

Entities you can set up under China Company Law

Description

Though in a foreign investment context, we often use the foreign invested enterprise to refer to the entities foreign investors may set up in China, nowadays most entities established by foreign investors are companies under the company law of China rather than an enterprise. In the Chinese legal jargon, a company is for sure regarded as an enterprise but an enterprise may not necessarily be a company.

With the new Company Law becoming effective on January 1, 2006, more investors have chosen to set up companies pursuant to the Company Law because rules in this regard are more clear, rational and orderly than those concerning enterprises.

Basically, there are two types of companies under the Company Law, namely, the limited liability company (the "LLC") and the company limited by shares (the "CLS"). These two types of companies differ substantially in many aspects. This article is to introduce some of those differences for your reference.

1. Equity form

The equity (or the [registered capital](#)) in a LLC is not divided in equal shares as in the case of a CLS but expressed in a percentage value. Accordingly, voting rights attached in the equity of a LLC is also expressed in percentage value instead of the number of shares held by a shareholder as in the case of a CLS.

A CLS's capital or equity is expressed in certain number of shares with a par value. This is the type of company that most foreign investors are familiar with.

As a result of this difference, a LLC will never be listed on stock exchange before converting into a CLS. Yes, a LLC can be converted into CLS, the so called corporate reorganization in China.

2. Number of shareholders

Though a LLC does not have any share, contributors of the equity interests of a LLC are also called shareholders. A LLC can only have its number of shareholders up to 50 and however there is no such a cap for a CLS. On the other hand, the promoters in forming a CLS shall be no less than 2 and no more than 200. This number 200 is very important in China securities law where it is compulsorily provided that it will constitute a public offering and thus be subject to a lot more complex security rules once the investors are more than 200 in number.

The new Company Law legalized the one-member LLC which existed widely in disguise (with at least one nominal shareholder) under the old company law regime.

3. Amount of registered capital

The minimum registered capital of a LLC is RMB 30,000 and that of a CLS is RMB 5,000,000.

[Note: please be advised that China Company Law has been revised late 2013 to remove both minimum registered capital requirement, leaving the amount of registered capital to be decided by the shareholders in the company's articles of association.]

The registered capital reform in 2013, namely the removal of minimum capital requirement has led to a sprawling growth of companies in practice with many serving as sham in deceiving third parties dealing with them. You may wish to read the other posts for more in this regard:

[China corporate reform on registered capital](#)

[registered capital, the greater, the better?](#)

4. Management Organs

A LLC with only a few shareholders or of a small scale does not have to set up a board of directors but to have one executive director who may enjoy and perform such powers and duties as customary to a board of directors or as stipulated by the articles of association. Further, such executive director may also serve as the general manager of the company at the same time.

A LLC with only a few shareholders or of a small scale does not have to set up a board of supervisors but to have one to two supervisors.

However, a CLS has to put in place a board of directors and a board of supervisors and a general manager.

5. Equity transfer

Unless otherwise agreed in the articles of association, the transfer of the equity interests in a LLC to a person who is not a member of the LLC in question shall be subject to the consents of more than half of the remaining shareholders. Upon equal conditions and terms, the other shareholders of the LLC shall have the pre-emptive right to purchase such equity interests.

The transfer of shares in a CLS is not subject to such rules, and thus more fluid.

6. Listing

A LLC can never go listed unless converted into a CLS. When a CLS is listed and traded on stock exchange, it will be subject to a slurry of capital and security rules that are not included in this simple post.

Date Created

November 1, 2011

Author

admin