



CORPORATE CAPITAL FORMATION SYSTEM OF CHINA: THE EVOLUTIONS, DEFICIENCIES AND IMPROVEMENTS


¹GE PUSHEN, ²HANNA BINTI AMBARAS KHAN, ³SUHAIMI AB RAHMAN

Abstract: *The capital formation system of China has made significant progress in the past 30 years. When China first enacted the company law in 1993, it had a strict statutory system. However, in 2005, the system was gradually relaxed upon revision of the law. In 2013, China again amended its company laws, and the system was changed from a capital formation to a full subscription system. The amendment is beneficial but it gives the autonomy of capital contribution to shareholders rather than companies. In the third review of the latest revised draft of the Company Law, the authorized capital system was introduced, which is not only innovative but also has far-reaching implications. The introduction of an authorized capital system will undoubtedly provide more autonomy space for companies, which is conducive to their flexible operation and innovative development. The objective of this paper is to analyze the necessity and feasibility of introducing the authorized capital system and to study the shortcomings of the Third Review Draft's provisions on the authorized capital system and make suggestions for improvement. This article uses the qualitative research method, mainly analyzing the text of the third review draft and literature related to the topic to collect data. It is found that the provisions on the authorized capital system in the third review draft are too simplistic, resulting in inconsistencies between the authorized capital system and the subscription system, a lack of authorization withdrawal mechanisms, a lack of relief mechanisms for improper issuance, and the limitation of the authorized capital system to limited liability companies.*

Keywords: *China company law, Capital System, Authorized Capital System, Statutory Capital System, Fully Subscribed Capital System, Deficiencies of the draft.*

1. Introduction

On September 1, 2023, the Fifth Session of the 14th Standing Committee of the National People's Congress reviewed the Third Review Draft of the Company Law of the People's Republic of China (hereinafter referred to as the "Third Review Draft"). This is the sixth revision of the Company Law in China within 30 years since the first company law was promulgated in 1993. The Company Law, as the fundamental law of the market economy, has actively responded to people's concerns and complied with market development and changes in the past 30 years of practice. It has played a huge role in improving China's market economy system, promoting the development of the market economy, and stimulating the vitality of the market economy. Based on incorporating opinions and suggestions from various aspects, the third review draft further revised and improved the company system, including democratic management of the company, strengthening the protection of the rights of small and



medium-sized shareholders, and strengthening the standardization of controlling shareholders and actual controllers. One of the highlights is the introduction of an authorized capital system in the company capital formation system, which has undergone profound changes in China's company capital system.

This study aims to explore the feasibility and necessity of introducing the authorized capital system in the Third Review Draft by introducing the development and evolution of the capital formation system in China's Company Law and to propose improvement suggestions for the shortcomings of the provisions on the authorized capital system in the Third Review Draft

The revision of the Company Law this time has received significant attention from Chinese society. The system of company capital formation, as a fundamental aspect within the Company Law, has sparked vigorous discussions. Consequently, this article's structure begins with a literature review, examining scholarly discourse surrounding the authorized capital system. Subsequently, we introduce the inheritance of China's company capital formation system and analyze its shortcomings across different historical periods. Following this, we analyze the necessity and feasibility of introducing the authorized capital system in the current revision of the Company Law in China. We then proceed to analyze the shortcomings of the authorized capital system in the third draft of this revision and propose suggestions for improvement.

This article uses the qualitative research method, mainly analyzing the text of the third review draft and literature related to the topic to analyze the necessity and feasibility of introducing the authorized capital system and making corresponding suggestions for the improvement of the authorized capital system stipulated in the third draft.

2. Literature review

This article explores the introduction and improvement of the authorized capital system. Early domestic research mainly focused on the concept of the authorized capital system, the advantages and disadvantages of the authorized capital system, and the application of the authorized capital system in other countries.

The authorized capital system is a type of capital formation system, Professor Xu Qiangsheng believes that the so-called corporate capital formation system is the system in which shareholders inject capital into the company, which is the "front-end" of the company's capital system and the basic guarantee of the company's independent personality and credit¹. As for the definition of an Authorized Capital System, Professor Fu Qiong believes that the company's capital formation system includes a statutory capital system, authorized capital system, and compromise capital system. The statutory capital system is mainly followed by civil law countries, emphasizing that the total amount of capital of a company must be determined when it is established. Only after all shareholders have fully subscribed or raised can a company be established. Its core feature is that the shares are issued

¹ Refer to Xu Qiangsheng's "Basic System Reengineering of Corporate Personality in China - Centering on the Capital System and the Position of the Board of Directors", published in *Global Legal Review*, Vol. 3, 2020, pp. 57-59.



in one go, and subsequent capital increases must be resolved by the shareholders' meeting, and the board of directors has no right to decide on its own². The authorized capital system is mainly adopted by countries in the Anglo-American legal system, which means that when a company is established, the company's shares do not need to be issued in one go or the proportion of capital contribution does not need to be subscribed in one go. Shareholders only need to subscribe or pay in a portion of the company to establish it, and the remaining portion is authorized by the shareholders' meeting charter to be issued or raised by the board of directors when necessary, without the need for a resolution of the shareholders' meeting. Its core lies in the board of directors having the right to independently decide to issue new shares or increase the proportion of capital contribution during the business process³. Professor Li Jianwei believes that the elements of the compromise capital system are generally the same as those of the authorized capital system, except that the authorized issuance of shares needs to be carried out within the statutory period, and the initial issuance of shares must not be less than the statutory minimum amount⁴. Professor Shi Tiantao believes that in the case of an authorized capital system, the law does not interfere with the issuance and payment of capital. Instead, the shareholders of the company set a total registered capital in the company's articles of association and delegate the power to issue capital to the board of directors responsible for the company's management and operation affairs⁵.

As for the advantages and disadvantages of the authorized capital system, Professor Li Jianwei believes that as the most important and active market entity, a company must fully leverage its advantages and functions in raising and mobilizing funds, and must be endowed with "flexibility" and "flexibility" in fundraising. Compared to this, the authorized capital system is more in line with such requirements⁶. Professor Li Yuzhuo and Li Haijuan believe that the Company Law establishes an authorized capital system with the pursuit of efficiency as its value concept, highlighting the pursuit of efficiency value by company capital, and at the same time, it is inevitable that due to its excessive tendency to pursue efficiency value, safety value may be overlooked, which is also the drawback of the authorized capital system⁷.

Recent research has focused on coordinating and improving the introduction of the authorized capital system in the third review of the revised draft, Professor Liu Jiayuan believes that to fully leverage the institutional advantages of the localized development of the authorized capital system, it is necessary to overcome potential institutional transition costs, conduct research on the operation and regulation of localized systems, and improve support systems⁸. Professor Shen Chaohui believes

² Refer to Fu Qiong's "Principles of Rethinking the Capital System of Companies", Law Press, 2004 edition, pages 62-67

³ Refer to Fu Qiong's "Principles of Rethinking the Capital System of Companies", Law Press, 2004 edition, pages 62-67

⁴ Refer to Li Jianwei's "Explanation of the Core Concepts of Corporate Capital", published in the first issue of Northern Law in 2016, pages 64-72

⁵ Refer to Shi Tiantao's "Corporate Capital System Reform: Interpretation and Analysis", published in Tsinghua Law Journal, No. 5, 2014, p. 130.

