



# CHINA REGULATORY ENFORCEMENT QUARTERLY

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# EXECUTIVE SUMMARY

The PRC regulatory landscape remains a hotbed of activity in Q1 2016 with government regulators tackling major scandals in the financial and healthcare sectors. While government regulators and corporations continue to focus on traditional corruption investigations, major cyber/data security breaches and social engineering frauds have also come to focus. These frauds are cross-border in nature, and those facilitating the frauds are spread across many countries around the world, which makes it extremely difficult to recover stolen assets and data. Moving forward into 2016, the following trends will influence the regulatory environment in China and the rest of Asia:

- **Corporate data increasingly vulnerable to breaches/attacks**

Increased corporate connectivity with the shift towards online data storage and cloud-based services has increased the potential points of vulnerability for data theft and breaches. Work-related communications and data transfers involving confidential company and customer information are becoming increasingly vulnerable to attacks. Reliance on smart connected devices is also creating numerous points of vulnerability for intelligence gathering and/or fraudulent activity. Increased connectivity and big data will present a new dimension of risks for multinational companies.

- **Sophisticated international cybercrime attacks**

International cybercrime syndicates are conducting increasingly sophisticated attacks against corporations, often forming cross-border teams, transferring victims' assets across a chain of bank accounts around the world, using offshore shell companies to evade detection, and posing as company executives to obtain key information and/or affect transfer of funds. The attacks are not limited to attempts to steal funds and other assets, such as IP and tangible commercial secrets. Recent media leaks and attacks against government entities are cases in point.

- **China's new extraterritorial influence**

Recently introduced laws, regulations and initiatives that increase Chinese authorities' regulatory and supervisory powers are starting to have an impact in mainland China and abroad. For example, the Enterprise Credibility Information Publicity Systems (which was reported in our Q1 2015 newsletter) are increasingly being used by the Administration for Industry and Commerce ("AIC") to publicly list the AIC's decisions on administrative commercial bribery cases across China. As these bribery decisions are made public, it has increased the risk of overseas enforcement claims. Additionally, China's new Anti-Terrorism Law coupled with its Sky Net initiative has resulted in the increased repatriation of fugitive Chinese government officials suspected of serious corruption overseas. By monitoring telecommunications activity, working with overseas law enforcement, and increasing collaboration, Chinese regulators are able to creatively find ways to exert influence in connection with enforcement initiatives beyond its mainland borders. For more information about China's Anti-Terrorism Law, please see our Q4 2015 newsletter.



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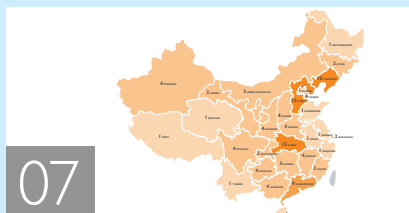
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This information is intended as a general overview and discussion of the subjects dealt with and is up-to-date as of March 31, 2016. However, laws and/or updates may have changed since this date. Some information contained in this report is based on media reports and public announcements, some of which may be considered secondary sources. This information is not legal advice, and should not be used as a substitute for taking legal advice in any specific situation. DLA Piper will accept no responsibility for any actions taken or not taken on the basis of this information.



## PRC LEGAL AND REGULATORY UPDATES

### **Whistle-blower protections for reporting crimes committed by Chinese government officials strengthened**

Jan 11 – The Central Leading Group for Comprehensively Deepening Reforms passed the Regulations on Protecting and Rewarding Whistle-blowers for Official Crimes (“**Whistle-blower Regulations**”) to further strengthen whistle-blower protections and encourage people to speak up against corrupt government officials. The People’s Procuratorate, which is the investigative body responsible for investigating crimes committed by government officials, is charged with protecting the personal safety and property of whistle-blowers and their close relatives. Under the Whistle-blower Regulations, whistle-blowers may also receive monetary rewards for providing leads that result in the investigation of official crimes.

### **G20 discussions outline Anti-Corruption Action Plan to further strengthen cross-border cooperation on fugitive repatriation**

Jan 26 – The first G20 Anti-Corruption Working Group meeting of the year was held in China, and it focused on international cooperation in high-risk sectors prone to bribery, such as the mining, customs, fisheries, forestry, and construction sectors.

