

NON-BANKRUPTCY ACCELERATION OF SHAREHOLDERS' CAPITAL CONTRIBUTION UNDER ARTICLE 54 OF THE PRC COMPANY LAW 2023

JIANQUN LIN¹, ROZANAH AB RAHMAN²,HANNA AMBARAS KHAN³

School of Business and Economics, Universiti Putra Malaysia,Guangzhou College of Commerce¹

School of Business and Economics, Universiti Putra Malaysia²

School of Business and Economics, Universiti Putra Malaysia³

linjianqun0225@gmail.com¹

rozanah@upm.edu.my²

hanna@upm.edu.my³

Abstract - This study presents an in-depth analysis of the legal framework and practical implications of Article 54 of the PRC Company Law 2023, focusing on the non-bankruptcy acceleration of shareholders' capital contribution. The study explores the legislative intent behind the provision and evaluates its effectiveness in scenarios outside of formal bankruptcy proceedings. Utilising a qualitative approach that combines legal doctrinal analysis with a comprehensive review of pertinent judicial cases, the study reveals the challenges and limitations in enforcing the acceleration of shareholders' capital contribution, as experienced by corporate creditors.

The findings reveal inconsistencies in judicial interpretations, which have led to a lack of legal predictability and undermined the confidence of corporate creditors in market transaction security. The study proposes targeted legislative enhancements aimed at strengthening legal protections for corporate creditors and fostering innovation in corporate capital and shareholder liability structures. These recommendations are designed to clarify two critical aspects of the acceleration of shareholders' capital contribution mechanism: first, the conditions under which a company is deemed "unable to pay off the due debts," which is a pivotal criterion for triggering the acceleration of shareholders' capital contribution; and second, the "entry rule," which pertains to the legal procedures and requirements that must be met for the acceleration of shareholders' capital contribution to be enforced. By addressing these two elements, the recommendations aim to facilitate a more equitable and efficient application of the acceleration of shareholders' capital contribution mechanism, thereby enhancing the legal predictability and confidence in market transaction security for corporate creditors.

The study contributes to the scholarly discourse on corporate law by offering insights into the operationalization of corporate creditors protection mechanisms and providing guidance for the judiciary on the consistent application of Article 54. It also informs policymakers on crafting a robust legal framework that ensures fairness and enhances the credibility of market transactions.

Keywords: non-bankruptcy acceleration of shareholders' capital contribution; corporate creditor protection; PRC Company Law 2023

INTRODUCTION

In the contemporary corporate landscape, safeguarding the interests of corporate creditors is essential for fair market transactions and economic stability. The Subscribed Registered Capital System (SRCS)¹, while fostering flexibility and innovation in corporate financing, has heightened the bankruptcy risks for corporate creditors. To address these concerns, the 2023 amendments to the PRC Company Law, particularly the significant revisions to Article 54, introduced a mechanism for the non-bankruptcy acceleration of shareholders' capital contribution. Despite legislative progress, the practical application of Article 54 has been fraught with challenges due to the vague criteria for

¹ The SRCS, also known as the declared capital system, is a corporate capital regime where shareholders are obligated to contribute capital to the company according to their subscribed shares, but the actual payment of such contributions is not required to be immediate upon the company's establishment. Instead, shareholders commit to pay the subscribed capital within a specified period or upon the occurrence of certain conditions.



determining how a company is deemed to be "unable to pay off the due debts" and the "entry rule", as well as the inconsistencies in judicial interpretations. This study aims to re-examine Article 54, scrutinise its legislative intent, and evaluate its efficacy in non-insolvency contexts, identifying shortcomings and proposing enhancements to strengthen the legal protection for corporate creditors.

