

Research on the "Right of Retraction" Of the Transferee Shareholders in The Process of Equity Transfer of a Limited Liability Company

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Abstract: Among the rights and obligations of the shareholders of limited liability company, the interleaving of the shareholders' preemption right and the shareholders' transfer right of repentance has aroused extensive attention and discussion. This paper discusses the legal basis of these rights and their practical application in corporate governance. By analyzing the scope of application of Article 20 of the Fourth Judicial Interpretation of the Company Law and the imperfection of the liability mechanism for damages, this paper reveals the existing problems under the current legal framework and puts forward relevant legal and practical suggestions. These studies provide theoretical support and practical guidance for improving the equity trading system of limited liability companies.

Keywords: Limited company, Preemption, Right of retraction, Equity transfer.

1. Introduction

In today's limited liability company governance structure, the balance of rights and obligations among shareholders is a key issue. Especially in the process of equity transfer, the interweaving of the shareholder's preemption right and the transferor's right of repentance directly affects the internal stability of the company and the coordination of shareholder relations. The purpose of this paper is to discuss the legal framework and its application and problems in practice.

The transfer right of shareholders is the right to cancel the share transfer agreement under certain conditions if the other shareholders choose to exercise the preemption right when the shareholders transfer the shares to other shareholders. This right not only involves the protection of rights under the corporate legal framework, but also directly affects the efficiency and fairness of corporate governance. Especially under the influence of relevant laws and regulations such as Article 20 of the Fourth Judicial Interpretation of the Company Law, how to balance the legitimate rights and interests of shareholders and the stability of the company has become a major challenge in real life.

The current academic research on the theory of shareholders' transfer of the right of retraction mainly focuses on the relationship between shareholders' preemption right and the right of retraction. Some theories claim that preemption right is regarded as forming right, emphasizing its protective effect on shareholders' interests. Others argue that pre-emption rights should be treated as claims to ensure the autonomy of the transferring shareholder. Such theoretical differences directly affect the application and effect evaluation of the right of estoppel in judicial practice.

Therefore, this paper aims to systematically sort out the different viewpoints of the legal circle on this issue, and combined with the actual case analysis, to explore the legal application status and possible problems of the transferee shareholder's right of retraction. Through in-depth research, this paper attempts to provide theoretical guidance for judicial practice and legislation, so as to balance the rights and

obligations between shareholders and maintain the stability and fairness of corporate internal governance.

2. The Basic Theory of The Equity Transferor of a Limited Liability Company

2.1. The Concept and Characteristics of The Equity Transferor of a Limited Liability Company Sub-Section Headings

The transfer right of shareholders means that when shareholders transfer equity to other shareholders, if other shareholders choose to exercise the preemption right, the transferring shareholders can cancel the equity transfer agreement under certain conditions to protect their interests and autonomy. The purpose of this right is to balance the rights and obligations of the shareholders, especially to protect the legitimate rights and interests of the transferring shareholders and the autonomy of decision-making in equity transactions. The shareholder's preemption right is a legal provision to ensure that shareholders have the priority to purchase the equity transferred by other shareholders under the same conditions to prevent equity dilution, which reflects the principle of equal treatment.

In terms of corporate governance, shareholders' preemption rights maintain the harmonious relationship between inside and outside the company and the rational use of capital. Such rights contribute to the long-term development of the company by safeguarding the fundamental rights of shareholders, promoting internal cooperation and fair decision-making, and facilitating the efficient flow of capital. In addition, the shareholder preemption right can prevent external forces from changing the control of the company through share purchase, and maintain the independence and stability of the company.