The G20 is a meeting of finance ministers and central bank governors from 19 industrialized and emerging economy nations, including China. The Anti-Corruption Working Group began drafting a two-year action plan for 2017-18 which includes several commitments by member countries to combat corruption in public and high-risk sectors.

### **Enforcement of health food regulations strengthened and registration process streamlined**

Feb 26 – The Administrative Measures on the Registration and Record Filing of Health Foods (“**Health Food Measures**”) issued by the China Food and Drug Administration (“**CFDA**”) will come into effect on July 1, 2016. This updates the existing registration model, which has been in place since 2005. The main changes introduced by the Health Food Measures include:

- Registration of health foods is limited to health food which is not listed in the Catalog of Raw Materials for Health Food published by the CFDA and nutritional health food which is imported into China for the first time. Some health food, which was previously required to be registered, now only requires record filing under the Health Food Measures.
- Applicants who obtain administrative licenses through fraud, bribery or other improper means could be barred from registration for up to three years and subject to criminal liability if such misconduct constitutes a crime. Applicants would also be subject to a fine ranging from CNY 10,000 to 30,000 (approx. USD 1,500 to 4,500).
- The health food registration process is further streamlined to reduce the time for granting production licenses.

### **China’s anti-graft campaign focuses on misuse of poverty relief funds**

Mar 16 – CAO Jianmin, procurator-general of the Supreme People’s Procuratorate of China, declared that China’s anti-corruption campaign will focus on the misuse and embezzlement of poverty relief funds. The central government anticipates investing an additional CNY 20.1 billion (approx. USD 300 million) in poverty relief funds for 2016 compared with 2015 to support poverty reduction efforts in rural areas.



## MAJOR ENFORCEMENT NEWS

### **Former CCTV executive sentenced to 15 years for accepting bribes from advertising agencies**

Jan 12 – Former Deputy Minister of Public Security, LI Dongsheng, was found guilty of receiving CNY 21.98 million (approx. USD 3.3 million) in bribes while he served as the vice head of China Central Television (“**CCTV**”), the largest TV broadcast network in China. LI took bribes from advertising agencies and individuals based in Beijing in exchange for securing agency contracts on behalf of CCTV. The bribes include sums which were given both to LI personally as well to his close relatives. LI was sentenced to 15 years in prison and CNY 1 million (approx. USD 150,000) confiscated as illegal gains.

### **Former vice-president of major state-owned iron and steel company accused of bribery**

Jan 19 – The former vice-president of a major state-owned iron and steel company was charged by the Shanghai People’s Procuratorate for receiving CNY 3.95 million (approx. USD 600,000) in bribes. According to media reports, most of the bribes were given to him by “old friends” who were in business with one of the company’s subsidiaries.

### **Five pharmaceutical companies fined for entering into anti-competitive agreements related to the sale of arthritis drugs in China**

Jan 28 – Five domestic Chinese pharmaceutical companies were fined CNY 3.99 million (approx. USD 600,000) by the National Development and Reform Committee (“**NDRC**”) for anticompetitive agreements involving price-fixing and market collusion. According to the NDRC, the companies agreed to market the drugs at a price almost two times higher than the regular price.

### **China’s biggest Ponzi scheme: online financing platform bilked USD 7.6 billion**

Feb 1 – Chinese authorities accused an online financing platform operator, which runs one of the most popular peer-to-peer platforms in China, of illegally soliciting funds from the public and fraud. Twenty-one suspects connected to the company were arrested by the police, including the chairman of its parent company. According to the police, the company fraudulently obtained more than CNY 50 billion (approx. USD 7.6 billion) from more than 900,000 investors. This online financing platform was launched in 2014 and lured investors with promises of high-interest pay-outs invested into various projects. However, 95% of its advertised investment projects were falsified. The collapse of the company is likely to result in one of the largest investment frauds in China in recent years.