This study is significant because it seeks to bridge the gap between legislative intent and practical application, offering insights into the operationalisation of corporate creditors protection mechanisms. It is expected to contribute to scholarly discourse, inform consistent judicial application, and guide policymakers in crafting a robust legal framework for corporate creditors protection. The scope of this paper is confined to analysing Article 54 within the PRC Company Law 2023, focusing on the non-bankruptcy acceleration of shareholders' capital contribution. The qualitative methodology integrates legal doctrinal analysis with a review of pertinent judicial cases to elucidate the law's practical implications and challenges. The study is structured to provide an interpretive analysis of Article 54, a judicial case analysis, a discussion of legal challenges with recommendations, and a synthesis of the findings and conclusions.

1. Interpretation of Article 54 in the PRC Company Law 2023

This study examines the concept of the "non-bankruptcy acceleration of shareholders' capital contribution", which pertains to the early fulfilment of shareholders' capital contributions outside the context of bankruptcy. The subsequent sections will delineate the pertinent definitions.²

The concept of the acceleration of shareholders' capital contribution refers to shareholders electing to fulfil their subscribed capital obligations prior to the expiration of the payment period stipulated in the company's articles of association. Under the SRCS, the law confers a term benefit upon shareholders, allowing them to legally agree upon the payment schedule for capital contributions within the articles of association. The law affirms and protects the shareholders' interest during the term until the expiration of the contribution period; however, under certain conditions, shareholders may be compelled by law to advance their capital contributions (Yue, 2024).³

Article 35 of the PRC Enterprise Bankruptcy Law, effective from 2007, and Article 22 of the Interpretation of the Company Law (II) 2014 Amendment, effective from 2008, establish the rule for acceleration of shareholders' capital contribution post-bankruptcy application acceptance. The rationale for this acceleration is rooted in the requirement for debt and claim liquidation during bankruptcy and dissolution proceedings, which may culminate in a company's cessation of existence, rendering the contribution period moot. This perspective is widely accepted in both the theoretical and the practical domains.⁴

The reforms to the PRC Company Law 2013 did not introduce provisions for the acceleration of shareholders' capital contribution, attributing the contribution period entirely to shareholder autonomy. This has led to issues such as the arbitrary inflation of contribution amounts and the exploitation of extended contribution periods to evade capital contribution responsibilities. Consequently, when a company is unable to settle its debts, creditors face difficulties in compelling shareholders to fulfil their capital contribution obligations in advance, resulting in numerous practical disputes. The applicability of the accelerated maturity rule in non-bankruptcy scenarios and its operational specifics have become contentious points in judicial practice. The Supreme People's Court has shown a tendency to facilitate acceleration through bankruptcy applications, leveraging

² A meticulous review of the existing literature reveals that the phrase "accelerated expiry of shareholders' capital contributions" does not represent an established legal term but has been articulated in Chinese scholarly discourse to encapsulate a specific concept. As a result, the term "accelerated expiry of shareholders' capital contributions" has emerged as a "localised" expression within the academic community.

³ Yue, W. B. (2024). Legislative choices for the capital contribution model of companies. *Socialist Market Economy Legal System*. 46, (1), 150-163.

⁴ Jiang, D. X. (2019). On the "accelerated maturity" of shareholders' capital contribution obligations: Affirming the functional value of "non-bankruptcy acceleration." *Social Sciences*, 41(2), 98-113.



Article 35 of the PRC Enterprise Bankruptcy Law to protect creditor interests.⁵ However, this approach may lead to the prolonged and costly realisation of rights and the potential abuse of bankruptcy procedures, impacting the rational allocation of judicial resources. To address these concerns, Article 6 of the Minutes of the National Court Commercial Trial Work Conference introduces provisions for the non-bankruptcy acceleration of shareholders' capital contribution, delineating two scenarios.

