

## Supreme People's Court

# Provisions of the Supreme People's Court on Several Issues Concerning the Application of the Company Law of the People's Republic of China (IV)

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On August 28, 2017, the Supreme People's Court (SPC) promulgated the Provisions of the Supreme People's Court on Several Issues Concerning the Application of the Company Law of the People's Republic of China (IV) (Fa Shi [2017] No.16, hereinafter Judicial Interpretation IV "JI IV"). JI IV clarifies the legal interpretation of the validity of resolutions, shareholders' right to information, right to claim distribution of profit, preemptive purchase rights, and derivative lawsuits in court proceedings. It is in effect since September 1, 2017.

### 1. Background of the Policy

Since 2005, three judicial interpretations have been promulgated with respect to the Company Law. After the revision and promulgation of the Company Law in 2005, the SPC published the Judicial Interpretation of the Company Law (I) to solve the issues in applying the old and new Company Laws. In 2008 and 2011, the SPC promulgated the Judicial Interpretation of the Company Law (II) and (III), respectively, and resolved problems in applying the law in court proceedings concerning investment by shareholders and liquidation and dissolution of companies.

With the increase of companies in recent years, troubles concerning enterprise management and shareholders' rights are also increasing, accounting for 60% of all corporate litigations. The promulgation of JI IV aims to strengthen judicial remedies for shareholders' rights and promote a stable operation and development of corporations.

Improvement of the Company Law significantly affects the appetite of domestic and foreign investors and their selection of investment destinations. JI IV provides a reference guideline for the application of the law and thereby further improves the investment climate.

### 2. Details of the Policy

JI IV clarifies the following areas: (1) Improving legal procedures for challenging the validity of a resolution, (2) strengthening protection for the shareholders' right to information, (3) providing judicial remedies for the shareholders' right to claim distribution of profit, and (4) establishment of rules on the preemptive purchase rights and remedies for damage of shareholders.

① Improving legal procedures for challenging the validity of a resolution

Description	Example
<ul style="list-style-type: none"> <li>✓ JI IV clarifies the circumstances under which the SPC shall support a party's claim that a resolution of a shareholders' meeting or board meeting is invalid.</li> <li>✓ It requires the claimant to be an eligible shareholder at the time of filing a lawsuit.</li> <li>✓ The SPC's decision to invalidate or cancel a resolution of a company's shareholders' meeting or board meeting does not affect any relationship between the company and bona fide third parties based on the civil code.</li> </ul>	<p>A unilateral resolution made by a shareholders in a JV to the other shareholder(s), and to which JI IV applies, may be challenged in the SPC as invalid, and the SPC shall support such claim.</p>

② Strengthening protection for the shareholders' right to information

Description	Example
<ul style="list-style-type: none"> <li>✓ A party who has ceased to be a shareholder of a company may demand to inspect the company's documents.</li> <li>✓ A company may refuse the demand of a shareholder to inspect the company's accounting books if the shareholder's intent is malicious, and may limit the scope of disclosure in such case.</li> <li>✓ A company cannot deprive shareholders of their right to information based on its articles of incorporation or a discussion among its shareholders.</li> <li>✓ Damages can be claimed against a director or senior manager who violates obligations regarding the shareholders' right to information.</li> </ul>	<p>A party who has ceased to be a shareholder may exercise its rights to inspect and duplicate a document if its rights and interests were damaged during time as shareholder.</p>

③ Providing judicial remedies for the shareholders' right to claim distribution of profit

Description	Example
<ul style="list-style-type: none"> <li>✓ If a company without a justifiable reason does not distribute dividends despite the submission of a shareholders' resolution to do so, a case can be filed with the SPC to order the company to distribute profits.</li> <li>✓ The SPC shall dismiss such case if a shareholders' resolution on profit distribution has not been submitted (except in the case of abuse of rights by a shareholder preventing profit distribution resulting in losses suffered by the other shareholder(s)).</li> </ul>	<ul style="list-style-type: none"> <li>➤ A shareholder in a JV may submit a profit distribution resolution, and may file a case with the SPC to gain distribution of profits (if the grounds for defense by the company for not distributing profits are rejected).</li> <li>➤ In the absence of a resolution on the distribution of profits, a proof of abuse of rights by a major shareholder(s) is required.</li> </ul>

④ Establishment of rules on the preemptive purchase rights and remedies for damage of shareholders

Description	Example
<ul style="list-style-type: none"> <li>✓ If a shareholder does not hear the opinions of other shareholders regarding a transfer of equity interest, or impairs their preemptive purchase rights by fraud or malicious collusion, the other shareholders may demand a preemptive purchase of the equity interest under equivalent conditions.</li> <li>✓ The SPC shall consider factors such as the number and face value of the shares, and the method and term of payment in its decision on the preemptive purchase under equivalent conditions.</li> <li>✓ The time period for exercising the preemptive purchase right is no less than 30 days.</li> <li>✓ If a non-shareholder transferee cannot achieve its contractual objectives due to the exercising of preemptive purchase rights by existing shareholders, the transferee may pursue the civil liability of the transferor.</li> </ul>	<p>If a shareholder in a JV transfers its equity interest, and the transfer impairs the preemptive purchase rights of other shareholders (as through the absence of advance notification, fraud, malicious collusion, etc.), the shareholders whose rights have been infringed upon may purchase such shares under equivalent conditions.</p>

3. Impact on Enterprises

The promulgation of Judicial Interpretation (IV) has a good reference to the various situations arising in relation to resolutions and profit distribution by companies, transfer of equity interest, disclosure of corporate information, etc. In the event of trouble with their JV partners in the above areas, enterprises will be following the legal interpretations in this Judicial Interpretation. We will continue to follow up on related information and share it as appropriate.

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