China Corporate & Securities March 12, 2014

PRC Company Law Amendment

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China recently adopted new amendments to the PRC Company Law. They took effect on March 1, 2014. The amendments eliminate the minimum capital requirements and ease statutory procedures for company establishment. How the amendments will be put into practice will be known when the implementing rules are published.

Minimum Registered Capital

The amendments will remove the minimum registered capital requirements, which are, under prior law, RMB 30,000 for most limited liability companies and RMB 5,000,000 for joint stock limited companies. Thus, investors may determine the registered capital of companies solely based on their business objectives and arrangements, except for companies subject to minimum registered capital requirements imposed by any other applicable law. For instance, a company in the value-added telecom service industry will have to comply with the minimum registered capital requirement of no less than RMB 1 million under the rules of the State Council.

The amendments will eliminate the requirement that no less than 30 percent of the registered capital of a limited liability company be cash. Investors may make 100 percent of their capital contribution in non-cash assets such as intellectual property or land use rights. However, it remains to be seen whether this is more than a theoretical possibility, as the implementing rules may include some minimum ratio of cash to non-cash contribution.

Record and Timing of Capital Contribution

Under the amendments, companies are no longer required to register the amount of paid-up capital with the Company Registry maintained by the local Administration of Industry and Commerce and need only record the amount in the company's shareholder registry.

Currently companies can only register payment of registered capital after an accounting firm has verified that payment has in fact been paid. With the elimination of the registration requirements, companies no longer have to have accountant's verification report.

Under the amendments, shareholders need not pay the first installment of their capital contribution, which is 20 percent of the registered capital, upon registration, as prior law required. Therefore, investors may not need to make immediate capital contributions at the time companies are established. Before the amendments, the Company Law required full payment of capital contributions within two years for a non-holding company (five years for a holding company) after the establishment of the company. This is no longer required.

Application to Foreign-Invested Enterprises (FIEs)

Foreign-invested enterprises (including equity joint ventures, cooperative joint ventures and wholly foreign owned enterprises) have also been subject to other statutory requirements for decades.

When the Company Law was first amended in 2008, the minimum registered capital requirement for domestic companies was reduced to RMB 30,000 (approximately US$5,000 at the current exchange rate), which, at least theoretically, should apply to FIEs. However, in practice, many local approving and registering authorities continued to insist on the pre-amendment standard of a minimum registered capital of US$120,000. This practice was allegedly supported by the discretion provided under the laws for FIEs, under which the registered capital of an FIE must be compatible with the FIE's business scope.

Although we believe that gradually, FIEs will be treated equally with domestic companies in many material aspects, whether these new amendments to the Company Law will apply to FIEs in the short run remains uncertain. Specifically, without any substantial revisions to existing regulations applicable to FIEs, local authorities still have great discretion to impose requirements that are more onerous than those applicable to domestic companies.

Impact of the New Amendments

The amendments, if fully implemented, will lessen substantially the regulatory burden for establishing a company in China and give investors flexibility to determine how much capital to contribute to a company and when and in what form to make the contribution. Many hope these amendments will apply to companies that were set up before March 1, 2014 and allow them to reduce their registered capital. Even then, companies established before the amendments came into effect may still have to go through the same, fairly onerous process for registered capital reduction.

Furthermore, in China, laws are subject to further implementing rules or interpretations issued by relevant authorities. As the amendments introduce fairly radical changes to existing practices, we cannot predict whether the agencies responsible for implementing the amendments will narrow the scope of the new amendments.

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the authors below.

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