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Chinese Company Law: an Overview

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1. *Chinese Law: Introductory Remarks*

1.1. *Relation Between Culture and Law in China*

Chinese legal system involves a significant relation between existing cultural roots inherent in the society and its institutional structures and activities.

Law in China reflects cultural values of the relevant community of people and it is largely affected by the complex of prevailing common practices in the society¹.

Chinese traditional culture, with its dominant political-philosophical dimension, appears to be resistant to the very notion of law, so that, historically, China seems not to have experienced a development of an

¹ Q. BU, *Will Chinese Legal Culture Constrain its Corporate Governance-related Laws?*, in L. MOCCIA, M. WOESLER, *China & Europe: Fostering the Mutual Understanding Between China and Europe by Multi-level Comparisons of their Cultures, Societies, and Economies*, Berlin, Bochum, Dülmen, London, Paris, 2014, pp. 212-213.

autonomous concept of “law” and legal tradition as happened elsewhere².

In the Chinese way of perceiving the law, it cannot be separated from traditional culture, which influences the structure and the functioning of the relevant law and its enforcement.

Law provisions should be compatible with fundamental cultural priorities of the Chinese community in order to be more effective.

Law seems to be a complex mixture of ethics, etiquette, religion and philosophy, while the concept of “source of law”, which is fundamental within the legal framework of any legal system, seems not to be very much considered³.

People are encouraged to comply with cultural values and, accordingly, with the law and the legal system, since cultural values are integrated in the provisions of the law, in the legal institutions, in the interpretation of legal texts and in the legal practices.

The notion of law seems therefore to have the instrumental role to guarantee order and social stability.

Legal and cultural dimensions are widely combined. Culture is considered to be as inherently normative, influencing the law-making process, the functioning of social institutions, the legal practices and the enforcement of the law.

Prevailing cultural values, on one side, may constrain actions and policies of decision-makers and may limit legal reform, while, on the other side, may affect the participants’ attitude toward the law and may determine the effectiveness of law provisions in the society.

1.2 *Influence of Confucius’ Principles in Chinese Law*

State and civil society in China are permeated by cultural values embedded in the Confucius’ philosophy and Confucius’ principles are deeply influential in shaping Chinese law, including Chinese corporate law⁴.

According to traditional Confucius’ philosophy, morality is separated from law.

In the Confucius’ texts, the concept of the normative order in the society

² L. MOCCIA, *The Idea of “Law” in China: An Overview*, in L. Golota, J. Hu, K. Van der Borght, S. Wang (eds.), *Perspectives on Chinese Business and Law*, Cambridge, Antwerp, Chicago, p. 60.

³ L. MOCCIA, *Prologo breve sulla «originalità» del diritto tradizionale cinese e sull’importanza del suo studio in prospettiva storico comparativa*, in *Riv. trim. dir. proc. civ.*, 2004, vol. 58, n. 3, pp. 991-1004.

⁴ BU, *Will Chinese Legal Culture Constrain its Corporate Governance-related Laws?*, cit., pp. 224-225.

is expressed by the term “*li*”, which means “rites”⁵, intending rules of proper conduct, secular as well as religious, aimed at assuring natural harmony in the relations among people.

Li may be considered as pre-legal moral normativity which expresses members’ endeavour to act according with the natural harmony of things.

Generally speaking, *li* refers to «a natural ordering of society integrated with a code of morality based on human nature which operates not by external compulsion but through individual conscience, in view of an idea of social harmony implying the individual’s obligation to act accordingly»⁶.

Li seems, therefore, to be relevant from a normative point of view, since it may be intended as a principle of “self-regulation” of society and individuals, according to the natural state of things in the frame of a fixed cosmic order.

The importance of *li* is expressed in term of moral standards and rules which are fundamental for the ideal social normative order.

Therefore, *li*, as the core of Chinese traditional culture, implies the seeking of what is right and good, the existence of individual and social obligations, the respect of hierarchical order of rank and rules, such as social disapproval in case of breach of the rules⁷.

In traditional Chinese culture, instead, the term “*fa*” is translated as law, written law in particular, in association with punishment.

From a general point of view, *fa* refers to a set of rules aimed at assuring good order of the social relationships and correct administration of the state.

According to traditional Confucian view, a well-ordered society requires the conformity of its members’ conduct to a proper self-regulating order, with the aim of achieving “harmony” as the highest of social normative order.

Confucian moral education was considered to be a strong incentive for citizens to cultivate civility and virtues⁸.

The modernization process of the Chinese legal tradition is initially marked by the fall of the Qing Empire in 1911, together with the establishment of the First Republic of China in 1912.

The need to modernize the country required to adapt and to reinterpret the Chinese traditional settings to the Western-style legal models.

After the birth of People’s Republic of China in 1948⁹, under the

⁵ MOCCIA, *The Idea of “Law” in China: An Overview*, cit., p. 60.

⁶ *Ibidem*, p. 61.

⁷ *Ibidem*, p. 61.

⁸ S. VEITCH, *Confucian Perfectionism: Political Philosophy for Modern Times*, in (2015) 45 3 Hong Kong Law Journal 1026.

⁹ F. MONTI, *Diritto societario cinese*, Roma, 2007, p. 21.

communist regime, China experienced a tension between national identity and Western legal models. The new regime appeared to aim at a sort of socialist modernization, with cultural principles and mental attitudes inherited from the past of Confucius' culture.

1.3 *Development Process of Chinese Law*

Traditional Chinese law and culture has been a significant influence in shaping new China's legal system¹⁰.

Following the Great Proletarian Cultural Revolution (1966 - 1976), China's leadership sought to re-establish a legal system.

Since that time the Chinese Communist Party leadership tried to implement governance according to the law, while reserved to itself the right not to set the terms of the law, but also to set the terms for the «*new "socialist spiritual civilisation" and its ethical content*»¹¹.

There was a "sort of vacuum" in the legal system after the Cultural Revolution¹².

The communiqué of the Third Plenary Session of the Eleventh Central Committee of the Chinese Communist Party held in December 1978 set the goals of the re-establishment of the legal system in China.

Indeed, 1978 was a significant year for China because in that year China began to carry out the economic reform and the "open door" policy¹³.

China therefore enjoyed high economic growth rates despite weak legal institution and the difficult implementation of the rule of law¹⁴.

The modernization process of the law and legal institutions of the People's Republic of China which started in 1979, following the ten-years period of the Great Proletarian Cultural Revolution, transformed Chinese

¹⁰ R. O'BRIEN, *The Survival of Traditional Chinese Law in the People's Republic of China*, in (2010) 40 1 Hong Kong Law Journal 173.

¹¹ *Ibidem*, p. 167.

¹² K. ZOU, *China's Legal Reform. Towards the Rule of Law*, Leiden, 2006, p. 73; M. PORTO, *Cina*, in R. Torino (ed.), *Sistemi giuridici. Diritto e geopolitica*, Milano, 2017.

¹³ The expression "Open Door Policy" was applicable before the founding of the People's Republic of China in 1949. After Deng Xiaoping took office in 1978, the term referred to China's policy of opening up to foreign business that wanted to invest in the country, setting into motion the economic transformation of modern China (K. ZOU, *China's Legal Reform. Towards the Rule of Law*, cit., p. 1).

¹⁴ R. PEERENBOOM, *Law and development in China and India*, in M. Sornarajah, J. Wang (eds.), *China, India and the International Economic Order*, 2010, p. 491.

law and legal institutions in many aspects¹⁵.

After the last quarter of twentieth century, legislation continued to be instrumental to the government system, confined to the residual notion of a sort of “rule of law” and aimed at assuring control and stability of Chinese society¹⁶.

From the early decades of the last century China experienced attempts to overcome traditional customs and rules. However, legislative new rules seemed to be still governed by the research of a harmonious society supported by political institutions and relevant values.

The traditional Confucian attitude towards law has been maintained and in Chinese culture is still present a code of informal rules ensuring social order, aimed at ensuring harmony in the social relationships¹⁷.

The negotiations for China’s entry to the World Trade Organisation (“WTO”) brought to the surface the necessity to modernize Chinese Law and its legal system¹⁸.

In the late 1980s, together with the advance of China’s economic, social and legal reforms at that time, China needed to rewrite some of the constitutional provisions in order to assure validity to the reform programmes implemented at that time.

A first round of amendments to the 1982 Constitution of the People’s Republic of China (the fourth China’s Constitution) came in 1988.

Constitution occupies an ultimate position in Chinese legal system, so that any constitutional changes should allow assessment of the consistency at central and local levels ensuring further legislative changes.

The fundamental law status of the Constitution is deemed to be firstly embodied in its rules on the most fundamental concerns of the country, including important principles and systems of national politics, economy, culture, society, diplomatic activities and so on¹⁹.

The constitutional economic system clauses have a fundamental role to govern the nature and direction of China’s development.

From 1988 to 2011, the 1982 Constitution was amended four times (in 1988, 1993, 1999 and 2004 respectively).

All four constitutional amendments have involved the economic system,

¹⁵ S. ZHU, *Modernizing Chinese Law: The Protection of Private Property in China*, in (2011) 28 *ProtoSociology*. China’s Modernization I 73.

¹⁶ MOCCIA, *The Idea of “Law” in China: An Overview*, cit., p. 61.

¹⁷ *Ibidem*, p. 92.

¹⁸ L. YUEH, *The Economy of China*, Cheltenham, 2010, pp. 152-153.

