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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: **[studentnumber.assessment8B]**. An example would be something along the following lines: 202021IFU-314.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 “studentnumber” 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 2021**. The assessment submission portal will close at **23:00 (11 pm) GMT on 31 July 2021**. 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 **8 pages**.

ANSWER ALL THE QUESTIONS

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

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 (correct)

Select the correct answer:

Which of the following are eligible to use the China Enterprise Bankruptcy Law of 2006 to enter into a court-involved bankruptcy procedure in China?

- (a) Individuals, when in financial difficulty.
- (b) Enterprises having an independent legal status.**
- (c) Enterprises or partnerships.
- (d) State-owned enterprises only.

Question 1.2 (correct)

Select the correct answer:

Which three bankruptcy options are provided by the China Enterprise Bankruptcy Law of 2006?

- (a) Reorganisation, scheme of arrangement and liquidation.
- (b) Receivership, settlement and liquidation.
- (c) Liquidation, settlement and company voluntary arrangement.
- (d) Reorganisation, settlement and liquidation.**

Question 1.3 (correct)

Select the correct answer:

How is a bankruptcy administrator appointed under the China Enterprise Bankruptcy Law of 2006?

- (a) The bankruptcy administrator is appointed by the debtor when the company files for bankruptcy in court.
- (b) 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.**

- (c) Both the debtor and creditors may appoint provisional bankruptcy administrators.
- (d) The court can only appoint a bankruptcy administrator after consulting with both the shareholders and the creditors.

Question 1.4 (correct)

Select the correct answer:

Which parties may file for bankruptcy in court under the China Enterprise Bankruptcy Law of 2006?

- (a) Only the debtor may file for bankruptcy.
- (b) Both the debtor and the creditors may file for bankruptcy.**
- (c) Only the shareholders of the debtor company may file for bankruptcy.
- (d) Both creditors and shareholders of the company may file for bankruptcy.

Question 1.5 (correct)

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

- (a) The debtor-in-possession model is categorically not available under the Chinese corporate reorganisation provisions.
- (b) Both debtor-in-possession and administrator-in-possession models are available under the Chinese corporate reorganisation provisions.**
- (c) Once the administrator-in-possession model is chosen, it cannot be converted into the debtor-in-possession model.
- (d) The debtor-in-possession model automatically applies once a reorganisation procedure is commenced.

Question 1.6 (correct)

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

- (a) Both the tax authorities and employees are treated as preferential creditors in China.**
- (b) The preference of tax authorities has been abolished by the China Enterprise Bankruptcy Law of 2006.
- (c) Tax authorities are ranked higher than employees in the priority hierarchy.
- (d) Tax authorities are paid before fixed charge holders.

Question 1.7 (correct)

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**:

- (a) 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.
- (b) A cram-down cannot be exercised by Chinese courts.
- (c) If the shareholders do not support / approve the reorganisation plan, the plan cannot be crammed-down by the court.
- (d) 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 (correct)

Select the correct answer:

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

- (a) 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.
- (b) China strictly applies the principle of territorialism and consequently no foreign bankruptcy proceeding or ruling can be recognised in China.
- (c) China has adopted the UNCITRAL Model Law on Cross-Border Insolvency and all foreign bankruptcy proceedings can be automatically recognised in China.
- (d) China only recognises foreign bankruptcy orders of its largest trading partners, such as the USA and the EU.

Question 1.9 (correct)

Select the correct answer:

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

- (a) 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.
- (b) 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.
- (c) The Chinese bankruptcy ruling can only be recognised in countries that have adopted the UNCITRAL Model Law on Cross-Border Insolvency.
- (d) 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 (correct)

Select the correct answer:

When drafting the China Enterprise Bankruptcy Law of 2006, which country's corporate rescue laws influenced Chinese lawmakers the most?

(a) The United States of America.

(b) Singapore.

(c) Australia.

(d) The United Kingdom.

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [2 marks] (0 points rewarded)

What bankruptcy test(s) should be met if a bankruptcy petition is filed **by a creditor** in China?

According to article 2 of the China Enterprise Bankruptcy Law of 2006, in the case, a creditor files a bankruptcy petition of a debtor must present bankruptcy tests either cash flow or balance sheet. (cash flow test only)

Question 2.2 [maximum 4 marks] (4 points rewarded)

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

Lawyers and accountants are two main professions that dominate the insolvency practitioner list in China.

Moreover, according to article 13 of the China Enterprise Bankruptcy Law of 2006, when the bankruptcy petition is accepted by the court, it simultaneously appoints the bankruptcy administrator. The Chinese courts generally use the list of the locally qualified bankruptcy practitioner (the majority are lawyers and accountants) and sometimes a bid will be made if the case proves to be complex and large.

