As part of a recent company law reform package, a veil-lifting provision was inserted into China's Company Law 2006. The efficacy of this new provision, however, appears to be problematic. This article argues that for China the purpose of creditor-protection can be better achieved through the tort rule of intentional indemnification contra bonos mores.

Introduction

This article considers the viability of adopting the tort of intentional indemnification contra bonos mores as the juridical basis for obtaining satisfaction for creditors of a Chinese company, where it is impossible to do this against the company's assets. One might wonder why this issue is relevant, as PRC Company Law 2005 art.20 gives the court the power to order a shareholder to be jointly liable for the company's debt, if it has abused its privilege of limited liability. The answer to this question can be summarised in two points. First, only a defaulting shareholder can be held liable under art.20. Article 20 is of no assistance when it is necessary to consider the joint liability of a person who is not a shareholder of the company. Secondly, certain concepts, such as “abuse” and “serious”, used in art.20 are not clearly defined. It is unclear as to what type of act constitutes an abuse of the separate personality and the limited liability principles. Likewise, what kind of injury amounts to “serious injury” of the interests of company creditors, etc., appears to be uncertain. The task of clarifying these concepts has been conscientiously left to the Supreme People's Court. However, before this is done in the form of judicial interpretations, the utility of art.20 is questionable.

The apparent lack of utility of art.20 raises the question as to whether it is possible for an aggrieved company creditor to obtain satisfaction on a juridical basis that is not provided in the PRC Company Law. This article argues that the German experience shows that it is indeed possible to do so and that the company creditor's claim can be based on the tort of intentional indemnification contra bonos mores.
The remainder of this article starts with an introduction to the way in which the tort of intentional indemnification contra bonos mores has been applied in Germany against defaulting shareholders to obtain satisfaction for company creditors. It will proceed to examine the “veil-lifting” law and practice in China prior to the enactment of art.20. This will be followed by a consideration on the viability of adopting the contra bonos mores rule as a juridical basis for obtaining satisfaction for company creditors against abusive shareholders in China.

**Intentional indemnification contra bonos mores**

Intentional indemnification contra bonos mores is one of the general rules of law of torts in some civilian systems. This rule is provided in §826 of BGB, the German Civil Code, which stipulates that a person who wilfully causes damage to another in a manner contrary to good morals is bound to compensate the other for the damage. The contra bonos mores rule provided under §826 is one of the three general provisions in BGB. The other two provide that a person who has injured another person's personal or property interests must compensate for the damage arising from such injury (§823 I) and that a person must compensate another person if the first-mentioned person has violated a statutory provision intended for the protection of others where the relevant provision is violated through the commitment of a fault and the second-mentioned person has suffered a loss (§823 II).

To establish liability of intentional indemnification contra bonos mores, the plaintiff must prove four elements.

1. the plaintiff has suffered damage;
2. the damage was caused by the conduct of the defendant;
3. the conduct of the defendant that caused the damage was contra bonos mores;
4. the defendant must have intended to cause the damage.4

Since proof of intention is required, the contra bonos mores provision under §826 is subjectively narrow, as compared to the other two general provisions. The §826 provision, however, is objectively wide, as it is intended to be an all-purpose residual provision.5 The categories of cases decided on the basis of §826 include, but are not restricted to, misstatement cases, cases where judicial decisions have been obtained through fraud, cases on inducing breach of contract and other trade disputes.6

The wide scope of the contra bonos mores provision makes it possible for it to be invoked against defaulting shareholders to obtain satisfaction for a company creditor when it is impossible for the company to discharge its debt. For example, in a 1988 case,7 the German Federal Court of Justice held a shareholder liable for what was, prima facie, the company’s debt on the basis of §826 of BGB. In that case, A and his wife B incorporated a company. This company engaged a number of tradesmen to erect a building on a piece of land owned by A personally. A sold the building when the project was completed and received the purchase price. The plaintiff tradesmen were unable to obtain full payment from the company, as it had been impecunious since its incorporation. The court held A liable for the company’s debt on the basis that A’s conduct was contra bonos mores. The court held that by using the company to enter into the contract and receiving the sale revenue personally, A had prevented the plaintiffs from obtaining value for their own work. The court observed that the conduct of A showed that the sole purpose of incorporating the company was to injure the interests of the tradesmen.
The German Federal Court of Justice invoked the notion of *contra bonos mores* again in its decision in a more recent case, the so-called *KBV* case. In that case, the plaintiff had entered into a contract to provide services to KBV GmbH (*KBV*). After the plaintiff had performed its part of the contract, *KBV* entered into a transaction with a third party, L GmbH (*L*), which had the effect of depriving *KBV* of part of its assets. The transaction was entered into by A, one of *KBV*’s two shareholders, and was consented to by B, the only other shareholder in *KBV*, who was also the company’s managing director. No insolvency proceedings were initiated against *KBV* because of its lack of assets. The unavailability of the defendant’s assets was caused by *KBV*’s transaction with *L*, which was procured by A and B.