In summary, the "non-bankruptcy acceleration of shareholders' capital contribution" concept posits that as long as a company exhibits an inability "to pay off the due debts", the shareholders' term interest is waived, and creditors may demand capital contributions within the scope of the contribution, irrespective of the expiration of the contribution period. This perspective, which challenges the term interest of shareholders under the contribution system, is highly controversial.⁶ The theoretical position is divided into affirmative and negative views, as well as those that favour compromise. The affirmative stance supports creditors being allowed to claim the accelerated fulfilment of capital contribution obligations regardless of insolvency status, fostering a rational order of contributions and debt repayment. Conversely, the negative view advocates accelerated maturity enforcement only at the stage of corporate insolvency to uphold the sanctity of the capital contribution contract and the principle of honouring contracts. Those favouring compromise suggest that circumstances should be differentiated, such as permitting accelerated maturity when a company faces difficulties or when involuntary creditors make claims.⁷

In practice, judicial decisions on the acceleration of shareholders' capital contribution have yielded divergent outcomes, with some courts favouring the non-bankruptcy acceleration of shareholders' capital contribution to reduce costs and realise creditor claims, while others have adopted a conservative approach to protect the interests of all creditors.

Article 54 of the PRC Company Law 2023 provides a clear legal framework for addressing "non-bankruptcy acceleration of shareholders' capital contribution" scenarios. This amendment, which carefully balances the interests of the company, the shareholders, and the creditors, has significant implications for both legal theory and practice. It innovates in the areas of company capital and shareholder liability, enhances legal predictability, and ensures fairness in judicial proceedings.⁸ The article also reflects the law's adaptability to new economic needs, reducing judicial inconsistency and enhancing credibility. Its core purpose is to safeguard the company's operation and solvency by enabling creditors to demand advanced capital contributions under specific circumstances, thereby providing financial support.

However, Article 54's condition of being "unable to pay off the due debts" requires further clarification since there are no explicit provisions in the law or judicial interpretations. This ambiguity has led to varied judicial decisions and ongoing discussions on the application in the Civil Code of the "entry rule" versus the direct payment mechanism.⁹

In conclusion, while Article 54 of the PRC Company Law 2023 offers a legal framework for the non-bankruptcy acceleration of shareholders' capital contribution, further refinement is needed to clarify

⁵ Yang, S.L. (2015). On the protection system of corporate creditors' interests from the perspective of the changes of the minimum registered capital system. *Commercial Research*, (453), 18-185.

⁶ Liu, K., & Zhang, Q. (2014). The legislative changes and problem solving of the corporate capital system in China. *Journal of Henan University of Economics and Law*, (5), 22-36. & Wu, Y. (2015). The abolition and challenges of the minimum registered capital requirement for companies. *People's Tribune*, (467), 99-101.

⁷ See Jiang, D. X., above n. 4 at 99

⁸ Yue, W. B. (2024). The logic of creditor protection in company law: From the perspective of the lack of function of behavioral law and the making-up function of organizational law. *Politics and Law*, (2), 80-96.

⁹ Liu, G. X. (2024). Several issues on the application of the new Company Law. *Law Application*, (6), 3-34.



the criteria for being "unable to pay off the due debts" and the application of the "entry rule". Future analysis will examine judicial practice, synthesise court perspectives, and distil practical experience to propose improvements to Article 54.

2. Legal Challenges

2.1 The Determination of a Company being "unable to pay off the due debts"

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The scholarly discourse surrounding the determination of a company's inability "to pay off the due debts" has yielded four predominant theories, each of which has distinct criteria. (i) Subjective Insolvency Theory: This perspective posits that a company's unwillingness to pay, whether overt or implied, signifies an inability to settle debts. This criterion is primarily subjective, focusing on the company's intent to repay rather than an objective assessment of its financial status. (ii) Balance Sheet Insolvency Theory: Proponents of this view suggest that a company should be considered insolvent only when its total liabilities surpass its assets, thereby leaving an insufficient fund to meet creditor claims. (iii) Liquid Assets Insufficiency Theory: This approach evaluates a company's solvency through its cash flow statement, income statement, and balance sheet. Insolvency is deemed to be present if the company's current assets fail to cover its debts. (iv) Enforcement Insolvency Theory: This perspective holds that a company's insolvency is contingent upon the judicial enforcement of its debts. Only when debts remain unpaid after enforcement can the company be officially deemed "unable to pay off the due debts".¹⁰

In the judicial arena, two principal viewpoints have emerged: (i) Subjective Insolvency Theory: This stance posits that a company, regardless of its capacity to pay, may be deemed unable to pay its debts if there is no justifiable reason to withhold payment. (ii) Enforcement Insolvency Theory: This perspective maintains that a company is insolvent only after a court enforcement action reveals an inability to satisfy creditors' claims.

