On the Limitation of Voting Rights of Shareholders with Defective Capital Contribution

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Abstract: Under the subscribed capital system, the qualification of shareholders is obtained based on the commitment of subscribed capital. Although the rights of shareholders are obtained based on the identity of shareholders, it does not mean that their rights can be fully enjoyed. In practice, there are disputes about whether and how the voting rights of shareholders with defective capital contribution are limited. This paper attempts to discuss this issue from different angles.

1. Introduction

Defining the legal attributes of defective capital contribution and voting right is the premise of research. Therefore, it is of great significance to clarify the specific connotation of defective capital contribution and the legal attribute of voting right in this paper, so as to pave the way for the justification of the limitation of voting right.

2. Definition and Classification of Defective Capital Contribution

Defective capital contribution refers to the behavior that the property and behavior used by shareholders to make capital contribution do not conform to or do not fully conform to the commitment of capital contribution when the laws and regulations, the articles of association or the capital contribution agreement set clear rules for shareholders to make capital contribution.

There are different views on the classification of defective investment. According to different standards, it can be divided into slight defective capital contribution and serious defective capital contribution, defective capital contribution in the process of establishment and capital increase, etc. Based on Article 16 of the interpretation of company law (3) and combined with the practical situation, the defective capital contribution can be divided into three categories: failure to perform the obligation of capital contribution, failure to fully perform the obligation of capital contribution and withdrawal of capital[1].

3. The Present Situation and Problems of the Limitation of Voting Rights of Shareholders with Defective Capital Contribution

3.1 The Current Situation and Problems of Legislation and Judicature
3.1.1 Legislative Level

In the aspect of legislation, the current law has basically set up a rule system for the limitation of shareholders' rights with defective capital contribution, but the specific right limitation is still not perfect. At present, there are no relevant regulations on how to deal with such problems of joint stock limited companies[2]. Article 16 of the interpretation of the company law (3) restricts the listed three rights of shareholders. After analysis, the characteristics of the limitation system of shareholders with defective capital contribution in China are as follows: first, it adopts the mode of reverse negation. Second, emphasize corporate autonomy. According to the relevant provisions, the premise of starting the restriction of shareholders' rights is the articles of association. Third, the scope of rights that can be limited in Article 16 is “shareholders' rights such as the right to claim for profit distribution, the right to preempt new shares, and the right to claim for the distribution of surplus property”. It is concluded that there is no systematic and cultural system of voting right of shareholders with defective capital contribution in China. It is not clear whether the voting right can be stipulated in Article 16, and whether it belongs to Article 16, etc.

3.1.2 Judicial Level

Due to the lack of legislation, there is no unified theory about whether the voting rights of shareholders with defective capital contribution are restricted in judicial practice. In recent years, the supreme law has begun to think that it is necessary to restrict the rights of shareholders with defective capital contribution, but some local courts hold different opinions. According to the selected cases after searching for such keywords as “defective capital contribution” and “voting right” in the judicial document website, in these cases, it is not directly against a shareholder's voting right to sue, but by identifying the effectiveness of the resolution of the shareholders' meeting to laterally verify whether the voting right of shareholders with defective capital contribution is limited.

According to the reasoning part of the judgment on this issue, there are mainly these reasons for supporting or not supporting the limitation: on the one hand, the reasons for supporting the limitation can be summarized as follows: first, according to the principle of “rights and obligations are unified, interests and risks are consistent”, although the defect of shareholders' capital contribution does not affect the acquisition of shareholders' identity, once the shareholders violate the obligation of capital contribution Therefore, their rights should also be limited. Secondly, in order to respect the autonomy of the company, Article 16 of the third interpretation gives the articles of association and the shareholders' meeting the right to limit the rights of shareholders with defective capital contribution. However, if the articles of association does not provide for this, it is not appropriate for the court to make a decision to limit the rights on its own initiative. On the other hand, the reasons for not supporting the limitation can be summarized as follows: first, the qualification of shareholders obtained by investors due to their capital contribution, even if they violate the obligation of capital contribution, can not deprive the identity of shareholders. Second, the right to vote belongs to the right of mutual benefit, which is different from the principle of limiting the right of self-interest. The establishment of the voting right is to ensure the normal management and daily operation of the company, without regard to the performance of shareholders' capital contribution obligations. Third, according to the principle of equal rights and obligations, the shareholders with defective capital contribution should bear the responsibility of supplementary liquidation for the company's debts, rather than not performing the remaining capital contribution obligationsl[3].
3.2 Theoretical Debate on the Limitation of Voting Rights