⁶ Refer to Li Jianwei's "Integration of Authorized Capital Issuance System and Subscription System - Reform of Company Capital System and Selection of Company Law Amendment", published in Modern Law, Issue 6, 2021, page 114.

⁷ Refer to Li Yuzhuo and Li Haijuan's "Value Concept, Forming Background and Evolution Trend of Corporation Capital System", published in Journal of Harbin University Of Commerce, No. 2, 2017, p. 122-128.

⁸ Refer to Liu Jiayuan's "On the Local Introduction and Operation Regulations of Authorized Capital System", published in



that For the potential corporate governance issues that may arise from the authorized shareholding system, regulatory mechanisms should be established in advance and after the event⁹. Professor Li Jianwei believes that if the authorized capital issuance system is introduced, a series of supporting updates to the current company's capital rules will still needed¹⁰. Professor Chen Jinshan believes that in the implementation of the authorized capital system and class shares, the Chinese Company Law needs to clarify the scope of issuance authorized by the shareholders' meeting to the board of directors after determining the functional positioning of class shares, in order to achieve the legislative intention of setting up class shares. This can not only facilitate financing but also be applied to anti-acquisition measures. At the same time, remedial measures should be considered when improper issuance causes damage to the interests of old shareholders¹¹.

3. Background: The Historical Evolution of the Formation System of China's Corporate Capital System

Since its promulgation in 1993, the Company Law of China has been revised in 2005 and 2013, and significant reforms have been made to the system of corporate capital formation. In addition, the Company Law made individual amendments to certain provisions in 1999¹², 2004¹³, and 2018¹⁴,

The Journal of Jilin University of Business and Economics, 2023, Issue 2, page 104.

⁹ Refer to Shen Chaohui, "The System Structure of Authorized Joint Stock System - Also Commenting on the Relevant Provisions of the 2021 Company Law (Revised Draft)", published in *Contemporary Law*, Issue 2, 2022, p. 108.

¹⁰ Refer to Li Jianwei's "Integration of Authorized Capital Issuance System and Subscription System - Reform of Company Capital System and Selection of Company Law Amendment", published in *Modern Law*, Issue 6, 2021, page 115.

¹¹ Refer to Chen Jingshan's "Restructuring the Regulation of Share Issuance under the Authorized Capital System", published in *The Journal of East China University of Political Science and Law*, 2022, Issue 2, page 68.

¹² In the 1999 revision of the Company Law, Article 67 of the original Company Law was revised to read: "The supervisory board of a solely state-owned company shall mainly consist of personnel appointed by the State Council or authorized institutions or departments of the State Council, and shall be attended by representatives of the company's employees. The members of the supervisory board shall not be less than three. The supervisory board shall exercise the powers stipulated in Article 54, Paragraph 1 (1) and (2) of this Law and other powers stipulated by the State Council Supervisors shall attend meetings of the board of directors as nonvoting delegates. Directors, managers, and financial personnel shall not concurrently serve as supervisors, "and an additional paragraph shall be added as the second paragraph in the original Article 229:" For a high-tech joint stock limited company, the proportion of the amount invested by the initiators with industrial property rights and non-patented technologies to the registered capital of the company shall be separately stipulated by the State Council

¹³ The amendment to the Company Law in 2004 removed the provision in Article 131 (2) of the original Company Law that "if the issuance price of stocks exceeds the par value, approval from the securities regulatory department of the State Council is required".

¹⁴ The amendment of the 2018 Company Law amended Article 142 of the original Company Law to read: "A company shall not acquire its own shares. However, except for one of the following circumstances:" (1) reduce the registered capital of the company; (2) merge with other companies holding its own shares; (3) use the shares for employee shareholding plans or equity incentives; (4) Shareholders request the company to acquire their shares due to objections to the company's merger or division resolution made at the shareholders' meeting; (5) Converting shares into convertible corporate bonds issued by listed companies; (6) It is necessary for a listed company to maintain its value and shareholder rights.

If a company acquires its own shares due to the circumstances specified in items (1) and (2) of the preceding paragraph, a resolution of the shareholders' meeting shall be obtained; If a company acquires its own shares due to the circumstances specified in items (3), (5), and (6) of the preceding paragraph, it may, in accordance with the provisions of the company's articles of association or the authorization of the shareholders' meeting, adopt a resolution at a board meeting attended by more than two-thirds of the directors.

After the company acquires its shares in accordance with the provisions of the first paragraph of this article, if it falls under the circumstances of the item (1), it shall be canceled within ten days from the date of acquisition; if it falls under the circumstances of the item (2) or (4), it shall be transferred or canceled within six months; if it falls under the circumstances of the item (3), (5), or (6) In any of the following circumstances, the total number of shares held by the company shall not exceed 10% of the total issued shares of the company and shall be transferred or canceled within three years.

If a listed company acquires its own shares, it shall fulfill its information disclosure obligations in accordance with the

respectively. As the amendments to these individual provisions did not involve substantial changes in the capital formation system, this article will not discuss them in detail.

3.1 The strict legal capital formation system stipulated by the 1993 Company Law

The Company Law promulgated in 1993 was born in the history of cleaning up and rectifying companies. Influenced by the limitations of the concept of planned economy to market economy transformation, it stipulated the strictest company capital system worldwide¹⁵. For shareholders' capital contributions, the 1993 Company Law required them to pay the registered capital in one lump sum upon the establishment of the company, and for companies in different industries, the Company Law stipulated different minimum registered capital limits¹⁶. For the form of investment, only monetary, industrial property, non-patented technology, and land use rights are allowed, and the proportion of investment in industrial property and non-patented technology is also subject to legal restrictions¹⁷. In addition, for the property contributed, capital verification must be carried out¹⁸. For the issuance of new shares, the authority is enjoyed by shareholders, and a shareholders' meeting needs to be held to make a capital increase resolution to achieve a capital increase¹⁹.

provisions of the Securities Law of the People's Republic of China. If a listed company acquires its own shares due to the circumstances specified in the first paragraph (3), (5), and (6) of this Article, it shall do so through public centralized trading. The company shall not accept its stocks as the subject of a pledge.

¹⁵ Refer to Xue Bo's "Evolution and Enlightenment of China's Capital System Legislation in the 40 Years of Reform and Opening Up", published in the third issue of the Humanities Journal in 2019.

¹⁶ Article 23 of the 1993 Company Law states that the registered capital of a limited liability company shall be the amount of capital contributed by all shareholders registered with the company registration authority.

The registered capital of a limited liability company shall not be less than the following minimum limits:

- (1) RMB 500000 for companies primarily engaged in production and operation;
- (2) A company mainly engaged in the wholesale of goods, with a total amount of RMB 500000;
- (3) RMB 300000 for companies primarily engaged in commercial retail;
- (4) Technology development, consulting, and service companies worth 100000 RMB.

If the minimum registered capital of a limited liability company in a specific industry needs to be higher than the limit specified in the preceding paragraph, it shall be separately stipulated by laws and administrative regulations

Article 78: The registered capital of a joint stock limited company shall be the total amount paid in capital registered with the company registration authority.