The divergence between theoretical propositions and practical applications might result in inconsistent judicial outcomes for similar cases, potentially undermining the judiciary's credibility. Therefore, it is imperative to refine the criteria for establishing an inability "to pay off the due debts" to ensure judicial consistency, legal predictability, and stability.

An analysis of academic discourse and judicial practice underscores the necessity for a unified approach to determining an inability "to pay off the due debts". Achieving this will not only bolster the uniformity of judicial decisions but also preserve legal authority and market order. Further scholarly inquiry and judicial elucidation are required to crystallise this benchmark.

2.2 Entry Rule

The scholarly community exhibits a bifurcated perspective regarding the entry rule, which is a pivotal mechanism in corporate finance law. Advocates of the entry rule contend that it is indispensable for

¹⁰ Zhu, C. Y. (2021). Reflections on the systematic remolding of China's corporate capital system. *Legal Science (Journal of Northwest University of Political Science and Law)*, (3), 48-64.

preserving the genuineness and completeness of a company's registered capital (translated as "registered capital" or "capital contribution", depending on the context). For instance, Wang and Li have underscored its significance in ensuring the sufficiency of corporate capital.¹¹ Similarly, Liu has elucidated that the rule is instrumental in precluding individual creditors from securing an inequitable advantage.¹²

In contrast, detractors have raised concerns that the entry rule might dilute the rights and interests of individual creditors. The entry rule has led to apprehension regarding the inadequate safeguarding of creditor rights and interests, and a more nuanced institutional construct is needed to reconcile the interests of disparate creditors.¹³

The judiciary reflects a similar dichotomy in its stance on the entry rule. Certain judicial quarters have endorsed the rule, advocating that it underpins the stability of corporate capital and guarantees a company's capacity to fulfil its obligations to all creditors. Nevertheless, other judicial forums have posited that the entry rule might, under certain circumstances, impede creditor gratification, particularly in instances where a company possesses sufficient assets but is impaired by inefficient management. The ensuing compilation encapsulates the judicial precedents aligned with and in opposition to the entry rule:

Table 1.1: Categorisation of Judicial Opinions Endorsing and Opposing the Entry Rule

Support for Entry Rule	Opposition to Entry Rule
The rule is seen as instrumental in maintaining the stability of corporate capital, ensuring the continuous operation of the company, and fulfilling responsibilities to all creditors.	The rule may, in certain circumstances, delay the satisfaction of creditors, particularly when the company has sufficient assets but faces managerial issues.
Emphasizes that the rule prevents individual creditors from gaining an unfair advantage through accelerated maturity, thereby protecting the collective interests of creditors.	Points out that the rule might infringe upon the term interests of individual creditors, especially when the company is not in urgent need of funds.
Suggests that the rule enhances transparency and accountability in corporate governance by requiring shareholders to contribute capital in advance to address financial difficulties.	Argues that the rule may not be applicable in enforcement proceedings, as these should consider the urgent needs of individual creditors.
Courts supporting the rule may believe it contributes to legal stability and predictability, providing clear legal expectations for companies, shareholders, and creditors.	Courts not supporting the rule may argue that it requires more nuanced institutional design to balance the interests of different creditors.

Source: Developed by the Author

¹¹ Wang, Y., & Li, Y. Z. (2022). Critique of the logic of capital credit and reshaping the protection mechanism for company creditors. *Political Science and Law Forum*.(4),108-119

¹² Liu, J. H. (2022). The concept and institutional reshaping of a creditor-friendly Company Law. *Journal of the National Prosecutors College*, 30(3),140-160.