¹⁹ L. XIANG, *A New Review of the Economic System Clauses in the Chinese Constitution*, in J. Shi (ed.), *Renmin Chinese Law Review, Selected Papers of the Jurist*, vol. 6, Cheltenham, 2019, p. 81.

and half (a total 14 clauses) of 31 clauses of the Constitution Amendment belong to a modification of this part²⁰.

The constitutional amendments made in 1988 brought a fundamental change to the 1982 Constitution.

Article 11 was amended to recognize the private sector emerging in 1980s as a result of economic reform and also created the condition for a significant rise of private sector in the following year.

A new paragraph was added to the Constitution, which stated that China permitted the private sector of the economy to exist and develop within the limits prescribed by law, and the private economy was a complement to the socialist public economy.

The deepening of the economic reform since early 1990s to establish a market economy brought to amend Article 11 again. Two more amendments, passed in 1999 and 2004 respectively, modified the status of private sector, which changed from “a complement to the socialist public economy” to “major components of the socialist market economy” providing that China “encourages” and “supports” their development²¹.

Law and regulation in China have been modernize primarily to allow the development of the market economy, which has been considered «the most dynamic driving force which cannot be ignored»²².

In this context, the idea of the rule of law has been gradually accepted by the Chinese system.

The 1999 Amendment to the Chinese Constitution expressly endorsed the concept of the rule of law providing that «the People’s Republic of China implements law to govern the state and construct the socialist country with rule of law».

This provision has been considered as a milestone in China’s overall legal reform.

Since that date, the term “rule of law” has frequently been used in China’s political, economic and social life.

After China entered into the World Trade Organisation in 2001, it was obliged to meet the requirements of such organization rules and regulations, particularly those governing trade and other economic activities.

As a World Trade Organisation member, China had to bring its relevant laws and regulations into line with those of the World Trade Organisation and China promised therefore to revise and adopt laws and regulations to

²⁰ *Ibidem*, p. 80.

²¹ ZHU, *Modernizing Chinese Law: The Protection of Private Property in China*, cit., pp. 74 e 75.

²² ZOU, *China’s Legal Reform. Towards the Rule of Law*, cit., pp. 73-74.

deal with the new situation²³.

Therefore, after its accession to the World Trade Organisation, China expended considerable effort to review its existing legislation²⁴, including the opportunity to increase the transparency and the legal publications in China²⁵.

The 16th Congress Communist Party of China, held in 2002, set a new goal for the development of the Chinese legal system, in order to have a relatively solid and comprehensive legal system and the 10th National People's Congress, in session between 2003 and 2008, continued the process of modernization of Chinese legislation²⁶.

In 2005, China's President instructed to put "building a harmonious society" at the top of their agendas in order to create a society capable to consider people above all. This vision increased the adoption of social elements in Chinese company law, also promoting a higher level of social responsibility in the framework of the corporate law²⁷.

About two decades have passed and China has experienced unprecedented change in many areas.

The addition of new economic and commercial laws is a reflection of the continuing evolution of the legal system of the country.

2. Evolution of Chinese Company Law

2.1. Chinese Company Law Before 1993

China, historically, was governed by command economy, while its institutions did not recognize private property rights²⁸.

Before the issuance of the Law of the People's Republic of China on Company Law (the "Company Law"), in 1993, China did have only

²³ *Ibidem*, p. 74.

²⁴ O'BRIEN, *The Survival of Traditional Chinese Law in the People's Republic of China*, cit., p. 169.

²⁵ T. HSIA, *Chinese Legal Publications: An Appraisal*, in J.A. Cohen (ed.), *Contemporary Chinese Law: Research Problems and Perspectives*, Cambridge, Massachusetts, 1970.

²⁶ ZOU, *China's Legal Reform. Towards the Rule of Law*, cit., pp. 73-74.

²⁷ J. ZHAO, *The Harmonious Society, Corporate Social Responsibility and Legal Responses to Ethical Norms in Chinese Company Law*, in (2012) 12 1 *Journal of Corporate Law Studies* 163.

²⁸ V.I. LO, X. TIAN, *Law for foreign business and investment in China*, New York, 2009, p. 24.

specific laws and regulations with respect to companies, which governed only certain kinds of companies or certain aspects of a company.

Those laws were formulated to be implemented in a planned economy rather than in a market economy²⁹.

Company's capital of the state-owned companies and collectively owned companies were usually subscribed by a certain government department, and approved documents were issued by the competent government department. The business goal, registered capital, manager and staff were also verified by the competent authorities³⁰.

In the initial period of company regulation after 1949, the People's Republic of China adopted a planned economy.

Companies were subject to the state planning system and company managers were appointed by the relevant government departments.

The companies were the objects of state planning and were subordinate to governmental departments, so that legal representative and company managers did not have the power to decide the company's business and development schedule³¹.

From 1957, under the planned socialist economy, the private economic initiative was substantially not admitted³².

Between 1957 and 1978³³, after the achievement of socialist reform, there were basically two kind of business entities: state-owned enterprises and collectively owned enterprises³⁴.

Prior to 1978, China did not feel the need to have national legislation to govern the operation of private companies, since its planned socialist

²⁹ Z. QING, *The Company Law of China*, in (1996) 6 2 *Indiana International & Comparative Law Review* 462.

³⁰ With these approval documents, a company would then apply to its local industrial and commercial administration for issuance of a business certificate (QING, *The Company Law of China*, cit., p. 462).

³¹ QING, *The Company Law of China*, cit., p. 462.

³² M. BIANCA, "Looking through the Chinese Wall": *l'evoluzione del diritto societario cinese*, in *Giur. comm.*, 2013, n. 1, pp. 774-791.

³³ In 1962 China passed the Regulation of the State-Owned Industrial Enterprises Work, which encouraged enterprises to cooperate in order to supply materials by appointed units. Companies established were administrative companies implementing production and sales plans according to state specifications. In 1964 there was a big reform in industrial enterprise management, when the Central Committee of the Chinese Communist Party set up a trust. All the trusts were established in accordance with administrative orders and were state owned monopolies in an integrated industrial complex (QING, *The Company Law of China*, cit., pp. 462-463).

³⁴ LO, TIAN, *Law for foreign business and investment in China*, cit., p. 24.

economy was comprised almost exclusively of state-owned enterprises managed as governmental agencies, while, in late 1970s, these enterprises started to have financial difficulties.

Therefore, in 1978, China instituted a series of programs aimed at transforming China's socialist economy into a market economy and also at encouraging foreign equity investment into China. Initially, foreign investors were permitted to set up closely held, and closely monitored, "limited liability companies" by means of joint ventures with domestic entities and, afterwards, companies were allowed to be wholly owned by foreign investors³⁵.

The 3rd Session of the 11th Congress of the Chinese Communist Party in 1978 advanced the legal reform and the open-door policy and it marked China's transformation from a planned economy to a market economy.

After specific law reforms, in China individuals were first allowed to become individual industrial or commercial household, so that an entrepreneur could engage in certain types of business activities with the assistance of his or her household and, afterwards, individuals were allowed to engage a few employees and to carry out a larger number of allowed business activities³⁶.

In 1980, the State Council approved the Provisional Regulation on the Promotion of Crosswise Economic Co-Operation which promoted all forms of cooperative bodies based on an enterprise's willingness and without restrictions on operation or ownership. This regulation was the basis of recently developed jointly run companies³⁷.

Even after such reforms, companies remained unregulated, without guidance as to the establishment, registration, operation, merger, and dissolution of companies.

In 1980's, the domestic economy in China was overheating, also due to the incomplete company laws and regulations and the weak implementation of the laws. As a result, the government took five rounds of nationwide clearing and rectification of trust business in 1982, 1985, 1988, 1993 and 1998, respectively³⁸.

³⁵ HUO, *The Company Law of the People's Republic of China*, in (1995) 13 2 Pacific Basin Law Journal 375.

³⁶ LO, TIAN, *Law for foreign business and investment in China*, cit., p. 24.

³⁷ Companies were set up in great number thereafter. By the end of 1986, the registered companies numbered approximately 300,000- including the state-owned, collectively owned, private, jointly run, and foreign invested companies (QING, *The Company Law of China*, cit., p. 463).

³⁸ Z. MENG, *Ownership of Trust Property in China: A Comparative and Social Capital*

The State had difficulties controlling all companies and, due to the chaos in the economic order, in 1985 the State Council issued the Notification on Further Clearance and Rectification of Companies and the Provisional Regulation Regarding Company Registration Management (Provisional Regulation)³⁹.

The Provisional Regulation restricted the establishment of companies by individuals and emphasized the government's control over companies.

In 1988, with the progress of the market economy, the State Council promulgated the Provisional Regulation for Private Enterprises.

By means of the Regulations, private enterprises (being for-profit economic organizations having private ownership and employing eight or more workers) were formally recognised. Furthermore, villagers, urban unemployed, retired people and individual households were authorized to establish private enterprises in the form of a sole proprietorship, a partnership or a limited liability company⁴⁰.

Therefore, the regulation confirmed the legality of private enterprises and advanced the commonly acceptable concept of limited liability company (LLC) and three forms of private enterprises were allowed: the sole proprietorship, the partnership, and the limited liability company.

Article 5 provided that «LLC means the enterprise that the investor's liability to the company is limited to its investment while the company shall take the responsibility with its whole assets».