The minimum registered capital of a joint stock limited company is RMB 10 million. If the minimum registered capital of a joint stock limited company needs to be higher than the above-mentioned limit, it shall be separately stipulated by laws and administrative regulations

¹⁷ Article 24 of the 1993 Company Law states that shareholders may make capital contributions in currency, physical objects, industrial property rights, non-patented technologies, or land use rights at a fixed value. For physical objects, industrial property rights, non-patented technologies, or land use rights that are used as capital contributions, evaluation and valuation must be conducted, property verification must be conducted, and valuation shall not be overestimated or underestimated. The evaluation and valuation of land use rights shall be handled in accordance with the provisions of laws and administrative regulations.

The amount of capital contribution based on industrial property rights and non-patented technologies shall not exceed 20% of the registered capital of a limited liability company, except for special provisions of the state regarding the adoption of high-tech achievements

¹⁸ Article 26 of the 1993 Company Law: "After all shareholders have paid their capital contributions, they must undergo capital verification by a statutory capital verification agency and issue a certificate to ensure the authenticity of the capital

¹⁹ Article 38 of the Company Law of 1993 stipulates that the shareholders' meeting shall exercise the following powers: (1) to decide on the company's business policies and investment plans; (2) to elect and replace directors, and to decide on matters related to the remuneration of directors; (3) to elect and replace supervisors appointed by shareholder representatives, and to decide on matters related to the remuneration of supervisors; (4) to review and approve reports of the board of directors; (5) to review and approve reports of the board of supervisors or supervisors; (6) Review and approve the company's annual financial budget and final accounting plans; (7) Review and approve the company's profit distribution plan and loss recovery plan; (8) Make resolutions on increasing or reducing the registered capital of the company; (9) Make resolutions on the issuance of corporate bonds; (10) Make resolutions on the transfer of capital



From this, it can be seen that the 1993 Company Law strictly adhered to the concept of capital credit, and regarded the registered capital of a company as a symbol of its ability to assume responsibility and protect creditors. In terms of adjustment measures, legislation often applies mandatory norms to restrict company capital, giving shareholders less autonomy, and the rules are very strict. After more than 10 years of practice, the drawbacks of the overly strict statutory capital system in the 1993 Company Law began to emerge. The overly strict legal capital system severely suppresses the enthusiasm for private investment, and many people who are interested in investing in the market can only "sigh" because they cannot bear such a high investment burden. The lack of enthusiasm for private investment seriously affects the development of the market economy and hurts the country's economic prosperity and competitiveness. Therefore, it is imperative to modify such a strict statutory capital system.

3.2 The relaxed statutory capital formation system stipulated in the 2005 Company Law

Due to the overly strict regulations on the formation of corporate capital in the 1993 Company Law, which seriously affected the development of the market economy, to deepen the development of the market economy and adapt to the new situation and challenges of economic development after China acceded to the WTO, the National People's Congress of China revised the Company Law significantly in 2005. Although the 2005 Company Law still adopted the statutory capital system in the capital formation system, compared to the 1993 Company Law, capital controls were significantly relaxed. For shareholder contributions, although the 2005 Company Law retained the minimum capital registration limit, compared to the 1993 Company Law, the limit has significantly decreased. In addition, the Company Law changed the one-time paid-in system to a "binary system"²⁰ that allow for installment payments within a certain period. In addition to requiring limited liability companies and joint stock companies to have their first paid-in capital not less than 20% of the registered capital, The remaining portion can be paid in full within 2 years from the date of establishment of the company, and investment companies can have a grace period of 5 years to pay in full. Limited

contributions by shareholders to persons other than shareholders; (11) Make resolutions on matters such as merger, division, change of company form, dissolution, and liquidation of the company; (12) Amend the company's articles of association

²⁰ Article 26 of the Company Law of 2005 states that the registered capital of a limited liability company shall be the subscribed capital of all shareholders registered with the company registration authority. The initial capital contribution of all shareholders of the company shall not be less than 20% of the registered capital, nor shall it be less than the statutory minimum registered capital. The remaining portion shall be fully paid by shareholders within two years from the date of establishment of the company; among them, an investment company may make full payment within five years. The minimum registered capital of a limited liability company is RMB 30000. If laws and administrative regulations have higher requirements for the minimum registered capital of a limited liability company, their provisions shall prevail. Article 81 of the Company Law of 2005 If a joint stock limited company is established through initiation, the registered capital shall be the total amount of share capital subscribed by all initiators registered with the company registration authority. The initial capital contribution of all initiators of the company shall not be less than 20% of the registered capital, and the remaining portion shall be fully paid by the initiators within two years from the date of establishment of the company. Among them, an investment company may pay in full within five years. Before fully paying in, shares shall not be offered to others.

If a joint stock limited company is established through fundraising, the registered capital shall be the total amount paid in capital registered with the company registration authority.

The minimum registered capital of a joint stock limited company is RMB 5 million. If laws and administrative regulations have higher requirements for the minimum registered capital of a joint stock limited company, their provisions shall prevail

liability companies established through public offering still implement a paid-in system²¹. For the forms of investment, the 2005 Company Law is no longer limited to the five forms of investment stipulated in the 1993 Company Law. Any non-monetary property that can be evaluated in currency and transferred can be used for investment²². As for the proportion of non-monetary capital contributions, the Company Law of 2005 was changed, and the Company Law of 1993 stipulated from the positive side that non-monetary property contributions should not exceed 20%, while from the negative side, monetary property contributions should not be less than 30%²³. After the completion of capital contributions, capital verification is still required to ensure the authenticity of capital²⁴. In terms of new share issuance, increasing or reducing capital still belongs to the authority of shareholders, and a resolution needs to be made by the shareholders' meeting, not by the board of directors²⁵.

The revision of the Company Law in 2005 significantly slowed down the regulation of capital formation. Although it still adheres to capital credit and emphasizes the importance of registered capital for company liability and creditor protection, it achieves a "soft landing" from capital credit to asset credit by limiting the initial paid-in ratio and subsequent investment period²⁶, reducing mandatory legal provisions and giving shareholders greater autonomy. The capital formation system is showing a trend of easing. However, although there have been significant improvements in the revision of the Company Law, there are still many restrictions on the autonomy of enterprise will, and the market mechanism has not been fully utilized. The threshold for company establishment is still too high, and the survival and development space of small and micro enterprises is limited, which suppresses the public's investment enthusiasm and enthusiasm²⁷. The capital formation system

²¹ Refer to Xue Bo's "Evolution and Enlightenment of China's Capital System Legislation in the 40 Years of Reform and Opening Up", published in the third issue of the Humanities Journal in 2019.

²² Article 27 of the Company Law of 2005 states that shareholders may make capital contributions in currency, as well as in tangible goods, intellectual property rights, land use rights, and other non-monetary assets that can be valued in currency and transferred in accordance with the law. However, this does not apply to assets that cannot be used as capital contributions in accordance with laws and administrative regulations.