### **Chinese subsidiaries of major multinational food processor fined for food safety violations**

Feb 1 – The Shanghai Jiading People’s Court has issued its judgment in relation to a two-year investigation of a major food safety scandal first exposed by the media in July 2014. Two Chinese subsidiaries of a major multinational food processor were fined a total of CNY 2.4 million (approx. USD 363,600) for selling expired beef and chicken to several major fast food restaurant chains in China. Ten employees of these two subsidiaries were held responsible and sentenced to prison for up to three years.

### **Third Round of Central Inspection identified banking executives misusing public funds for personal entertainment expenses**

Feb 4 – The Central Inspection Team of the Chinese Communist Party’s Central Commission for Disciplinary Inspection (“**CCDI**”) completed the third round of inspections for 2015. The inspection targeted 31 entities including

administrations and commissions directly supervised by the central government and state-owned enterprises, including key players in the banking and financial sectors. The CCDI identified misconduct involving the misuse of public funds, conflicts of interests, incompetent leadership, and violations of the “Eight Rules”. Officials of several major financial institutions allegedly misused public funds for personal entertainment purposes, including playing golf, personal travel, lavish meals and other entertainment activities.

The Political Bureau of the Central Committee of the Communist Party of China (“CPC”) adopted the “Eight Rules” in 2012. These rules require CPC officials to: (1) keep close relationships with the people; (2) strictly regulate the organization of meetings and events; (3) reduce the unnecessary issuance of official documents; (4) regulate arrangements of official visits; (5) improve arrangements for security guards; (6) improve media reporting; (7) restrict publication of personal writing; and (8) uphold integrity and thrift.

### **China FDA commands investigations into vaccine scandal that affected 24 provinces in China**

Mar 20 – The CFDA issued two notices on the same day demanding local food and drug supervisory departments and business operators to investigate and trace the origin and distribution of CNY 570 million (approx. USD 88 million)

## **OVERSEAS ENFORCEMENT**

### **U.S. software company settled with DOJ and SEC for FCPA offenses in connection with its China operations**

Feb 16 – A U.S.-based technology company and its two Chinese subsidiaries agreed to pay more than USD 28 million to settle parallel civil and criminal actions involving violations of the U.S. Foreign Corrupt Practices Act (“FCPA”) with the U.S. Department of Justice (“DOJ”) and the U.S. Securities and Exchange Commission (“SEC”). The SEC’s investigation found that two Chinese subsidiaries of the U.S. company provided non-business related travel and other improper payments to various Chinese government officials for the purpose of winning business. According to DOJ/SEC press releases, the company’s Chinese subsidiaries

worth of improperly stored vaccines. These vaccines could potentially have lost their effectiveness as they were not properly refrigerated in storage and during transportation. Two individuals from the Shandong province had allegedly been illegally bulk-selling these vaccines to 24 provinces across China since 2010. It is reported that at least 300 people were involved in the illegal sale and distribution of the vaccines. The scandal has gathered widespread public attention and reignited drug-safety concerns in China.

