal obligation do little to clear up this confusion. For example, the Shenzhen Stock Exchange requires that the interests of the company be a "starting point" in decision making. This implies that other interests, provided they are not the personal interests of the director, might also be considered.[131]

That said, in the non-SIC context Chinese courts have been willing to declare that not only should directors put the firm's interests over their own, but also over "any other third parties' interests".[132] In recent years it has also appeared that, noting the absence of a formal rule akin to the "business judgement rule" in common law jurisdictions,[133] that judges have appeared less reticent to second-guess operational decisions.[134] Questions might remain as to if, in the context of SICs, this might extend to capture the state as such a third-party. That proposition may appear unlikely, especially given that the lack of legislative explanation of the duties described above means that "finding of a breach is much dependent on an individual judge's discretion."[135] Again, the likelihood that a judicial officer reprimanded a director for considering the state interest would not appear high.

Notions such as these are not entirely foreign even to common law jurisdictions. Statutory intervention in jurisdictions including Australia and the United Kingdom has made it possible for directors, and indeed the courts, to consider interests such as those of employees in addition simply to those of the company.[136] It has also been largely mooted that companies in these jurisdictions, and indeed others, can consider social impacts in their operations, even where not entirely in the short-term interest of their company.[137] For example, the decision to support charitable enterprises unrelated to the scope of the business or invest only in so-called "ethical investments" which generally result in lower financial returns may not optimize outcomes for the company itself, but would not necessarily represent breaches of directors duties if undertaken.[138] As was noted by Paul Finn in the Australian context, the "maintenance of a company's prosperity as a going concern can require its directors to take steps to please and to appease persons other than the company and its shareholders".[139] That is, a focus on the interests of the company need not be myopic, but may be considered with reference to what enables the company to act as a going concern.[140]

The extension of these principles to the consideration of the state in the Chinese context does not appear to be a significant extrapolation. Not only is such an interpretation more likely to be contextually considered appropriate, but it appears clear that the approval of the state is a necessary condition for the ongoing viability of the SIC. Therefore, it would seem fair to suppose that benefitting the state's interests would

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130 Wei, *supra* note 37, at 43.
131 Jaramillo, *supra* note 12, at 163.
132 Zhou Yu Su Shi Deng Sunhai Gongsi Liyi Zeren Jiufen Yi'an Ershen Minshi Panjue Shu (周宇诉施邓损害公司利益责任纠纷一案二审民事判决书) [Zhou Yu v. Shi Deng], (2016)沪 01 民终 13372 号 (Shanghai First Interm. People's Ct 2016).
133 Wang, *supra* note 34, at 213.
134 Weng, *supra* note 76, at 1310.
135 Wei, *supra* note 37, at 50.
136 *Id.* at 46. *See also* Companies Act 1985 (UK); *Corporations Act 2001* (Cth) § § 596AA, 596AB, 596AC (Austl.); ROBERT BAXT ET AL., CORPORATIONS AND ASSOCIATIONS: CASES AND MATERIALS 344 (4th ed. 2003).
137 *See* 2023 Company Law, art. 19
138 *Id.*
139 Paul Finn, *Fiduciary Obligations: 40th Anniversary Republication with Additional Essays*, 76 CAMBRIDGE L.J. 444, 444–57 (2017).
140 *See* AUSTRALIAN INSTITUTE OF COMPANY DIRECTORS, *supra* note 83.

benefit those of the company in that sense. As has been emphasized, one would also question whether a Chinese court would interpret these provisions in a manner contrary to the stated intent of the state. Given the deep intertwining of SICs with the state, and their role as representatives of state interests, it is likely that a director could argue that there is no inherent tension between their duties to the state and to the company, as the company represents an extension of the state with the aim of furthering the interests of the state.[141]

Thus, when this provision is considered in conjunction with the obligations described above that the company consider social interests, and the likelihood that this would be interpreted to include the interests of the state, the idea that the "best interests of the company" might, in appropriate circumstances, involve acting in the interests of the state does not appear exceptionally farfetched, especially where the company in question is owned and run by the state. The question might be, then, what this looks like in practice and how far can this balancing exercise reasonably be taken under the auspices of these provisions.

### B. First Instance Balancing by Directors

This interpretation of the new iteration of duties incumbent upon companies and directors appears to provide the directors themselves significant latitude in exercising their functions, and in determining and indeed balancing just what is in the interests of the company and the state. There are two scenarios which readily come to mind where this issue may arise.

First, consider a scenario where a potential action undertaken by the board of directors benefits the state but has no real or only a marginal effect on the company.[142] The propriety of such an action will depend heavily on the context and the extent of the benefit generated. This will be a decision for individual directors based on their own views on the matter. Legally, however, it is unlikely that the 2023 Company Law would prevent directors from undertaking such action. Considering art. 180 and its consequences,[143] such a decision would not breach the duty of loyalty, it does not speak to the effort or time required by the duty of diligence, and it is not necessarily contrary to the best interests of the company. Whilst it may not actively and significantly be in the "best interests of the company", in this scenario it is unlikely to be materially adverse to such interests and cause harm.[144] It would, however, possibly fall under the ambit of art. 20 of the 2023 Company Law[145] and art. 86 of the Civil Code[146] in being an action for the public social good, as understood in the Chinese context. It would also likely fall, as discussed elsewhere in this article, under the general duties of the directors, the expectations of the Communist Party of China, specific governmental policies as in effect from time to time, and the

[141] Karen Jingrong Lin et al., *State-owned enterprises in China: A review of 40 years of research and practice*, 13 CHINA J. ACCT. RSCH. 31, 36 (2020).
[142] For example, the decision to symbolically endorse state actions or include some form of symbolic reference to the state in the company's governance documents.
[143] 2023 Company Law, art. 180.
[144] One might argue that some harm is present in ways such as the precipitation of opportunity costs. Even if this were so, it would be difficult to show in the vast majority of cases that this was so, and even harder to characterise this opportunity cost as demonstrating a breach of duty.
[145] 2023 Company Law, art. 20.
[146] Civil Code, art. 86.

general expectations of the state as a shareholder in the company. Thus it would seem that such actions for the benefit of the state by directors, especially of an SIC, would not be prevented by law and would be in line with the imperatives the legal regime creates. In practice, then, it will be a question for the directors as to if such actions were taken. This appears to therefore be a source of significant discretion for directors. In any event, it does not seem likely a shareholder or other interested party would seek to challenge this kind of decision by directors.