The German Federal Court of Justice held that the two shareholders were obliged to compensate the plaintiff for the loss that it has suffered because of its inability to recover from the defendant. The court held, inter alia, that the two shareholders’ liability could be established on the basis of §826 of BGB, given that A and B had deliberately harmed the interest of the plaintiff, the company creditor *contra bonos mores*. The harmful action of the shareholders was *contra bonos mores* because it constituted an abuse of the legal form of a company. The deprivation of the company’s assets on the part of the shareholders amounted to an abuse of the legal form of the company because the shareholders appropriated the company’s assets without taking into account the company’s ability to discharge its debt obligations. The privilege of limited liability granted to the shareholders of a private company under 13(2) of BGB was subject to the precondition that the company’s assets must be committed to the preferential satisfaction of company creditors throughout the company’s existence.

**Lifting of the corporate veil: the law and practice in China before 2006**

Before the enactment of PRC Company Law 2005, which came into force on January 1, 2006, the primary legal basis for disregarding a company’s personality in favour of a creditor was a judicial interpretation issued by the Supreme People’s Court (SPC) in 1994, i.e. *Guanyu Qiye Kaiban de Qiye Bei Chexiao Huozhe Xeye Hou Minshi Zeren Chengdan Wenti de Pifu* (The Reply by the Supreme People’s Court on the Civil Liability of an Enterprise Which Has Incorporated Another Enterprise where That Another Enterprise has been Dissolved or has Ceased to Operate). This judicial interpretation was issued to answer a question raised by Guangdong Higher People’s Court on the civil liability of an enterprise for the debt of an enterprise that it, the first-mentioned enterprise, had founded, where the latter (the debtor enterprise) had been dissolved or had otherwise ceased to operate.

Under this judicial interpretation, where the above-mentioned circumstances (i.e. where the debtor enterprise had been dissolved or had ceased to operate) occur, if the amount of the contributed capital in the debtor enterprise is different from that of the registered capital and the debtor enterprise is unable to meet its liability with its own assets, the founder enterprise is liable for the difference between the amount of the contributed capital and that of the registered capital of the debtor enterprise. Since the founder enterprise is normally a shareholder in the enterprise it had founded, the effect of the above-mentioned judicial interpretation is that a shareholder (the founder enterprise) is to be jointly liable for the debt of the company (the debtor enterprise). Although the above-mentioned judicial interpretation was issued in a specific context, which was discussed above, it had served as the legal basis for the courts’ power to disregard a company’s personality in all other contexts during the period between the enactment of China’s first Company Law in 1993 and the promulgation of the PRC Company Law 2005.

The decided cases on the so-called “lifting of the corporate veil” so far indicate that corporate personality has been disregarded in China chiefly for the purpose of holding shareholders liable for the debt of the company where the assets of the company were insufficient to cover the debt. One of the characteristics of these cases
is that the lack of company assets in those cases was often caused by shareholders' fraudulent activities. These include capital withdrawal, evading liability through the use of duplicate corporate structures or corporate groups, or through liquidation fraud. It is possible to evade liability through liquidation fraud in China because the shareholders of a limited liability company themselves act as the liquidators when the company is in liquidation.13 Accordingly, the most typical circumstances in which a shareholder has been held jointly liable for company debt have been the ones where the above-mentioned forms of fraud have been perpetrated.