2.2. Legislative Purpose and Interest Balance of The Transfer of Shareholder's Right of Retraction Under Shareholder's Preemption Right

When discussing whether shareholders should have the "right of repentance", the deduction from the nature of the right may be too abstract and one-sided, and neglect the actual value of the system of the right of repentance. In the civil and commercial legal system, different types of rights involve different interests' protection and pursuit, so the balance of multi-interests should be considered comprehensively. Jurists such as Hake and Wang Zejian emphasize that the formulation of legal norms should be based on the measurement of the interests of all parties, rather than simply deducing conclusions from abstract logic. Especially in the company law, when the relationship between multiple stakeholders is adjusted, priority should be given to the balance of interests under specific circumstances, rather than relying only on conceptual classification to determine the legitimacy of the legal system.

The evaluation of whether shareholders should have the "right of retraction" should not be judged simply on the basis of the attributes of the preemption right, so the substantial protection of interests may be ignored. The correct method is to deduce the essence of the preemption right based on whether the "right of retraction" is reasonable and justifiable in a particular situation. The preemption right of shareholders in the company law aims at maintaining the internal stability and human compatibility of the company, preventing external third parties from interfering with the existing shareholder structure and increasing its economic and management burden.

Therefore, the recognition of "right of retraction" is based on the comprehensive measurement of multi-party interests, which does not threaten the company's insider compatibility, but respects and realizes the shareholders' freedom of commercial transaction to the greatest extent. This arrangement helps to balance the relationship between the closed nature of the limited liability company and the freedom of shareholders to dispose of the equity, and avoid excessive legal intervention in the latter.

At the intersection of law and commercial value, it is of great significance for shareholders of limited liability company to grant the right of retraction. First, it provides shareholders with protection and flexibility, allowing them to reverse equity transfers in the event of market changes, strategic adjustments or insufficient information to safeguard long-term interests and financial security. Second, this right promotes the stability and transparency of the corporate governance structure by establishing conditions and procedures to ensure the legality of transactions and the normativity of corporate governance.

The transfer of the right of retraction also affects the market reputation and shareholder relationship management, enhances the trust of market participants, and promotes the good relationship and cooperation among shareholders. Within the legal framework, it provides a balance mechanism that not only protects the rights and interests of the transferor, but also considers the overall interests of the company and the market, protects the rights of private property, and maintains the normal operation of the company's business and market stability.

2.3. The Relationship Between Shareholder's Preemption Right and Right of Retraction

Whether the transferring shareholder has the right to "regret" inevitably involves the shareholder's preemption right. The two not only affect each other in law, but also are closely intertwined in the legal framework of equity transfer of limited liability companies. Many scholars believe that the key to determine whether the shareholder's "right of retraction" is legal is to determine the essence of the shareholder's preemption right, that is, the "nature of the decision theory" of the shareholder's "right of retraction".

According to this view, if the exercise of the preemption right can produce a definite legal effect, the transferring shareholder cannot exercise the "right of repentance". On the contrary, if the exercise of the pre-emptive right fails to achieve legal effect, the transferring shareholder may decide not to transfer the equity and exercise the "right of withdrawal".

The conflict between the preemption right and the "right of retraction" reflects the interest game between the transferring shareholders and other shareholders in the equity transfer. It may be helpful to clarify the relationship between the transfer shareholder's "right of retraction" and other shareholders' right of preemption to view the establishment process of "right of retraction" from the Angle of different interest pursuit. Some people who hold the view that the interests of other shareholders take precedence believe that other shareholders should be given absolute protection of the underlying equity, and the preemption right is regarded as the formation right. However, some people who support the priority of transferring shareholders' interests believe that the right of transferring shareholders to decide on equity transfer matters should be respected as much as possible, and the right of preemption is regarded as the right of claim.

However, treating the preemption right as the forming right may lead to its transformation from the right in the corporate organization contract to the ordinary equity sale contract, and its claim is limited by the validity of the contract, the exercise period, the object of the request, etc. This approach not only limits the way for other shareholders to claim their rights, but also weakens the degree of legal protection of pre-emption rights, which is contrary to the original intention of protecting shareholders' interests.

