China Family Law: spouse interests in real properties and corporate equities

Description

As a part of family law practice, divorce cases are increasing in China esp in first-tiered cities such as Shanghai, Beijing and Shenzhen.

With the number of cross-border marriages between Chinese and foreigners, it is good for the foreigner spouse to understand the legal environment in China in case of an inevitable divorce, in particular, in terms of the financial rights and obligations.

Nowadays, in China, much as in other countries, the most significant assets or properties one can have are real estate and corporate equities. This post will mainly discuss rules related to these two types of marital properties.

I. General Rules about Community Properties

China has upheld the community property system all the time whereby properties obtained or acquired by one spouse after marriage will be automatically jointly owned by the other spouse, and upon divorce, such joint properties/assets will be normally split half to half. At the same time, China Marriage Law permits the couple to write up an agreement to stipulate otherwise. In other words, the couple to choose to apply the separate property rule between them.

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However as a matter of law, properties owned by one spouse prior to marriage will always be his or hers throughout the marriage so long as demarcated clearly.

II. Real Properties

With the property markets in China rocketing for more than a decade, a large number of families hold real properties (apartments, villas, offices, commercial real estate etc.) hobbling up fortune without shedding a drop of sweat. Upon divorce, splitting of real estate is often the focus of the parties.

A few rules that you may wish to know about real estate in the family setting are summarized here for you:

1. The property bought by one spouse prior to marriage remains the personal asset of that spouse provided that only that mentioned spouse’s name appears on the title deed of that property. However in practice, that spouse may have taken out a mortgage loan that is paid off over a period of time into their marriage, and in this case, the other spouse though not initially contributing any financial help in purchasing the property, is however entitled to claim a portion of the increased value that accrues during the life of marriage, for the reason that the money used for paying off the mortgaged loan after marriage is the community property of the couple half of which belongs to the other spouse, thus entitling the other spouse to claim a commensurate portion of the increased value. That said, if the real property is bought with no mortgage loan to be paid over time after marriage, then the increased value of the real property

shall still remain the personal property of the spouse that initially buys the property. In other words, the other spouse has no valid claim to the increased value.

2. You can add your name onto the title deeds of the properties owned by your spouse no matter the properties are acquired before or after the marriage. Legally, if the property is owned by the spouse before marriage, the addition of the other spouse' name will entitle the other spouse to claim half of the properties in question upon divorce which would otherwise not be possible if the addition does not take place. Addition of a spouse's name costs you almost nothing, so does removing one spouse's name off title deed.
3. Properties gifted or bequeathed to one spouse become community property unless it is clearly indicated in the gifting document or will that the properties are gifted or bequeathed to only one spouse.

III. Corporate Equity Interests/Shares

Another type of significant assets is corporate equity interests or shares in companies, listed or not. This can be complicated and confusing. It is crystal clear if the equity interests or shares are bought with community property cumulated after marriage in which case the value of the equities and shares will remain community property subject to splitting upon divorce.

However with respect to the equities or shares invested or bought prior to marriage but subsisting into marriage, the increased value of the investments can cause dispute as to whether and how the increased value should be split.

The laws are not straightforward. China Marriage Law provides that earnings from production and business operation shall be community property without referrence to investment activities. Then China Supreme Court in its second interpretation of China Marriage Law provides that earnings derived from investment made with one spouse's personal property shall be community property of the couple without specifying what type of earnings it means, and then in 2011, China Supreme Court in its third interpretation of China Marriage Law says that the post-marriage earnings derived from personal property of one spouse shall be considered as community property unless such earnings are fruits of those personal properties or natural/unearned increment in value (??????????????????????????????????????). But these attempts to make the issue clear have not been very successful indeed.

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In practice, the equities interests in companies can take the following forms: (1) one or both spouses set up, own and manage a company, thus holding equity interests therein, (2) one or both spouses invest in a non listed company and but not participate more or less in management of the company and instead participate only at the shareholder meeting level, (3) one or both of them buy listed shares on stock exchanges and keep them throughout their marriage till divorce, where they are only passive investors without participation in the any way in the operation of the listed company, (4) one or both of spouses work to speculate stock by buying and selling frequently.

Assuming that the 4 type equity interests are all formed prior to marriage but increase in value during marriage, then how the laws should apply in those cases.

It has been established that post-marriage property/earnings made at the cost of the labor of one

spouse shall be considered as community property, so it is not difficult to conclude that the increased value in case (1) and (4) shall be split upon divorce, and in case (3), the increased value shall remain the personal property.

However, with respect to equity interests in case (2), it will surely invite controversies and disagreements. Unlike a passive investor in stock market where the investor spouse will do nothing, a spouse shareholder actively involved in shareholder meeting activities may be thought to be contributing labor and skill in growing the corporate value and therefore the value of his or her shareholding in the said company as well, but on the other hand, unlike the spouse shareholders in case (1) who are heavily involved in the daily management of the company in question, shareholders who only participate at shareholders meeting level may not have a clear correlation with the value increment or we can only say that the spouse shareholder may only have a remotely causation in respect of the value increment. So in this case, should the increased value be equally split or it should be totally left to the discretion of the court favoring the spouse shareholder?

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