Non-monetary assets as capital contributions should be evaluated and valued, verified, and not overvalued or undervalued. If there are provisions in laws and administrative regulations regarding evaluation and pricing, their provisions shall prevail. The monetary contribution amount of all shareholders shall not be less than 30% of the registered capital of a limited liability company.

²³ Noted above

²⁴ Noted above

²⁵ Article 38 of the Company Law of 2005 stipulates that the shareholders' meeting shall exercise the following powers: (1) to decide on the company's business policies and investment plans; (2) to elect and replace directors and supervisors not held by employee representatives, and to decide on matters related to the remuneration of directors and supervisors; (3) to review and approve reports of the board of directors; (4) to review and approve reports of the board of supervisors or supervisors; (5) Review and approve the company's annual financial budget and final accounting plans; (6) Review and approve the company's profit distribution plan and loss recovery plan; (7) Make resolutions on increasing or reducing the registered capital of the company; (8) Make resolutions on the issuance of corporate bonds; (9) Make resolutions on the merger, division, dissolution, liquidation, or change of corporate form of the company; (10) Revise the company's articles of association; (11) Other powers stipulated in the company's articles of association.

If the shareholders unanimously agree in writing to the matters listed in the preceding paragraph, they may not hold a shareholders' meeting and make a decision directly, with all shareholders signing and stamping the decision documents.

²⁶ Refer to Li Jianwei's "Integration of Authorized Capital Issuance System and Subscription System - Reform of Company Capital System and Selection of Company Law Amendment", published in Modern Law, Issue 6, 2021, page 105.

²⁷ Refer to Shi Tiantao's "Corporate Capital System Reform: Interpretation and Analysis", published in Tsinghua Law Journal, No. 5, 2014, p. 130.

still needs improvement.

3.3 The complete subscribed capital system stipulated in the 2013 Company Law

In order to stimulate market vitality and boost entrepreneurial enthusiasm, in the context of changing government functions streamlining administration, and delegating power, the Company Law was significantly revised again in 2013. The magnitude of this revision can be described as a "revolutionary" change²⁸. Firstly, in the capital formation system, shareholder contributions no longer have a minimum registered capital limit, making it possible for a "1 yuan company". Except for companies that are explicitly required by law to adopt a paid-in system, shareholders no longer need to make actual capital contributions when registering a company. As long as shareholders fully subscribe to the registered capital in one go, the company can be established²⁹. Correspondingly, due to the change to the subscription system, the capital verification process has also been canceled. In addition, for the form of capital contribution, there are no longer restrictions on the structure of monetary and non-monetary contributions, and the provision of the 2008 Company Law that "monetary contributions shall not be less than 30% of registered capital" has been removed³⁰. For the issuance of new shares, it is consistent with the 2008 Company Law, The shareholders' meeting still needs to make a resolution³¹.

The full subscription system confirmed in 2013 has solved the long-standing dilemma of enterprise establishment in one fell swoop, which is conducive to reducing the cost of investing in entrepreneurs and stimulating investors' enthusiasm for investment³². It provides solid institutional support for enhancing the vitality of China's market and promoting development and innovation. There are various opinions in the academic community on the nature of the subscribed capital system. Some scholars believe that the complete subscribed capital system should be an authorized capital

²⁸ Refer to Li Jianwei's "Integration of Authorized Capital Issuance System and Subscription System - Reform of Company Capital System and Selection of Company Law Amendment", published in *Modern Law*, Issue 6, 2021, page 107.

²⁹ Article 26 of the 2013 Company Law states that the registered capital of a limited liability company shall be the subscribed capital of all shareholders registered with the company registration authority.

If there are other provisions in laws, administrative regulations, and decisions of the State Council regarding the paid-in registered capital and the minimum registered capital of a limited liability company, such provisions shall prevail.


³⁰ Article 27 of the Company Law of 2013 states that shareholders may make capital contributions in currency, as well as in tangible goods, intellectual property rights, land use rights, and other non-monetary assets that can be valued in currency and transferred in accordance with the law. However, assets that cannot be used as capital contributions as stipulated by laws and administrative regulations are excluded.

Non-monetary assets as capital contributions should be evaluated and valued, verified, and not overvalued or undervalued. If there are provisions in laws and administrative regulations regarding evaluation and pricing, their provisions shall prevail.

³¹ Article 37 of the 2013 Company Law]. The shareholders' meeting shall exercise the following powers: (1) to decide on the company's business policies and investment plans; (2) to elect and replace directors and supervisors who are not held by employee representatives, and to decide on matters related to the remuneration of directors and supervisors; (3) to review and approve the report of the board of directors; (4) to review and approve the report of the board of supervisors or supervisors; (5) Review and approve the company's annual financial budget and final accounting plans; (6) Review and approve the company's profit distribution plan and loss recovery plan; (7) Make resolutions on increasing or reducing the registered capital of the company; (8) Make resolutions on the issuance of corporate bonds; (9) Make resolutions on the merger, division, dissolution, liquidation, or change of corporate form of the company; (10) Revise the company's articles of association; (11) Other powers stipulated in the company's articles of association.

If the shareholders unanimously agree in writing to the matters listed in the preceding paragraph, they may make a decision without holding a shareholders' meeting, and all shareholders shall sign and stamp the decision document.

³² Refer to Shi Tiantao's "Corporate Capital System Reform: Interpretation and Analysis", published in *Tsinghua Law Journal*, No. 5, 2014, p. 133.



system. For example, Professor Fan Jian believes that "this capital system reform has brought about the establishment of the authorized capital system in China"³³. Some scholars also believe that the fully subscribed capital system is neither a statutory capital system nor an authorized capital system, and is an innovative capital formation system. For example, Professor Wang Yanchuan believes that "the subscribed capital system is different from the strict statutory capital system or the authorized capital system, and it belongs to China's institutional innovation"³⁴. However, it is generally believed that the full subscription system is still the statutory capital system, Professor Zhao Xudong believes that "the reformed company capital system still belongs to the statutory capital system in terms of legal types, and believes that the change of China's company law from the statutory capital system to the authorized capital system is a misreading and misunderstanding of the capital system model"³⁵. And Professor Gan Peizhong believes that "after this capital restructuring, the framework of the statutory capital system has still been preserved"³⁶.

The author believes that the statutory capital system and the authorized capital system are the division of the sources of the company's capital contribution obligations, while the concept opposite to subscribed capital is paid in, and the two are regulations on how the contribution obligations are fulfilled. Therefore, it is not possible to infer whether the company's capital formation system is a statutory capital system or an authorized capital system through simple "subscription". It is still necessary to differentiate and analyze the complete subscription system based on the core difference between the statutory capital system and the authorized capital system. The statutory capital system requires a company to fully pay or subscribe to its registered capital at the time of registration. The right to increase capital in the future lies with the shareholders' meeting, and the board of directors has no right to decide on capital increase on its own. Contrary to the statutory capital system, the authorized capital system allows companies to only issue a portion upon registration, and the remaining portion can be issued by the board of directors authorized by the shareholders' meeting based on the company's operating conditions. By using this standard to measure the full subscription system determined by the 2013 Company Law, it can be seen that it still belongs to the category of the statutory capital system, but the statutory capital system is more relaxed in terms of investment restrictions, giving shareholders great autonomy.