Second, and perhaps more importantly in the context of this article, are scenarios where the action taken which is in the interest of the state as a whole may be detrimental to the interests of the SIC specifically as a company. That is, on a plain and narrow reading, the action would not be in the "best interests of the company". For present purposes we will not consider scenarios where this detriment is existential or of great significance, as such scenarios would prima facie see the actions of directors violate a duty of care in balancing the relevant interests and duties, even in the context of SICs.[147] It would be hard, absent some other source of authorization, to justify that this was an act of a director carrying out the role as a director and agent of the company. Rather, we will focus on scenarios where the detriment is certainly present, but is more moderate, or represents simply a reduction in a positive outcome for the firm.

Such a scenario likely represents the clearest example of where these duties may conflict. After all, as noted it seems that there exists a requirement under the 2023 Company Law to prioritize the interests of the company, yet at the same time numerous state organs have also released directives emphasizing that "irrespective of the economic costs incurred, [SICs] must comply with the Party's policies and follow the Party's orders in order to ensure the Party-state achieves its objectives".[148] For example, the state may wish that SICs operated to decrease unemployment in a specific region. A director may make decisions which induce the company to increase or maintain its employment levels, even where it may not be commercially opportune. On a larger scale, it may be that the state wished for prices of a commodity, such as electricity, that the SIC produced to be reduced or minimised. It would of course not be in the company's direct interest to seek this aim if it impacted the financial bottom line. an SIC may also seek to overproduce is certain other areas, or engage in projects which may have geopolitical benefits for the state but be financially inopportune. There are many such examples of this kind of conduct which comes to mind.

In such a scenario it would appear that pragmatically many directors might wish to act in line with their external obligations. It is worth noting that when the directors of SICs are members of the ruling party they will be under obligations by virtue of the Party's constitution to put "the interest of the Party and the people… above everything" and to ensure that the Party's policies are implemented.[149] As Wang notes, "[g]iven that all or most of the top executives and many other

[147] Indeed, even stretching the argument that something can be in the long-term or overall interests of the company if it was to its immediate detriment to its logical extremes appears unlikely to capture such a scenario, at which point a director would be violating their duties under art. 180.

[148] *Guoyou Qiye Yao Fahui Zhidu Youshi Dandang Zhengzhi Zeren* (国有企业要发挥制度优势担当政治责任) [SOEs should Shoulder Political Responsibilities based on its institutional advantage], STATE-OWNED ASSETS SUPERVISION AND ADMINISTRATION COMMISSION OF THE STATE COUNCIL, http://dangjian.people.com.cn/n/2013/1021/c117092-23277026.html; Wang, *supra* note 12 at 662.

[149] Wang, *supra* note 12 at 654.

employees at [SICs] are CCP members, the obligations imposed upon the Party members… have profound implications in the corporate governance practices of [SICs]."[150]

At the same time, it may be so that a director does not wish to act in line with a perceived "interference" from the state. In either scenario, what actions are open to the director and the board?

Here it would seem that a director, or at least the board acting as a whole, may be faced with a balancing exercise and a significant discretion. It would be for the board to determine if the action could be considered in the long-term interests of the company, even though it created potential short-term detriments. If they deemed that it could be, then they may seek to balance the company interests with those of the state to make the decision, being both in the interests of the public good and on one interpretation being in the interests of the company itself. As we have discussed above, this would be a permissible decision. The directors therefore are given the ability to decide whether to characterize the option to act in the state interests to the company's detriment as such. Noting the infancy of the relevant provisions here, there also does not appear to be case law which is directly on point which provides that this balancing would not be permissible.

It would appear likely that directors who, even informally, owe duties to the state would be inclined to act in the furtherance of the state up until the point that it became genuinely untenable for the SIC. If the desire to act in the state interest would undermine the genuine capacity for the SIC to operate as a going concern, then the board may be unable to act in that manner. Given that SICs exist as arms of the state to benefit the state, the failure of an SIC would not only reflect poorly on the state, but render it unable to fulfil its purposes in aiding the state. Given as much, a director may wish to act in the interests of the company, which would then be in the interests of the state, to not undertake the decision. How this is communicated to, or agreed with, the state is a matter for those directors at that point.

Even if the perceived benefits relied upon to justify a decision did not manifest in the short or long term, despite the lack of "business judgement rule" in China which might have itself exonerated the directors the courts might be reticent to interfere in any event.[151] As mentioned, unless there was significant negligence, misfeasance, or existential harm it is unlikely that the judiciary would step in to punish a director acting to assist the very state of which the courts are an organ.

In practice, it would appear that the requirement to act in the "best interests" of the SIC would only be invoked against directors' decisions if it were plainly detrimental to the company. This suggests that, in most scenarios, actions taken in the interests of the state, even to the short-term detriment of the company, could nonetheless not be considered as acting against the company's interest. Even if this were wrong, however, and acting in such a manner were a violation of the duties contained in art. 180 to act in the company's best interests,[152] then it is likely that the other routes presented in this article would be relied upon by either the director or the state to justify such an action.

