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**SUMMATIVE (FORMAL) ASSESSMENT: MODULE 8B**

**CHINA (PRC)**

This is the **summative (formal) assessment** for **Module 8B** of this course and must be submitted by all candidates who **selected this module as one of their elective modules**.

**The mark awarded for this assessment will determine your final mark for Module 8B**.In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

**INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT**

**Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.**

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.

2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way**. **DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.

3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).

4. You must save this document using the following format: **[studentID.assessment8B]**. An example would be something along the following lines: 202223-336.assessment8B. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentID” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked**.

5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words**.

6.The final submission date for this assessment is **31 July 2024**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2024**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.

7. Prior to being populated with your answers, this assessment consists of **9 pages**.

**ANSWER ALL THE QUESTIONS**

**QUESTION 1 (multiple-choice questions) [10 marks in total]**

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and mark your selection on the answer sheet by highlighting the relevant paragraph **in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

**Question 1.1**

Select the correct answer:

The **China Enterprise Bankruptcy Law 2006** applies to:

1. Natual persons in financial difficulty.
2. Enterprises having an independent legal status.
3. Partnerships.
4. Sole traders.

**Question 1.2**

Select the correct answer:

The China Enterprise Bankruptcy Law 2006 provides three major **insolvency procedures**, namely:

1. Reorganisation, scheme of arrangement and liquidation.
2. Receivership, settlement and liquidation.
3. Liquidation, settlement and company voluntary arrangement.
4. Reorganisation, settlement and liquidation.

**Question 1.3**

Select the correct answer in relation to the **appointment of the bankruptcy administrator**:

1. The bankruptcy administrator can only be appointed by the debtor when the company files for bankruptcy in court.
2. Only the court can appoint a bankruptcy administrator. Creditors may request a replacement bankruptcy administrator to be appointed if the court-appointed administrator is proven to be incompetent or biased at a later stage of the proceedings.
3. Both the debtor and creditors can appoint provisional bankruptcy administrators when filing.
4. The court can only appoint a bankruptcy administrator after getting consent from both the debtor and the creditors.

**Question 1.4**

**Select the correct answer:**

Which party is **eligible to file** a company bankruptcy petition to the court?

1. Directors can file for company bankruptcy in a court.
2. Both the debtor and the creditors may file for bankruptcy.
3. Only the debtor is allowed to file.
4. Both creditors and shareholders of the company may file for bankruptcy.

**Question 1.5**

Regarding the “control” model in corporate reorganisation under the China Enterprise Bankruptcy Law of 2006, which of the following statements is **correct**?

1. The debtor-in-possession model is not available under the Chinese corporate reorganisation provisions.
2. Both debtor-in-possession and administrator-in-possession models are available under the Chinese corporate reorganisation provisions.
3. Once the administrator-in-possession model is chosen, it cannot be converted into the debtor-in-possession model.
4. The debtor-in-possession model is automatically selected once a reorganisation procedure is commenced.

**Question 1.6**

Regarding preferential creditors in China, which of the following statements **is correct**?

1. Both the tax authorities and employees are treated as preferential creditors in China.
2. The preference of tax authorities has been abolished by the China Enterprise Bankruptcy Law of 2006.
3. Tax authorities are ranked higher than employees in the priority hierarchy.
4. Tax authorities are treated as unsecured creditors in China and are not given preferential treatment.

**Question 1.7**

A corporate reorganisation plan that has been voted on must be approved by the court before it takes effect. Indicate which one of the following statements is **correct**:

1. If the reorganisation plan was voted down (rejected) by one or more class of creditors, the court may still approve the plan if certain statutory conditions are met; a cram-down is therefore available under Chinese law.
2. A cram-down approval is not available under the China Enterprise Bankrupty Law 2006.
3. If shareholders do not support / approve the reorganisation plan, the plan cannot be crammed-down by the courts.
4. Only a reorganisation plan that has been fully supported by all classes of stakeholders entitled to vote can be sent to the court for approval.

**Question 1.8**

As regards the recognition of foreign bankruptcy proceedings in China, select the **correct answer**:

1. A foreign bankruptcy proceeding can be recognised in China, provided there is a judicial assistance treaty with China or reciprocity with China has been established.
2. China strictly applies the principle of territorialism and consequently no foreign bankruptcy proceeding or ruling can be recognised in China.
3. China has adopted the UNCITRAL Model Law on Cross-Border Insolvency and all foreign bankruptcy proceedings can be automatically recognised in China.
4. China only recognises foreign bankruptcy orders from countries which have joined the Belt & Road Initiative.