3.4 Introduction of the authorized capital system in the revised draft

Ten years have passed since the company law overhaul in 2013. Although the Standing Committee of the National People's Congress revised individual provisions of the Company Law in 2018, with the development and changes in the social economy, it is necessary for us to revise the

³³ Refer to Fan Jian's "Analysis of the Credit Responsibility System after the Reform of the Company's Capital Registration System", published in *China Business Daily* on August 23, 2014, 3rd edition

³⁴ Refer to Wang Yanchuan's "Issues and Future Improvements of the Subscribed Capital Contribution System - From the Perspective of Creditor Protection", published in Zhu Ciyun's "Collected Works on Commercial Law" (Volume 27), Law Press, 2016 edition, page 191.

³⁵ see Zhao Xudong: "Capital Legal Responsibility under the Change of Capital System - Rational Interpretation of the Revision of Company Law", *Law Research*, 2014, Issue 5, p. 28.

³⁶ [see Gan Peizhong: "On the Environment, Logical Defects, and Institutional Remedies of the Disruptive Reform of the Corporate Capital System", *Science and Law*, 2014, Issue 3, p. 498.



Company Law again to better adapt to the reality of society. According to the latest three review drafts, According to the latest three review drafts, this revision of the Company Law allows joint stock companies to make choices based on their own business judgment, authorizing the board of directors to issue shares within 50% of the issued share capital within another three years.³⁷

4. Analysis of the Introduction of Authorized Capital System in the Third Review Draft of the Revised Company Law: necessity and feasibility

4.1 The necessity of introducing an authorized capital system


The introduction of the authorized capital system is undoubtedly a major highlight of this revision of the Company Law, which is consistent with the global trend of reducing investment restrictions, reducing financing costs, and improving company financing efficiency, and is in line with the development trend of countries around the world from the legal capital system to the authorized capital system. This revision not only reflects the progress and development of China's Company Law but also injects new vitality into the improvement of corporate governance structure and the development of the market economy.

The authorized capital system can compensate for the shortcomings of the subscribed capital system. The subscribed capital system still belongs to the statutory capital system. Although shareholders are allowed to not pay their capital contributions during the issuance of new shares, they are still required to fully subscribe to their capital contributions. After shareholders commit to fully subscribe to their capital contributions, they are obligated to make capital contributions. If shareholders fail to fulfill their capital contribution obligations in the future, they need to bear corresponding responsibilities. Therefore, for some large companies, even under the background of a subscription system, shareholders still have concerns about subscribed capital, The third draft requires shareholders to make full capital contributions within 5 years after subscribing³⁸, which further increases shareholders' concerns.,and limits the company's financing. Under the authorized capital system, the shareholders' meeting authorizes the board of directors to issue new shares in installments based on business conditions, which reduces the pressure on subscribers, eliminates their concerns, and is more conducive to financing. Secondly, when a company adopts a subscribed capital system, the freedom of capital contribution is given to shareholders, allowing them to make decisions on the amount, method, and deadline of capital contribution based on their wishes. However, there is a mismatch in this autonomy: companies should determine financing behavior

³⁷ Article 152 of the Third Review Draft of the Revised Company Law: "The company's articles of association or shareholders' meeting may authorize the board of directors to decide within three years to issue shares not exceeding 50% of the issued shares. However, payment of shares by non-cash payment method shall be subject to resolution of the shareholders' meeting

³⁸ Article 152 of the Third Review Draft of the Revised Company Law: "The company's articles of association or shareholders' meeting may authorize the board of directors to decide within three years to issue shares not exceeding 50% of the issued shares. However, payment of shares by non-cash payment method shall be subject to resolution of the shareholders' meeting

³⁸ Paragraph 1 of Article 47 of the third revised draft of the Company Law: "The registered capital of a limited liability company shall be the capital contribution subscribed by all shareholders registered with the company registration authority. The capital contribution subscribed by all shareholders shall be determined by the shareholders according to the company's articles of association stipulate that payment must be made within five years from the date of establishment of the company."



based on their own funding needs and usage, and it should be up to the company to decide when to raise funds and the scale of financing. The subscribed capital system is determined by the board of directors for the issuance of new shares, which compensates for this mismatch and returns the autonomy of financing to the company itself.

The authorized capital system returns the authority to issue shares to the commercial judgment. For a limited liability company, shareholders are the owners of the company and entrust the board of directors to manage the company's operations. Compared to shareholders' meetings, the board of directors has a better understanding of the company's current business situation, a better grasp of internal and external information, and can make better business judgments. The right to issue shares is closely related to a company's investment and financing matters, and should be a part of the commercial judgment in the logic of corporate governance, and should also be exercised by the board of directors. The institutional arrangement of the authorized capital system in this regard is more in line with the logic and development laws of corporate governance³⁹.

Adopting an authorized capital system can help improve the efficiency of business decision-making. Under the subscribed capital system, the issuance of new shares falls within the scope of the authority of the shareholders' meeting, requiring tedious procedures for convening the shareholders' meeting and the formation of effective resolutions. This process is time-consuming and labor-intensive, seriously affecting the efficiency of business decision-making. In an era of rapidly changing market conditions, this inefficient decision-making process is likely to lead to the loss of valuable business opportunities and bring losses to the company. On the contrary, the authorized capital system simplifies the process of issuing new shares, requiring only a resolution from the shareholders' meeting and eliminating cumbersome procedures, which is more conducive to quickly responding to market opportunities.

4.2 Feasibility of Introducing Authorized Capital System

The main reasons for opposing the introduction of the authorized capital system are as follows. Firstly, it is unfavorable for the protection of company creditors. Under the authorized capital system, the number of authorized issued shares recorded in the articles of association and the implied amount of company capital is illusory and inflated numbers, and the protection of company creditors cannot be implemented⁴⁰. Secondly, in the context of an underdeveloped system of directors' fiduciary duties, the authorized capital system is not conducive to shareholder protection. Giving the right to issue new shares entirely to the board of directors is also unfair in protecting shareholder rights⁴¹. Thirdly, the practical significance of the China Securities Issuance Regulatory Commission's restriction on the authorized capital system of listed companies. In the strictly regulated securities

³⁹ Refer to Liu Jiayuan's "On the Local Introduction and Operation Regulations of Authorized Capital System", published in the Journal of Jilin University of Business and Economics, 2023, Issue 2, page 104.

⁴⁰ Refer to the writing group of the key textbook "Commercial Law" for Marxist theoretical research and construction engineering. Business Law [M]. Beijing: Higher Education Publishing Society, 2019: 129

⁴¹ Refer to Li Gengkun and Jia Siyao, "Introduction and Improvement of China's Authorized Capital System - From the Perspective of the Revised Draft of the Company Law", published in the fourth issue of "Theoretical Circle" in 2023, pp. 70-71



issuance review system, even if the board of directors resolves to issue shares in accordance with the articles of association or the authorization of the shareholders' meeting, the implementation of the resolution still needs to be registered or approved by the China Securities Regulatory Commission and the stock exchange⁴². Fourthly, the authorized capital system cannot solve the problems arising from the current subscribed capital system.

