

Insight into company chops (Seals) in China



To many western companies entering the East Asian market, the use of chops is often an alien concept. In China, chops have been instrumental in commercial and governmental transactions since imperial times. While in the west, the trend has moved towards the use of signatures as a means of validating a document, or binding a contractual relationship, in China the chop remains the primary tool for these purposes. A chop serves as a signature stamp representing a legal organization/entity or a natural person, and performs similar functions as the signature in western organizations.

Once a company is successfully registered with the local Administration of Industry and Commerce, it can apply for its

Company Official Chop from the local Public Security Bureau (PSB). All Company Official Chops must be approved by the PSB with a specimen of the stamp registered with the PSB. The specimen stamp can be used by the PSB to determine the authenticity of a Company Official Chop stamp in the event of a dispute arising.

There are also specific regulations in place regarding engraving and use of chops, issued directly by the State Council. These regulations strictly specify the shape, size and design of chops for legal entities and organizations.

Types of Chop

A legally registered company in China is required by law to have at least a Company Official Chop in order to



conduct its business activities. It is also general business practice to create various chops to serve different business requirements. These chops have various restrictions on use, depending on their type. Listed below are some chops commonly used by companies in China:

The **Company Official Chop** is the most significant chop in the company, providing the possessor the authority to conduct business activities on behalf of the company. Technically, anyone who has possession of the **Company Official Chop** can legally bind the company. The Company Official Chop is required on all official business documents such as contracts, internal/external memorandums, bank account applications and documents filed with government before they are deemed valid.

The **Legal Representative Chop** represents the signature (i.e. the authority) of the company's designated legal representative, which is filed with the Administration of Industry and Commerce, the government body responsible for the administration of the industrial and commercial sectors. In most cases the legal representative of a company is the Board Chairman

or the CEO/General Manager. The **Legal Representative Chop**, usually in combination with the Company Official Chop, is required for numerous legal and official documents, for example, applications for business licenses and tax certificates.

The **Finance Chop** is used predominantly for a company's financial transactions. It is generally required for banking transactions such as cash withdrawals, wire transfers or changes to account information. The Finance Chop is usually delegated to and controlled by the Finance Officer of a company for conducting daily financial transactions. The company's banks also keep a specimen stamp of the Finance Chop to verify the company's documents presented to the banks, for example bank cheques.

The **Contract Chop** can be used in place of the Company Official Chop to execute contracts, but is limited to this purpose alone. A company can also have various contract chops which are valid for only specific types of contract.

The **Human Resource Chop** can be used for all Human Resource activities including signing labor contracts with employees, authenticating

employment verification letters, registering employees with government bodies and issuing internal memos.

Some companies (especially in retailing and catering industries) have a **Tax Invoice Chop** specifically for the purpose of validating their Tax Invoices.

Fraud Risks

Although some people perceive that chops can be easily fabricated and are thus susceptible to fraud, in reality the risk of this is similar to that of signature fraud, in that forgery of chops can expose both the company and the individual to legal ramifications. Article 32 of the Contract Law of the PRC states that "where the parties conclude a contract in written form, the contract is established when it is signed or sealed by both parties." Though the law allows for a signature to establish a contract, common practice requires both a signature and a Company Official Chop. The Company Official Chop can be replaced with a Contract Chop and the authorized signature can be replaced by the Legal Representative Chop. Anyone who fraudulently obtains property / goods by any of the following means



can be subject to a three year prison sentence and a fine:

1. Executing a contract using a fictitious name or the name of others without their prior permission;
2. Using forged, altered, or invalid negotiable instruments or other false certificates of property rights as guarantees on a contract;
3. Performing a portion of the contractual obligation, with no intention of fulfilling the entire contract, as a means to deceive the opposite party;
4. Going into hiding after receiving goods, payment, advance payment, or property as a guarantee from the opposite party;
5. Defrauding the opposite party's property through other means.

As is common in Chinese laws relating to financial crime, there is also a clause which encourages a stricter sentence "if the amount of money is considered significant", from ten years, up to life imprisonment. However, the law does not elaborate on specific circumstances which would qualify as "significant".

If a Company Official Chop is misplaced, the company must report the incident to the PSB immediately and wait for its approval to have a new Company Official Chop made. If this is made without prior PSB approval, both the company and the chop maker can be charged with forgery of a Company Official Chop.

Internal Controls to safeguard the chops and protect the companies from fraudulent use of chops:

As chops are some of the most important assets of a company, it is important that sufficient internal controls are put in place in order to protect their security and proper use. Weak controls over company's chops can have far reaching consequences for companies.

There are some key areas which are essential for protecting the appropriate usage of chops:

1. It is important that Chops are physically safeguarded by the authorized custodians with clear policies in case of the absence of the custodian for leave or any other reason.

2. The authorized use of a specific chop should be delegated to a custodian whose role/function is relevant to the use of such chops, for example the Finance Officer should have access to the Finance Chop but not the Human Resources Chop.
3. A log should be developed and maintained by the authorized custodian to keep record of any use of the chop in his/her possession. The log should contain the information of each use including the date/time, user's name, signature and purpose of use.
4. The company should have clear written policies in place which define the following:
 - a. the circumstance and/or purpose for the use of each chop;
 - b. the authorized custodian for each chop; and
 - c. the custodian's responsibility for the chop

The chop should not be used or passed onto anyone without proper approval from authorized personnel.

A specific area where problems can arise is in relation to an outgoing legal representative. As a legal representative plays a key role in representing the entity/organization in all respects of business activities, he will also be responsible for approving his own termination related documents. To mitigate the possibility of this situation arising, it is sometimes good practice to have the legal representative sign and chop termination related documents on appointment.