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[150] *Id.*
[151] Wang, *supra* note 34 at 213.
[152] 2023 Company Law, art. 180.

## IV. THE DISTINCT ROLES OF SHAREHOLDERS AND DIRECTORS

Much has been made to this point in this paper as to the notion and nature of mandate, and how it manifests in the relationship between directors and their "principals" when interpreting specific provisions of the Company Law. In addition to this indirect role in interpretation remains the fact that this dynamic is in fact reflected in the Company Law by the specific governance structures mandated. Unlike the trend seen in western nations and under western corporate law—where power and authority appears to be increasingly centralized in a board of directors and shareholders are provided residual powers at infrequent shareholder meetings[153]—the Company Law affords shareholders a broader set of responsibilities. This is even so where the 2023 Company Law has increased the importance of directors generally as a governance mechanism.[154] This role provided to shareholders is especially strong in the case of SICs. As we will see, not only is this a reflection of mandate, but may allow for shareholders, not beholden themselves to the duties of directors,[155] to require the board to consider and act on a second duty to the state. This is particularly likely where the sole or majority shareholder is itself the state, as in SICs.

### A. Governance Structures under the Company Law

Under the Company Law, Chinese companies must, subject to a few exceptions,[156] structure themselves with three key governance bodies, each endowed with distinct powers and responsibilities. This system is often referred to as the "two-tier-board system"[157] although it actually involves three main entities: the shareholders' meetings, the board of directors, and the board of supervisors.[158] In some circumstances, the latter may be replaced by an audit committee.[159]

In this model, the shareholders through the shareholders' meeting act as the highest source of authority and influence in the company.[160] Shareholders are empowered to make most major corporate decisions, including those on issues ranging from general strategic matters to the articles of association, and are responsible for appointing, removing, and instructing the board of directors.[161] They also have the right to inspect company documents[162] and if necessary take legal action against directors.[163] To that extent, many of the powers exercised by shareholders reflect those delegated to the board of directors in other jurisdictions, and thus shareholders in the Chinese context have been described as more powerful than their equivalents elsewhere.[164] This, as argued by Wei Yuwa, was considered by Chinese legislators as "necessary and suitable for the actual circumstances of China as

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153 Wei, *supra* note 37, at 31–3.
154 ZHU, *supra* note 129, at 119, 159.
155 Though, it is acknowledged, beholden to other duties elsewhere in the Company Law regarding the exercise of their powers which may be similarly, such as those preventing "abuse" of rights to cause losses to the company or other shareholders, see 2023 Company Law, art. 21.
156 2023 Company Law, arts. 60, 69, 112, 121.
157 Wei, *supra* note 37, at 34.
158 Aldrich & Chen, *supra* note 74, at 186–87.
159 Wei, *supra* note 37. This committee plays, in practice, essentially the same role as the board of supervisors. Whether a company has an audit committee or a board of supervisors does not impact the present analysis.
160 *Id*. at 35.
161 *See* 2023 Company Law, arts. 59, 71, 112, 117.
162 *Id.* arts. 57 & 110.
163 *Id.* arts. 188–191.
164 Wang, *supra* note 12, at 649.

Chinese corporate practice had only just begun" and to "give more protection to shareholders, so that they can exercise their rights effectively".[165]

The position is different however for SICs as a result of Chapter 7 of the Company Law.[166] In SICs, the duties and responsibilities typically exercised by shareholders are carried out on behalf of the state by the State Council or local people's government, unless otherwise delegated,[167] to the extent that the state owns that company. Importantly, the Communist Party of China organizations within SICs shall "play a leadership role in accordance with the provisions of the CPC Constitution, study and discuss major business and management matters of the company, and support the company's organizational structures in exercising their powers".[168] These mechanisms for state influence are, naturally, even stronger in the context of wholly-owned state companies, which do not have shareholders' meetings but instead sees the powers generally afforded to such a meeting simply exercised by the institution operating the company on behalf of the state.[169]

Meanwhile, the board of directors is responsible more so for the daily operations of the company. They determine specific business plans and also supervise the management team.[170] Importantly, the board is tasked with ensuring that the decisions and directives of shareholders, as made in shareholder meetings, are implemented and carried out.[171] They take directions directly from the shareholders, and must act to carry out their wishes as desired.[172] This no doubt reflects again the concept of mandate as discussed above.

Finally, the board of supervisors acts to monitor the board of directors.[173] It ensures compliance with pertinent legislation, company policies, and the directives set forth by shareholders.[174] The board of supervisors serves as an independent oversight mechanism to mitigate risks associated with misconduct and suboptimal decision-making.[175] This function is comparable to that of independent directors in other jurisdictions; however, within the Chinese context, it operates concurrently with the system of independent directors who are also part of the board of directors.[176] Supervisors are given the power under the Company Law to review finances, challenge directors and management, review performance, and make recommendations to the shareholders regarding directors.[177] They do not engage in operational management activities like the board of directors. As noted, under the 2023 Company Law, a board of supervisors in certain companies including SICs may be replaced by an audit committee which complies with various requirements.[178]

In addition to these main governance arms, there are also relevant

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[165] Wei, *supra* note 37, at 35-36; *See* BAOSHU WANG & QINZHI CUI, THE PRINCIPLES OF COMPANY LAW 25–6 (1998).
[166] *See* 2023 Company Law, *supra* note 1, Ch. 7; Wei, *supra* note 37 at 34.
[167] 2023 Company Law, *supra* note 1, art. 169.
[168] *Id.* art. 170.
[169] *Id.* art. 172.
[170] *Id.* arts. 67 & 120.
[171] *Id.*
[172] Wei, *supra* note 37, at 36
[173] MINKANG GU, UNDERSTANDING CHINESE COMPANY LAW 211 (2017).
[174] *Id.* 211–213.
[175] *Id.*
[176] Wei, *supra* note 33, at 36; YUWA WEI, COMPARATIVE CORPORATE GOVERNANCE: A CHINESE PERSPECTIVE 121 (2003).
[177] 2023 Company Law, arts. 76–83, 130–133.
[178] *Supra* note 160.