Firstly, the introduction of an authorized capital system will not worsen the protection of creditors. With the transformation and evolution of the company form from a "human company" to an "asset company", the credit foundation of modern companies has shifted to a debt-paying ability based on the company's assets, and there are two opposing concepts of capital credit and asset credit based on different trust in "assets"⁴³. Under the statutory capital system, capital, as a manifestation of a company's ability to fulfill its responsibilities, constitutes the last barrier to protecting the interests of creditors. It seems that the more registered capital a company has, the stronger its ability to repay debts, and the more effective the protection of creditors is. Therefore, the statutory capital system constructs a series of rules to ensure the authenticity, certainty, and immutability of a company's capital. Ultimately, registered capital is just a static number, and in the process of a company's operations, its assets are constantly changing, either in profit or loss, resulting in a difference between the company's net assets and registered capital. After the shareholders complete their contributions to the company, these contributions become the independent property of the company, and the company conducts production and operation based on this, taking responsibility for its profits and losses, and assuming independent responsibility to the extent of all the company's assets. From this, it can be seen that the true manifestation of a company's responsibility is not its capital, but rather its net assets. In this context, it seems unnecessary to overemphasize the protection of creditors by registered capital. Whether under the statutory capital system or the authorized capital system, the issuance of new shares will increase the company's net assets, increase the company's liability capacity, and increase the possibility of creditors' debts being repaid. Therefore, breaking the excessive reliance and superstition on capital credit, establishing an authorized capital system based on asset credit theory, and completely changing the rule design of company share issuance are inevitable choices for the progress of company law⁴⁴.

Secondly, the authorized capital system can provide relatively complete relief for the protection of shareholder rights and interests, which can better protect shareholder rights and interests. Directors who belong to the company's management are not the ultimate beneficiaries of the company's residual interests and do not have legitimate incentives in business to improve the company's operations⁴⁵. After the introduction of the authorized capital system, the Board of Directors can issue new shares within the scope of authorization. The Board of Directors may indeed violate its fiduciary

⁴² Noted above

⁴³ See Ma Genxin and An Zhenlei, "Reshaping Capital Formation: Localization Construction of Authorized Capital System" in *Economic and Trade Law Review*, Issue 3, 2023, p. 102

⁴⁴ Noted above

⁴⁵ Refer to Li Jianwei's "Integration of Authorized Capital Issuance System and Subscription System - Reform of Company Capital System and Selection of Company Law Amendment", published in *Modern Law*, 2021, Issue 6, page 116.



obligations and improperly issue shares, resulting in damage to shareholder rights and interests. However, the right of the Board of Directors to issue new shares comes from the shareholders' meeting and authorization, and the shareholders' meeting can fully limit the authority of the Board of Directors to issue shares. In addition, when the company's business situation changes after authorization, the shareholders' meeting can also revoke the authorization to the Board of Directors, change the company's articles of association, return to the statutory capital system, and transfer the authority to issue new shares to itself, to achieve pre-emptive relief for shareholders' rights damage. In addition, the legislative provisions on the authorized capital system in the third review draft of our country are not perfect and have not formed an effective constraint mechanism to regulate improper issuance by the board of directors. However, from a comparative perspective, countries around the world have established certain restraint mechanisms for the issuance of new shares by the board of directors, achieving in-process remedies to regulate improper issuance and protect shareholder rights. Finally, since the implementation of the subscription system in the Company Law in 2013, the fiduciary obligations of directors have also received widespread attention from both theoretical and practical circles. The revision of the Company Law and the third review draft stipulate the fiduciary and diligent obligations of directors, Article 189 of the third review draft stipulates that "if a director or senior management violates laws, administrative regulations, or the company's articles of association and damages the interests of shareholders, shareholders may file a lawsuit with the people's court. If a director violates the provisions of laws, regulations, or the company's articles of association and causes damage to the shareholders' rights and interests due to improper issuance, the shareholders can file a lawsuit to achieve post-relief and demand compensation from the director who violates the fiduciary duty.

Thirdly, the supervision of the China Securities Regulatory Commission on the listing of shares does indeed extend the time for share issuance, which seems to affect the effectiveness of the authorized capital system. However, whether implementing the authorized capital system or the statutory capital system, the issuance of new shares by listed companies will be subject to the supervision of the China Securities Regulatory Commission. The core difference between the authorized capital system and the statutory capital system lies in whether the right to issue new shares is granted to the board of directors or the shareholders' meeting, which solves the problem of power distribution within the company. At this level, issuing new shares by the board of directors is significantly more efficient than issuing them at a shareholders' meeting.

Finally, the reason for denying the authorized capital system cannot be established as it cannot solve the problem of the subscription system. The problem of a complete subscription system should be solved by improving the subscription system itself, rather than demanding an authorized capital system. The introduction of the authorized capital system is aimed at addressing the shortcomings of the statutory capital system, making changes to the capital formation system, granting the company's board of directors flexibility in corporate governance, financing, mergers and acquisitions, and other equity capital operations, thereby improving the overall efficiency of the company's

operations and better-realizing shareholder interests⁴⁶.

5. Finding: the shortcomings in the authorized capital system of the revised draft


The introduction of the authorized capital system is undoubtedly a major innovation in China's capital formation system, which is of great significance for improving efficiency, stimulating economic vitality, and promoting commercial development. The introduction of the authorized capital system is not only a simple provision that the shareholders' meeting can authorize the board of directors to issue new shares, but also needs to consider its coordination with the existing system, the balance of interests among stakeholders in the new system, and a series of issues that need to be continuously improved in design and filled in gaps. However, the drawback is that the third review draft of the revised draft only has two provisions on the authorized capital system, which are too simple and the system design is not perfect.

5.1 Incoordination between authorized capital system and subscription system

The authorized capital system and the subscribed capital system are two different levels of issues, with the authorized capital system being opposite to the statutory capital system, and the subscribed capital system being opposite to the paid-in system. The authorized capital system determines from the internal authority level of corporate governance that, with the authorization of the shareholders' meeting, the board of directors can issue new shares, which solves the issue of authority for issuing new shares. The subscription system is the issue of whether shareholders need to pay their capital contributions when issuing new shares, and the problem solved is the specific way of fulfilling their capital contribution obligations. According to the current provisions of the Company Law, limited liability companies can choose to adopt the "authorized capital system+subscription system" model. However, the authorized capital system and the subscription system are not coordinated.

