

# Corporate governance structure of foreign invested companies

## Description

Chinese foreign investment regulation originated earlier than the enactment of the first Company Law of China (1994) and this together with other reasons gave rise to the irregular corporate governance structure of foreign invested enterprises (which term generally excludes foreign invested companies limited by shares) where there was generally no shareholder meeting and instead the board of directors or a management committee was vested with the powers to decide on every important corporate matter and there was often no supervising mechanism either.

Later, with the introduction of the old Company Law, effective as of July 1, 1994, equity joint venture enterprises and wholly foreign owned enterprises were required to be set up in the form of a limited liability company, a type of entity under the old Company Law. However, the past corporate governance practice was largely carried on without any change and the ambiguity with respect to supervising mechanism and other issues still subsists thereafter.

Now upon the advent of the new market-oriented Company Law coming into force on January 1, 2006 and its ancillary rules (the "Ancillary Rules", as jointly issued by the State Administration of Industry and Commerce, Ministry of Commerce, State Administration of Foreign Exchange Control and State Administration of Customs), the picture of the corporate governance pattern is clear and complete.

However that does not mean the new Company Law has unified the corporate governance structure of foreign invested companies and domestic companies. The old legacy of the practice of having the board of directors as the top power organ in lieu of a shareholder meeting within a foreign invested company is reaffirmed by the Ancillary Rules with a view to keeping foreign investment regime consistent and avoiding turmoil in foreign investment practice. Further, it is made clear in the Ancillary Rules that a foreign invested company shall have in place a supervising mechanism, either a board of supervisor or one to two supervisors.

### 1. Sino-foreign equity joint venture company

The board of directors is the top decision-making organ having the power to decide on any and all important matters relating to the joint venture. It shall be noted that though the Company allows for an executive director instead of a board in the case of small domestic companies, it is not allowed in the case of a foreign invested company.

A board of supervisors shall be set up except that for small companies, one to two supervisors instead of a board may suffice for purpose of company registration.

Other corporate organs such as managers may be installed as stipulated in the articles of association.

### 2. Cooperative joint venture company

It is the same as in the case of a Sino-foreign equity joint venture company described above.

### 3. Wholly foreign owned company

The Ancillary Rules requires that a wholly foreign owned company shall establish its corporate governance structure in conformance with the new Company Law, much the same as a domestic company.

It shall have a shareholder meeting except in the case of a one-member company.

It shall have a board of directors except in the case of small companies with only a few shareholders in which an executive director in lieu of a board shall be instated.

It shall have a board of supervisors except in the case of small companies with only a few shareholders in which one to two supervisors in lieu of a board shall be instated.

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