requirements in the Company Law that in a company, and in accordance with the provisions of the Communist Party of China's Constitution, there shall be an "organization of the Communist Party of China" which is "established to carry out party activities".[179] This is so even where the company is not an SIC. This body of course is not necessarily involved in the governance of the company per se, but it is prudent to demonstrate the structural intertwining of company and state, even in non-SICs.[180] In practice, each SIC generally has at least one such organization, which is usually known as Party Group (dangzu 党组), Party Committee (dangwei 党委), or Party Branch (dangzhibu 党支部),[181] and as mentioned there are legal requirements in the 2023 Company Law as to the significance of the role these bodies shall play in SICs.[182]

The critical ramification of this structure for present purposes is that the board of directors, and the directors themselves, in Chinese companies are provided significantly less scope for discretion and directional decision-making. Rather, the directors function primarily to execute the directives of shareholders and to implement those decisions and vision thereof in a manner reminiscent of mandate. In situations where the relevant shareholder is the state, it seems that the directors will thus take on a duty to abide by the directives of the state, including where they involve acting in the interests of the state.

### B. The Instructions of the Shareholder State

Where the role of the director is to carry out the mandate of the shareholders, and thus their legal obligation is to carry into effect the wishes of the shareholders as directed, the instructions from shareholders would be a source of legal justification for considering such actions as valid exercises of directors' powers.[183]. If the meeting of shareholders was to determine that the company should be operated to benefit the state, either entirely or in part, then the board of directors would need to implement the relevant directives of the shareholders.

This would appear to mirror the idea, which has been affirmed in the context of the 2018 Company Law by various decisions of Chinese courts,[184] that activities which would otherwise constitute a violation of the duties owed by directors could be authorized by a shareholder meeting.[185] Such authorization or instruction would likely be considered by the Chinese judiciary as relevant to considering if any legal duties have been duly fulfilled, noting that it is likely the "court

[179] 2023 Company Law, art. 18.

[180] These bodies also do, in practice, often have significant influence in the relevant governance bodies. Indeed, the 1997 CCP *Notice on Party Building in SOEs* requires these organizations to "participate in the decision-making on material and important matters of the [SIC] and provide support to the factory leader/general manager, shareholders' general meeting, board of directors and supervisory board to perform their duties according to law", see Wang, *supra* note 12 at 656.

[181] *Id.* at 655.

[182] 2023 Company Law, art. 172.

[183] Assuming that the instructions themselves were relevantly legal.

[184] *See* Tai Lin International Holding Co Ltd (Tailin Guoji Konggu Youxian Gongsi) su Li Dunren Sunhai Gongsi Liyi Zeren Jiufen An Ershen Minshi Panjue Shu (Tai Lin International Holding Co Ltd（台林国际控股有限公司）诉李敦仁损害公司利益责任纠纷案二审民事判决书) [Tai Lin International Holding Co., Ltd. v. Li Dun Ren], (2017)沪 01 民终 10634 号 (Shanghai First Interm. People's Ct. 2017); He Shijun Deng su Sheng Minglong Gongsi Liyi Zeren Jiufen An Ershen Minshi Panjue Shu(何世俊等诉盛明龙公司利益责任纠纷案二审民事判决书) [He Shijun and others v. Sheng Minglong], (2019)沪 01 民终 14607 号(Shanghai First Interm. People's Ct. 2019); Liquan yu Shanghai Jiancheng Shiye Youxian Gongsi Sunhai Gongsi Liyi Zeren Jiufen Ershen Minshi Panjue Shu (李泉与上海简诚实业有限公司损害公司利益责任纠纷二审民事判决书) [Liquan v. Shanghai Jiancheng Industrial Co., Ltd.], (2019)沪 02 民终 9555 号 (Shanghai Second Interm. People's Ct. 2019).

[185] Weng & Godwin, *supra* note 20, at 65.

will take the responsibilities held by the particular director in the particular company into consideration when deciding if the duty has been breached".[186] After all, if the governance structure required by the Company Law means that directors must follow the mandates of their shareholders, and these mandates of binding legal effect require consideration of the interests of the state, then the court will have to consider that the director's responsibilities required them to act to discharge their duty in this way.[187]

This implies that if the state, acting as the majority or sole shareholder of an SIC,[188] instructs the board of directors that the company's operations should benefit the state, then the board would have a valid basis to act in accordance with such directives, owing to the distribution of authority under the governance structures described above. The interests of the state would be considered, and certain decisions prioritizing state interests would be made by the board who is required to carry out the will of the shareholder(s)..[189]

It seems likely that such a directive would be made frequently in SICs.[190] Indeed, statements promulgated by the state have already led to situations where some commentators have described that "the board of directors or general manager is required to 'consult and respect the opinion of the Party organization' before making any important decisions, and brief the Party organization on the implementation of said decision".[191] This is so notwithstanding the fact that the Chinese government seemed, for an extended period, to implement various legal reforms which reduced the role of the state in the day to day operations of these SICs.[192] Whether or not such directives would be binding on directors is another matter, and for certainty it is likely the case that the relevant instruction must come from the shareholder meeting, or the body exercising the powers thereof in the appropriate form, in order to attract the legal force described above in terms of the actions of directors.