In 2013, “Yu miaogan and Liang Dali shareholders' meeting resolution validity dispute appeal case” triggered whether to limit the voting rights of shareholders with defective capital contribution? One party thinks that the voting rights of shareholders with defective capital contribution should not be limited. Because the voting right belongs to an inherent right, which is based on the status of shareholders. It should not be deprived or restricted by the articles of association or the resolution of the shareholders' meeting. Since it is clear that shareholders with defective capital contribution enjoy the status of shareholders, their rights can not be deprived or restricted. On the other hand, shareholders' voting rights should be limited.

The author agrees with the latter point of view. According to Article 42 of the company law, this article reflects that limited companies can restrict shareholders' voting rights based on the articles of association. From the negative argument, it can be concluded that China adopts the bottom line thinking, that is, the attitude of not prohibiting shareholders' voting rights. Limiting the voting rights of shareholders with defective capital contribution conforms to the principle of the unity of rights and obligations, and can show fairness and justice in practice. To sum up, the voting rights of shareholders with defective capital contribution should be appropriately limited.

4. Analysis on the Legitimacy of Voting Right of Shareholders with Defective Capital Contribution

4.1 The Logic of Power Limitation

First of all, the right to vote is based on the commitment of capital contribution. Under the subscription system, the actual payment of shareholders has nothing to do with the identity of shareholders, and the qualification of shareholders is the right to vote[4]. But there are some legal consequences, such as not making capital contribution, withdrawing capital and not returning it after urging. Therefore, the shareholders who have not been removed shall have the right to vote in accordance with the law. Secondly, to fulfill the commitment of investment is a necessary prerequisite for the exercise of complete voting rights. Shareholders' voting rights are limited to the proportion of their subscribed capital contribution. Article 42 of the company law reflects the relationship between the exercise of voting rights and the situation of capital contribution, but there are great differences in the understanding of “proportion of capital contribution” in practice. Based on the understanding of the company law system, the author thinks that shareholders' voting rights should be based on the proportion of subscribed capital.

4.2 The Legitimacy of Power Limitation

According to the principle of unity of rights and obligations, rights and obligations have the relationship of unity of opposites. When it comes to the voting rights of shareholders with defective capital contribution, if they do not fulfill their capital contribution obligations properly, they will not enjoy the complete rights of shareholders. Only in this way can they follow the legal principle of unification of rights and obligations. According to the principle of fairness, shareholders should be treated with the same standard. If the shareholders with defective capital contribution can also enjoy the complete right to vote, it is obviously against the principle of fairness, and it is difficult to form a benign incentive mechanism for the shareholders who abide by the contract. Therefore, in order to prevent major shareholders from using resolutions to damage the legitimate rights and interests of the company, the voting rights of shareholders with defective capital contributions should be limited.
4.3 The Rationality of Power Limitation: Based on the Consideration of Law and Economics

For the defective shareholders, litigation or administrative supervision can be used to remedy after the event, but the time cost of limiting rights after the event is significantly higher than that of prior regulation. In judicial practice, limited liability companies mostly choose to give up litigation because of the consideration of personnel relations and litigation costs. Therefore, it is more reasonable to limit the right in advance.

Shareholders with defective capital contribution tend to be opportunistic and expect to obtain as much capital share as possible through as little actual capital contribution, so as to enjoy more voting rights and exert greater influence on the company's decision-making. If we do not restrict their rights, but allow shareholders to hold “excessive” voting rights to control the company, this tolerance will inevitably enlarge the bad incentive of defective capital contribution, and even produce “deprivation effect”. Therefore, the limitation of rights is helpful to prevent the defective investment from producing bad incentives and unlimited amplification.