**Question 1.9**

Select the correct answer:

In terms of the **stated universal effect** of a Chinese bankruptcy proceeding, the practical approach is that:

1. The Chinese bankruptcy administrator can use the court bankruptcy ruling to bar foreign creditors from taking legal action against the company’s assets in all foreign courts.
2. The Chinese bankruptcy administrator must seek recognition of the Chinese bankruptcy ruling abroad, otherwise the Chinese bankruptcy ruling will not be effective in other jurisdictions.
3. The Chinese bankruptcy ruling can only be recognised in countries that have adopted the UNCITRAL Model Law on Cross-Border Insolvency.
4. The Chinese bankruptcy ruling will never be recognised in other jurisdictions since China has not adopted the UNCITRAL Model Law on Cross-Border Insolvency.

**Question 1.10**

Select the correct answer:

The introduction of the corporate rescue procedure under the China Enterprise Bankruptcy Law 2006 was most **influenced** by the jurisdiction of:

1. The United States of America.
2. Japan.
3. Singapore.
4. The United Kingdom.

**QUESTION 2 (direct questions) [10 marks]**

**Question 2.1 [2 marks]**

If a creditor wants to bring a defaulting debtor company into a bankruptcy liquidation procedure in China, which bankruptcy test should be fulfilled before the court can accept the filing?

For a creditor filed bankruptcy petition, the cash-flow bankrupty test must be satisfied to establish that the debtor is involvent, namely that the debtor is unable to pay a debt that is true and due.

**Question 2.2 [maximum 4 marks]**

Name the two professions in China that dominate Chinese regional bankruptcy administrator lists **and** briefly explain how they are appointed in practice.

The two dominant professions are lawyers and accountants. The power of selection of the firms included rests generally by provincial supreme people’s courts, which seek collaboration from the relevant local associations. Such associations are controlled by local government justice and finance departments. In practice, whether or not a firm is included on the list is contingent on the firm’s size.

**Question 2.3 [maximum 4 marks]**

Please briefly describe the major features of fixed charges and pledges as the major forms of security in China.

Fixed pledges are generally used with respect to immovable property such and buildings and land (although occasionally granted over vehicles and machinery), noting that all land is owned by the state, which is leased to private parties.

A charge must be registered under the Chinca Civil Code 2020 and is invalid until it is so registered.

Charges are generally respected by the courts, taking into account that the holders of said charges are generally state owned banks The only threat to charges are employee claims, which generally receive priority, even outside of bankruptcy procedures.

Pledges are used less frequently. A pledge becomes valid after the pledged asset comes into possession of the secured creditor, and no registration is required (unless the asset is intangible).

**QUESTION 3 (essay-type questions) [15 marks in total]**

**Question 3.1 [maximum 8 marks]**

“The China Enterprise Bankruptcy Law of 2006 is a rescue-oriented piece of insolvency legislation, emphasising rescue over liquidation.”

Discuss why, at least in theory, this statement is true.

With respect to its origins and drafting, the Law was influenced heavily by Chapter 11 procedures and the US Bankruptcy Code 1978, itself a rescue oriented procedure.

Chapters 8 and 9 of the law deals with corporate rescue mechanisms, highlighting the intent of drafters to promote the use of corporate rescue.

Of the three procedures available under the law, two are inherently rescue options. The first option, reoganisation, borrows most elements from US Chapter 11, and can be filed without being bankrupt or passing bankruptcy tests. Similar to the US counterpart, it offers a debtor-in-possession control model (albeit such possession is not granted automatically, and must be sanctioned by the court).

The second procedure is settlement, also a rescue procedure, reserved for voluntary filing by the debtor itself. It must be accompanied by a settlement plan, to be voted on by creditors. In practice, settlement is difficult to implement given lack of necessary detail in the relevant statute, and lack of incentive for secured creditors to participate / support.

In practice, there are only a handful of court-involved bankruptcy proceedings (including rescue procedures) in any given year. The vast majority insolvent businesses in China simply continue to exist in the market, or cease operation without using a formal bankruptcy process.

**Question 3.2 [maximum 7 marks]**

Briefly explain the process for the proof of claims in a corporate liquidation procedure and the procedure that is followed should the value or existence of a creditor’s claim be disputed.

Creditors should contact the bankruptcy administrator, and then complete and submit the requisite claim form. Generally, the administrator will verify the creditors’ claims to the company’s books and records, and/or consult with the company’s finance team.

Should there be a dispute with respect to the value or validity of the claim, the creditor may litigate in the same court for judgement.

The final result of such litigation serves as the ultimate amount of the claim.

**QUESTION 4 (fact-based application-type question) [15 marks in total]**

**Question 4.1 [maximum 8 marks]**

The bankruptcy liquidator of an Australian company finds that some of the company’s assets are located in Beijing, China. A Chinese creditor has taken legal action in the Beijing Second Intermediate People’s Court, which has issued an injunction freezing the assets of the Australian company in China. The liquidator has approached you for advice on how the Australian bankruptcy proceeding can be recognised in China. Advise the liquidator.

China has not adopted UNCITRAL Model Law, and is not a common law jurisdiction. Accordingly, the recognition of foreign judgements is dealt with largely by legislation.