Nonetheless, it might still be considered so that the director must, unless explicitly and specifically told otherwise, act for the interests of the company as a company and independent of the state, as would be the case for a director in other circumstances, owing to art. 180.[193] Yet if the instruction is given in the appropriate manner by shareholders that the interests of the state must be considered, either in general for all operations or in a specific circumstance, then it would appear that the director may then consider any duties to the state only as instructed or as necessary based on the wishes of the shareholders.

In such a circumstance, the organizations of the Communist Party

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[186] Wei, *supra* note 38, at 43.

[187] Importantly, however, this would likely need be framed as altering what would or could be considered the "best interests of the company", rather than permitting that which was not in those interests, as it would not be clear that such shareholder mandates could be contrary to the explicit terms of the law. That said, the requirement in art. 180 of the 2023 Company Law is that a director act with care in that interest, rather than ensure that interest, so it could also be argued that the director would still be acting with care in the best interests, albeit within the confines dictated by the relevant shareholders.

[188] Or even if a minority shareholder with sufficient support from other shareholders.

[189] It has been argued that, at least in theory, where shareholder meetings vote to authorise what would otherwise be breaches of fiduciary or other legal duties by directors that such approval should on be given on an ad hoc basis as opposed to generally. But this does not appear to be a settled principle. For further discussion of this issue, see Weng & Godwin, *supra* note 20, at 65.

[190] *See* the policy directives promulgated by the state at *supra* note 30 and accompanying text; Zhang & Freestone, *supra* note 128.

[191] Wang, *supra* note 12, at 656.

[192] Zhang & Freestone, *supra* note 128.

[193] 2023 Company Law, art. 180.

within the SIC , who again "play a leadership role" which involves "study[ing] and discuss[ing] major business and management matters" as well as assisting "the company's organizational structures in exercising their powers",[194] would seem likely to exercise their powers and functions to further the state interest. They would also seek to assist the board in doing so. Such is this interaction between the shareholder state with the corporate governance of the SIC at a structural level that at the very least they would be unlikely to act against directors seeking to assist the state.

It is also unlikely that the board of supervisors in an SIC would seek to intervene to prevent directors from exercising their functions for the interests of the state,[195] especially where it is likely that the state will appoint state officials to comprise the membership of that body who themselves will owe specific duties to the state and its interests.[196] Indeed, in 2017 the General Office of the State Council released the Guidance on Further Improving the Corporate Governance Structure of SOEs, which included reference to the fact that "[i]n addition, it is essential to give a full play to the leading and political core role of the Party, to lead the ideological and political work of the companies, to support board of directors, board of supervisors and management to perform their duties in accordance with the law, and to ensure the implementation of the Party's and national policies....[t]o give a full play to the supervisory role of inspection, supervision and audit. Besides, the Party members among directors, supervisors, and management team of [SICs] shall regularly report to the Party group (Party committee) about the performance of their duties, integrity and self-discipline every year".[197] It therefore appears clear that the mandate of the shareholder state will be that the directors acting on their behalf shall act in the interests of the state, or at least give such interests significant consideration.

The requirements provided by the 2023 Company Law for the appointment of independent directors into SICs[198] may militate against the notion that such a duty must be owed at all times by directors of SICs, or that such a directive will be made in a blanket sense. The inclusion of such independent directors is theoretically intended to ensure that the business operates appropriately and considers external perspectives. Again, the specific requirement that SICs have both independent directors and a supervisory board may imply directly that they are to act in the best interests of the company as an entity distinct from the state.[199] Then again, these directors are appointed and removed by the state, may at times be less active or engaged than other directors, may simply be used to apply their expertise in the task of benefitting the state as opposed to providing an additional check on the board, or may otherwise act in alignment with the interests of the state.[200] It might be the case that, in the absence of the explicit instruction, with the power of law over directors as described, strong

[194] *Id.* art. 170.
[195] Wei, *supra* note 37, at 38.
[196] *Id.*
[197] Lu & Zhu, *supra* note 13 at 133.
[198] Interestingly, in the case of SICs wholly-owned by the state, more than half of the board must be outside directors, and there must be employee representatives. The directors are, as discussed, appointed by the institution operating the SIC: 2023 Company Law, art. 173.
[199] Wei, *supra* note 37, at 38.
[200] *See* Byoung-Hyoun Hwang & Seoyoung Kim, *It pays to have friends*, 93 J. FIN. ECON. 138 (2009); Jeffrey L. Coles et al., *Co-opted Boards*, 27 REV. FIN. STUD. 1751 (2014); LU & Zhu, *supra* note 13 at 131.

independent directors appointed to the board would seek to oppose the consideration of the state as opposed to the company. Perhaps this would in fact reflect their role on the board, and be a strong governance practice for the modern corporatized SIC. Nonetheless, for the same reasons as described above, these independent directors, as directors under the 2023 Company Law, would still be subject to the directives and wishes of the shareholders, and would therefore not present an inhibition to considering the interests of the state if instructed by the shareholders in this manner. Despite their independence from the state as the state, they are not independent from the state as a shareholder. They must still follow shareholder instructions as with any other director.

Overall, in situations where the state, as the shareholder, instructs the directors—who are duty-bound to follow the legal wishes of the shareholder(s)—to consider or act in the interests of the state, it would appear that, except in extreme cases, the directors would be required to comply with such instructions due to the governance structure and hierarchy established by the Company Law. This obligation is not only as strong, if not stronger, in SICs compared to other companies but is also more likely to arise in practice.[201] Thus, if such a directive were given to directors of SICs, they could likely rely on it to reconcile their duty to the state with their existing duties to the company. Importantly, however, this reliance would be contingent upon the specific nature of the direction or mandate provided by the shareholders, or the shareholder state. It may also thus be the case that unless and until such directives are given by the shareholders or the state, directors must act in the traditional sense, only in the "best interests of the company" itself without specific recourse to the interests of the state, as mandated by art. 180 in the revised 2023 Company Law.[202] Once the direction is given, and only once it is given, could they consider the state interests if this justification was, by itself and with no others posited by this article, accepted owing to the legal obligation they would owe to follow such directives.