Another mainstream view is the "priority claim theory", that is, the right of preemption is the right of the right holder to demand a sale contract with the transferor. According to this view, the purchase of equity by priority shareholders is essentially divided into two stages: offer and acceptance. Some scholars argue that the right of compulsory contracting should be adopted, that is, the law is required to force the transfer shareholder to accept the offer of the priority shareholder, so as to avoid the nullity of the preemptive right in the contracting stage. However, this practice may deprive the transferring shareholders of their free choice in the equity transfer transaction, thus damaging their legitimate rights and interests.

In a word, the different theories about the shareholder's preemption right are reasonable, but they all face the challenge that it is difficult to realize the interests of relevant subjects. At present, scholars have not reached a consensus on the nature of pre-emption right, and paying too much attention to this issue may not help to study the practice of transferring shareholders' "right of retraction". We should start from the

current situation of law application and legislative purpose to find the legitimate basis for the transfer of shareholders to exercise their rights, rather than limited to the logical analysis of conceptual law.

3. Problems Existing in The Transfer of The Right of Retraction by The Equity Transferor of a Limited Liability Company

3.1. The Scope of Application of Article 20 Of Judicial Interpretation of Company Law (IV) Is Too Narrow

Article 20 of the Fourth Judicial Interpretation of the Company Law stipulates: "Where the transferring shareholder of a limited liability company does not agree to the transfer of the equity after the other shareholder has claimed the priority to purchase, the people's court shall not support the other shareholder's claim of priority to purchase." From the perspective of this article, the pre-emption right of shareholders of limited liability company is actually divided into two steps to achieve. First, other shareholders have the right to request the purchase of the transferring shareholder's equity under the same conditions, which is similar to an offer. Second, the transferring shareholder must agree to the other shareholders to exercise the pre-emption right, which is similar to a commitment. Therefore, the shareholder with the right of first refusal cannot exercise this right unilaterally, but must do so by requesting the consent of the transferred shareholder. In essence, the shareholder's pre-emptive right is regarded as a claim right.

The provision of Article 20 of Interpretation 4 of the Company Law may in fact deprive the shareholders of the right of preemption while maintaining the incorporation of the company. This situation has gone beyond our usual understanding of section 71 of the Companies Act. The purpose of judicial interpretation is to concretize rules whose meaning is not clear so as to facilitate their application and operation. However, if judicial interpretation leads to substantial changes to existing legal provisions that deviate from the original intent of the legislation, it is beyond its purview. When formulating judicial interpretations, the Supreme People's Court should try to avoid putting forward interest adjustment plans that are divorced from the original intention of legislation or lack of legal basis, so as to ensure that the position and method of judicial interpretation are consistent with the original intention of legislation.

At the same time, this provision may deviate from the original intention of the system, conflict with a number of legal principles, and may lead to confusion in practice, and even encourage dishonest behavior. In view of the background that the Company Law is difficult to be comprehensively amended in a short period of time, the Supreme People's Court should amend this provision as soon as possible to avoid adverse effects on the protection of shareholders' rights and interests in judicial practice due to its application

3.2. The Mechanism of Liability for Damage Compensation of "The Right to Surrender Remorse" Is Not Perfect

The second half of Article 20 of Interpretation 4 of the Company Law points out that if the transferring shareholder

exercises the right of regret and other shareholders are unable to realize the right of preemption, then other shareholders can claim reasonable compensation. Liability for damages can be divided into two types in contract law: liability for contracting negligence and liability for breach of contract.

The formation of liability for contracting negligence requires the establishment of contractual obligations. When the transferring shareholder notifies the other shareholders of the transfer of the shares on the same terms, the other shareholders may make preparations for the future acquisition of the shares based on their trust in the legal priority. If the transferring shareholder suddenly exercises the right of regret, although this may be regarded as contracting negligence, its liability for damages can only be limited to the failure of the transaction stage because the contract has not been formed. According to the traditional viewpoint of civil law, this kind of compensation should belong to the liability of contracting negligence. However, the certainty that preemption gives other shareholders is difficult to compensate for by relying on compensation benefits, because they focus not only on the price paid, but more importantly on future shareholder equity and expected returns.