The Regulation was important in order to develop a socialist market economy and to try to be more compliant with international practices⁴¹.

The economic reform of 1990s brought to a remarkable development of company law in China⁴² and provided China with the reformation of state-owned enterprises, the expansion of foreign investment and the implementation of private enterprises in the national economy.

In 1992, detailed descriptions for the setting-up procedures for a limited liability company (LLC) and for a joint stock company (JSC) were introduced by the Standards for Limited Liability Companies Opinion and its companion, the Standards for Companies Limited by Shares Opinion⁴³.

By means of the amendment passed in 1993, Chinese Constitution adopt-

Perspective, Singapore, 2017, pp. 17-18.

³⁹ QING, *The Company Law of China*, cit., pp. 463-464.

⁴⁰ LO, TIAN, *Law for foreign business and investment in China*, cit., p. 24.

⁴¹ QING, *The Company Law of China*, cit., pp. 463-464.

⁴² QIU, LIN, *Chinese Company Law*, cit., p. 188.

⁴³ HUO, *The Company Law of the People's Republic of China*, cit., p. 375.

ed the “socialist market economy”, to orientate the economic development⁴⁴.

As the representatives of the National People’s Congress and other interested parties encouraged the formulation of the Company Law, the State Council formally proposed the limited liability company draft law to the Standing Committee of the National People’s Congress.

In accordance with the chairman of the Standing Committee of the National People’s Congress decision, the Law Work Committee of the Standing Committee placed limited liability company draft and joint-stock company regulations in the Company law by revising the Standard Opinions⁴⁵.

In December 1992, the Law Work Committee handed a draft of the Company Law to the Thirtieth Session of the Seventh National People’s Congress for examination.

In June 1993, after many revisions, the Company Law draft was handed to the Second Session of the Eighth National People’s Congress to review the text.

The Company Law was approved by the Fifth Session of the Standing Committee of the Eighth National People’s Congress.

The 1993 Company Law represents an important arrival point of the Chinese legislation produced in this stage of Chinese legal evolution.

2.2. *The 1993 Law of the People’s Republic of China on Company Law*

The People’s Republic of China did not have any formal national company law until the National People’s Congress promulgated the Law of the People’s Republic of China on Company Law in 1993 (the “Company Law”)⁴⁶.

The Company Law came into force on 1994 and, since then, it has been amended many times.

The 1993 Company Law was important because, for the first time, in mainland China the organization and activity of business entities were regulated.

The Company Law was therefore the foundation of modern socialist

⁴⁴ R. ULATOWSKI, *Evolution of the Chinese Economic Model and its International Implications*, in L. Golota, J. Hu, K. Van der Borgh, S. Wang (eds.), *Perspectives on Chinese Business and Law*, Cambridge, Antwerp, Chicago, 2018, p. 3.

⁴⁵ QING, *The Company Law of China*, cit., pp. 463-464.

⁴⁶ M. GU, *Understanding Chinese Company Law: A comparative introduction*, Hong Kong, 2006, p. 1.

enterprises and the market economic system⁴⁷.

The 1993 Company Law was divided into eleven chapters with 230 articles. The first chapter dealt with general principles, while the second chapter with the establishment of limited liability companies and their organizational structures. The third chapter dealt with the establishment of joint-stock companies and their organizational structure. The fourth chapter concerned the issuance and transfer of shares of joint-stock companies. The fifth chapter related to company debenture, while the sixth chapter dealt with company finance and accounting. The seventh chapter covered mergers and divisions, while the eighth chapter governed company's bankruptcy, dissolution and liquidation. The ninth chapter concerned branches and subsidiaries of foreign companies. The tenth chapter described legal liability, and the eleventh chapter was the appendix⁴⁸.

The main purpose of the 1993 Company Law was stated in Article 1: «The Company Law of the People's Republic of China (hereinafter referred to as the "Law") has been enacted in order to standardize the organization and activities of companies, protect the lawful rights and interests of companies, shareholders and creditors, safeguard the social and economic order and promote the development of the socialist market economy».

The modern concept of company has played a very important role in standardizing Chinese enterprises, especially the State-owned enterprises.

For decades, the concept of the company in China was not clear. It does not differ from the concept of general enterprise. The Provisional Regulation Regarding Company Registration Management of 1985 provided that the "company" in that regulation meant «the economic entity engaging in production, trade or service industry which is established pursuant to the formalities provided by this regulation and has its own assets and conducts business on its own decisions and undertakes its own losses and taking the economic liabilities in accordance with the laws»⁴⁹. Therefore, the definition of "company" in the Regulation of 1985 did not substantially differ from the definition of "general enterprise".

The 1993 Company Law provides that limited liability companies and joint-stock companies are legal enterprise entities⁵⁰.

⁴⁷ QING, *The Company Law of China*, cit., p. 461.

⁴⁸ *Ibidem*, p. 465.

⁴⁹ Provisional Regulation Regarding Company Registration Management, art. 2 (1985).

⁵⁰ The 1993 Company Law only governs LLC's and JSC's within Chinese territory. It does not govern other forms of companies within Chinese territory, so the Company Law does not give a common definition of all forms of companies. The General Principles of Civil Law requires that a legal entity should meet the following requirements: be established

The 1993 Company Law only governs limited liability companies and joint-stock companies within Chinese territory, while in China, before the enforcement of the Company Law, there were a great deal of companies.

Article 229 of the Company Law dealt with non-limited liability companies and non-joint-stock companies established before the enforcement of the Company Law. Pursuant to such provision, the companies established pursuant to laws, regulations, local laws, and the Standard Opinions on limited liability companies and joint-stock companies before the enforcement of this law, as well as those not in compliance with this law, had to meet the legal requirements within a stipulated time.

The Company Law has been amended multiple times⁵¹ since then and the most current version of the Company Law took effect in 2018.

2.3. Amendment to the 1993 Company Law

On October 27, 2005, an amendment to the Company Law was adopted and it became effective on January 1, 2006⁵².

The 2006 amendment modified the 1993 Company Law by providing

pursuant to laws; have its own assets or capital; have its own name, organizational structure and residence; and independently take civil liability (QING, *The Company Law of China*, cit., p. 465).

⁵¹ The Company Law of the People's Republic of China was adopted on December 29, 1993, by the Fifth Session of the Standing Committee of the Eighth National People's Congress and was effective from July 1, 1994. It was revised and re-promulgated on December 25, 1999 in accordance with the Decision of the 13th Session of the Standing Committee of the Ninth People's Congress on Amending the Company Law of the People's Republic of China by the Thirteenth Session of the Standing Committee of the Ninth National People's Congress. It was revised for the second time on August 28, 2004 in accordance with the Decision of the 11th Session of the Standing Committee of the 10th National People's Congress of the People's Republic of China on Amending the Company Law of the People's Republic of China. Revised at the 18th Session of the 10th National People's Congress of the People's Republic of China on October 27, 2005. Revised for the third time on December 28, 2013 in accordance with the Decision on Amending Seven Laws Including the Marine Environment Protection Law of the People's Republic of China at the 6th Session of the Standing Committee of the 12th National People's Congress. It has been promulgated and came into effect as of March 1, 2014. Amended for the fourth time in accordance with the Decision of the Standing Committee of the National People's Congress on Amending the Company Law of the People's Republic of China (2018) adopted at the Sixth Session of the Standing Committee of the 13th National People's Congress on October 26, 2018.

⁵² A translation of the Company Law, as amended in 2005, is available at http://www.leggicinesi.it/view_doc.asp?docID=23.

for the establishment requirements of a company. The amendment completed the institutions of the establishment and the capital of companies⁵³.

Such amendment modified the protective mechanism for shareholders, especially minority shareholders and improved the protection mechanism for shareholders⁵⁴.

By means of the 2006 amendment it has been improved the withdrawal mechanism for the shareholders of limited liability companies and the regulations of the litigation on behalf of shareholders⁵⁵.

The 2006 amendment revised also the liability mechanism of a company. Since such amendment tried to offer a less-strict requirement of establishing a company, the corresponding liability mechanism was very important⁵⁶.

The current version of Company Law was announced in 2013 and entered into force on March 1, 2014.

On December 28, 2013, the Standing Committee of the National People's Congress of the People's Republic of China released its "Decision on Amending the Marine Environmental Protection Law of the People's Republic of China and Other Six Laws", deciding to amend the Company Law⁵⁷.

The amendment to the Company Law, which took effect in 2014, provides with significant innovations in the company registration system, especially in registered capital aspects⁵⁸.

The 2013 amendment contains issues of interest to foreign investors, such as the abolition of the minimum registered capital, of the deadlines for its payment and of the cash contribution requirements⁵⁹.

⁵³ In detail, it lowered the minimum registered capital on a large scale. In the 1993 Company Law, the LLC required capital depending on the different operating ranges, which varied from 100,000 to 500,000 yuan. However, in the 2006 version, according to Article 26, it required 30,000 yuan without the registration of operating ranges.

⁵⁴ The 2006 amendment authorized the right of shareholders to examine the accounting book of the relevant companies.

⁵⁵ QIU, LIN, *Chinese Company Law*, cit., p. 186.

⁵⁶ To that aim, in order to prevent abuse of the company system, the 2006 amendment provides the system of "pierce the corporate veil" (the principle which refers to a situation in which Courts put aside limited liability and hold a corporation's shareholders or directors personally liable for the corporation's actions or debts).