Capital fraud

Capital fraud normally occurs where the company is a limited liability company (LLC).14 The discussion of this topic therefore is restricted to situations where the company is an LLC. The capital system adopted under the PRC Company Law is one of registered capital, rather than authorised capital. Under this capital system, capital contributors of an LLC must pay up a certain amount of capital, the value of which must be certified by an authorised capital verifier, which is normally a certified public accountant, before the company can be registered. 15 Capital contributions made in the form of cash are normally paid into a capital account. The value of a company's capital is recorded in the company registry administered by the company regulator, the Bureau of Industry and Commerce Administration (BICA), when the company is registered. Once the company is incorporated, the capital money can be used for business purposes but cannot be withdrawn by shareholders for other purposes.16

The main purpose of the capital system is to provide company creditors with a form of loan security.17 Capital contribution fraud, such as capital withdrawal, therefore amounts to a fraud against company creditors. Accordingly, capital fraud has been used as a ground for holding the defaulting shareholder liable for the company's liability. An example where the corporate veil has been lifted on the ground of capital fraud is Amoy Xiahua Display Device System Co Ltd v Yantai Dongchen Science and Technology Co Ltd.18 In this case, Wang, the second defendant, and Ma, the third defendant, incorporated a company, which was the first defendant. The total capital input by the two shareholders was RMB 300,000. Immediately after the incorporation of the company, Wang and Ma withdrew RMB 200,000 from the capital account in the name of salary payment and duty trip expenses. Shortly thereafter, the plaintiff and the defendant entered into a distributorship contract, whereby the defendant was appointed to be the distributor of the products manufactured by the plaintiff in a certain area in north China.

The plaintiff delivered some goods to the first defendant pursuant to the contract but the first defendant did not make full payment and still owed RMB 389,961 to the plaintiff at the time of action. On the same day, BICA made a decision to revoke the first defendant's business licence, as the latter did not file its annual return.

The plaintiff sued the first defendant and its two shareholders for the sum owed. Wang and Ma argued, inter alia, that they had no responsibility for the debt of the company. The court decided that the two shareholders must share the company's debt liability. The ratio of the decision was that Wang and Ma's withdrawal of RMB 200,000 from the capital account the day following the registration of the company amounted to capital withdrawal, which contravened the capital withdrawal prohibition provisions under the PRC Company Law.

Defrauding creditors through the use of duplicate corporate structures

A second way in which the corporate form is used to evade debt is to incorporate two or more separate companies, which have the same shareholders, personalities and property, and use one of them, which is in fact an empty shell, to incur debt. The debt liability could then be avoided on the excuse that the company incurring the
debt does not have enough assets to discharge its liability and the company that is an alter ego of the debtor company, which does have assets, is a separate legal person. An example of this mode of defrauding creditors is Hainan Zhongjian Number Six Engineering Bureau Sales Agency Company v Hainan Huaqiang Property Development Co Ltd (the Huaqiang case).

In that case, the plaintiff and the defendant entered into a construction contract on December 9, 1992. Under the contract, the defendant promised to erect a number of blocks of buildings in a residential area. The plaintiff was to pay 30 per cent of the contract price within three months of the contract. The remainder of the contract price was to be paid in three installments. The defendant was to complete the project by the end of July 1994. The plaintiff paid 30 per cent of the contract price according to the relevant terms in the contract. The defendant, however, failed to complete the project by the due date of completion.

The trial court made a compensation order against the defendant. Two other companies, Zhong Qiang Company (ZQ) and Zhong Hua Company (ZH), were held jointly liable for the defendant's debt. The decision on the joint liability of ZQ and ZH was made on the basis that the three companies were really three different corporate structures established for the same company. The three companies had the same legal representative, the same bank accounts and the same domicile. The finance of the three companies was also managed by the same finance and accounting department. The appeal court upheld the decision of the trial court on this issue. Neither court, however, identified the precise legal basis for the joint liability of ZQ and ZH for the debt of the defendant company. This was not strange, given that the case was decided almost immediately after the PRC Company Law 1993 was enacted, when company law jurisprudence in China was at its nascent stage.

In a more recent case of this kind, Guangdong Development Bank Huizhou Branch v Guangdong Foreign Economic Development Huizhou Co (the GD Bank case), the court made a similar decision on the basis, amongst other things, that confusion of the personalities of two or more companies was in contravention of the principles of, inter alia, capital maintenance and the companies in question no longer met the conditions prescribed under General Principles of Civil Law of the People's Republic of China (GPCL) art.37 for being treated as separate legal persons. The court did not expand on how the above-mentioned principles were contravened. Presumably the reason is that the use of duplicate corporate structures means one of the “companies” does not have capital and is consequently unable to bear civil liability independently.

