國楓律師事務所
GRANDWAY LAW OFFICES

Newsletter

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Update

China Releases Administrative Measures for Personal Information Protection Compliance Audits

On February 12, 2025, the Cyberspace Administration of China (CAC) issued the *Administrative Measures for Personal Information Protection Compliance Audits* (the "Measures"), which will take effect on May 1, 2025.

The Measures, comprising 20 articles, define personal information protection compliance audit as a supervisory activity that reviews and evaluates whether the personal information processing activities of data processors comply with laws and administrative regulations. The Measures stipulate that if a data processor meets one of the three specified conditions, the relevant protection department may require the processor to engage a professional organization to conduct a compliance audit of its personal information processing activities. If a data processor conducts a compliance audit on its own or commissions a

professional organization to do so in accordance with the protection department's requirements, it must follow the Guidelines for Personal Information Protection Compliance Audits included in the Measures.

GAC Revises the Discretionary Criteria for Customs Administrative Penalties (II)

On February 19, 2025, the General Administration of Customs (GAC) published the *Announcement on Revising the Discretionary Criteria for Customs Administrative Penalties (II)* (the "Criteria (II)") on its website, which will take effect on March 1, 2025.

The Criteria (II) consists of four chapters and seventeen articles. It primarily deletes 18 items that are inconsistent with the newly revised Frontier Health and Quarantine Law and adds 16 new items. A new "First-Time Violation Penalty Exemption" list has been added, clearly specifying ten first-time violation penalty exemptions, such as failing to declare health quarantine inspection items as required, failing to declare or misdeclaring the export of bamboo, wood, and straw products, and evading import and export commodity inspections by not declaring. The "first-time" period is set within 24 months, and the scope of violation determination is set within the same inspection and quarantine business field for administrative and criminal violations. In addition, the Criteria (II) also adjusts and improves the existing discretionary items, expands the scope of the minor penalty exemption list, and adds common violation scenarios for imported and exported grain and imported food products.

China Releases Action Program for Stabilizing and Promoting Foreign Investment in 2025

On February 19, 2025, the General Office of the State Council transmitted the *Action Program for Stabilizing and Promoting Foreign Investment in 2025 from the Ministry of Commerce and the National Development and Reform Commission* (the "Program"), which has been effective from February 17, 2025. The program focuses on the orderly expansion of independent openness, elevating investment promotion efforts, strengthening the effectiveness of open platforms, and improving service guarantees, outlining twenty key tasks.

The Program requires the complete removal of foreign investment access restrictions in the manufacturing sector. It calls for revising the negative list of market access and ensuring that areas outside the list adhere to the principle of equal treatment for domestic and foreign investment. The Program also aims to expand the range of industries encouraged for foreign investment, update and expand the catalog of industries encouraged for foreign investment, direct foreign investment toward modern service industries, and support increased foreign investment in the central, western, and northeastern regions. Additionally, it seeks to increase efforts to attract investment in key areas, supporting foreign-funded enterprises in participating in China's new industrialization process, particularly in high-tech sectors. The Program also enhances trade facilitation measures for foreign-funded enterprises, ensuring efficient issuance of certificates of origin under preferential trade agreements and enabling foreign-funded enterprises to benefit from tariff concessions on exports to agreement partners.

GAC Announcement on Gate Management in Special Customs Supervision Areas

On February 17, 2025, the General Administration of Customs (GAC) issued the *Announcement on Matters Related to Gate Management in Special Customs Supervision Areas* (the "Announcement") on its website, which will take effect on March 1, 2025.

The Announcement stipulates that without customs approval, vehicles or personnel are not allowed to carry goods through non-cargo channels to enter or exit special customs supervision areas. Customs may conduct gate inspections on goods entering or exiting special customs supervision areas based on their risk levels and by referring to the *Administrative Measures of the Customs of the People's Republic of China on the Inspection of Import and Export Goods*. Gate inspections are conducted at inspection sites within the special customs supervision areas. If the goods are vulnerable to natural factors such as temperature, static electricity, or dust, making inspection unsuitable at the designated sites, customs may conduct inspections at specified locations upon the written application of enterprises within the special customs supervision areas or their agents. Enterprises or their agents within the special customs supervision areas should cooperate accordingly. The administrative management institutions within the special customs supervision areas must fulfill their operational management responsibilities, improve the operation and maintenance of gate facilities and equipment, enhance the staffing for gate management, and improve the information database for gate passage records. The retention period for gate passage records should be no less than three years, and video record data should be kept for no less than three months. During the operation management process at gates and other areas, any violations of customs-related laws and regulations should be promptly reported to customs.