⁵⁷ A translation of the Company Law, as amended in 2013, is available at http://www.leggicinesi.it/view_doc.asp?docID=763.

⁵⁸ Many of the implemented reforms were inspired by the Shanghai Free Trade Zone, a free-trade zone in Shanghai approved by the State Council on August 22, 2013.

⁵⁹ An important amendment concerns the abolition of the minimum registered capital; the previous legislation required a minimum registered capital of RMB 30,000 for

Officially, the purpose of this reform was to make the corporate legislation more efficient, with the aim of simplifying and liberalizing investments in China⁶⁰.

On April 22, 2019 the Supreme People's Court published Provisions on Several Issues Relating to the Application of the Company Law of the People's Republic of China (V).

The Provisions are related to disputes of shareholders' rights and they seem to be in line with the government's efforts to strengthen China's business environment⁶¹.

The Provisions are composed by 6 articles⁶² and were issued in order

a limited liability company, RMB 100,000 for a sole-shareholder limited liability company and RMB 5,000,000 for a joint stock company. The amendment cancels those requirements, even though the whole investment must be adequate according to the activities done and the amount of capital stock must be expressly stated in the Articles of Association. Certain limits expected in specific fields, still remain valid. The 2013 amendment also provides with the abolition of the deadline for the payment of the registered capital. According to the previous legislation, the members were required to pay their contributions within two years from the date of issuance of the business licence, under penalty of suspension of their commercial activities if they did not comply. According to the new company law, the members may now determine when to make the payment of the due contributions. It has been also provided for the cancellation of the requirement of minimum cash contributions by company members. The Company Law originally provided that at least 30% of the registered capital had to be cash. The cancellation of that limit allows considerable decision-making autonomy to company members who may determinate to what extent the company capital should be cash and to what extent it should consist of other assets.

⁶⁰ On February 7, 2014, the Registered Capital Registration System Reform Plan was approved with the goal to make easier the entry of domestic and foreign companies in the Chinese market. The annual inspections, performed by the Chinese authorities before the reform to check the company documents, have now been replaced by annual reports prepared by the same companies, which will be available not only to competent authorities, but also to the public, in order to allow transparency and full disclosure of company information.

⁶¹ In 2017, Provisions of the Supreme People's Court on Several Issues Relating to Application of the Company Law of the People's Republic of China (IV) enhance such protection on shareholders' information rights, profit distribution right, equity transfer right and provides a more detailed process for shareholders' derivative actions. In 2018, China Securities Regulatory Commission revised Guidelines on Governance of Listed Companies, which specifically emphasize that the legitimate rights and interests of minority shareholders should be protected.

⁶² The original text of the Provisions of the Supreme People's Court on Several Issues Relating to Application of the Company Law of the People's Republic of China (IV) provides (according to the following unofficial translation) that:

«Article 1. For an affiliated transaction harming the interests of a company, if the

to ensure a correct interpretation and application of the Company Law, as promulgated in 2006 and amended in 2018.

plaintiff company claims that the controlling shareholder, the actual controller, directors, supervisors or senior executives shall compensate for the losses caused thereby in accordance with the provisions of Article 21 of the Company Law, but the defendant defends only on the grounds that it has performed the procedures as prescribed by laws, administrative regulations or the articles of association of the company, including information disclosure, the consent of the board of shareholders or of the general meeting of shareholders, etc. for the transaction, the people's court shall not uphold such defence. If the company does not file a lawsuit, any shareholder meeting the requirements specified in Paragraph 1 of Article 151 of the Company Law may initiate legal proceedings with the people's court in accordance with the provisions of Paragraphs 2 or 3 of Article 151 of the Company Law. Article 2. Where an affiliated transaction contract falls under any of the circumstances of invalidation or revocability, and the company does not take legal actions against the contract counterparty, any shareholder meeting the requirements specified in Paragraph 1 of Article 151 of the Company Law may lodge a lawsuit with the people's court in accordance with the provisions of Paragraphs 2 or 3 of Article 151 of the Company Law. Article 3. Where a director who is dismissed by a valid resolution of the board of shareholders or the general meeting of shareholders before expiry of his/her term of office claims that the dismissal is not legally effective, the people's Court shall not uphold such claim. If, after being dismissed, a director files a lawsuit due to a dispute over indemnity with the company, the people's court shall, according to laws, administrative regulations, the articles of association of the company or the contract, determine whether the company shall give indemnity and the reasonable amount of indemnity by taking into account the factors such as the reasons for dismissal, the rest of his/her term of office and his/her remuneration. Article 4. After a resolution on distribution of profits is made by the board of shareholders or the general meeting of shareholders, the company shall complete the profit distribution within the period specified in the resolution. If no period is specified in the resolution, the provisions of the articles of association shall apply. If no period is specified in either the resolution or the articles of association or the period specified therein exceeds one year, the company shall, within one year from the date when the resolution is made, complete the profit distribution. If the period for completion of profit distribution as specified in the resolution exceeds that specified in the articles of association, the shareholders may apply to the people's court for revoking the provisions on such period in the resolution according to the provisions of Paragraph 2 of Article 22 of the Company Law. Article 5. In hearing a case involving major disputes between shareholders of a limited liability company, the people's Court shall give importance to mediation. If the parties agree to settle their disputes in any of the following ways not violating the mandatory provisions of laws or administrative regulations, the people's court shall uphold such agreement. (1) buy-back of the shares of some shareholders by the company; (2) transfer of the shares of some shareholders to other shareholders; (3) transfer of the shares of some shareholders to others; (4) reduction in capital of the company; (5) division of the company; (6) any other way that can resolve the disputes, resume the normal operation of the company and avoid dissolution of the company.[...]. Article 6. The present Provisions shall come into effect on April 29, 2019». The aforementioned translation is unofficial and available at <https://www.gwa-asia.com/whats-new/china-supreme-peoples-court-new-provisions-of-the-company-law>.

The issued Provisions introduced some alternative ways to resolve disputes between limited liability companies' shareholders, under certain circumstances as set out by the Court. The Provisions also regulate in a more detailed manner certain distributions of profits' resolutions and related Court's revocation of such resolutions.

The above Provisions have been effective starting from April 29, 2019.

3. *Types of Companies in China*

3.1. *General Remarks*

During the 1950s there were five forms of companies in China. During the drafting of the Company Law, it has been suggested to add the provision of unlimited companies and joint liability companies to the two popular company forms, *i.e.* limited liability companies and joint stock companies.

Legally, the Company Law only deals with two types of company.

However, it would not be correct to say that other types of company (created later on by other rules and regulations) would have nothing to do with Chinese company regulation⁶³.

Apparently, the Company Law has not been amended to adopt other company forms.

So far, there is no sign that the Company Law would be used to govern the joint stock cooperative companies because they are currently governed by various national and local regulations⁶⁴.

A limited liability company is usually recognized as a "private" or "closed" company, while a joint stock company is recognized as a "public company".

Moreover, an important distinction is between "public company" and "listed company".

In a listed company⁶⁵ the shares are traded over the stock exchanges,

⁶³ G. MINKANG, *Understanding Chinese Company Law: A Comparative Introduction*, Hong Kong, 2010, pp. 26-28.

⁶⁴ For example, joint stock cooperative companies have been officially endorsed in China since the Fifteenth Party Congress (MINKANG, *Understanding Chinese Company Law: A Comparative Introduction*, *cit.*, pp. 26-28).

⁶⁵ A listed company is a joint stock company whose shares will be traded over stock exchanges (Art. 121). Therefore, a listed company needs to satisfy not only requirements for a joint stock company, but also additional requirements as follows: (i) the shares have

while in a public company the shares are issued to the public but are not necessarily traded over the stock exchanges. Therefore, every listed company is a public company but not *vice versa*⁶⁶.

3.2. Legal Person Status: Distinctive Aspects

According to Article 36 of General Principles of the Civil Law of the People's Republic of China⁶⁷ (the "Chinese Civil Law"), a legal person shall be an organization with capacity for civil rights and capacity for civil conduct. A legal person independently enjoys civil rights and assumes civil obligations in accordance with the law.

Therefore, on the basis of the intent of the organization, the main difference is between profit organization and non-profit organization.

Profit organizations are regulated as an enterprise legal person or a corporate juridical person starting business activities.

The enterprise legal persons are regulated as commercial organizations and, according to Article 41 of the Chinese Civil Law, they may include wholly state-owned enterprise, collectively-owned enterprise, privately-held enterprise, economic associations, Chinese-foreign equity joint venture, Chinese-foreign contractual joint venture and foreign-capital enterprise⁶⁸.

already been issued to the public with the approval of the China's Securities Regulatory Commission, (ii) the total amount of the company's share capital shall not be less than Y30,000,000; (iii) the amount of shares issued to the public shall be more than 25 per cent of the total amount of the company's shares; and (iv) the company has not committed any significant illegal acts and there are no false records in the financial accounting statements for the previous three years (MINKANG, *Understanding Chinese Company Law: A Comparative Introduction*, cit., p. 27).

⁶⁶ *Ibidem*, p. 27.

⁶⁷ Adopted at the Fourth Session of the Sixth National People's Congress on April 12, 1986 and promulgated by Order No. 37 of the President of the People's Republic of China on April 12, 1986.

