What is a legal person under Chinese laws

Description

You may frequently encounter the phrase “legal person” when perusing legal articles about Chinese laws, in particular, corporate and business laws. However, you may inadvertently take the “legal person” in China as the same in your home country when it is actually not. which may lead to unmindful loss.

What is a legal person under Chinese laws?

The definition of “legal person” is provided in Article 36 of China Law on General Civil Principles:

> A legal person is an organization that has the capacity for civil rights and civil conducts, and enjoys civil rights and assumes civil obligations independently in accordance with laws.

In the following Article 37, a legal person shall satisfy the condition set out below:

1. it is incorporated in accordance with laws;
2. it has necessary assets or funding;
3. it has its own name, structure and premises;
4. it assumes civil legal liabilities on its own.

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The key and most fundamental element is the fourth condition: the legal person must assume and discharge legal liabilities on its own without recourse against its members, or shareholders, thus distinguishing a legal person entity from non-legal-person entities in practice.

With the enactment of China Company Law, in practice, most legal person business entities take the form of a company, either a limited liability company or a company limited by shares, as created under China Company Law. So basically, the condition of “assumes civil legal liability on its own” is equivalent to the doctrine of limited liability in corporate laws.

Then what legal implications does a legal person entity have?

As a legal person, its liabilities will be discharged against its own assets and capital and creditors will not be able to pursue liabilities against the shareholders of the legal person. If the legal person’s own assets are not adequate to repay its debts and liabilities, the legal person will be declared bankrupt, in which case creditors will have to enter a loss on its balance sheet.

This is an important point that shall be closely heeded by foreign businesses that deal with Chinese legal person entities, because many Chinese legal-person entitles are nearly just a shell. Pursuant to

China Company Law, a limited liability company (a legal person) can be set up with a minimum capitalization of RMB 30,000 or USD 500. This can give rise to great pitfall for foreign businesses that trade with Chinese companies who have a small registered capital (capitalization). In the past, I have been approached by quite a number of clients that wanted to sue their Chinese suppliers who defaulted under contract. But very often, such Chinese suppliers (traders in many cases) are newly formed with a small registered capital of RMB 100,000 only. So it will raise a big question mark as to enforcement of judgment even if the clients win the case in the end.

So when you trade with Chinese merchants, don't just get impressed with their beautiful websites. Check out who they are and if necessary, do some basic due diligence on the Chinese companies, and then decide on the transaction terms in your contracts.

Difference between Legal Person and Legal Representative

I realized that it is a nice point to make here to distinguish "legal person" from "legal representative". For what a legal representative is, please refer to another post on this blog here.

The confusion is caused because in the business world, business people who are not familiar with laws very often mistakenly call a legal representative "Fa Ren" (Chinese). In fact, the word "Fa Ren" is indeed the official translation of "legal person" in Chinese.

For a legal professional, a "Fa Ren" shall refer to a legal person only, not a legal representative. A legal representative is called "Fa Ding Dai Biao Ren" in Chinese, which is often abbreviated as "Fa Ren". However, as explained already in the posts, they are distinctly different in terms of their legal implications.

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