Administrative Measures for Business Entity Registration Archives Formally Released

On February 17, 2025, the State Administration for Market Regulation (SAMR) published the *Administrative Measures for Business Entity Registration Archives* (the "Measures") on its website, which will take effect on March 20, 2025.

The Measures consist of 31 articles, covering the overall requirements for registration archive management, collection and preservation of archives, informatization of archives, transfer of archives, inquiry and utilization of archives, and legal responsibilities. The Measures refine the norms for registration archive management and specifies requirements for electronic registration archive management. The Measures set forth provisions regarding the scope of archiving, filing standards, storage requirements, management systems, and retention periods of registration archives. It is clarified that during the existence of a business entity, registration archives should be continuously preserved. After the cancellation of a business entity, the retention period for registration archives is generally 20 years. The registration authority should periodically assess the preservation value of expired registration archives to decide whether to destroy them or transfer them to the national comprehensive archives of the same level for permanent preservation.

China Promotes High-Quality Development of New Energy Storage Manufacturing Industry

On February 10, 2025, eight departments, including the Ministry of Industry and Information Technology (MIIT), issued the *Action Program for High-Quality Development of the New Energy Storage Manufacturing Industry* (the "Program"), with immediate effect. The Program proposes that by 2027, China's new energy storage manufacturing industry will have a prominent international competitive advantage across the entire supply chain, and the echelon of leading enterprises will be further strengthened.

The Program proposes to cultivate high-quality industrial enterprises, accelerate the development of a number of industry-leading enterprises, and foster a group of specialized and innovative "small giants," manufacturing champions, and high-tech enterprises. It also aims to establish a number of green factories and green supply chain management enterprises. The Program emphasizes the need to enhance the level of intelligent manufacturing and promote the widespread application of blockchain, big data, artificial intelligence, 5G, and other new-generation information technologies in the new energy storage manufacturing industry. In terms of policy support, the Program clarifies that central and local policy resources should be integrated and utilized effectively to support the research and development of key technologies for new energy storage. It also calls for the provision of facilitation services for the transportation of energy storage products for enterprises and encourages insurance institutions to develop insurance products for new energy storage power stations.

CIETAC Officially Releases Procedures for Administering Cases Under the UNCITRAL Arbitration Rules

On February 17, 2025, the China International Economic and Trade Arbitration Commission (CIETAC) released the *Procedures for Administering Cases Under the United Nations Commission on International Trade Law Arbitration Rules* (the "Procedures") on its official WeChat account, which will take effect on March 1, 2025.

The Procedures consist of seven chapters, including "General Provisions", "Composition of the Arbitral Tribunal", "Arbitration Proceedings", "Awards", "Expedited Arbitration", "Cost Management", and "Supplementary Provisions", totaling twenty-five articles. They are applicable to cases where parties have agreed in their arbitration agreement to apply the UNCITRAL Rules and have CIETAC as the arbitration administering institution. When parties agree to submit disputes to CIETAC for arbitration or to have arbitration procedures managed under the UNCITRAL Rules, or agree to apply the Procedures in arbitration or arbitration management, or make other similar agreements, it is deemed as consent to apply the Procedures as a revision and supplement to the UNCITRAL Rules. The Procedures may also apply to investor-State arbitrations administered by CIETAC under the UNCITRAL Rules based on treaties providing protection for investments or investors.

Shanghai Lingang Issues Negative List and Management Measures for Data Outbound Governance

On February 8, 2025, the Shanghai Lingang Administrative Committee published the *Notice on Issuing the Management Measures and Negative List for Data Outbound of the Pilot Free Trade Zone (2024 Edition)* (the "Notice") on its website, with immediate effect.