¹³ Liu, J. H. (2024). On the Advantages and Disadvantages of the Registered Capital Subscription System: A Discussion on the Dynamic Balance between Term Interest and Transaction Safety. *Academic Forum*.(1),44-59.



Following the revision of the PRC Company Law 2023, although legislative and judicial interpretations did not explicitly stipulate the adoption of the "entry rule", judicial practice has predominantly favoured the "the direct settlement rule" from a case law perspective. For instance, in a case adjudicated by the Jiangyan District People's Court of Taizhou City, Jiangsu Province, the court determined that, in accordance with Article 54 of the PRC Company Law 2023, creditors are vested with the prerogative to demand early payment of capital contributions from shareholders (Jiangyan District People's Court, 2024). Additional cases subscribing to this view are listed in Table 1.6 for reference.

The discourse on the entry rule underscores the intricacies of company law in reconciling the interests of shareholders and creditors. Future scholarly inquiry should concentrate on enhancing the objectivity and applicability of the criteria to ensure the stability and predictability of the legal framework.

3. Recommendations

Section 3 builds on the previous discussion by honing in on the concrete implementation of the acceleration of shareholders' capital contribution,. This section meticulously analyses the criterion of being "unable to pay off the due debts" and the "entry rule", as delineated in Article 54 of the PRC Company Law 2023. It also explores the precise definition of this criterion in practical application. Moreover, it examines how various judicial bodies have adjudicated based on this standard and outlines the potential ramifications of these rulings on the protection of corporate creditors.

Subsequently, the text presents specific legislative recommendations designed to clarify and refine the conditions and procedures for the acceleration of shareholders' capital contribution,. These proposals aim to offer more robust legal protection for corporate creditors while ensuring transparency and fairness in corporate governance. By engaging in a critical analysis of the current legal framework and an appraisal of judicial practice, the discourse endeavours to reconcile the interests of shareholders and creditors, encourage the ongoing refinement of the legal system, and augment the law's adaptability and efficacy.

3.1 Criterion of Cessation of Payment

This section offers an in-depth analysis of the legal provisions regarding the criterion of being "unable to pay off the due debts" under Article 54 of the PRC Company Law 2023, and the challenges encountered in its judicial application are discussed. The discourse reviews the academic debate surrounding the alignment of this criterion with the concept of cessation of payment, noting the impact of these theoretical divergences on legal application and judicial practice.¹⁴

The PRC Company Law 2023 posits being "unable to pay off the due debts" as the sole condition for the acceleration of shareholders' capital contribution. However, the practical interpretation of this provision, particularly in cases of insolvency or wilful non-performance, warrants further elucidation.¹⁵ Judicial practice has witnessed the adoption of varied standards by different courts, reflecting a spectrum from leniency to strictness.

To demystify the conditions under which a company is deemed to be unable to pay its debts as they fall due, there is an exigency for enumerative stipulations. These include delineating procedures by which companies or creditors can invoke the acceleration of shareholders' capital contribution and establishing preconditions for seeking judicial redress. With the advent of the PRC Company Law 2023, it is imperative that pertinent judicial interpretations be expeditiously revised to bolster the

¹⁴ See Liu, J. H., above n. 13 at 46

¹⁵ See Liu, G. X., above n. 9 at 10



institutional framework for the proper application of the acceleration of shareholders' capital contribution.¹⁶

Upon scrutinising the interplay between Article 54 of the PRC Company Law 2023 and Article 2 of the PRC Enterprise Bankruptcy Law, discernible disparities emerge, despite superficial textual similarities. The criteria in the PRC Company Law 2023 for being "unable to pay off the due debts" differ from the insolvency causes outlined in the PRC Enterprise Bankruptcy Law. The latter imposes more rigorous standards, necessitating proof of the insufficiency of the debtor's assets to cover all debts or an evident lack of payment capacity, as opposed to the Company Law, which focuses on the debtor's ability to satisfy discrete debts.¹⁷

Interpretation 1 of the PRC Enterprise Bankruptcy Law delineates three elements of being "unable to pay off the due debts": the lawful establishment of creditor-debtor relationships, the expiration of debt performance deadlines, and the debtor's failure to fully settle debts. This interpretation effectively transitions the "inability to pay" concept from the bankruptcy law to a "cessation of payment", emphasising the debtor's external conduct in debt settlement over asset status (Supreme People's Court, 2013).