## V. Imposing Duties Through the Articles of Association

Even if the provisions of the 2023 Company Law discussed to this point did not explain the legal basis for a dual duty which might permit a director of an SIC to act in the interests of both the company and the state, the primacy and power afforded to the articles of association of a company under the law may still provide this justification if the terms of this document for the relevant SIC so provided.

### A. Empowering Provisions of the Company Law

The central provision relating to a company's articles of association in the 2023 Company Law is art. 5.[203] That article provides that a company's articles of association must be formulated in accordance with the law, but also more pertinently that they will be legally binding on "the company, shareholders, directors, supervisors,

[201] As described above and below, the state has made clear in various forums that this is what is expected of such directors.
[202] 2023 Company Law, art. 180.
[203] *Id.* art. 5.

and senior managers".[204] This provision, therefore, gives force of law to the contents of a company's articles of association to the extent that, assuming compliance with other laws, they purport to bind a director in some way. This, at least on its face, would seem to include requiring directors to act in certain ways or to promote certain interests, again assuming they were not contrary to law. Similarly, art. 179 requires directors to abide by, inter alia, the articles of association.[205] This is given further weight by the power afforded to the board of supervisors to make recommendations that a director be dismissed for violating the company's articles of association,[206] and the fact that a director who violates those articles of association may bear liability for any losses caused.[207] The articles of association are also delineated as the location which shall stipulate the "business scope" of companies,[208] the bounds within which directors must ensure the company operates.[209] There appears, therefore, to be a significant weight given to this document and a clear requirement that directors abide by its terms, being a manifestation of the will of the shareholders.

The ability to include matters in a company's articles of association is broad. For limited liability companies, art. 46(8) permits the inclusion of, amongst a number of specifically outlined matters, "other matters deemed necessary by the shareholders' meeting".[210] These provisions can be inserted or amended by a shareholders' meeting or through an equivalent process under art. 59(8).[211] The same is true for joint-stock companies under arts. 95(13)[212] and 112.[213] For SICs, this power is found in art. 172,[214] and is exercised by the relevant state body rather than shareholders as described above but is identical in its scope.

It is worth recalling both that art. 173 requires directors of SICs to exercise powers in accordance with the 2023 Company Law[215] and that as mentioned there exist requirements elsewhere that directors abide by the terms of the articles of association.[216] In practice, therefore, this means that should the shareholders, or in the case of SICs the state, implement valid provisions into the articles of association, the directors would be under a binding requirement to exercise their functions in accordance with their terms. To do so would be a part of their legal duties. Requirements of acting with due diligence or in the company's interests would of course be considered in the context of what the director had the legal capacity to do, and a director would not have the legal capacity to act against the articles of association, even if they considered it "more" in the company's interests. This may be especially so where documents such as the CSRC Guidelines for Articles of Association of Listed Companies stipulate that companies can provide further requirements regarding or altering the duty of diligence or care in their articles of association "pursuant to specific needs".[217]

Thus if the will of the shareholders, or the state in the relevant SICs,

[204] *Id.*
[205] *Id.* art. 179.
[206] *Id.* art. 78(2).
[207] *Id.* arts. 188, 190.
[208] *Id.* arts. 9, 46, 95.
[209] 2019 Guidance, art. 98.
[210] 2023 Company Law, art. 46.
[211] *Id.* art. 59.
[212] *Id.* art. 95.
[213] *Id.* art. 112.
[214] *Id.* art. 172.
[215] *Id.* art. 173.
[216] 2019 Guidance, art. 98.
[217] 2019 Guidance, art. 98.

was to include in the articles of association a requirement that directors consider and act in the interests of the state, the ability to do so would be given legal force and legitimacy by the 2023 Company Law and a legally binding duty would be placed on the directors of the company to abide by such a clause.

### B. Mandate and its Consequences

The ability for the requirement to act in the interests of the state to be included in a company's articles of association may be provided, or at least not prevented, by the Company Law. This inclusion very much reflects the notion of "mandate," which requires directors to act as directed by their mandators. The concept of mandate, and importantly its foundational differences from common law fiduciary duties, was discussed above in explicating the historical derivation of directors' duties in China. Understanding this conceptual difference is crucial for interpreting how these duties, even where codified in greater depth as in the 2023 Company Law, are likely to function or be interpreted in practice. This concept again may arise in considering the interplay between the Company Law and a company's articles of association. After all, rather than merely subjecting directors to duties by virtue of their placement in a legal position involving trust, directors are to act in accordance with the directives and wishes specifically provided by the shareholders.

In other jurisdictions, even those basing their fiduciary principles on trust, the discretion afforded to directors in carrying out their functions, whilst often broad, is of course limited by things such as the terms of a company's articles of association.[218] The strength of these restrictions is no doubt only affirmed in a mandate-based context. The role of the director is to carry out the wishes of the principal, being the shareholders, as directed. They must act in accordance with instructions provided. As discussed above, this will fundamentally alter the defined scope of specific duties and reduce the overall autonomy provided to the director. These requirements, alongside the fact that these obligations are defined in a manner more reminiscent of contract, would appear to provide greater power to the shareholders to define just what they deem to be in the company's interests, and just how the directors should carry out their wishes.