The Management Measures and the Negative List focus on the construction of Shanghai's "Five Centers" and three leading industries. The Management Measures are divided into six chapters and 21 articles, including General Provisions, Working Mechanism and Responsibilities, Implementation and Management of the Negative List, Measures to Promote Data Outbound, Supervision and Management, and Supplementary Provisions. They primarily concentrate on the formulation process of the negative list, division of responsibilities, scope of application, and safety supervision, serving as the basic norms for formulating the negative list and carrying out daily supervision.

The Negative List takes into account the requirements of industry regulatory authorities, data classification and grading rules, data sensitivity, and other factors. The first batch covers three key areas: finance (reinsurance), shipping (international shipping), and commerce (retail and catering, accommodation), including two types of data: important data and personal information. It involves six specific scenarios and 84 data items.

Article(s)

Legal Framework and Risk Prevention of Employee Stock Ownership Platforms in the Technology Sector

by Rachel Chen

I. Introduction

In the context of mergers and acquisitions (M&A) in the technology sector, Employee Stock Ownership Plans (ESOPs) play a pivotal role in enhancing corporate governance, stabilizing key personnel, and maintaining competitiveness. Given the rapid evolution of capital markets, companies increasingly rely on equity incentive schemes to attract and retain high-value employees while mitigating the risks of talent attrition caused by M&A. However, the structuring of stock ownership platforms involves complex legal and tax considerations, including regulatory compliance, shareholder rights protection, tax efficiency, and exit mechanisms.

For technology companies with high growth potential, frequent equity structure changes, and complex M&A transactions, ensuring a legally compliant, risk-mitigated, and operationally efficient ESOP framework is critical. This article provides a legal analysis of mainstream stock ownership platforms, evaluates the key risks faced by employees in M&A transactions, and offers compliance recommendations to enhance ESOP design, mitigate regulatory and tax risks, and ensure post-M&A stability.

II. Legal Structures of Employee Stock Ownership Platforms in the Technology Sector

Technology companies generally implement ESOPs through direct shareholding or indirect shareholding via a structured platform. The three primary models for indirect shareholding include Limited Liability Companies (LLCs), Limited Partnerships (LPs), and Asset Management Plans/Trusts, each with distinct legal and tax implications.

1. Limited Liability Company (LLC) as a Holding Vehicle

(1) Structure

Employees collectively establish an LLC that holds equity in the technology company, allowing them to participate in ownership through the holding entity.

(2) Legal and Tax Considerations

This model provides structural clarity and allows employees to exercise shareholder rights indirectly. However, it is subject to the 50-shareholder limit under Chinese law, which restricts large-scale participation. A major drawback is double taxation—the LLC is subject to corporate income tax (25%), and employees are taxed at 20% on dividends, significantly reducing net returns.

From a governance perspective, employee entry and exit are procedurally complex, requiring shareholder approvals and corporate registration amendments. Departing employees who refuse to transfer shares may disrupt the incentive mechanism. Additionally, founders often retain majority control over the LLC, ensuring corporate stability but limiting employees' voting rights.

(3) Applicability

Best suited for small-scale, core team incentives, but impractical for broader employee participation due to tax inefficiencies, governance constraints, and structural inflexibility.

2. Limited Partnership (LP) Model

(1) Structure

Employees participate as Limited Partners (LPs), contributing capital, while a General Partner (GP) (typically the founder or a designated entity) manages the partnership. The LP holds equity in the technology company, granting employees economic benefits without direct governance rights.

(2) Legal and Tax Considerations

The LP model is widely favored due to its tax efficiency—the partnership is tax-transparent, meaning profits are taxed at the LP level only, avoiding corporate-level taxation. Centralized GP control preserves corporate stability, while flexible exit mechanisms facilitate seamless employee transitions. Moreover, LP registers are non-public, ensuring privacy regarding employee stock ownership.