During the legislative process, the deletion of the phrase "obvious lack of solvency" from the First Review Draft to the Second Review Draft of the Revised PRC Company Law 2023 signifies how the legislature intended to differentiate the conditions for accelerated maturity from bankruptcy thresholds. This amendment reflects a legislative emphasis on the independence of the accelerated maturity procedure and a departure from the solvency assessment criteria in the PRC Enterprise Bankruptcy Law (Law Commission of the Standing Committee of the National People's Congress, 2023).

Scholars are divided in their interpretations of Article 54 of the PRC Company Law 2023, with some identifying a distinction between being "unable to pay off the due debts" and the insolvency criterion in the Bankruptcy Law's insolvency criterion, thus advocating a cessation of payment concept. In judicial practice, courts have tended towards a lenient interpretation, applying the accelerated maturity rule when a company is unable to pay debts as they fall due, irrespective of the expiration of shareholders' capital contribution terms.¹⁸

The author aligns more closely with the cessation of payment concept by positing that the criterion of being "unable to pay off the due debts" in Article 54 of the PRC Company Law 2023 should be distinct from the insolvency threshold of the Bankruptcy Law. This interpretation harmonises with the strict criteria of the Bankruptcy Law and maintains the internal logical consistency of the commercial legal system. Judicial decisions often concur with this view to protect creditor interests and foster legal fairness and efficiency.

The author advocates that the determination standard for being "unable to pay off the due debts" should be differentiated from the insolvency threshold of the Bankruptcy Law, shifting its connotation from an "inability to pay" to a "cessation of payment" in judicial practice. Although the Bankruptcy law has a more stringent definition of an "inability to pay", focusing on the debtor's capacity rather than intent, the accelerated maturity procedure of the Companies Act does not demand the complex social value judgements inherent in the Bankruptcy Law. The author contends that companies should be permitted to avert the acceleration of shareholders' capital contribution by demonstrating

¹⁶ Zhao, X. D., & Liu, B. (2024). *New Company Law Application and Interpretation of Cases Published by the Supreme People's Court*. 1st ed. (p. 155).

¹⁷ See Liu, J. H., above n. 13 at 47

¹⁸ See Jiang, D. X., above n. 4 at 101



solvency, underscoring the significance of judicial fact-finding and the pursuit of logical consistency within the commercial legal system.¹⁹

The author proposes that the conditions for establishing being "unable to pay off the due debts" could be interpreted as follows: (1) the legal establishment of a debt relationship between a company and its creditors; (2) the expiration of the deadline for the company's debt fulfilment to its creditors; and (3) the company's failure to fully discharge its debts, which implies the company's actual non-payment without necessitating an execution process.

Furthermore, the evolution of judicial practice has set forth new theoretical demands. As case types diversify and the legal landscape shifts, theories must continually evolve to accommodate judicial needs. Court rulings might prompt the academic community to delve deeper into the definition of being "unable to pay off the due debts" and explore ways to balance the protection of creditor and shareholder interests.

In conclusion, an interactive dynamic exists between judicial practice and theory. Theory offers guidance to judicial practice, while judicial practice propels theoretical advancement. In adjudicating on the application of Article 54 of the PRC Company Law 2023, court decisions must be grounded in existing theory while considering case-specific circumstances and societal impact to achieve legal fairness and efficiency. Through this synergy, the legal system's continuous refinement would be fostered, enhancing the law's adaptability and efficacy.