Whilst fiduciary duties are owed by the fiduciary to the beneficiary, it was and remains possible under a mandate for the benefit to accrue not only to the mandator but also to a third party.[219] This is permissible so long as the mandator retains some benefit that is not entirely abrogated.[220] The application of this view of a mandate, as opposed to the traditional fiduciary obligations owed to those who have placed the fiduciary in their position, aligns with the notion that directors under Chinese law could owe duties to consider the interests not only of the company but also of a third party such as the state. This alignment is particularly pertinent in SICs, where the largest or sole shareholder is the state. In such cases, there is generally no need to distinguish between the interests of the shareholders and those of the state, except

[218] Also known in other contexts as the company's "constitution" or similar.
[219] THOMAS, *supra* note 46, at 306.
[220] *Id.*

in situations involving minority shareholder oppression. The concept of mandate providing greater autonomy of instruction, the scope of matters able to be included in the articles of association, and ultimately the role of the directors vis-à-vis the shareholder state all point toward the fact that a dual duty to the state as well as to the company may be imposed.

Interestingly, it also appears that in the common law context, even accounting for the nature of fiduciary duties imposed, that company constitutions have been permitted to include clauses which allow for directors to act in the interests of another if there are conflicts with the interests of the company.[221] Even though not absolute in its application, this has been especially so in instances where the director has been nominated by some specific group, such as being appointed as an employee representative by employees.[222] These principles, when transposed to our current context, appear applicable. This applicability is only heightened by considering notions of mandate and the role played by the state in appointing directors to SICs. If the shareholders wish for the articles of association to allow directors to act in the interests of the state, then it would appear they have the ability to implement the relevant provisions to do so, especially where it becomes increasingly difficult in practice and principle to separate the interests of the shareholder state and the SIC as an entity.

### C. Implementation in Practice

Given the scope of matters able to be included in a company's articles of association, and the legal effect this document is given on the duties and responsibilities of directors, it appears that an SIC could validly impose requirements in such a document that its directors must, in their management of the company, consider and act in the interests of the state as well as the company. In doing so, it would of course remain the discretion of the shareholders, or the state, in amending the articles of association or including such a term from inception as to exactly how this requirement was framed.[223] That is, whilst it seems the possibility for SICs to balance state and company interests in their articles of association certainly exists, it will be up to each SIC as to how this is incorporated. Nonetheless, the directors would be bound to follow the term or terms as included.

The SIC would, of course, need to ensure that this provision was not contrary to the terms of the Company Law.[224] However, in practice, it seems unlikely that this would pose significant barriers.[225] If the scope of the company's work is deemed to entail furthering the interests of the state,[226] or if the articles of association noted that one of the aims or purposes of the company is to achieve this, then there would likely be no inability to act in line with the specifically enumerated duties in the

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[221] *See*, *e.g.*, *Levin v Clark* [1962] NSWR 686.

[222] *See* Jonathan R. Povilonis, *The Use and Misuse of Fiduciary Duties: Corporate Social Responsibility and the Standard of Review*, 13 WM. & MARY BUS. L. REV. 1 (2021); Robert J. Sadler, *Employee Representatives on Boards of Directors: Limiting Directors' Fiduciary Duties*, 24 J. INDUS. REL.'S. 282 (1982); Jean Jacques du Plessis, *Board Composition: between independent directors, minority representatives and employee representatives* 144, *in* COMPARATIVE CORPORATE GOVERNANCE (Afra Afsharipour & Martin Gelter eds., 2021).

[223] This might look like a clause requiring consultation with the relevant state body, the active requirement that a director consider this interest, or some other form of inclusion.

[224] 2023 Company Law, art. 5.

[225] This is not only for the reason that it is the state seeking to impose these obligations, but also for the reasons discussed above about why this, prima facie, would not be contrary to the terms of art. 180, at least at the stage of implementation alone.

[226] Noting that as discussed a company must operate within its scope of operations, yet this scope of operations is to be contained in the articles of association.

Company Law. A clause even so specific as to require that a director act also in the interests of the state in furthering the interests of the company would be of binding legal effect on the relevant directors.[227] The mandating shareholders have decided that the directors must exercise their powers in accordance with these requirements in the articles of association. They have validly implemented them. They possess legal remedies against directors who do not follow them. At a more conceptual level, the democratic will of the member(s) who comprise the organization, even where it possesses separate legal personhood, is that the resources and powers of the organization be used in this way. The directors, therefore, must act in accordance with the terms as now included in the articles of association.

It appears highly probable that state owned enterprises would seek to include such clauses in their articles of association, given the imperatives outlined in the official guidance documents discussed above, amongst others. Research from Stanford University's Center on China's Economy and Institutions reflects as much, describing that since "China's central government launched a set of initiatives called the 'party-building' or dangjian [党建] policy in 2015 intended to strengthen and formalize the role of the CCP in China's [SICs]" there had been significant moves to amend SICs' articles of association to reflect the control, role, or duty to, the state.[228] According to that research, at present the balancing that SICs have seen fit to implement provisions which can be grouped into three categories, being "more symbolic provisions, such as simply referencing the CCP constitution in the firm's corporate charter; provisions that allow the CCP to appoint, manage, or supervise corporate personnel; and provisions concerning the party's decision-making powers within the firms."[229] At that time, 96.3% of SICs had adopted "symbolic" provisions, 52.3% had adopted "personnel" provisions, and 58.9% had adopted "decision-making" provisions.[230] 74.4% required the board consult with the party committee in making decisions.[231]

Thus, even if the Company Law itself does not require or directly authorize a director to act in the best interests of the state, it is likely that an SIC could bind a director to do so with legal effect equivalent to their existing duties under the Company Law, albeit indirectly through the company's articles of association. Indeed, it seems like, understandably, many SICs already include such provisions which this paper now argues have this binding legal, rather than merely symbolic, effect. The practical effect of this legal route for reconciliation appears directly contingent on the specific company and the particular contents of its articles of association. The discretion afforded to directors, or the specific consideration of state interests, would be that contained in the bespoke documents. Thus, all interested parties would need to take note of the actual contents of these articles of association in order to best understand how directors can or might act, and how the interests of the company will be balanced with those of the state. This is reflected in the

