# Inheritance of Corporate Shares of a China Company (IV)

## Description

We have already written a few articles regarding inheritance by foreigners of corporate shares (a stock company limited by share) or equity interests (a general limited liability company) in a China company, where typically the deceased is a Chinese citizen being a shareholder in a China domestic company and the heirs (often spouse and children) have already emigrated to a foreign country and been naturalized into foreign citizenship.

Our recent experience is that local authorities (including company registry, foreign investment commission) in Beijing and Shanghai agrees that upon inheritance of the shares or equity interests, the domestic company shall remain a domestic entity in nature despite that there is or are foreign shareholders in the company, resonating with the Shanghai court's decision over a case where the trading company is still a domestic company with two German heirs shareholders.

While the remaining-domestic rule may not hold true throughout the country before a uniform guideline handed down from top authority, it shall not be taken for granted if any new case arises. Other cities in China have no obligation to follow the suits of Beijing and Shanghai, and local officials could hold otherwise insisting that the domestic company shall be transformed into a foreign-invested company. Best policy is always to check out with local authorities and argue in the best interests of the client. In practice, there could be difficult situation for the foreign heirs either way.

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### I. In the case of the company remaining domestic entity

If this is the case, the advantage is that the foreign heirs may be allowed to hold shares or equity interests in a company that is engaged in businesses or industries that are restricted to or precluded from foreign investors, which means the foreign heirs can still benefit from their shareholdings in a often profitable business that they, as foreigners, otherwise cannot invest.

On the other hand, the disadvantage is obvious and can be really a pain, namely, the foreign heir shareholders cannot take out of China their profits or dividends paid by the company. The reason is that China does not have any rules allowing a domestic company to pay profits or dividend out of China, and accordingly no bank in China will have the guts to help you to convert your RMB dividend into USD or other currencies and wire the same out of China. China still keeps a strict control over the cross-border money flow fearing panic capital flight.

### II. In the case of company being transformed into foreign-invested entity

Assuming that the company in question is required to be changed into a foreign-invested entity (equity joint venture), then by contrast to the case of the company remaining domestic entity, the advantage and disadvantage are reversed.

The foreign heirs will not be able to continue to hold shares or equity interest in the company (which shall have to be disposed of ) that is engaged in businesses or industries in which foreign investment is

restricted or prohibited, and on the other hand, for those companies whose businesses can be invested by foreign investors, the foreign heir shareholders could take out the profits or dividends distributed by the company as a normal foreign investor. Oh what's more, so far, foreign individual investors are still exempted from paying personal income tax on the dividend received from foreign invested companies in China.

**III. Way out of the plights**

So what is the way out of the respective plights of the foreign heir shareholders?

(1) for the money repatriation problem, so far there is no way out of the predicament unless you are willing to try some "gray" ways of getting your money out of China, but just be sure you are 100% safe.

The only option that is legal and lawful is to cash in on the shares or equity interests after the completion of the inheritance of the assets. Pursuant to the foreign exchange regulation concerning personal transfer of assets out of China, foreigners who inherit estate in China are allowed to cash in on the inheritance and take the proceeds out of China through Chinese banks that are licensed to deal with foreign exchange transactions.

If the sale of the inherited properties/assets is a choice, then it is just a matter of finding a buyer that offers a good price. Very often, it can be an impossible mission if the estate inherited is the minority equity position in a private closely held limited liability company where there may be no buyer interests to purchase the equity.

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(2) in the case of the plight that the foreign heir shareholders are not allowed to hold investment in a China company in which the deceased is a shareholder, it could be more tricky. While the regulations prevent the foreign heirs from being shareholders in the company, the law does recognize the right of the heirs to inherit the proprietary interests in the shares/equity interests. In other words, the foreign heirs cannot inherit the shareholdership, but they cannot be deprived of their right to the value of the shareholding left by the deceased.

The catch-22 situation is that: on one hand, the law does not allow the foreign heirs to inherit the shareholdership and become shareholders, and on the other hand, if the shares or equity interests are not registered in the name of the foreign heirs, they cannot be sold. A dead person cannot sell.

The only possible way out of the stalemate is to take the matter to court and get the court to deliver a judgment ordering what should be done on part of the company and the foreign heirs or even other interests parties like the shareholders. The possible result is that the court would order the company to buy back the shares and pay the value to the foreign heirs or order a shareholder to do the same.

Much is not clear yet as we have not seen such precedent cases, but it is our belief that under the current legal environment, our ideas above may hold true in practice.

Interested readers can join our Group "China Family Laws" on Facebook for more discussion of China family law issues.

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