Question 2.3 [maximum 4 marks] (4 points rewarded)

Name the two main types of security available under Chinese law **and** explain how and where they are registered.

1. Fixed charge

A charge can be created over both movable and immovable property in favour of a secured creditor (usually a bank). A charge can be created over the debtor's assets or even over the assets of a third party, provided the third party's consent has been obtained in advance.

It has to be registered under the China Property Law of 2007 and is not valid until it has been registered. A security certificate is issued to the charge holder once the charge has been properly recorded at the government agency. In addition, for immovable property

the registration authority is the local office of the China Housing Management Authority.

2. Pledges

These can be made assets such as shares, trademarks, cheques, and patents. For movable assets, no registration of a pledge is required. Many intangible assets can also be pledged but should be registered.

For trademarks, the registration authority is the China Industries and Commerce Regulation Bureau Central Office. A pledge on patents should be registered at the China Intellectual Property Authority Central Office. For shares of listed companies, the registration authority is the China Securities Depository and Clearing Corporation Limited. In the case of shares of a non-listed company, the registration of a pledge takes place at the local office of the China Companies House where the enterprise is registered.

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

Question 3.1 [maximum 8 marks] (5 points rewarded)

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

Discuss this statement and indicate whether you agree or disagree with it, providing reasons for your answer.

I totally agree with this statement due to the fact that article 2 of the China Enterprise Bankruptcy Law of 2006 (CEBL) claims that a voluntary reorganization petition can be made when a debtor (company) is **not yet bankruptcy** but is likely to be in this situation in the near future. Moreover, a voluntary reorganisation filing does not require evidence that the company is already bankrupt.

So, rescue-oriented the CEBL comprises three substantial bankruptcy procedures: Reorganization, composition and liquidation.

According to chapters 8 and 9 of CEBL, the Chinese lawmakers **encourage the** use of corporate rescue. In these chapters, reorganizations and composition, regulations state different rules in favour of rescue a company such as petition for and period of reorganization, adoption and implementation of reorganization plan, among others.

Additionally, after the enactment of the first rescue-oriented CEBL, China started to develop its insolvency profession establishing its own regional qualified insolvency practitioner lists, where courts can choose between listed professionals (especially lawyers and accountants) who will be administrators or liquidators.

“(…) China promulgated its first rescue-oriented Enterprise Bankruptcy Law of 2006 (the EBL 2006) with the objectives of facilitating more corporate reorganizations, establishing a market-based corporate insolvency profession and of enhancing cross-border insolvencies”¹.

Another aspect is that article 70 of CEBL states that the debtor or its shareholders holding 10% or more of the company's equity can apply to court for a **conversion** from liquidation to reorganization.

¹ Zhang, Z (2020) *Resolving Corporate Insolvencies in China: The Gap between Law and Reality*. Miami International & Comparative Law Review, 27 (2).

In conclusion, the China Enterprise Bankruptcy Law of 2006 is modern, advanced, rescue-oriented bankruptcy statute, but the big challenge is to implement this regulation in practice where there only are a small number of bankruptcy cases per year.

(DIP, conversion to rescue, cramdown could have been mentioned)

Question 3.2 [maximum 7 marks] (7 points rewarded)

Briefly explain the process for the proof of claims in a reorganisation procedure and the procedure that is followed should the value or legality of a creditor's claim be disputed.

Proof of claim

Creditors are required to file their claims within a time period stipulated by courts, this period commences from the date of publication by the court of the announcement of its acceptance of the bankruptcy petition and runs for a minimum of 30 days and a maximum of three months.

Creditors must prove their claims, they must request the reorganisation administrator and will usually be required to fill in a claim form provided by the administrator. In many cases, the reorganisation administrator will check the company's books and consult with staff from the company's financing unit for verification.

Major eligible claims include debts that exist at the time of the court's acceptance of the application for bankruptcy; unmatured debts; conditional debts or debts subject to time limits; claims pending litigation or arbitration; debts owed to joint creditors; indemnity obligations owed to a guarantor of the debtor or to another joint debtor who has discharged debt on the behalf of the debtor; and damages under a contract terminated by the administrator or the debtor under the provisions of the Bankruptcy Law.

Disputed claim

In case of a dispute or controversy over the legality or the accuracy of the claim, creditors might discuss before the same court for a judgment. For most effectiveness, many courts develop an expedited process to resolve these claims.