### **“Sky Net” campaign continues to repatriate top wanted fugitives from abroad**

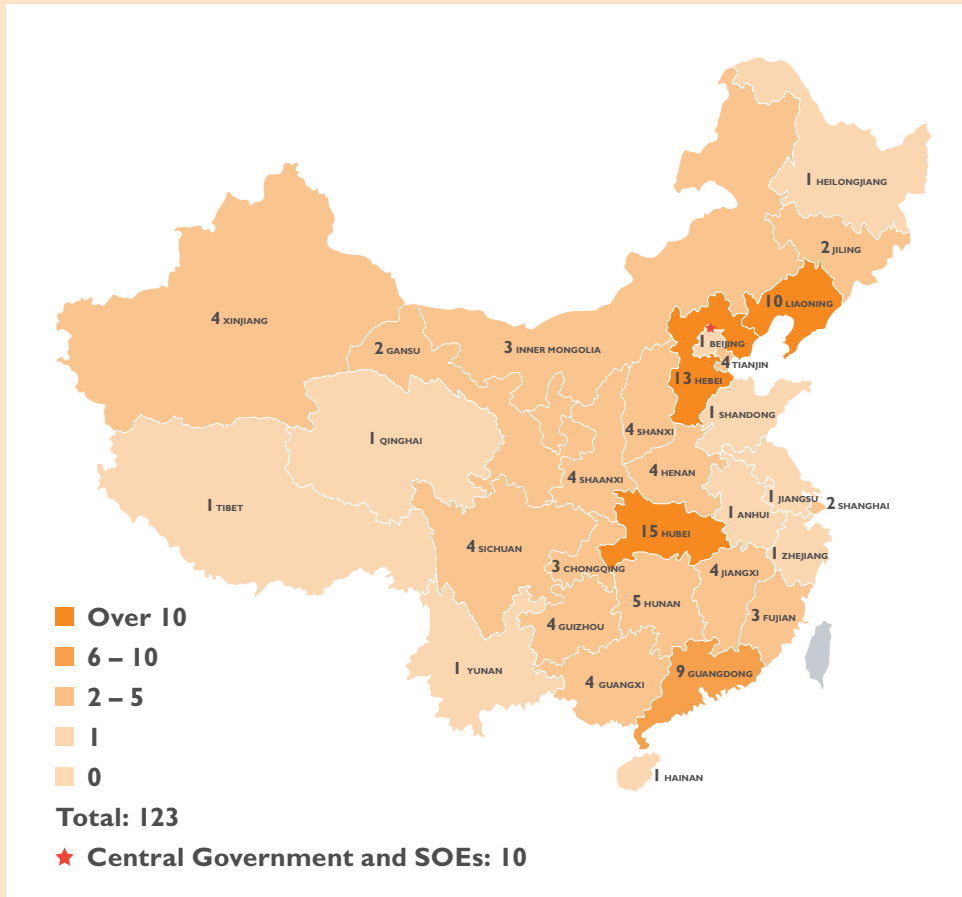
March 27 – According to media reports, 25 fugitives from China’s 100 most wanted list were successfully repatriated through operation “Sky Net”. On March 27, ZHANG Liping, the former chairman and general manager of a footwear company based in Shanghai, who was accused of falsifying value-added tax invoices, voluntarily returned to China from Peru. ZHANG was ranked No. 63 on China’s 100 most wanted list.

“Sky Net” is a multi-agency operation involving the collaboration of four Chinese government agencies/organs: Organization Department of the Communist Party of China’s Central Committee, Supreme People’s Procuratorate, Ministry of Public Security, and the People’s Bank of China.

routinely relied on local third parties to assist the company in sales to Chinese SOE customers. The company also provided what it called “training” to SOE employees through those third parties. The “training” sessions were usually hosted in popular tourist destinations in the United States, such as New York, Las Vegas, San Diego, Los Angeles, and Honolulu. The training component was minimal compared to the sightseeing or recreational activities.

For additional information on overseas enforcement actions, please contact DLA Piper.

## Heat Map of PRC Officials Under Investigation



### Notable individuals put under investigation in Q1 2016 include:

- DENG Qilin, former chairman and party committee secretary of a major iron and steel company based in Wuhan
- AI Baojun, former deputy mayor of the city of Shanghai
- LV Xiwen, former member of deputy secretary of Municipal Party Committee of the city of Beijing
- DAI Weijie, former president of No. 3 People's Hospital of the city of Chongqing
- WEI Hong, former governor of Sichuan Province



## DRAFT AMENDMENTS TO THE ANTI-UNFAIR COMPETITION LAW RESHAPE COMMERCIAL BRIBERY

On February 25, 2016, the draft amendments to the Anti-Unfair Competition Law (“**AUCL**”) were released by the State Council for public comment. The draft amendments extend the scope of the administrative commercial bribery offense and address other issues, including the use of third parties to commit commercial bribery, employer liability, and updated accounting books and records requirements. The draft amendments also introduce new law enforcement measures and increased penalties for offenders who commit commercial bribery. There is presently no clear indication when the amended AUCL will be officially released. We expect that it is likely to come out in the second half of 2016.