**Defrauding creditors through the use of a company group structure**

“Corporate group” can be defined in more than one way but the phrase is generally used to refer to “a number of companies which are associated by common or interlocking shareholdings, allied to unified control or capacity to control”. A company group structure can and has been used to defraud the creditors of a company within the group. This can be done, for example, by using a subsidiary company's assets for a personal purpose of the controller of the holding company. That was the scenario in China Eastern Airlines Co Ltd Amoy Sales Department v Renshan Ticketing Agency Co Ltd (the Renshan case). In that case, Xu was the controlling shareholder of Renshan Commercial & Trading Co (RC). He was also the chairman of the board of directors and the legal representative of the same company. RC and Xu's then wife Wang subsequently incorporated another company, Renshang Ticketing Agency Co Ltd (RT). RC held 60 per cent of issued shares in RT. Xu was the legal representative of RT and Wang was appointed as the supervisor of the company.

Almost immediately after RT was incorporated, it transferred almost all of its capital money to the plaintiff to settle the debt that Xu owed to the plaintiff personally. Nine months later, RT entered into a domestic airline
passenger transportation sales agency contract with the plaintiff, whereby RT was appointed as a sales agent of the plaintiff. One month before the above-mentioned contract was executed, RC failed to make its annual return and, as a consequence, BICA revoked its business licence. RT subsequently defaulted on its contract with the plaintiff by failing to advance a sum of ticket moneys. Xu was now the majority shareholder in RT, holding 60 per cent of its shares.

Given that RT, the defendant, was seriously under-capitalised, the main issue in the case was whether Xu should be personally liable for RT's debt. The court answered this question in the affirmative. The court held that three conditions must be met before the corporate veil could be lifted. First, the alleged abuser of the company's legal personality should be those shareholders who have actual control over the company. Secondly, the defendant must have abused the company's separate personality for the purpose of avoiding liability. Finally, the defendant's conduct must have caused injury to other people or the society as a whole.

The court pointed out that although Xu was not RT's shareholder when payment was made out of RT's account to settle Xu's personal debt, he was both the controlling shareholder and the legal representative of RC, the holding company of RT, as well as the legal representative of RT. Xu therefore had actual control power over RT. The first condition was thus met. Further, Xu had abused this controlling power. He did so by discharging his personal debt with the company's assets. Although what Xu had done was different from capital withdrawal in ordinary circumstances, in substance it amounted to such an act. The capital withdrawal that Xu committed would definitely have affected RT's ability to discharge its obligations. The second condition was therefore satisfied. Moreover, Xu's act has largely stripped RT of its capital, which ultimately prevented the plaintiff from enforcing its legal rights as a creditor, and this inflicted harm on other individuals or the society as a whole. The third condition was therefore fulfilled.

*88 Liquidation fraud

A typical way of defrauding creditors is to use the company to incur a debt and then procure deregistration of the company without liquidating assets of the company. The purpose of having the company deregistered is to deprive a creditor of its opportunity to recover the debt. The reason why it is possible to do so lies in some loopholes in liquidation provisions. Under PRC Company Law, a company can be dissolved either because of the choice made by the shareholders or as a consequence of a dissolution order. A shareholder-determined dissolution occurs when a terminating event prescribed in the company constitution has occurred, or when the shareholders' meeting has resolved to terminate the company, or where dissolution is necessary as a result of the merger or division of the company.25 Under the 2005 Company Law, shareholders with at least 10 per cent of voting power may request a court order to dissolve the company where the continuing existence of the company is financially unviable.26 A company must dissolve when it is ordered to close down27 or when, as is provided under the 2005 Company Law, its business licence is revoked.28

Under the 1993 Company Law, when a company was dissolved voluntarily, the shareholders themselves were to act as liquidators.29 When a company was ordered to close down because it had breached the law or regulations, the “department in charge” was to organise liquidation.30 Under the 2005 Company Law, where the company is an LLC, liquidators will be composed of shareholders, regardless of the reason of termination.31 The “powers” of the liquidators include(d) notifying creditors about the company's winding up by notice or announcement. 32

It should be noted that under the 1993 Company Law, revocation of business licence was not listed as an event
that would call for government (“department in charge”)-organised liquidation. This meant that whether the liquidation process must be commenced when a company's business licence was revoked was technically uncertain. Even if it was, it was uncertain, prima facie, whether the liquidation should be organised by the shareholders or by the government (“department in charge”). This uncertainty regarding liquidation procedure was compounded by BICA's refusal to be treated as the department in charge for non-voluntary liquidation.