⁶⁸ Pursuant to Article 41 of Chinese Civil Law: «an enterprise collectively-owned or wholly-state owned shall be qualified as a legal person when it has sufficient funds as stipulated by the state; has articles of association, an organization and premises; has the ability to independently bear civil liability; and has been approved and registered by the competent authority. A Chinese-foreign equity joint venture, Chinese-foreign contractual joint venture or foreign-capital enterprise established within the People's Republic of China shall be qualified as a legal person in China if it has the qualifications of a legal person and has been approved and registered by the administrative agency for industry and commerce in according with the law» (unofficial translation available at <http://www.asianlii.org/cn/legis/cen/laws/gpotclotproc555/>).

The privately-held enterprise is the typical commercial form commonly organized as limited liability company.

The limited liability Company and the joint stock company have legal capacity. According to Article 3 of the Company Law, «a company is an enterprise legal person, which has independent corporate property and enjoys corporate property rights. A company shall be liable for its debts to the extent of all of its property».

Connected with the legal personality, the privately-held enterprise presents also the peculiarity of the independent property, the restrictive shareholder withdrawals and the legal representative system⁶⁹.

With reference to non-corporate enterprises, according to Article 50⁷⁰ of the Chinese Civil Law, “legal person of government units” refers to the different levels and various state bodies that can be qualified with legal person status and obtain funds from the national or local government finance, commonly seen as government agencies at all levels, and the People’s Courts.

The “institution legal person” refers to a social welfare organization established by law and qualified with a legal person status, operating in the culture, education, sports, science and technology sectors.

A “mass organization” is instead considered a legal person referring to the social organizations established by the masses in a voluntary way, in accordance with legal procedures and undertakes the non-productive or non-profit activities (such as trade unions, federations and research groups)⁷¹.

A different type of organization is an “incorporate organization” qualified as a commercial form not having a legal person status.

The “incorporated organizations” may be divided in two types: on one side, the individually-owned business, regulated by Articles 26-29 of the Chinese Civil Law⁷² and, on the other side, the relative administrative

⁶⁹ QIU, LIN, *Chinese Company Law*, cit., pp. 193-194.

⁷⁰ According to Article 40 of Chinese Civil Law principles: «An independently funded official organ shall be qualified as a legal person on the day it is established. If according to law an institution or social organization having the qualifications of a legal person needs not go through the procedures for registering as a legal person, it shall be qualified as a legal person on the day it is established; if according to law it does need to go through the registration procedures, it shall be qualified as a legal person after being approved and registered» (unofficial translation available at <http://www.asianlii.org/cn/legis/cen/laws/gpotclotproc555/>).

⁷¹ QIU, LIN, *Chinese Company Law*, cit., p. 194.

⁷² Articles 26-29 of the Chinese Civil Law, under Section 4 (Individual Businesses and Leaseholding Farm Households), provided that: «Article 26 “Individual businesses” refers to businesses run by individual citizens who have been lawfully registered and

regulations and individual partnership enterprises, regulated by Articles 30-35 of the Chinese Civil Law⁷³ and in the Partnership Enterprise Law of the People's Republic of China⁷⁴ (the "Partnership Law").

These commercial forms are used to operate business under a small capital basis, as individual operation, qualified as commercial entity where the means of production is owned by individuals, based on the individuals' personal activity and the proceeds of this activity is owned by individuals.

The limited partner enjoys a limited liability for partnership debts based on his subscribed capital contribution, but the difference with a limited liability shareholder system is that a limited partner does not carry out

approved to engage in industrial or commercial operation within the sphere permitted by law. An individual business may adopt a shop name. Article 27 "Leaseholding farm households" refers to members of a rural collective economic organization who engage in commodity production under a contract and within the spheres permitted by law. Article 28 The legitimate rights and interests of individual businesses and leaseholding farm households shall be protected by law. Article 29 The debts of an individual business or a leaseholding farm household shall be secured with the individual's property if the business is operated by an individual and with the family's property if the business is operated by a family» (unofficial translation available at http://www.china.org.cn/china/LegislationsForm2001-2010/2011-02/11/content_21898337.htm).

⁷³ Articles 30-35 of the Chinese Civil Law, under Section 5 (Individual Partnership) provide that: «Article 30 "Individual partnership" refers to two or more citizens associated in a business and working together, with each providing funds, material objects, techniques and so on according to an agreement. Article 31 Partners shall make a written agreement covering the funds each is to provide, the distribution of profits, the responsibility for debts, the entering into and withdrawal from partnership, the ending of partnership and other such matters. Article 32 The property provided by the partners shall be under their unified management and use. The property accumulated in a partnership operation shall belong to all the partners. Article 33 An individual partnership may adopt a shop name; it shall be approved and registered in accordance with law and conduct business operations within the range as approved and registered. Article 34 The operational activities of an individual partnership shall be decided jointly by the partners, who each shall have the right to carry out and supervise those activities. The partners may elect a responsible person. All partners shall bear civil liability for the operational activities of the responsible person and other personnel. Article 35 A partnership's debts shall be secured with the partners' property in proportion to their respective contributions to the investment or according to the agreement made. Partners shall undertake joint liability for their partnership's debts, except as otherwise stipulated by law. Any partner who overpays his share of the partnership's debts shall have the right to claim compensation from the other partners» (unofficial translation available at http://www.china.org.cn/china/LegislationsForm2001-2010/2011-02/11/content_21898337.htm).

⁷⁴ Adopted at the 24th session of the Standing Committee of the 8th National People's Congress on February 23, 1997; amended at the 23rd session of the Standing Committee of the 10th National People's Congress of the People's Republic of China on August 27, 2006.

partnership affairs and cannot represent the limited partnership⁷⁵.

A limited liability company and the joint stock company have legal capacity.

According to Article 3 of the Company Law, «a company is an enterprise legal person, which has independent corporate property and enjoys corporate property rights. A company shall be liable for its debts to the extent of all of its property».

3.3. *Limited Liability Company*

3.3.1. *Establishment and Registration*

The limited liability company has legal capacity, which is linked with three main functions: independent property, independent authority and independent limited liability.

In line with the 2005 Company Law, a limited liability company refers to a company whose shareholders assume an amount equivalent to the amount of contributed capital to offset its total assets against the responsibility assumed for company debt⁷⁶.

In 2013 the Company Law has been revised in order to simplify the set-up requirements and reduce the cost of establishment.

According to Article 23 of the Company Law, to establish a limited liability company it is necessary to fulfill the following conditions: (i) the number of shareholders has to be conform to the statutory number; (ii) the capital contribution subscribed by all shareholders has to be consistent with that prescribed in the articles of association; (iii) the shareholders must have jointly formulated the company's articles of association; (iv) the company must have a name and an organizational structure established in conformity with the requirements for limited liability companies; and (v) the company must have a domicile.

Compared to the previous provision of Article 23 of the Company Law, the amendment deselected the limitation of the minimum registered capital system, which means that “one yuan to establishing a company” could be feasible⁷⁷.

With reference to the number of shareholders, according to Article 24 of the Company Law, a limited liability company shall be invested in and

⁷⁵ QIU, LIN, *Chinese Company Law*, cit., p. 194.

⁷⁶ MONTI, *Diritto societario cinese*, cit., pp. 138-145.

⁷⁷ QIU, LIN, *Chinese Company Law*, cit., p. 196.

established by no more than 50 shareholders⁷⁸.

With reference to registered capital of the limited liability company, it shall be the capital contributions subscribed by all shareholders as registered with the company registration authority⁷⁹.

Where laws, administrative regulations and the decisions of the State Council stipulate the actual paid registered capital and another amount on the minimum registered capital of a limited liability company, such stipulations shall prevail.

According to the amendment to Article 23 of the Company Law, also the paid-in capital system of a limited liability company is modified in a subscription capital system.

Pursuant to Article 7, the company business license no longer records the paid-in capital. However, under Article 26 of the Company Law there are still some types of companies complying with the paid-up registered capital system and the minimum registered capital system. Secondly, as per Article 27 of the Company Law, the provision stating that “the monetary contribution shall occupy 30% of the registered capital” is deleted, so that a company could contribute entirely, for instance, in technology investment⁸⁰.

Current Article 27 of the Company Law, in particular, provides that shareholders may bring capital contribution in currency or in non-currency property that may be valued in currency and transferable according to the law such as physical objects, intellectual property and land use rights, except for property that may not be used as capital contribution according to the laws or administrative regulations. To this aim, non-currency property contribution, such as capital, shall be valued and verified, and shall not be over-valued or under-valued. Where laws or administrative regulations have provisions on valuation, such provisions shall prevail.

Capital contribution may be made by each shareholder, subscribing as specified in the articles of association of the company on time and in full.⁸¹

⁷⁸ To incorporate a limited liability company, the articles of association have to specify the following particulars: (i) the name and domicile of the company; (ii) the business scope of the company; (iii) the registered capital of the company; (iv) the names and domiciles of the shareholders; (v) the method, amount and time of capital contribution by the shareholders; (vi) the organization of the company and its methods of establishment, functions and powers, and rules of procedure; (vii) the legal representative of the company; and (viii) other matters that the shareholders deem necessary to be specified. Shareholders shall sign and affix their seals on the company’s articles of association.

⁷⁹ Article 26 of the Company Law.

⁸⁰ QIU, LIN, *Chinese Company Law*, cit., p. 196.