3.2 The Direct Settlement Rule

Section 2.2, entitled "the direct settlement rule", delves into the complexities surrounding the approach taken in the newly revised PRC Company Law 2023 to the "entry rule", a topic that has garnered significant attention in both scholarly and practical spheres. The rule mandates that when a company encounters an inability to settle debts as they fall due, shareholders must advance their subscribed capital contributions, which are to be allocated to the company's assets rather than paid directly to individual creditors.²⁰ This stipulation contrasts with the direct payment mechanism outlined in the Civil Code concerning the subrogation rights of creditors, thereby igniting extensive debate on the safeguarding of creditor interests.

Some scholars have posited that under the Civil Code, creditors exercising subrogation rights can obtain satisfaction directly from the debtor's counterparty. However, Article 54 of the revised PRC Company Law 2023 explicitly directs that advanced contributions by shareholders are to be attributed to the company rather than paid directly to creditors, thereby somewhat limiting the rights of creditors.²¹ It has been contended that while the Civil Code makes general provisions, the Company Law, with its special provisions, should take precedence in cases of ambiguity or omission regarding the "entry rules", necessitating reliance on the Civil Code's relevant provisions (Shanghai High Court, 2024).

Zhao and Zou have argued in favour of the "entry rule", suggesting that it ensures equitable payment among creditors and supports the company's capitalisation and the collective interests of creditors.²² Conversely, Jiang has proposed that under certain circumstances, allowing shareholders' capital contribution liabilities to directly satisfy creditors who have initiated legal action, particularly when the company meets insolvency conditions but does not file for bankruptcy, could protect the lawful

¹⁹ See Liu, G. X., above n. 9 at 11

²⁰ See Liu, J. H., above n. 13 at 48

²¹ Li, N. N. (2024). Perspective | The new Company Law comes into effect today! The impact of the new Company Law from the perspective of creditors. Law News Agency. Retrieved from <https://mp.weixin.qq.com/s/Zx5RbYzw00b1hMlz-eypyQ>

²² Zhao, X. D., & Zou, X. G. (2024). The theoretical basis and systemic development of the contribution acceleration and disenfranchisement system. *China Review of Administration of Justice*. (3), 29-38.



rights and interests of proactive creditors.²³ Additionally, some scholars have recommended flexibility in choosing whether funds should be credited to the company or individually satisfied to creditors based on varying circumstances, noting that individual creditor satisfaction does not preclude other creditors from pursuing a company's insolvency (Shanghai High Court, 2024).

The controversy over the "entry rule" post-implementation of the PRC Company Law 2023 was exemplified in a case before the Beijing Xicheng District People's Court. The plaintiff, Li, sued shareholder Zhang for the company's failure to pay outstanding wages, demanding that Zhang fulfil his capital contribution obligations in advance as per the PRC Company Law 2023. The court ruled in favour of the plaintiff, determining that the company was unable to settle its debts and that shareholder Zhang should accelerate his capital contribution. This judgement challenges the traditional "entry rule", permitting creditors to recover assets directly from shareholders, thereby indicating enhanced judicial protection of creditor interests. Nonetheless, the debate over the "entry rule" pertains to whether to adhere to the principle of crediting shareholders' contributions to the company before creditor payment; how to protect creditors while considering the interests of shareholders over time - to prevent unnecessary harm - remains a delicate issue in judicial practice. The case underscores the challenges and dilemmas involved in strengthening creditor protection in the judicial application of the PRC Company Law 2023.

Liu advocates adherence to the entry rule, emphasising the source and function of Article 54 of the PRC Company Law 2023, viewing it as a solution to capital maturity mismatch and a matter of operational and managerial financing costs and mechanisms that is akin to a simple bankruptcy clause for creditors. He believes the acceleration of shareholders' capital contribution regime carries the dual functions of corporate funding mismatch and bankruptcy provisions, arguing that judicial interpretation should distinguish between them.²⁴