The above-mentioned uncertainties on the obligation or procedure of liquidation in the case of government-organised deregistration provided an opportunity and incentive for those shareholders who wanted to evade their debt obligations to procure company termination by prompting BICA to revoke the company's business licence. A popular way of achieving this has apparently been to default on the annual return requirement. BICA has the power to, and it normally does, revoke a company's business licence when the company defaults on its annual returns. A typical response of the People's Courts to such abusive activity has been to lift the corporate veil. An example is *Urban and Rural Construction Co Ltd v Yang* (the Yang case). In this case, Yang and two others incorporated J Co in November 1995, with Yang being the majority shareholder. Before J Co was formally incorporated, Yang entered into an oral contract with the plaintiff, whereby the latter promised to erect a building for the proposed company (J Co).

It appears from the case report that the contract price was not fixed at the time of this oral contract. The construction project was completed in 1996. In June 1997, J Co sold the property in question for RMB 4 million to a third party, which paid the whole purchase price. Three months later, the plaintiff and J Co reached an agreement in writing, confirming the amount of the contract price. J Co promised to complete its payment by October 31, 1998. However, it has since only repaid less than 9 per cent of the purchase price. J Co failed to lodge its annual return in 1998 and as a consequence, BICA revoked its business licence. The plaintiff therefore took the present action against the three shareholders of J Co for the balance of contract price and the litigation cost.

The trial court decided that the three shareholders were liable for the company's debt. It held that three shareholders transferred the property in question to a third party before the company had paid off the contract price to the plaintiff. They also had the company deregistered (by failing to lodge the annual return) without having liquidated the company. All these had deprived J Co of its ability to discharge its debt and amounted to evading debt in bad faith. The appeal court upheld the decision of the trial court.

Neither the trial court nor the appeal court mentioned why J Co had lost its ability to discharge its debt because the real property in question had been sold to a third party. In fact, J Co should still be able to discharge its debt to the plaintiff since the third party has paid off its purchase price. A company would not cease to exist until the liquidation process was completed. What might have happened is that the shareholders of J Co had pocketed the proceeds from the sale of the property.

**The contra bonos mores rule as a juridical basis for the defaulting shareholders' liability in China**

Whether the *contra bonos mores* rule can serve as a juridical basis for the defaulting shareholders' liability in China turns on two further questions, namely whether the rule exists in China's tort regime and whether the results of all of the four categories of cases discussed above can be achieved on the basis of this rule, given that to the best knowledge of the present author no corporate veil has been lifted in other circumstances in China. Since capital and liquidation fraud cases and cases on defrauding creditors through an abuse of the corporate group structure or duplication corporate structure may be resolved under the *contra bonos mores* rule in different ways, these two groups of cases will be considered under different headings.
The provision of the intentional indemnification contra bonos mores rule under China's tort regime

It is possible to base an action on the basis of intentional indemnification contra bonos mores only if this rule exists in China's civil law regime. The tort part in General Principles of Civil Law of the People's Republic of China (GPCL), China's provisional civil law code, does not contain a provision which is identical to §826 of BGB. Mr Justice Kong Xiang Jun, a justice of the Supreme People's Court, however, believes that art.106 of GPCL covers what is provided under §826 of BGB.41 Article 106 provides that “… [c]itizens and legal persons who encroach upon State or collective property or the property or person of another through irresponsibility shall bear civil liability”.42 If the view of Mr Justice Kong Xiang Jun on the effect of art.106 is correct, it will be possible to base an action against a shareholder who has made use of a corporate structure to injure the interest of a company creditor on the doctrine of contra bonos mores, which is contained in art.106. It is noted that the contra bonos mores rule is provided under art.1 of the draft Tort Law of the People's Republic of China (Second Draft) prepared by Professor Yang Lixin, a prominent Chinese civil law scholar.43 This suggests not only that the importance of this rule is recognised in China but also that it is very likely that the rule will be provided in the forthcoming Tort Law of the People's Republic of China.

Capital and liquidation fraud cases

The facts in Yang, the liquidation fraud case considered above, were similar to that in the 1988 German case discussed above.44 Like A in that case, Yang also procured the construction contract in the name of the company and then sold the property to a third party before the tradesmen were paid. The only difference is that in the 1988 German case A received the sales revenue direct whereas, in Yang, the shareholders were trying to prevent the tradesmen from receiving the compensation for their work through procuring a deregistration of the company without liquidating the company. Given the short time span between the incorporation and deregistration of the company, there is a very strong argument that the sole purpose of incorporating the company was to harm the interests of the tradesmen. It follows that the decision in Yang could have been arrived at by applying the principle of intentional indemnification contra bonos mores.