Some scholars believe that the transfer of equity by the transferring shareholder notifying other shareholders of the same conditions should be regarded as an offer, and the acceptance and exercise of the pre-emptive right by other shareholders is an undertaking. However, there are two problems in this view: first, it is difficult to solve the problem of less compensation for contracting negligence; second, the notice of equal conditions is not uncertain, because according to the provisions of Article 19 of the fourth interpretation of the Company Law, the notice should include the number of shares, price payment conditions and other elements, and the contract terms have been basically determined. Theoretically, a contractual relationship should be formed.

Under the framework of the formation right, the contractual relationship between the transferring shareholder and the other shareholder has been formed when the other shareholder exercises the preemption right. According to the principle of good faith, even if the transferring shareholders exercise the right of regret, they still need to bear the contractual responsibility and pay the corresponding compensation for breach of contract. The scope of the liability for breach of contract is usually larger than the liability for contracting negligence, which can better compensate for the losses of other shareholders, especially from the perspective of economic interests, the compensation for breach of contract can more fully compensate the interests of the injured.

To sum up, the formation right theory can better protect the interests of other shareholders when transferring shareholders exercise the right of regret, because it ensures that the injured party can obtain more adequate economic compensation. In the context of the existence of the right of regret, although other shareholders cannot force the transfer shareholders to execute the equity transfer contract, they can at least ask for proper compensation for the performance of the interests, which is a reasonable and effective solution.

4. Literature References

Shen (2024) studied the estoppel right of the transferee shareholder in the equity transfer of a limited liability company, and discussed the procedural and substantive requirements in the implementation of its law. Despite the confirmation of its right by the judicial circle, its theory and

regulations still have disputes and challenges [1]. Zhao and Yi (2021) discussed the problem of the proof and construction of whether the transferring shareholder should have the "right of retraction" under the shareholder's preemption right. The research emphasizes on examining the legitimacy of the right from the Angle of legislative purpose and interest balance, and thinks that it is helpful to maintain the human compatibility and multi-interest balance of the limited company. In order to realize the unification of law implementation and theory, it is suggested that the exercise conditions and time limit of "right of repentance" should be clearly stipulated in the amendment of Company law [2]. Li (2023) discussed the legitimacy of whether the transferring shareholders should have the "right of retraction" under the shareholder's pre-emptive right. From the Angle of legal interest measurement, the effect of laws and regulations and pragmatism, it emphasizes balancing the interests of all parties while protecting the compatibility of limited companies. It is suggested that the time and conditions for exercising the "right of retraction" should be set in the law amendment to ensure its rationality and effectiveness [3]. Chen (2023) discussed the improvement of the rules for the exercise of the right of remorse of shareholders' equity transfer in limited companies. The article points out that Article 20 of the Interpretation of the Company Law (IV) gives the right of transfer shareholder's remorse, but the current regulations do not specify the conditions and restrictions of exercise, which leads to the understanding deviation and contradiction in judicial practice. It is suggested to set up detailed regulations on the exercise of the right of estoppel at the legal level in order to maintain the balance of interests of all parties and judicial justice [4]. Ren (2023) discussed the application and problems of Article 20 of the Company Law Interpretation (IV) in the behavior of shareholders' remorse after equity transfer. Taking a specific case as an example, the article analyzes the legal and practical challenges of the act of estoppel, and advocates the deletion of the clause in order to safeguard the fairness of the company law and the rights of shareholders [5]. Wang (2023) discussed the reasonableness of granting the transfer shareholder the right of repentance under the preemption right system in China's company law. The article holds that allowing retraction conforms to the principle of equality and voluntariness, and is conducive to the free circulation of equity and the maintenance of the trust interests of other shareholders, so it has a certain rationality and legitimacy [6]. Wang (2023) discusses the legitimacy of "right of retraction" in equity transfer. The article holds that the "right of retraction" is not in line with the legal basis of the legal compatibility of the limited company and lacks the legal legitimacy. It is suggested that the relevant provisions should be perfected in the future amendment of the company law to avoid interfering in the contractual relationship between shareholders [7]. Zhang (2022) discussed the design of the right of retraction mechanism in equity transfer. The paper holds that the establishment of the right of estoppel is in line with the legislative purpose of the company law and the contract law, and puts forward some suggestions to improve the right of estoppel under the mode of "notice + consent", so as to balance the distribution of interests among shareholders and the maintenance of corporate compatibility [8]. Wang (2022) studied the regulation on the exercise of "right of retraction" of transferring shareholders under the preemption right. This paper discusses the nature of the right, the conflict