[227] By virtue of, at least, art. 179, see 2023 Company Law, art. 179.
[228] *CCP Influence over China's Corporate Governance*, STANFORD CENTER ON CHINA'S ECONOMY AND INSTITUTIONS (Nov. 1, 2022), https://sccei.fsi.stanford.edu/china-briefs/ccp-influence-over-chinas-corporate-governance.
[229] *Id.*
[230] *Id.*
[231] *Id.*

fact that since 2015 there has been "significant variation in [SIC] adoption of the dangjian policy in their corporate charters".[232] Despite this variation, it remains crucial to recognize that the overwhelming majority of SICs have implemented such provisions in their articles of association. This means that directors of these companies are likely provided with a legal source of justification in this manner.[233] Investors ought therefore inspect these documents to fully understand the nature of the obligations imposed on directors. After all, if all other legal justifications discussed in this article were insufficient, directors of SICs could still rely on the terms explicitly included in their specific company's articles of association to reconcile their dual duties.

## VI. CONCLUDING REMARKS

It might be argued by some observers on one side that, from a purely governance best practice standpoint, or even perhaps based on certain political perspectives, that directors of companies—even where the company is wholly or mostly controlled by the state—should owe duties only to the best interests of that company to the reasonable exclusion of other parties, including the state. This article neither endorses nor opposes any specific views on that matter. Whatever one's normative take on that question, it remains so that, in practice, directors of Chinese SICs will owe and act upon duties of various forms not only to their companies but to the state.[234] In seeking to understand the legal basis for these obligations, this paper has sought to better understand the scope of any potential reconciliation between these dual duties under the Company Law itself, rather than dismissing this pragmatic reality as the result of a supervening political force. This, it argues, is preferable to leaving such reconciliation unresolved or to be conducted without any legal basis, as doing so provides greater clarity and certainty to all parties involved in the governance, operation, and indeed ownership of SICs.

Having detailed why the relevant principles or sources of understanding must be grounded in the Chinese context and jurisprudence, and subsequently delved into the 2023 Company Law alongside other related sources of law, it appears that three potential bases—potentially co-existent or overlapping—may provide the legal basis for directors of SICs to understand their dual duties to company and to state. First, the drafting of provisions which impose duties on the operation of companies and on directors are drafted widely and in sufficiently vague terms as to capture a responsibility to work for the betterment of the state. Second, the structure provided for whereby the board of directors, and/or the supervisory board, is beholden to shareholders creates a system where the wishes of those shareholders may become binding directives for directors, and the best interests of shareholders, including where relevant the state, must inform decision-making. Finally, the authority permitted to company articles of association by the 2023 Company Law, and the matters they may deal with, would allow the state to mandate that directors act with such a duty to act in the interests of the state if it included it within that foundational document.

The consequences of each potential justification might appear more

[232] *Id.*
[233] *Id.*
[234] Wang, *supra* note 12, at 666.

so a matter of form, rather than substance. This may especially be the case for an investor, and in particular a foreign investor, For such investors, the primary interest lies in the final outcomes or actual decisions made and how these affect them, rather than in the specific governance processes. That said, it may be that the procedural differences in these sources would manifest practically. If directors act at first instance based on the first justification, they are provided with significant discretion in balancing these competing duties. Under second justification, it may be that the director shall, unless explicitly and specifically told otherwise, act only for the interests of the company as a company, and then consider any duties to the state only as instructed or as necessary based on the wishes of the shareholders as communicated. Finally, if the third justification was appropriate and applicable, then the reconciliation of these duties, unless also accompanied by another justification, would, legally, vary between each SIC on the basis of the specific contents of its articles of association.

As noted, the amendments made to the Company Law in 2023 are wide-ranging and a positive step in the right direction for China's legal regime surrounding corporate governance. The 2023 Company Law appears to be a strong foundation from which future developments in Chinese corporate governance may stem.[235] The textual basis for a variety of duties incumbent upon directors is now considerably more clear than in the past. Commercially, directors will begin to understand what these duties look like in practice. Legally, once the courts are called upon to give further content to the relevant duties, their exact operation in China will be distilled and the contents of what still remains to some extent vague duties will begin to take shape. This will be a crucial development both internally in China and for those seeking to invest or understand corporate governance in the Chinese context. At some stage in the future it may be so that, as has occurred in the past, further amendments will be made to the Company Law. Perhaps at that time the requirements of each specific directors' duty, as well as the exact nature of the duties for directors in SICs, will be outlined. For now at least, it may be required to approach these questions from first principles in the manner this article has sought to.

Ultimately, in that vein, the legal consideration this paper gives to matters which will fall invariably to decisions grounded in governance, politics, and the Chinese commercial context may appear removed from these realities of how directors will act. Yet with the continued emphasis of the rule of law in China[236] and the modernizing reforms represented in the 2023 Company Law, considering the functions and duties of directors appointed by the state through this legal lens may be of value in ensuring the prosperity of SICs, the success of shareholders, and ultimately the effectiveness of directors in the world's second largest economy. It will provide a greater certainty and a clearer framework as to what may justify the actions of directors in SICs, and in doing so better elucidate the scope of these duties which remain nebulous in the text of the Company Law and in practice. Nonetheless, it may be of use for the operation of these duties, generally framed in the text of the Company Law, to be clarified further through official documents from

[235] Including, of course, in the areas of governance *structures* and the best practice in that space to ensure effective corporate operation. Such developments and practices have not, however, formed the basis of this article's discussion.
[236] Hou, *supra* note16.

the relevant Chinese state organs or through later amendments to the Company Law.