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New Company Law - Key Changes the Investors in China Need to Know

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In a major legal development that will impact investors across China, the amendment of the PRC Company Law has been finalized. The amendment to the PRC Company Law was adopted on 20 December 2023 and will take effect as of 1 July 2024 (the "New Company Law"). In this article, we summarize, some of the key changes related to the corporate governance, registered capital and equity transfer. Investors should be familiar with these changes. It is advisable that investors be prepared to amend the articles of association of their companies in China to accommodate these changes in due course.

1. Corporate Governance

1) Legal Representative

The New Company Law has expanded the candidate pool for the position of legal representative such that any director who handles company affairs on behalf of the company or the general manager could serve in the position. Currently the PRC Company Law requires the legal representative to be either the Chairman of the Board of Directors (or the sole executive director if there is no Board of Directors) or the general manager.

If the legal representative resigns, a new legal representative shall be appointed within 30 days from the date of the legal representative's resignation.

The New Company Law confirms that the company shall bear the legal consequences of civil activities undertaken by the legal representative in the name of the company. Restrictions on the powers of the legal representative imposed by the articles of association or the board of shareholders may not be invoked against a bona fide counterparty. Subject to the articles of association and PRC law, the legal representative may be personally liable for liability arising to the company from the legal representative's negligence.

2) Directors

The New Company Law indicates that if a director resigns, he/she shall notify the company in writing, and the resignation shall take effect on the date when the notification is received by the company. That said, the resigning director shall continue to perform his/her duties till his/her replacement assumes office if there are less than 3 directors (statutory quorum) remained in the board of directors.

A limited liability company (as opposed to a company limited by shares) that is small in size or has a small number of shareholders is not required to form a board of directors but may have one director who exercises the powers and functions of the board of directors as provided for in the New Company Law. The term "executive director" is no longer a legal concept in the New Company Law.

The board of shareholders/sole shareholder may by resolution remove a director. The dismissed director may claim compensation against the company if there is not a legitimate reason for the early termination of the appointment.

The statutory quorum fora board meeting shall be more than half of all directors and a board resolution shall be adopted by a simple majority of all directors constituting the Board.

3) Duties of General Manager

The statutory duties of general manager under the current PRC Company Law have been entirely removed from the New Company Law which allows the duties of the general manger to be set out in the Company's articles of association or delegated by its board of directors.

4) No mandatory supervisor

Under the New Company Law, supervisors are no longer mandatory for a limited liability company that is small in size or has a small number of shareholders. A Board of Directors audit committee can also substitute for a Board of Supervisors.

2. Registered Capital

1) Capital contribution

The New Company Law requires the registered capital of a limited liability company to be fully paid within 5 years from the establishment date of the company. Existing companies with a term of capital contributions exceeding the aforesaid 5-year period shall adjust its schedule of capital contribution, unless the laws, administrative regulations or the State Council states otherwise. The detailed rules of implementation are yet to be issued.

2) Disproportionate capital reduction

The New Company Law confirms that a disproportionate capital reduction is allowed provided it is agreed by all shareholders of a limited liability company. This may provide an exit mechanism for financial investors.

3. Transfer of equity interests in a limited liability company
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The consent of non-transferring shareholder(s) is no longer required for equity transfer to a non-shareholder party. A pre-emptive right applies. The transferring shareholder shall inform other shareholders in writing the quantity, price, payment method and schedule of the potential equity transfer. The non-transferring shareholders who do not respond within 30 days from receiving the written notice will be deemed to have waived their pre-emptive rights.

The transferring shareholder shall notify the company in writing and request updating the register of shareholders. From the time when the transferee is recorded in the register of shareholders, the transferee may exercise the rights as a shareholder of the company.

We would be pleased to assist you in making necessary changes to relevant articles of association in line with the New Company Law. Please contact us if you have any queries on corporate governance, registered capital and equity transfer in respect your investment in China.

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