Challenges include the 50-partner limit, which restricts large-scale participation unless multiple parallel partnerships are established. Employees may also feel detached from direct ownership, as they hold partnership interests rather than direct shares. GP control, while beneficial for governance, presents fiduciary risks, necessitating robust partnership agreements to safeguard LP rights. Furthermore, pre-IPO regulatory scrutiny may require full transparency regarding beneficial ownership, affecting shareholder calculations under listing regulations.

(3) Applicability

This model is ideal for high-growth technology firms due to its tax benefits, flexibility, and ability to preserve corporate control, though compliance with tax and regulatory requirements is crucial.

3. Asset Management Plans/Trust Structures

(1) Structure

A licensed financial institution (e.g., a trust or asset management firm) establishes an investment vehicle that holds equity in the technology company, with employees participating as beneficiaries rather than as direct shareholders. This structure is commonly used in publicly listed companies' ESOPs.

(2) Legal and Tax Considerations

The key advantage is regulatory compliance and avoidance of shareholder limits, making it ideal for large-scale ESOPs. However, high management fees (often ⩾2% annually) and low liquidity (due to fixed lock-up periods) may reduce attractiveness for startups. Additionally, these plans typically require employee self-funding, which may deter early-stage participants.

(3) Applicability

This model is well-suited for listed or IPO-bound companies, but it presents high costs and regulatory complexity, making it less viable for private technology firms.

III. Legal Risks of Employee Equity Incentives in M&A Transactions

M&A transactions introduce significant legal, governance, and tax risks that may undermine employee stock ownership structures.

1. Shareholder Rights Protection

M&A transactions often restructure shareholding patterns, potentially invalidating or modifying existing ESOPs. Acquiring companies may refuse to honor legacy ESOP agreements, resulting in equity dilution or cancellation. This risk is especially critical for key technical personnel, whose retention is essential for maintaining a company's competitive edge.

To mitigate risk, ESOP agreements should explicitly protect employee stock rights and outline continuity measures in case of M&A.

2. Transfer and Execution Risks

Post-M&A, employees may need to convert their equity into acquirer shares or options. If the transition is not properly structured, incentive values may be reduced or nullified.

Potential risks include:

Changes in vesting schedules, strike prices, or valuation methodologies, leading to diminished employee benefits.

Mandatory equity conversions without employee consent, creating dissatisfaction and potential legal disputes.

To prevent disruptions, M&A agreements should specify equity transfer mechanisms and provide a structured transition process.

3. Tax Compliance Risks

Stock incentive adjustments can trigger unintended tax liabilities. Employees may be required to pay personal income tax on stock conversions, and jurisdictional differences in tax classifications (e.g., treating gains as "property transfer income" at 20% vs. "business income" at 35%) may increase tax exposure.

Pre-transaction tax planning is critical, particularly leveraging deferral mechanisms under applicable tax regulations.

IV. Compliance Strategies for ESOP Optimization

1. Strengthening Equity Incentive Plan Design

Legal Safeguards: M&A agreements should clearly define ESOP continuity provisions, including equity conversion formulas and grandfathering clauses.

Hybrid Holding Structures: Combining LLC and LP structures may optimize control and flexibility.

2. Protecting Shareholder Rights

Priority Repurchase Rights: Employees should have first refusal rights during equity buybacks.

Anti-Dilution Measures: Agreements should safeguard employee shareholding ratios in capital restructurings.

3. Tax Efficiency and Compliance

Deferred Taxation Strategies: Companies should leverage regional tax incentives and implement deferred taxation mechanisms to optimize employee tax liabilities.

Regulatory Compliance: ESOP structures should comply with CSRC and tax authorities' transparency requirements, particularly for pre-IPO companies.

V. Conclusion

M&A transactions in the technology sector require well-structured ESOPs to balance corporate governance, regulatory compliance, and employee incentives. Strategic ESOP design, including limited partnerships, regulatory safeguards, and proactive tax planning, is essential to minimize risk and ensure long-term equity incentive effectiveness. By integrating robust compliance mechanisms and digital governance tools (e.g., blockchain-ledger documentation), enterprises can strengthen workforce retention and sustain competitive advantage in high-stakes M&A environments.

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