Firstly, the subscription system conflicts with the authorized capital system in facilitating financing functions. The purpose of the subscription system is to lower the threshold for company investment, reduce the pressure on shareholders to contribute, and at the same time, reduce idle company funds. The authorized capital system allows companies to issue capital in installments, reducing the threshold for financing and establishment. At the same time, it grants the board of directors the right to issue new shares for financing as needed, facilitating financing and improving the efficiency of fund utilization. It seems that the two systems have the same function, and combining them will achieve the effect of "one plus one equals two or even greater than two". However, in reality, the parallel implementation of the authorized capital system and the subscription system will bring a very strange phenomenon: the company's board of directors decides to issue new shares based on the need for fund utilization, and shareholders subscribe one after another, but none of them have actually paid in. It seems that the company's financing has been completed, but in reality, the company has not been able to obtain usable funds through financing,

⁴⁶ Refer to Shen Chaohui, "The System Structure of Authorized Joint Stock System - Also Commenting on the Relevant Provisions of the 2021 Company Law (Revised Draft)", published in *Contemporary Law*, Issue 2, 2022, p. 105.




and the purpose of obtaining funds for the company's use through the issuance of new shares by the board of directors has not been achieved. Although the third review draft requires that subscribed capital must be fully paid within five years, this regulation does not solve the above problem. What would happen if the board of directors added restrictions during financing and required shareholders to make actual contributions? Because shareholders could have paid their capital contributions within 5 years but were restricted and deprived of their right to subscribe by the board of directors, this will greatly dampen the enthusiasm of shareholders for capital contributions, leading to difficulties in financing for the company. The company has to make concessions in other aspects in order to obtain financing, which reduces the effectiveness of financing and even infringes on the rights and interests of the company and shareholders. It can be seen that the subscription system will reduce the financing function of the authorized capital system. Secondly, the combination of a subscription system and an authorized capital system will bring about institutional complexity, leading to frequent disputes. Since the introduction of the subscribed capital system in China in 2013, the shortcomings of the subscribed capital system have gradually emerged, especially in terms of funding obligations, and disputes have emerged endlessly. Authorized capital production, as a brand new capital system, has not yet fully established its institutional framework, and people's understanding of its philosophy and operating mechanism is still not deep enough. The superposition of these two systems has led to the ambiguity of rules, which will further exacerbate the occurrence of disputes.

5.2 Inadequate authorization revocation mechanism

The source of share issuance is the general meeting of shareholders. In specific circumstances, the general meeting of shareholders can naturally revoke the authorization to the board of directors and regain the authority to issue new shares. When issuing new shares, if the original shareholders do not contribute, their equity will inevitably be diluted. Directors may exploit information asymmetry, abuse their rights, and dilute the original shareholder's equity through the issuance of new shares, causing them to lose control. The first review draft of the revised draft paid attention to this issue. Article 164 of the first review draft stipulates that "if the company's articles of association or the shareholders' meeting authorizes the board of directors to decide to issue new shares, the resolution of the board of directors shall be passed by more than two-thirds of all directors. If the number of voting rights represented by the issuance of new shares exceeds 20% of the total voting rights represented by the company's issued shares, the resolution of the shareholders' meeting shall be obtained.". But the third review draft deleted this provision. Instead, restrictions on the issuance rights of the board of directors are imposed by specifying the maximum authorized issuance period and the maximum proportion of authorized total shares to be issued. However this restriction is clearly not enough to solve the problem of directors using information asymmetry to dilute the original shareholder's shares and lose control.

5.3 Lack of relief mechanisms for improper issuance

The so-called improper issuance refers to the behavior of the board of directors issuing new



shares in violation of laws, regulations, or the company's articles of association, where the price of the issued shares is significantly too low, or another issuance of new shares is not primarily for financing purposes. The third review of the revised draft did not establish a relief mechanism for improper issuance, resulting in a lack of due protection for the interests of shareholders and the company.

5.4 Restrict the authorized capital system to limited liability companies

The third review draft of the revised draft will limit the authorized capital system to limited liability companies. Limited liability companies can choose whether to authorize the board of directors to issue new shares. If not authorized, limited liability companies will still implement the statutory capital system. For limited liability companies, the third review of the revised draft did not give them the right to choose and implement a unified statutory capital system. The reason for doing so is generally believed to be that limited liability companies are relatively small in scale, with a low degree of separation between ownership and management rights, and granting the authority to issue new shares to the board of directors may not be feasible or necessary. But in fact, there are many large-scale limited liability companies with a high degree of separation between the two rights, which have a practical demand for the authorized capital system. Under the current legal system, if these companies want to implement an authorized capital system, they must first change their corporate form to become a limited liability company, which is cumbersome and reduces efficiency.

6. Suggestions for Improving the Authorized Capital System

6.1 Clearly stipulate that shareholders need to make actual contributions when adopting the authorized capital system.

As mentioned earlier, the subscription system will reduce the financing function of the authorized capital system. When considering foreign legislation, most authorized capital systems also require paid-in capital contributions. Article 34 (1) of the Japanese Company Code stipulates that unless all initiators agree, subscribers who subscribe to company shares shall make timely and full payments⁴⁷; The Company Law of Taiwan, China has also made the same provision⁴⁸. We can learn from the provisions of the Company Law of Japan and Taiwan, China, and China, and clearly stipulate that when the subscribed capital system is adopted, the board of directors must pay in capital when authorized to issue new shares.

6.2 Increase the situation of revocable authorization for change of control and clarify the

⁴⁷ Article 34 (1) of the Japanese Company Code of 2005 The initiators, after subscribing for the shares issued at the time of establishment, must promptly and fully pay the cash related to the capital contribution or deliver all non-cash assets related to the capital contribution. However, obtaining the consent of all initiators does not prevent the joint stock company from carrying out necessary registration, registration, and other creation or transfer of rights against third parties after establishment.

⁴⁸ Article 131 of the Taiwan Company Law of China states that when the promoters have fully subscribed for the shares to be issued for the first time, they shall immediately make full payment for the shares and appoint directors and supervisors. The selection method referred to in the preceding paragraph shall apply mutatis mutandis to the provisions of Article 198. The capital contribution of the initiators, in addition to cash, may be offset by the property and technology necessary for the company's business

Article 132: "When the initiators do not fully subscribe to the shares to be issued for the first time, they shall be fully subscribed. When the shares are offered in accordance with the provisions of Article 157, special shares may be issued.




effectiveness of issuing in violation of authorization revocation rules

According to the above content, the third review draft does not determine the situation of revocation of authorization, which is unfavorable for the protection of existing shareholders. Suggest restoring the provision of revoking authorization in the first review draft. At the same time, drawing on the provisions of Article 206 (2) of the Japanese Company Code, when the issuance of new shares results in a change of control and shareholders holding more than 10% of the voting rights object, the issuance authority should be reviewed and decided by the shareholders' meeting. Considering that the purpose of revocation of authorization is to prevent the dilution of the original shareholder's shareholding and change of control caused by the issuance of new shares by the board of directors, for large listed companies, the equity structure of the company is relatively dispersed, and small changes in equity ratios often affect the transfer of control. The issuance of new shares by the board of directors also deliberately avoids the share ratio stipulated in Article 164, making it difficult for shareholders to regain decision-making power in the situation stipulated in Article 164 after delegating power⁴⁹

In addition, it is suggested that legislation should directly clarify that the issuance of shares in violation of Article 164 of the third review draft of the revised draft is invalid, and the company and new shareholders should return each other's shares. The new shareholder should return the shares to the company, and the company should cancel them. At the same time, the company should return the new shareholder's capital contribution and pay interest at the bank loan interest rate for the same period. If there are other losses, the company can claim compensation.