Li offers a divergent perspective by advocating the resolution of company and shareholder liabilities in a single litigation through the non-bankruptcy acceleration of shareholders' capital contribution, aligning with the content of Article 54 of the PRC Company Law 2023 and providing an optimised and convenient remedy for a company's creditors. He argues that Article 54 is not an insolvency provision and that the legislation has clearly differentiated the conditions for the commencement of insolvency proceedings. He emphasises that equitable satisfaction should be considered in the insolvency context, whereas in the non-insolvency context, creditors should be paid in order of priority. Moreover, Li suggests that other creditors could achieve equitable satisfaction by initiating insolvency proceedings and that a judgement against a shareholder for supplementary liability does not directly acquire priority.²⁵

This study advocates the adoption of the "direct settlement rule" under the framework of Article 54 of the PRC Company Law 2023, allowing creditors to recover assets directly from shareholders when a company is unable to settle its debts as they fall due, rather than insisting that shareholders' contributions be classified as company assets and then settling claims. This stance is predicated on the Creditor Priority Theory, suggesting that under certain circumstances, creditors' rights and interests should be given priority protection to ensure the timely realisation of claims and maintain transaction security.²⁶

The implementation of the direct settlement rule not only provides creditors with a prompt and effective remedy but also incentivises shareholders to fulfil their capital contribution obligations, thereby enhancing the company's solvency. Furthermore, the principle aids in improving judicial

²³ See Jiang, D. X., above n. 4 at 103

²⁴ See Liu, G. X., above n. 9 at 12

²⁵ See Li, N. N., above n. 21

²⁶ Zou, H. L. (2024). The Development of the Subscribed Capital System Based on Corporate Autonomy. *Global Legal Review*, (1), 5-20.



efficiency and circumventing the protracted litigation and resource wastage associated with insolvency proceedings.²⁷ It also reflects the protection of proactive creditors, ensuring reasonable compensation when a company confronts financial difficulties.

However, the application of the direct settlement rule does not disregard the maintenance of company capital and the rights of other stakeholders. Instead, it necessitates a careful balance of the company's ability to continue as a going concern and the interests of shareholders over time while protecting creditor interests. In judicial practice, courts must carefully consider the specific circumstances of a case to achieve a balance between the interests of all parties and ensure the law's fairness and efficiency (Shanghai High Court, 2024).

In light of these observations, it is recommended that judicial interpretation and practice refinement be used to further clarify the conditions, boundaries, and procedures for the application of the direct settlement rule. This would facilitate the correct understanding and application of Article 54 of the PRC Company Law 2023, ensuring the integrity of a company's capital and the stability of market transactions while protecting the rights and interests of creditors. In doing so, the interests of creditors, companies, and shareholders can be better harmonised to achieve the law's ultimate dual purpose: fairness and justice.

CONCLUSION

This in-depth analysis of Article 54 of the 2023 PRC Company Law clarifies the application and challenges of the non-bankruptcy acceleration of shareholders' capital contribution in legal theory and practice. The study demonstrates that while Article 54 provides additional protective mechanisms for corporate creditors, further clarification and refinement are needed in its practical operation.

The recommendations proposed in this paper aim to elucidate the criteria for being "unable to pay off the due debts" and the "entry rule", as well as optimise the conditions and procedures for the acceleration process. These suggestions are designed to offer more robust legal protection while ensuring transparency and fairness in corporate governance. By critically analysing the current legal framework and appraising judicial practice, the author endeavoured to reconcile the interests of shareholders and creditors, encourage the ongoing refinement of the legal system, and augment the law's adaptability and efficacy.

Ultimately, this study highlights the interactive dynamics between legal theory and practice. Theory provides guidance for judicial practice, while judicial practice propels theoretical advancement. In adjudicating on the application of Article 54 of the PRC Company Law 2023, court decisions must be grounded in existing theory while considering case-specific circumstances and societal impacts to achieve legal fairness and efficiency. Through this synergy, the continuous refinement of the legal system is fostered, enhancing the law's adaptability and efficacy.

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²⁷ Peng, B. (2024). Shareholders' obligation to contribute capital under the new "Company Law." *China Review of Administration of Justice*, (3), 39-48.



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