⁸¹ According to Article 28 of the Company Law, if a shareholder fails to make the due capital contribution, it shall, in addition to making capital contribution in full to the

If a shareholder makes its capital contribution in currency, it shall deposit the full amount of capital contribution in currency in a bank account opened by the limited liability company⁸². If capital contribution is made in non-currency property, the transfer procedures for the property rights therein shall be handled according to the law⁸³.

Company's property is formed by the contributions from shareholders.

Shareholder shall receive dividends in proportion to its paid-up capital contribution. When the company increases its capital, the shareholder shall have the priority right to subscribe for capital contribution in proportion to its paid-up capital contribution, except where all shareholders agree not to receive dividends in proportion to the paid-up capital contribution or not to exercise priority right to subscribe for capital contribution in proportion to the paid-up capital contribution.

Once the contributions are made, the shareholders cannot withdraw their shares of their company assets randomly since this would lead to a partial liquidation of the company. However, shareholders can withdraw from the company by underselling their shares as transferable assets⁸⁴. According to Article 35 of the Company Law, in fact, after a company is established, its shareholders may not withdraw their capital contribution.

3.3.2. *Organizational Structure*

The management authority of a limited liability company is carried out by a majority of partners, while more fundamental decisions, like capital increase resolutions, require unanimity, which is not easy to achieve with numerous changing owners. The Company Law thus provides a committee

company, be liable for breach of contract to the shareholders that have made their capital contributions on time and in full.

⁸² Article 30 of the Company Law provides that: «If, after establishment of a limited liability company, the actual value of the non-currency property contributed as capital for the establishment of the company is found markedly lower than the value as set forth in the articles of association of the company, the shareholder making such contribution shall make up for the difference. The other shareholders as at the time of the company's establishment shall bear joint and several liability for such difference» (unofficial translation available at http://www.fdi.gov.cn/1800000121_39_4814_0_7.html#_Toc381707437).

⁸³ According to Article 29: «After the shareholders subscribed the capital contribution in full as prescribed in the articles of association, a representative designated by all shareholders or an agent jointly appointed by them shall submit a company registration application and documents such as the company's articles of association to the company registration authority to apply for registration of establishment» (unofficial translation available at http://www.fdi.gov.cn/1800000121_39_4814_0_7.html#_Toc381707437).

⁸⁴ QIU, LIN, *Chinese Company Law*, cit., p. 196.

organ having authority with respect to company affairs.

Company governance structure is formed by three organs: the board is a decision-making organ, the board of directors is an executive organ which is responsible for the board, to direct and manage the company's affairs, and the senior managers, appointed or dismissed by the board and responsible for the company's daily management and administrative affairs. It is also provided a separate supervisory board to oversee the directors, managers and other personnel.

The organs can be adapted by the articles of associations⁸⁵.

A limited liability company shall have a board of directors of three to thirteen members⁸⁶, unless otherwise stipulated according to Article 51 of the Company Law, which provides that a limited liability company shall have a board of supervisors, which shall have no fewer than three members.

A limited liability company with comparatively few shareholders and comparatively small in scale may have one to two supervisors instead of a board of supervisors⁸⁷.

A limited liability company may have a manager, who shall be employed or dismissed by the board of directors. The manager shall be accountable to the board of directors and shall exercise many functions and powers⁸⁸.

⁸⁵ *Ibidem*, p. 196.

⁸⁶ For a description of the functioning of the organizational structure in Chinese companies, under 2005 Company Law: M. STELLA RICHTER, *L'organizzazione della funzione amministrativa nelle società di capitali di diritto cinese*, in *Riv. società*, 2008, n. 4, pp. 709-723.

⁸⁷ According to Article 51 of the Company Law «The board of supervisors shall include the representatives of the shareholders and an appropriate ratio of representatives of the company's staff and workers, in which the ratio of the staff and workers' representatives shall not be lower than one third. The specific ratio shall be specified in the articles of association of the company. The staff and workers' representatives on the board of supervisors shall be democratically elected through the staff and workers' congress, the staff and workers' general meeting or other means. The board of supervisors shall have a chairman that shall be elected by more than half of all supervisors. The chairman of the board of supervisors shall convene and preside over the meeting of the board of supervisors. If the chairman of the board of supervisors is unable to or does not perform his duty, the meeting of the board of supervisors shall be convened and presided over by a supervisor jointly designated by more than half of the supervisors. Directors and senior officers may not concurrently serve as supervisors» (unofficial translation available at http://www.fdi.gov.cn/1800000121_39_4814_0_7.html#_Toc381707437).

⁸⁸ According to Article 49 of the Company Law, the manager shall be accountable to the board of directors and shall exercise the following functions and powers: «(i) to be in charge of the production, operation and management of the company, and to organize the implementation of the resolutions of the board of directors; (ii) to organize the implementation of the annual business plans and investment plans of the company; (iii) to draft the plan for the establishment of the company's internal management organization;

The board of shareholders of a limited liability company shall be composed of all the shareholders. The board of shareholders shall be the organ of authority of the company and shall exercise its functions and powers⁸⁹, pursuant to the Company Law⁹⁰.

A shareholder of a limited liability company shall be liable for the company to the extent of the capital contribution it subscribes.

A wholly state-owned company doesn't have a shareholders' meeting and members of the board of directors are appointed by the State-owned assets supervision and administrative institution.

3.3.3. *Dissolution and Liquidation*

The Company Law provides for a liquidation procedure for limited liability companies, which is different from the bankruptcy liquidation.

The liquidation is carried out for the reasons of dissolution described in the company's articles of association, or in the event that the decision to

(iv) to draft the basic management system of the company; (v) to formulate the specific rules and regulations of the company; (vi) to request the employment or dismissal of the deputy manager(s) and person(s) in charge of financial affairs of the company; (vii) to decide on the employment or dismissal of management personnel other than those to be employed or dismissed by the board of directors; and (viii) other functions and powers delegated by the board of directors. Where the articles of association of the company otherwise provide for the functions and powers of the manager, such provisions shall prevail. The manager shall attend meetings of the board of directors as a non-voting attendee» (unofficial translation available at http://www.fdi.gov.cn/1800000121_39_4814_0_7.html#_Toc381707437).

⁸⁹ According to Article 37 of the Company Law: «The board of shareholders shall exercise the following functions and powers: (i) to decide on the business policies and investment plans of the company; (ii) to elect and replace directors and supervisors that are not appointed from representatives of staff and workers, and to decide on matters concerning the remuneration of directors and supervisors; (iii) to consider and approve reports of the board of directors; (iv) to consider and approve reports of the board of supervisors or supervisors; (v) to consider and approve the company's proposed annual financial budgets and final accounts; (vi) to consider and approve the company's profit distribution plans and plans for making up losses; (vii) to pass resolutions on the increase or reduction of the company's registered capital; (viii) to pass resolutions on the issuance of corporate bonds; (ix) to pass resolutions on matters such as the merger, division, dissolution, liquidation or change of the corporate form of the company; (x) to amend the articles of association of the company; and (xi) other functions and powers specified in the articles of association of the company. If the shareholders unanimously express consent to the matters set out in the preceding paragraph in writing, the decision may be made, without convening of the board of shareholders, directly with a document of the decision bearing the signatures and seals of all shareholders» (unofficial translation available at http://www.fdi.gov.cn/1800000121_39_4814_0_7.html#_Toc381707437).

⁹⁰ Article 36 of the Company Law.

dissolve the company is taken by the board of shareholders or the general meeting, or in case of merger or division of the company, or if its business license has been revoked, or in the event of a compulsory dissolution, such in the case it is ordered to close down or to be revoked according to the law or it is ordered to be dissolved by a People's Court decision.

The liquidation group shall be committed to sell out the company's credits and debts. Where a liquidation group has not been formed to carry out liquidation within the specified time limit, the creditors may apply to the People's Court for the designation of relevant personnel to form a liquidation group and carry out liquidation. The People's Court shall accept the application, and shall, in a timely manner, organize a liquidation group to carry out liquidation⁹¹.

The liquidation group shall formulate a liquidation plan and submit the same to the board of shareholders, general meeting or the People's Court for confirmation.

In accordance with the subscribed capital system, capital contributions not yet paid up shall be classified as liquidation property. According to Article 186 of Company Law, the property of the limited liability company remained after the property is respectively applied to payment of the liquidation expenses, the wages, social insurance premiums and statutory compensation of staff and workers and the outstanding taxes, and to full payment of the debts of the company, shall be distributed in proportion to the capital contributions of its shareholders.

During liquidation, a company shall continue to exist, but it may not engage in new business activities unrelated to liquidation.

In case the liquidation group discovers that the company's property is insufficient to pay its debts in full, it shall apply to the People's Court for declaration of insolvency, according to the law, and, after the insolvency declaration of the People's Court, the company's liquidation group shall turn over the liquidation matters to the People's Court.

Where a company is declared bankrupt according to the law, it shall be subject to insolvency liquidation according to the laws on enterprise insolvency⁹².

⁹¹ Article 183 of the Company Law.

⁹² With reference to the bankruptcy procedure, see: L. SHUGUANG, *Bankruptcy Law in China: Lessons of the Past Twelve Years*, in *Harvard Asia Quarterly*, 2001, http://www.leggicinesi.it/dottrina/LiShuguang_Bankruptcy.pdf; M. RICCI, *La disciplina del fallimento nel diritto cinese*, in *dircomm.it*, 2012, <http://www.dircomm.it/2012/n.2/02.html>; D.A. PALMER, J.J. RAPISARDI, *The PRC Enterprise Bankruptcy Law: The People's Work in Progress*, Washington, D.C., 2009.