The reason why it is determined that the issuance of shares in violation of authorization revocation regulations is invalid is that: Firstly, the determination of mandatory and arbitrary norms in the Company Law is very difficult, and the accurate determination of the nature of norms is of great significance for determining the effectiveness of corresponding legal acts. Therefore, it is advisable to directly clarify the normative attributes and the legal effects of violating this provision in the Company Law. Secondly, when issuing shares in violation of authorization withdrawal rules, how to handle the issuance behavior involves balancing the trust interests of bona fide counterparties and the control interests of existing shareholders. Protecting the interests of one party will inevitably harm the interests of the other party. From a legal perspective, if the board of directors violates the revocation of authorization rules by issuing new shares, the board of directors does not have legal authorization, and its behavior constitutes unauthorized agency. Moreover, the company's articles of association contain records of shareholders authorizing the board of directors to issue company capital, which is sufficient to constitute the appearance of rights. Therefore, it meets the constitutive requirements of apparent agency. This issuance behavior should be effective for bona fide counterparties and should protect the trust interests of bona fide counterparties. However, if the issuance of new shares is deemed effective at this time, the control of the original

⁴⁹ Refer to Liu Jiayuan's "On the Local Introduction and Operation Regulations of Authorized Capital System", published in the Journal of Jilin University of Business and Economics, 2023, Issue 2, page 105.



shareholders will be lost, and this damage is too great for the original shareholders. After years of sedimentation and operation, the original controlling shareholder has gained control of the company. Once the control is changed, years of effort and effort are destroyed, and even if they resort to court, the losses suffered are difficult to assess and compensate. In addition, when the company's control is transferred, the transfer of control is likely to be irreversible, and the original shareholders are constrained by the new controlling shareholders, making it difficult to regain control of the company. In contrast, if the issuance of new shares is deemed invalid, although it damages the trust interests of bona fide counterparties, the degree of damage is easier to assess and the damage to the counterparties is lighter. After weighing the pros and cons, it is advisable to explicitly exclude the application of the rule of agency by estoppel through legislation, and directly stipulate that the issuance of shares that violate the authorization withdrawal rule is invalid. This can more directly protect the interests of existing shareholders and avoid irreversible losses caused by the change of control caused by the issuance of new shares.

6.3 Establish a pre-, in-process, and post-relief mechanism for improper issuance

At present, China lacks corresponding relief mechanisms for improper issuance of new shares, leading to a lack of relief channels for stakeholders who have suffered losses. Suggest setting up remedies for improper issuance at three levels: pre, during, and post.

As a pre-emptive remedy, the board of directors should establish an obligation to disclose information and a shareholder objection mechanism, requiring the board of directors to inform shareholders of relevant information about the issuance of new shares before issuing them, including the number of shares to be issued, the proposed issuance price, whether the issuance of new shares will cause a change in control, and the degree of dilution of existing shares after the issuance of new shares. At the same time, shareholders are granted the right to raise objections within a period. The objections raised by shareholders shall be reviewed by the board of directors, and a decision on whether to modify the issuance plan shall be made based on this. If the board of directors does not make any modifications, the shareholders may request the supervisory board to stop the issuance or request an extraordinary shareholders' meeting to make corresponding resolutions regarding the issuance of new shares.

As a remedy in the matter, the provisions of Article 210 of the Japanese Company Code⁵⁰ can be referred to, granting damaged shareholders the right to request the court to suspend the issuance of new shares. If the court makes a decision to temporarily suspend the issuance, the company's new share issuance will be suspended.

As a post-event remedy, the damaged shareholders can request the court to confirm that the issuance of new shares is invalid, unfounded, or revocable. If a director suffers losses, he/she may also demand that the director who violates his/her fiduciary duty bear compensation liability.

⁵⁰ Article 210 of the 2005 Japanese Company Code states that in the following situations if there is a risk of shareholders being in an unfavorable position, shareholders may request the company to stop issuing stocks or disposing of treasury stocks related to the issuance mentioned in Article 199 (1): (i) when issuing such stocks or disposing of treasury stocks violates laws, regulations or the company's articles of association Issuing such stocks or disposing of treasury stocks in a severely unfair manner.



6.4 Allow limited companies to choose whether to apply the authorized capital system

As mentioned earlier, although it is generally believed that the ownership and management rights of limited liability companies are not completely separated, there are many large and highly separated limited companies in practice, which also have a strong demand for efficient financing. It is advisable to include limited liability companies within the scope of companies that can choose to apply the authorized capital system and leave it to the autonomy of the company's will so that the company can make choices based on its actual situation and choose the appropriate capital formation model for the company according to its situation.

7. summary and conclusion

China's company law has undergone thirty years of development and achieved significant achievements, playing an important role in promoting the development of China's market economy. This article provides a detailed overview of the legislative evolution of China's company law in terms of the capital formation system. From the strict statutory capital system implemented by the first Company Law in 1993, to the somewhat relaxed statutory capital system in 2005, and then to the establishment of the fully subscribed capital system in 2013, as well as the introduction of the authorized capital system in this revision of the Company Law, China has gradually relaxed its control over company capital and expanded the space for company autonomy. This development trajectory is in line with global trends, highlighting the pace of China's corporate law aligning with the world.

This article believes that the introduction of the authorized capital system in the revision of China's Company Law marks significant progress. The introduction of the authorized capital system not only compensates for the shortcomings of the subscription system but also returns the right to issue shares to the company, thereby significantly improving the efficiency of the company's business decision-making. In addition, the introduction of the authorized capital system will significantly reduce the financing costs of Chinese companies and further improve their financing efficiency. More importantly, the introduction of the authorized capital system in Chinese company law is not only necessary but also practical and feasible. This move will not weaken the protection of creditors as people are concerned but rather provide more comprehensive protection and relief for shareholder rights.

Although the introduction of the authorized capital system in the third review of the revised draft of the Company Law is a significant change and has significant implications for improving commercial efficiency, the provisions of the authorized capital system in this revision are too simplistic, and there are still shortcomings in the system design. Firstly, there is a conflict between the authorized capital system and the subscribed capital system, and it is necessary to address the coordination issue between the two. Secondly, the lack of authorization revocation mechanisms and remedies for improper issuance results in inadequate protection for existing shareholders. Thirdly, limiting the scope of application of the authorized capital system to limited liability companies and excluding limited liability companies is open to debate.

To make up for the shortcomings of the third review of the revised draft, the author proposes the

following suggestions. Firstly, it should be clearly stipulated that when adopting the authorized capital system, shareholders need to make actual contributions to reconcile the inconsistency between the authorized capital system and the subscribed capital system. Secondly, increase the situation of revocable authorization in the event of a change of control, and specify that share issuances that violate revocable authorization are invalid. Thirdly, establish a supporting remedy mechanism for improper issuance. Before issuing new shares, the board of directors should inform shareholders of relevant information about the new share issuance, including the number of shares to be issued, the proposed issuance price, whether the new share issuance will cause a change in control, and the degree of dilution of the original shares after the new share issuance. During the issuance process, damaged shareholders should be granted the right to request the court to stop the issuance of new shares. If the court decides to temporarily suspend the issuance of new shares, the company's issuance of new shares should be suspended. After the issuance, the affected shareholders may request the court to confirm that the issuance of new shares is invalid, unfounded, or revocable. Shareholders who have suffered losses may also demand that directors who violate their fiduciary obligations bear compensation liability. Finally, limited companies should also be allowed to choose whether to apply the authorized capital system.

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