Article 5 of the Law provides that a foreign court bankruptcy binds the company’s assets located in China; however, the ruling must first be recognised by a Chinese chourt before taking effect. This recognition should be based on judicial assistance treaty with the foreign country, or on the principle of reciprocity.

Australia does not have a judicial assistane treaty with China, and accordingly must rely on reciprocity. The Chinese courts require the foreign countrys’ courts to already have a recognition precedent in favour of a Chinese party, and will generally not recognise a foreign bankruptcy judgement in lieu of same.

There is yet to be a successful Australian bankruptcy ruling to be recognised in China, the liquidators’ proposed application appears challenging. Indeed, most foreign recognition applications are rejected by the Chinese courts simply on the basis that there is no assistance treaty or reciprocity. Even in the event that one of these requisites are met, often the courts will rely on procedural defects to reject the application

**Question 4.2 [maximum 7 marks]**

Huaxing Microchip Limited is a large high-tech manufacturing company based in Shanghai. In 2019, the company was unable to repay a RMB 23 million loan to the Construction Bank of China (Shanghai Branch) and was petitioned for bankruptcy liquidation by the Bank at the Shanghai First Intermediate People’s Court. Three days after submitting the petition, the Court accepted the liquidation filing and appointed Granter Partners, a local law firm included in the local bankruptcy administrator list, as the liquidation administrator.

Shortly after the commencement of the bankruptcy of Huaxing Microchip Limited, the CEO of Naking Limited, a controlling shareholder holding 32% of the equity of Huaxing Microchip Limited, approaches you for advice.

**Using the facts above, answer the questions that follow.**

**Question 4.2.1 [maximum 4 marks]**

The CEO of Naking Limited tells you that the various businesses of Huaxing Microchip Limited are still viable and that a piecemeal liquidation of the company will not be in the interests of any of the stakeholders. Since Huaxing Microchip Limited appears to have a bright future if the current debt crisis can be resolved, you are asked to explain whether (and if so, how) the current liquidation procedure can be converted to a reorganisation procedure.

Article 70 of the China Enterprise Bankruptcy Law 2006 provides that the debtor or its shareholders holding 10% of more equity may apply to the court for conversion from liquidation to reorganisation. As the CEO holds 32% of the equity, this condition is satisfied.

Huaxing Microchip Limited (HM) may be converted to a reorganisation procedure can apply to the Shanghai First Intermediate People’s Court for the debtor-in-possession model to be applied. If such an application is approved, control will return to the debtor, and the bankruptcy administrator will act as a reorganisation supervisor.

Pursuant to Article 73 of China Enterprise Bankruptcy Law 2006, the debtor will control the company’s operations, including the drafting of a reorganisation plan for creditors to vote on, which may preserve the viable businesses of HM.

Such a plan, which may comprise debt foregiveness and/or equity adjustment, must be approved by creditors and sanctioned by the court, and must include a business restructuring sub-plan.

**Question 4.2.2 [maximum 3 marks]**

Assuming that the bankruptcy liquidation of Huaxing Microchip Limited is successfully converted to a reorganisation procedure, a reorganisation plan for Huaxing Microchip Limited is eventually voted on by the various stakeholders. Due to the fact that Huaxing Microchip Limited is insolvent, the reorganisation plan *inter alia* proposes that the shares of all previous shareholders be entirely cancelled. Unhappy that its equity in Huaxing Microchip Limited will be wiped out by the reorganisation plan, Naking Limited understandably votes against the plan. However, since the plan has only been voted down by the shareholders and approved by all the classes of creditors, the reorganisation administrator submits the reorganisation plan to the Shanghai First Intermediate Court for approval.

Advise the CEO of Naking Limited as to whether a cram-down approval by the court is possible, and if applicable, what conditions should be met before the court could hand down a cram-down approval.

Article 85 of the China Enterprise Bankruptcy Law 2006 suggest that the plan must be passed by shareholders. Notwithstanding, Article 87 provides that a court may cram-down a plan that has been voted down by one or more class of stakeholder.

Article 87 provides that for a cram-down to be enacted by the court, the plan must:

* Be approved by secured creditors (or secured creditors must be fully paid out of secured assets); and
* Be approved by employees and tax authorities (or they must be paid in full); and
* Be approved by unsecured creditors (or they must not be paid less than they would receive in a liquidation); and
* Be approved by shareholders where their equity is affected (or their treatment must be fair and equitable); and
* Pay stakeholders within classes fairly, with priority between shareholders and creditors maintained; and
* Be feasible.

All things being equal, considering that the courts have found HM to be insolvent, it is likely that it will also find cancellation of shares to be in satisfaction of the equitable treatment condition. Indeed, absolute priority between shareholders and creditors must be maintained, and taking into consideration creditors are unlikely to be paid in full under the plan, shareholders are likely to be worth nil.

**\* End of Assessment \***