3.4. Joint Stock Company

3.4.1. Establishment and Registration

A joint stock company refers to a company whose total capital is divided equally amongst shares of equivalent value to offset its total assets against the responsibility assumed for company debt.

The establishment of a joint stock company can be carried out in two different ways: promotion and stock floatation⁹³.

According to Article 77 of the Company Law, the promotion mode refers to establishment of a company by means of subscription by the promoters for all the shares to be issued by the company, while the floatation mode refers to establishment of a company by means of subscription by the promoters for a portion of the shares to be issued by the company, and offer of the balance to the public or to specified targets. The founders apply different provisions to the different modes, such as the percentage of the stocks that the founders subscribed, which shall not be lower than 35%⁹⁴.

A joint stock company established by the capital floatation mode conducts financing directly to the public⁹⁵. It is therefore reserved a capital paid-in register under this circumstance and the promoters are not allowed to introduce more stockholders before the founders pay up for the stocks they subscribed⁹⁶.

When promoters offer shares to the public, the shares shall be

⁹³ MONTI, *Diritto societario cinese*, cit., pp. 146-151.

⁹⁴ According to Article 76 of the Company Law, the following conditions shall be fulfilled for the establishment of a company limited by shares: «(i) the number of promoters conforms to the quorum requirement; (ii) the total amount of share capital subscribed for or the total paid-up share capital raised by all the sponsors specified in the articles of association of the company; (iii) the share issue and preparation matters conform to laws and regulations; (iv) the company's articles of association have been formulated by the promoters; in the case of establishment by means of share offer, the articles of association shall have been adopted at the inaugural meeting; (v) the company has a name, and an organizational structure established in accordance with the requirements for companies limited by shares; and (vi) the company has a domicile» (unofficial translation available at http://www.fdi.gov.cn/1800000121_39_4814_0_7.html#_Toc381707437).

⁹⁵ QIU, LIN, *Chinese Company Law*, cit., p. 205.

⁹⁶ According to Article 91 of the Company Law: «After promoters and subscribers pay their subscription monies or make their capital contributions as substitutes for subscription monies, they may not withdraw their share capital, except where the shares are not fully taken up on time, the promoters fail to convene the inaugural meeting on time or a resolution not to establish the company is adopted at the inaugural meeting» (unofficial translation available at http://www.fdi.gov.cn/1800000121_39_4814_0_7.html#_Toc381707437).

distributed by a securities company established according to the law, with which a distribution agreement shall be concluded.

3.4.2. *Organizational Structure*

In the joint stock company is required to set up the following organs: the shareholders' meeting, the board of directors, the senior managers and the board of supervisors.

The same provision concerning the power of shareholders' assembly of a limited liability company is applied to the shareholders' assembly of a joint stock company.

According to Article 108 of the Company Law, a joint stock company shall have a board of directors of five to nineteen members. The members of the board of directors may include representatives of the staff and workers of the company.

A company limited by shares shall have a manager, who shall be engaged or dismissed by the board of directors. The board of directors of a company may decide that a member of the board of directors shall serve concurrently as the manager.

A joint stock company shall have a board of supervisors of no fewer than three members. The board of supervisors shall include representatives of the shareholders and an appropriate ratio of the representatives of the company's staff and workers, where the ratio of the staff and workers' representatives shall not be less than one third. The specific ratio shall be specified in the articles of association of the company.

A shareholder of a joint stock company shall be liable for the company to the extent of the subscribed shares.

According to Article 122 of the Company Law, a listed company shall have independent directors, which should be independent as regards personality, economic interest, generation procedure, exercising authority and professionalism.

3.4.3. *Dissolution and liquidation*

The liquidation process described with reference to the limited liability companies is also applicable to the joint stock companies.

The property of the company remained after the property is respectively applied to the due payments, according to Article 186 of Company Law⁹⁷,

⁹⁷ According to Article 186 of Company Law, «After a liquidation group has thoroughly examined the company's property and prepared a balance sheet and a schedule of property, it shall formulate a liquidation plan and submit the same to the board of shareholders, general

shall be distributed, in the case of a company limited by shares, in proportion to the shareholdings of its shareholders.

4. *Foreign Investment Enterprises*

4.1. *Brief Introduction to the Chinese Foreign Investments Rules*

In 1979 China opened itself to foreign investments adopting its first law on equity joint ventures. In the 1980's laws on wholly foreign-owned enterprises and cooperative joint ventures were issued.

Since then, an assortment of investment vehicles were at disposal of foreign investors who wanted to expand overseas, depending on their business strategies, financial means, human resources, and legal framework of their countries⁹⁸.

In China there have been five major vehicles for foreign investors to do business in China: representative office, branch, Chinese-foreign equity joint venture, Chinese-foreign cooperative joint venture and wholly-owned enterprise.

The representative office and branch did not have the status of Chinese legal person and were preparatory in nature and involved a limited scope and amount of business activities.

The Chinese-foreign equity joint venture, Chinese-foreign cooperative joint venture and wholly-owned enterprise were collectively referred to as foreign investment enterprises and were legal persons representing the core instruments for direct investment in China⁹⁹.

From 1990's China allowed foreign investors to establish foreign meeting or the people's court for confirmation. The property of a company remained after the property is respectively applied to payment of the liquidation expenses, the wages, social insurance premiums and statutory compensation of staff and workers and the outstanding taxes, and to full payment of the debts of the company shall be distributed, in the case of a limited liability company, in proportion to the capital contributions of its shareholders and, in the case of a company limited by shares, in proportion to the shareholdings of its shareholders. During liquidation, a company shall continue to exist, but it may not engage in new business activities unrelated to liquidation. Company property may not be distributed among its shareholders prior to full repayment in accordance with the stipulations of the preceding paragraph».

⁹⁸ LO, TIAN, *Law for foreign business and investment in China*, cit., p. 73.

⁹⁹ For a description of the legal framework of the Chinese company law for foreigners before the Foreign Investment Law, see: QIU, LIN, *Chinese Company Law*, cit., pp. 209-214.

companies limited by shares¹⁰⁰.

On March 15, 2019, at the Second Session of the 13th National People's Congress, it adopted the Foreign Investment Law of the People's Republic of China (the "Foreign Investment Law"), which came into effect on January 1, 2020.

The Foreign Investment Law replaced three separate foreign investment laws enacted in the early years of China's economic reform: the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures¹⁰¹, the Law of the People's Republic of China on Wholly Foreign-Owned Enterprises¹⁰² and the Law of the People's Republic of China on Chinese-Foreign contractual joint ventures¹⁰³.

Together with the adoption of the Foreign Investment Law, several related regulations and notices, which were issued at the end of 2019, also took effect.

¹⁰⁰ LO, TIAN, *Law for foreign business and investment in China*, cit., p. 73.

¹⁰¹ The Law on Chinese-Foreign Equity Joint Ventures was adopted at the Second Session of the Fifth National People's Congress on July 1, 1979 and promulgated by Order No. 7 of the Chairman of the Standing Committee of the National People's Congress on July 8, 1979; amended according to the Decision on Amending the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures made at the Third Session of the Seventh National People's Congress on April 4, 1990, and amended for the second time according to the Decision on Amendment to the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures adopted at the Fourth Session of the Ninth National People's Congress on March 15, 2001 (Unofficial translation is available at http://www.china.org.cn/business/laws_regulations/2007-06/22/content_1214773.htm).

¹⁰² The Law on Wholly Foreign-Owned Enterprises was adopted at the fourth meeting of the Standing Committee of the Sixth National People's Congress on April 12, 1986; amended for the first time in accordance with the Decision of the Standing Committee of the National People's Congress on Amending the Law of the People's Republic of China on Wholly Foreign-Owned Enterprises at the 18th Meeting of the Standing Committee of the Ninth National People's Congress on October 31, 2000; and amended for the second time in accordance with the Decision of the Standing Committee of the National People's Congress on Amending Four Laws including the Law of the People's Republic of China on Wholly Foreign-Owned Enterprises at the 22nd Meeting of the Standing Committee of the Twelfth National People's Congress on September 3, 2016 (unofficial translation of the law is available at <http://en.pkulaw.cn/display.aspx?cgid=565613090e841b27bdfb&lib=law>).

¹⁰³ The Law on Chinese Foreign Contractual Joint Ventures was adopted at the First Session of the Seventh National People's Congress on April 13, 1988 and promulgated by Order No. 4 of the President of the People's Republic of China on April 13, 1988; amended according to the Decision on Revision of the Law of the People's Republic of China on Chinese-Foreign Contractual Joint Ventures adopted at the 18th Meeting of the Standing Committee of the Ninth National People's Congress on October 31, 2000 (unofficial translation is available at <http://www.asianlii.org/cn/legis/cen/laws/ccjv1452/>).

It amended the previous regime and aimed at expanding and promoting the foreign investments, in order to protect rights and interests of foreign investors, to standard the management of foreign investment, to impel the formation of a new pattern of all-round opening-up, to fix the regulation of foreign investments and to promote the growth of the socialist market economy.

The new Foreign Investment Law and the related regulations represented an important step for foreign investment in China.