In fact, Xiahua, the capital fraud case discussed above, is also similar to the German case referred to above in that in both cases the shareholders incurred a debt where the company was impecunious. The company in Xiahua became impecunious because of the shareholders' capital fraud. In both cases the defaulting shareholders tried to preclude the creditors from recovering their debts. In Xiahua this was done, again, by having the company terminated through procured deregistration without liquidating the company. Given that the only business activity that the company in Xiahua had undertaken during its short life was acting as the plaintiff's distributor through which the relevant debt was incurred, there would be no difficulty in establishing that the sole purpose of incorporating the company in that case was to injure the interests of the company's creditor.

Cases on defrauding creditors through abuse of corporate group form or the use of duplicate corporate structures

These two categories of cases can be decided by treating the conduct of the defendants as one that infringes the company creditor's obligational rights. Infringing another person's obligational right is a sub-category under the tort of intentional indemnification contra bonos mores.45 A person commits this tort when that person, who is not a party to the contract in question, has committed an intentional act or has conspired with a party to the contract to injure the contractual right of the other party to the contract.46

In the Renshan case, RT breached its contractual obligation to advance ticket moneys to the plaintiff by the due
date. Xu, in his capacity as RC (the holding company)'s controller and RT (the subsidiary)'s legal representative, who in those days also had to be the chairperson of the company's board of directors, assisted the RT in its breach of contract. Xu did so by directing the RT to empty its coffers for an impermissible purpose and by making the decision for the company not to make the advancement in question to the plaintiff when it was due. Xu therefore infringed the obligational rights of the plaintiff over the contract.

With regard to cases where duplicate corporate structures are used to evade obligations, assuming that A Co is used to incur debt, while B Co and C Co are used to hold assets, it is possible to regard B Co and C Co as having conspired with A Co to injure the contractual rights of A Co's creditor. This is because A Co, B Co, and C Co have the same controller, which means that all of the three companies knowingly participated in the above-described scheme to defeat the contractual (debt) claim of A Co's creditor.

As was mentioned above, the liability for intentional indemnity contra bonos mores can be established only if intention can be proven. For the purpose of establishing a shareholder's liability to a company creditor, proving intention is not excessively burdensome. The German Federal Court of Justice ruled in a recent case that the intention requirement is fulfilled if the claimant is able to prove that the defendant could appreciate that its impugned act might compromise the company's ability to meet its obligations. In all of the cases considered above, with the possible exception of the Yang case, the companies in question were largely stripped of their assets. In Yang, if the defendants had indeed pocketed the proceeds from the sale of the company property, such a wrongful act would also amount to deprivation of the company's assets. In some of these cases, the shareholders also tried to deprive the creditors of their recourse against the companies' assets by procuring deregistration of the companies. It would not be hard for the claimants to prove that the defendants could appreciate that their wrongful act might compromise the company's ability to discharge its obligations. Indeed, the very purpose of their impugned acts appears to be the deprivation of the company's ability to discharge its debts.

Conclusion

Up to now, China has been following the common law way of resolving the problem caused by shareholders' abuse of their privilege of limited liability, namely, by lifting the corporate veil of the company. This article demonstrates that, under Chinese law, it is possible to protect company creditors' interests against possible abusive activities by shareholders without resorting to veil-lifting. When a shareholder has abused its privilege of limited liability, it may well have committed a tort of intentional indemnity contra bonos mores against company creditors. An aggrieved company creditor should therefore be able to obtain compensation through a tort action against the defaulting shareholder, where the company is unable to discharge its debt because of an abusive conduct of the defaulting shareholder.

The significance of the tort avenue is not restricted to its ability to overcome potential problems caused by the apparent lack of efficacy of the veil-lifting provision in China's Company Law. The cause of action in tort offers a better means of protecting company creditors' interests against shareholders' abusive activities than veil-lifting in general. Veil-lifting entails a suspension of the operation of the separate entity principle, a fundamental company law rule made by the Parliament. The rules on veil-lifting would therefore need to provide for exceptions to the separate entity rule. Unfortunately, even for common law jurists, such rules still remain principles in search. The common *90 law courts have so far not identified a logically consistent set of veil-lifting rules. The level of uncertainty relating to veil-lifting rules is therefore high.