### **Definition of commercial bribery expanded**

The current AUCL does not have a detailed definition on the administrative commercial bribery offense. It generally prohibits any business operator who bribes its business counterparties for the purpose of a sale or purchase of commercial products. It further provides that under-the-table kickbacks that are not recorded in companies' accounting books constitute bribery. The draft amendments now propose a wider definition of “commercial bribery” as “a business operator providing or promising to provide economic benefits to the counterparty in a transaction or a third party who may have influence over the transaction, in order to entice the party to seek business opportunity(ies) or competitive advantage(s) for the business operator.” Compared with the current AUCL, this definition covers benefits provided to third parties who are not directly

involved in the underlying transactions and therefore casts a wider net to catch potential offenders who may try to bypass the current regulations by using third party intermediaries to funnel improper payments or benefits to the counterparties. Furthermore, the draft amendments also expanded the definition of the term “business operator” to include manufacturers of commercial products and all service providers on top of the commercial traders and providers of for-profit services as defined in the current AUCL.

### **Employer’s vicarious liability for employee conduct**

The draft amendments further specify that an act of commercial bribery by a business operator’s employee to obtain business opportunities or competitive advantages for the business operator should be considered an act of the employer. This rule also makes it clear that an employer will not be held liable when its employee takes bribes against the interests of the employer. The draft amendments have not addressed how the employer’s vicarious liability rule may apply when an employee gives bribes to a business counterparty against the interests of the employer.

### **Inaccurate or incomplete accounting books and records may constitute commercial bribery**

Under the current AUCL, a business operator is permitted to give a discount to a counterparty or a commission to an intermediary provided that the discount or commission is accurately recorded in the accounting books and records. The draft amendments further strengthen the books and



records provision by making it an offense of commercial bribery if business operators engaging in a transaction fail to accurately record all payments of economic benefits in their contracts and respective accounting books.

### **Economic benefits obtained during the course of public service**

The draft amendments establish an offense of commercial bribery which prohibits business operators from committing commercial bribery offense during the course of “public services”. Previously, no such term “public services” appeared in the AUCL. Although no guidance has been provided on what “public services” entails, it is likely that public hospitals, schools, utilities, and transportation providers would be considered “public services.” Therefore, if relevant PRC Criminal Law bribery provision thresholds are not met, it is possible that a business operator could still be held liable under the draft amendments for commercial bribery during the course of “public services”.

### **No cap for penalties tied to commercial bribery**

The current AUCL imposes a fine for commercial bribery of between CNY 10,000 to CNY 200,000 (approx. USD 1,500 to 30,000), along with confiscation of illegal gains. The draft amendments impose fines of between 10% to 30% of the business revenue generated in relation to the illegal conduct.

Compared to a fixed maximum penalty, this increases the potential costs for a business operator who violates the commercial bribery provisions particularly where the bribe generates large business revenue streams.

### **Increased enforcement powers and flexibility in discipline guideline**

On top of the existing administrative enforcement measures under the current AUCL, the draft amendments expressly provide additional enforcement measures to the relevant supervisory and inspection agencies. These new measures include the power to seize properties in relation to suspected violations, inquire into the bank accounts and related accounting books and records of business operators suspected of violations, freeze funds where attempts are made to transfer or conceal illegal funds, and order business operators under investigation to cease any suspected illegal conduct.

The draft amendments also grant enforcement agencies wide discretion in imposing penalties against violators. Cooperation may result in a lighter or mitigated penalty being imposed, while significantly larger penalties of between CNY 20,000 to CNY 200,000 (approx. USD 3,000 to 30,000) could be imposed for non-cooperation, where false materials are provided, or where evidence is concealed or destroyed, thereby impeding the investigation.

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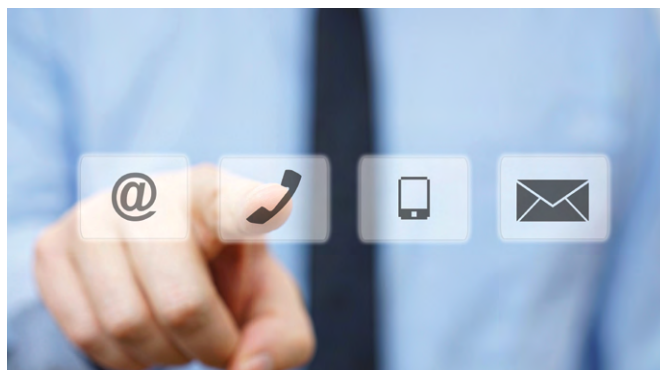


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