4.2. *The Foreign Investment Law*

4.2.1. *Definitions and General Principles*

The Foreign Investment Law¹⁰⁴ defines a “foreign investment” as an activity directly or indirectly conducted by a foreign natural person, enterprise or other organization (the “foreign investors”). Article 2 of the Foreign Investment Law includes the following circumstances: (i) a foreign investor establishes a foreign-funded enterprise within the territory of China, independently or jointly with any other investor, (ii) a foreign investor acquires shares, equities, property shares or any other similar rights and interests of an enterprise within the territory of China, (iii) a foreign investor makes investment to initiate a new project within the territory of China, independently or jointly with any other investor; and (iv) a foreign investor makes investment in any other way stipulated by laws, administrative regulations or provisions of the State Council.

A foreign-funded enterprise refers to an enterprise that is incorporated under the Chinese laws within the territory of China and is wholly or partly invested by a foreign investor.

In short, Article 2 of the Foreign Investment Law redefines the terms “foreign investment”, “foreign investors”, and “foreign-invested enterprises”, by distinguishing “foreign investment” into “direct investment” and “indirect investment”, both of which are subject to the adjustment of the Foreign Investment Law and the supporting laws.

Before the issuance of the Foreign Investment Law, only foreign direct investments were regulated by the three laws, which have been replaced by the Foreign Investment Law, on wholly foreign owned enterprises, Chinese-foreign contractual joint ventures and Chinese-foreign equity joint ventures.

Article 2 of the Foreign Investment Law also adds merger and

¹⁰⁴ Unofficial translation of the Foreign Investment Law is available at <https://investmentpolicy.unctad.org>.

acquisition transactions into the scope of foreign investment, while, before that law, foreign investment only included setting up.

In practise, Article 2 abolishes the distinction between wholly foreign owned enterprises, Chinese-foreign contractual joint ventures and Chinese-foreign equity joint ventures, which were used since then, and refers the enterprises of foreign investment uniformly as “foreign-invested enterprise”.

Article 3 of the Foreign Investment Law provides that China shall adhere to the basic state policy of opening-up and encourage foreign investors to make investments within the territory of China and, at the same time, the State shall implement policies on high-level investment liberalization and convenience, and shall establish and improve the mechanism to promote foreign investment and create a stable, transparent, foreseeable and level-playing market environment.

Articles 4 and 28 of the Foreign Investment Law clarify that China will adopt the management system of pre-establishment national treatment and negative list for foreign investment.

The pre-establishment national treatment refers to the treatment given to foreign investors and their investments during the investment access stage, which is not lower than that given to their domestic counterpart.

The negative list refers to special administrative measures for the access of foreign investment in specific fields as stipulated by the Chinese government. The government will give national treatment to foreign investments outside the negative list.

Foreign investors shall not invest in any field forbidden by the negative list for access of foreign investment and for any field restricted by the negative list, foreign investors shall conform to the investment conditions provided in the negative list.

Fields not included in the negative list shall be managed under the principle that domestic investment and foreign investment shall be treated uniformly.

The negative list system has been piloted in the Shanghai Free Trade Zone since 2013 and was expanded countrywide in 2018, but the Foreign Investment Law represents the first time that the negative list system is fixed in the form of law.

4.2.2. Investment Promotion and Investment Protection

According to Article 9 of the Foreign Investment Law, national policies on supporting the development of enterprises shall equally apply to foreign-funded enterprises in accordance with the law.

The government shall establish and perfect the service system for foreign investment, and provide foreign investors and foreign-funded enterprises with consultation and services in respect of laws and regulations, policies and measures, investment project information and other aspects.

It shall establish multilateral and bilateral cooperation mechanisms for the promotion of investment with other countries, regions and international organizations, so as to enhance international exchanges and cooperation in terms of investment.

It is provided that the government shall not expropriate any investment made by foreign investors. Only under special circumstances, the government may expropriate or requisition an investment made by foreign investors for public interests in accordance with the law. Such expropriation or requisition shall be made pursuant to statutory procedures and fair and reasonable compensation will be given in a timely manner.

A foreign investor may, in accordance with the law, freely transfer inward and outward its contributions, profits, capital gains, income from asset disposal, royalties of intellectual property rights, lawfully obtained compensation or indemnity, such as income from liquidation, within the territory of China.

According to Article 22, intellectual property rights of foreign investors and foreign-funded enterprises shall be protected, such as the legitimate rights and interests of holders of intellectual property rights and relevant right holders.

4.2.3. Investment Management and Legal Liability

Article 34 and Article 37 of the Foreign Investment Law establish a foreign investment information reporting system in China for the management of the foreign investment companies.

According to Article 34, the foreign investors or the foreign funded enterprises shall submit the investment information to competent departments for commerce through the enterprise registration system and the enterprise credit information publicity system.

The contents and scope of foreign investment information to be reported shall be determined under the principle of necessity; investment information, available through interdepartmental information sharing, will not be required to be submitted again.

Authorities will not be allowed to request any investment information that can be obtained by interdepartmental information sharing.

Article 37 of Foreign Investment Law provides the penalties of noncom-

pliance. In case any foreign investor or foreign-funded enterprise violates the provisions of the law and fails to report their investment information as required by the foreign investment information reporting system, competent department for commerce shall order it to make corrections within a prescribed time limit.

In case a foreign investor invests in a field forbidden by the negative list, relevant competent department shall order the said investor to stop its investment activity, dispose of the shares and assets thereof or take any other necessary measures within a prescribed time limit, and restore the government to what it was prior to the investment; if there is any illegal gain, such gain shall be confiscated¹⁰⁵.

Where an investment activity of a foreign investor breaches any special administrative measures for restrictive access provided in the negative list, relevant competent department shall order the investor to make corrections within a prescribed time limit, and take necessary measures to meet the requirements of the aforesaid measures; if the foreign investor fails to make corrections within the time limit, specific measures shall be taken.

In addition, where an investment activity of a foreign investor violates any provision in the negative list, the said investor shall bear corresponding legal liability.

4.3. Implementing Rules and Measures on Security Review of Foreign Investment

The State Council adopted the Regulation on the Implementation of the Foreign Investment Law of the People's Republic of China (the "Implementing Regulation") on December 12, 2019, and it took effect on January 1, 2020.

The Implementing Regulation provides additional rules and clarification on general provisions and principles set out in the Foreign Investment Law.

In brief, the Implementing Regulation provides with national treatment for foreign invested enterprises in many areas, including government funding, land supply, tax reductions and exemptions, permitting, standards formulation, public procurement, and project approvals and it implements the rights of for foreign invested enterprises to participate in rule-making, standards formulation and government procurement.

Furthermore, the Implementing Regulation provides, *inter alia*, that government authorities have to take measures and establish systems

¹⁰⁵ Article 36 of the Foreign Investment Law.

for transparency in rule-making and administration and to provide rules concerning expropriation of foreign investors' investments and the protection of intellectual property.

In addition to the Implementing Regulations, many other supporting documents regarding foreign investment have also entered into effect on 1 January 2020, such as the Interpretations of the Supreme People's Court on Several Issues Concerning the Application of the Foreign Investment Law of the People's Republic of China issued on 26 December 2019, the Measures for the Reporting of Foreign Investment Information issued on 30 December 2019, the Notice regarding Foreign Investor Information Reporting Related Matters issued on 31 December 2019 and the Circular on Effective Work on Registration of Foreign-invested Enterprises for the Implementation of the Foreign Investment Law issued on 28 December 2019. On December 19, 2020, China's National Development and Reform Commission and Ministry of Commerce jointly issued the Measures on Security Review of Foreign Investment, which took effect on January 18, 2021. The Measures mandate pre-closing filing and authorize the "Foreign Investment Security Working Mechanism" to review certain foreign investment in various covered sectors¹⁰⁶.

The Implementing Regulations, the Measures and the other legal acts connected with the Foreign Investment Law brought many changes to the foreign investment regime in China and shall lead the growth of the Chinese legal framework.

5. *Conclusive Remarks*

Over the past decades a progressive transformation of law and legal institutions in China took place in the frame of China's modernization process.

The recognition and protection of private property, the amendment to the Constitution, the evolution of the bankruptcy law¹⁰⁷, the Company Law, the Foreign Investment Law and the other commercial and economic

¹⁰⁶ On the Measures on Security Review of Foreign Investment: <https://investmentpolicy.unctad.org> and www.lexology.com.

¹⁰⁷ With reference to the bankruptcy regulation in China: L. SHUGUANG, *Bankruptcy Law in China: Lessons of the Past Twelve Years*, cit.; RICCI, *La disciplina del fallimento nel diritto cinese*, cit.; PALMER, RAPISARDI, *The PRC Enterprise Bankruptcy Law: The People's Work in Progress*, cit..

legislation, contributed to the development of Chinese law and legal institutions.

Although China's traditional legal system continues to influence the development of the modern legal system, the continuing significance of China's traditional legal system appears to be indirect, with the remote persistence of traditional elements¹⁰⁸.

The current phase of development of Chinese company law needs to create a new form of ethics and moral rules, a sort of modernization of law, involving legal reforms, legal practices and expert lawyers, in order to ensure a modern concept of law (and legality) separated and autonomous from the political issues and from the moral (and ethic) rules.

The future modernization of the legal framework of company law in China shall be strictly linked to a wider implementation of the legal procedure, the legal practices and the overall legal system, in connection with a concrete development of the rule of law.

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¹⁰⁸ O'BRIEN, *The Survival of Traditional Chinese Law in the People's Republic of China*, cit. p. 172.

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