of interest and the problems in judicial practice, and puts forward clear rules on the exercise period, conditions, methods and effectiveness, aiming at balancing the interests of all parties and preventing abuse, so as to ensure its fairness and rationality [9]. Mo (2022) discusses the legislative and practical disputes over shareholder's right of retraction in the transfer of equity in limited liability companies. The establishment of the right of retraction aims to maintain the balance of shareholders' rights and interests, but there are challenges in understanding and application in practice. Starting from the case, the paper puts forward some suggestions to limit and regulate the exercise of the right of estoppel, and emphasizes that it should be exercised reasonably and in a limited way to ensure market fairness and the interests of all parties [10]. Wu (2022) conducted an in-depth discussion on the legal position and exercise of shareholders' "right of retraction" in the transfer of shares of limited liability companies. Although there is uncertainty in legal regulation and practice, it is of great significance to maintain the balance of shareholders' rights and interests [11]. Wang (2022) emphasized the legal norms and implementation paths required for the proper exercise of the "right of remorse" to ensure its effectiveness and legitimacy, providing valuable theoretical basis and guidance for relevant legal practice. This paper systematically discusses the "right of retraction" in equity transfer from its legal nature and applicable conditions. The author first analyzes the legal essence of the act of "retraction" and points out that as a quasi-legal act, it is not an independent civil right. Combined with practical cases, the author further defines the application conditions of "right to regret" and emphasizes that unless there is abuse, its application on the basis of the legitimacy of shareholder status should not be hindered. Through theoretical deduction and practical observation, this paper provides clear guiding principles for judicial practice [12].

5. Conclusion

The shareholder's preemption right and the transferor's right of retraction have important legal and practical significance in the equity transfer of limited liability company. The existence of preemption right aims to protect the investment of existing shareholders and the stability of corporate governance structure, and prevent the improper interference of external forces on the control of the company. However, the recognition of the transferor's right of retraction is also necessary, which allows the transferor to revoke the intention of equity transfer under certain circumstances in order to cope with market changes, insufficient information or strategic adjustments, so as to protect its legitimate rights and interests and financial security. At present, the existing problems mainly focus on the narrow scope of application of article 20 of Judicial Interpretation of Company Law (IV) and the imperfect mechanism of liability for damages. The narrow scope of application of judicial interpretation may weaken the preemption right of other shareholders, which is contrary to the original intention of the company law, and needs further amendment to protect the balance of interests of all parties. In addition, the type and scope of liability for damages also need to be clarified by law to ensure that the injured party can receive adequate economic compensation, so as to promote market fairness and transparency.

To sum up, in view of the issue of the assignment of the right of retraction by the equity transferers of limited liability companies, it is suggested that the balance of multiple

interests should be comprehensively considered in legal practice and academic research, and relevant laws, regulations and judicial interpretations should be constantly improved to promote the stability of corporate governance structure and the development of market economy. In addition, attention should be paid to the application and implementation of the law to ensure that it can effectively safeguard the legitimate rights and interests of all parties and the normal operation of the market order in actual operation.

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