The tort avenue, in contrast, does not entail a negation of the separate entity rule or the limited liability rule, as a
contra bonos mores action does not involve an attribution of the company's debt liability to the defaulting shareholder. The tortious liability is owed by the errant shareholder to the company's creditors directly. A further merit of the tort avenue is that it is rooted in the German style civil law system and China's civil law has been developed under the strong influence of the German Civil Code. It would therefore be doctrinally easier to adopt the contra bonos mores rule as a juridical basis for solving this problem.

As the protection of company creditors against the abusive conduct of shareholders is better achieved through the tort avenue than through art.20, the People's Courts may wish to consider adopting intentional contra bonos mores as the juridical basis for obtaining satisfaction for company creditors against defaulting shareholders, at least where art.20 is of no assistance.

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1. Article 20 provides that a company shareholder who has abused the company's separate personality an its own limited liability for the purpose of debt evasion shall bear joint liability for the company's debt, if its abuse has seriously injured the interest of the company creditors: PRC Company Law 2005 art.20.
2. Such a person may be a company that is not a shareholder in the debtor company, as is in the Huaqiang case and the GD Bank case, to be discussed below, or a shareholder in a company that is the holding company of the debtor company, as is in the case of the Renshan case, considered below.
7. BGH NJW-RR 1988, 1181.
11. Professor Jiang Daxing, School of Law, Nanjing University, interview, August 20, 2007. The State Council and the Supreme People's Court issued a number of documents that had similar effects as the above-mentioned 1994 Supreme People's Court judicial interpretation prior to the enactment of the PRC Company Law 1993. For details, see X. Zhao and G. Zhang, Xin Gongsifa Zhidu Sheji (System Design of New Company Law) (Beijing: Law Press China, 2006), pp.370-371.
12. The relevant power given to the courts under art.20, PRC Company Law 2005 was provided for achieving this purpose too: An and Huang (eds), Zhonghua Renmin Gongheguo Gongsifa Shiyi (An Interpretation of the PRC Company Law) (2005), p.43. Article 20 does not empower the courts to lift the corporate veil where a corporate personality is abused by company officers. A company officer who has abused the company's corporate personality will have to be dealt with under the company officers' duty regime under PRC Company Law 2005:
In contrast, in common law jurisdictions, the corporate veil has been pierced typically where the assets of the company are insufficient to meet its liability or where the company has been used as a shield by an individual, who does not need to be a shareholder but who is usually in a position to control the company involved, to evade his or her legal obligations: R. Baxt, K. Fletcher and S. Fridman, *Corporations and Associations: Cases and Materials*, 9th edn (Sydney: Butterworths, 2003), p.192.

13. PRC Company Law 2005 art.184. The predecessor of this provision was PRC Company Law 1993 art 191.
16. PRC Company Law 1993 art.34; PRC Company Law 2005 art.36.
22. Under GPCL art 37(4), a legal person must be able to bear civil liability independently.
25. PRC Company Law 1993 art.190; PRC Company Law 2005 art.181(1)-(3).
30. PRC Company Law 1993 art.192.
32. Some of the “powers” can arguably be understood as “duties” as well, as the liquidators could be liable if they exercised powers improperly: PRC Company Law 1993 art.198; PRC Company Law 2005 art.190.
33. PRC Company Law 1993 art.193(2); PRC Company Law 2005 art.185(2).
35. BICA issued a circular to this effect (Professor Jiang Daxing, School of Law, Nanjing University, interview, August 20, 2007).
36. BICA has the power to revoke the business licence of a company, where the company, inter alia, did not make an annual return in accordance the relevant provisions: PRC Enterprise Legal Person Registration Administration Regulations reg.30.
37. Professor Jiang Daxing, School of Law, Nanjing University, interview, August 20, 2007.
39. PRC Enterprise Legal Person Registration Administration Regulations reg.30.
40. A company would only be formally deregistered at the completion of liquidation: PRC Company Law 1993 art.197.
42. The General Principles of Civil Law of the People's Republic of China (Beijing: Foreign Languages Press, 2000), p.37. Note, however, the Chinese equivalence of “irresponsibility” in the above-cited text is “guocuo”, which should really be translated as “fault”.
44. Text to fn.7 above.
47. PRC Company Law 1993 arts 45, 113.
49. Text to fn.5 above.
50. BGH, GmbHR 2007, 930 at [30].

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