5. On Perfecting the System of Limiting the Voting Rights of Shareholders with Defective Capital Contribution

5.1 Macro Institutional Framework -- the Path of Combining Autonomy with Legislation

Company legislation can make provisions on the limitation of shareholders' equity of defective capital contribution. In limited company, the legislation should leave enough autonomy space for shareholders when making such restrictions, which determines that such restrictive provisions should belong to the “presumption applicable clause” in arbitrary norms[5]. Article 34 of the company law belongs to this situation, which stipulates that the dividend right and the preemptive right of new capital subscription of shareholders of a limited company shall be in accordance with the proportion of paid in capital contribution. If all shareholders agree otherwise, it shall be excluded. Some scholars also suggest that the “presumption of inapplicability clause” can be applied to the limitation of some shareholders' rights, that is, the articles of association of a company can choose to apply the rule of limiting certain shareholders' rights in the form of special clauses. If the articles of association of a company do not explicitly choose, it is presumed that the company does not apply this rule.

In a word, the combination of autonomy and legislation should take the strategy of corporate autonomy and legislation in order to achieve the effective effect of power limitation. In practice, the controlling shareholders will manipulate the company, not only the resolution of the shareholders' meeting does not put forward the restriction of voting rights, but also the articles of association do not mention the restriction of voting rights. In this case, if there is no direct legislative restriction, the restriction system will be overhead. Therefore, while respecting the autonomy of the company, there should be legislative protection. Only in this way can we really impose practical restrictions on the voting rights of shareholders with defective capital contribution, so as to protect the interests of shareholders, the company and creditors.

5.2 Micro System Design: Suit Measures to Local Conditions

For the shareholders who have not fulfilled their commitment to make capital contribution at the time of the establishment of the company, their voting rights should be limited when they explicitly refuse to make capital contribution or discover their defective capital contribution. If they still fail to pay after being urged, their qualification as shareholders will be lost and their voting rights will be eliminated. If they make up their capital contribution later, their voting rights will be restored.
when they make up their capital contribution completely. In addition, for the shareholders who fail to fulfill the obligation of capital contribution during the capital increase, the voting rights corresponding to the capital increase commitment should be limited, that is, the shareholders have the right to enjoy part of the voting rights based on the capital contribution that has been properly performed.

Under the subscription system, it is very common to delay the investment, so the company should take positive actions to protect the interests of the company. For example, if the company makes a call within a reasonable period before the expiration of the investment period, once the investment period is expired and the obligation is not fully fulfilled, the voting right will be automatically limited. This will improve the efficiency of post regulation and minimize the company's loss. In addition, for the shareholders who pay the capital contribution in installments according to the articles of association, if they do not pay the capital contribution in each period, it will constitute delay in performance, and they should be deprived of their voting rights at the end of the next period after the reminder. If the investment obligation is properly fulfilled in the early stage, the voting right can only be partially enjoyed based on the paid in situation after the reminder.

For the shareholders who withdraw all their capital contribution, their voting rights should be limited in the delisting procedure. Once the behavior of capital withdrawal is found, its voting right should be automatically restricted according to the provisions of legislation or the articles of association, without the need for the resolution of the shareholders' meeting. This restriction continues until the company fails to pay or return the capital contribution within a reasonable period after the company's demand. The company will remove its shareholder identity through the resolution of the shareholders' meeting, and its voting right will disappear completely. In addition, the voting rights of the shareholders who withdraw part of their capital contribution are limited from the time when the defective capital contribution is found. The voting rights can be limited by articles of association, resolutions or laws until the return of their capital contribution.

6. Discussion

The limitation of voting rights of shareholders with defective capital contribution should be designed and regulated scientifically and concretely. First of all, the legitimacy of limited rights is sufficient. The close relationship between investment and voting rights, legal principles and principles of law and economics are strongly supported from different angles. Secondly, after clarifying the limitation of voting rights, we should build the limitation system as soon as possible, so as to make up for the legal gap and guide the judicial adjudication. In a word, the limitation of voting rights of shareholders with defective capital contribution is of great significance to the maintenance of corporate capital under the subscription system reform, which is conducive to the correction of the instrumentalism of voting rights, and the general idea of classifying and limiting voting rights according to the proportional equity standard can also be used for reference by other rights limitation systems.

References