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

Question 4.1 [maximum 8 marks] (7 points rewarded)

The bankruptcy liquidator of an Australian company finds that some of the company's assets are located in Shanghai, China. A Chinese creditor has taken legal action in a local (Chinese) court, which has issued an injunction freezing the assets of the Australian company in Shanghai. The liquidator has approached you for advice on how the Australian bankruptcy proceeding can be recognised in China. Advise the liquidator.

According to article 5 of the China Enterprise Bankruptcy Law of 2006, a foreign bankruptcy ruling can be recognised in China if some assets are located in this Asian country. In this particular case, due to the Australian country has assets in China it is possible to use this mentioned article.

However, this company must comply with one of the two rules:

- (i) There is a judicial assistance treaty between China and that foreign country over civil and commercial matters. At present, there is no treatment with include Australia.
- (ii) If there is no treaty, it is still possible to seek recognition and the foreign bankruptcy representative needs to prove that there is judicial reciprocity between China and Australia.

However, reciprocity is non-existent unless and until there is a Chinese judgment recognised in Australia and Chinese courts rarely take the first step to exercise reciprocity or comity. Without the existence of a treaty or reciprocity, it is very unlikely that a foreign judgment will be recognised in China. Our recommendation is that the Australian company's liquidator should initiate new litigation in China instead of trying to recognise the Australian liquidation in China.

(reciprocity exists between the two)

Question 4.2 [maximum 7 marks]

Yangtze Steel Limited is a large steel manufacturing company based in Shanghai. In 2010, the company was unable to repay a RMB 23 million loan to the Bank of China (Shanghai Branch) and was petitioned for bankruptcy liquidation by the Bank at the Shanghai Second Intermediate People's Court. Three days after submitting the petition, the Court accepted the liquidation filing and appointed Jingchen Partners, a local law firm included in the local bankruptcy administrator list, as the liquidation administrator.

Shortly after the commencement of the bankruptcy of Yangtze Steel Limited, the CEO of SanLong Limited, a controlling shareholder holding 32% of the equity of Yangtze Steel Limited, approaches you for advice.

Using the facts above, answer the questions that follow.

Question 4.2.1 [maximum 4 marks] (4 points rewarded)

The CEO of SanLong Limited tells you that the various businesses of Yangtze Steel Limited are still viable and that a piecemeal liquidation of the company will not be in the interests of any of the stakeholders. Since Yangtze Steel 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.

According to article 70 of the China Enterprise Bankruptcy Law of 2006, if the creditor file the liquidation application, the debtor or capital contributor holding more than one-tenth (10%) of the debtor's registered capital may file the reorganization application after the People's Court accepts the insolvency case but before the debtor is declared insolvent.

In this particular case, Yangtze Steel Limited has 32% of shares and the court has accepted the liquidation filing but has not declared insolvent to the debtor, in this case, it is possible that the CEO of Yangtze Steel Limited can convert this liquidation into a reorganization.

So, the debtor may file the conversion request, it must be submitted to the court that then judges take a decision about this request, this conversion is not frequently used in China.

Question 4.2.2 [maximum 3 marks] (2 points rewarded)

Assuming that the bankruptcy liquidation of Yangtze Steel Limited is successfully converted to a reorganisation procedure, a reorganisation plan for Yangtze Steel Limited is eventually voted on by the various stakeholders. Due to the fact that Yangtze Steel Limited is insolvent, the reorganisation plan *inter alia* proposes that the shares of all previous shareholders be cancelled. Unhappy that its equity in Yangtze Steel Limited will be wiped out by the reorganisation plan, SanLong 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 Second Intermediate Court for approval.

Advise the CEO of SanLong Limited as to whether the Court can approve such a plan under the current law in China.

Article 87 states of the China Enterprise Bankruptcy Law of 2006 that the court may cram-down a reorganization plan that has been voted down by the shareholders.

A reorganisation plan seeking cram-down approval by the court must (i) be voted in favour of by the secured creditor class and, if not, secured creditors must be fully paid out of the secured assets (in addition to fair compensation for the delayed foreclosure); (ii) be voted in favour of by the employee and tax authority classes and, if not, these two classes must be paid in full; (iii) be voted in favour of by the ordinary unsecured creditor class and, if not, this class of creditors must not be paid less than they would have received under a liquidation procedure; (iv) be voted in favour of by the shareholders where their equity is affected by the plan and, if not, the treatment of equity holders is fair and equitable; (v) pays the stakeholders in the same class fairly, with the priority between shareholders and creditors upheld; and, (vi) be feasible.

In this case, the court must not approve this plan because it affects shareholders to cancel the shares, they have the right to retain their shares, this treatment is not fair and equitable for shareholders.

(it is fair to do so)

43 out of 50 points rewarded

*** End of Assessment ***