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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] (9 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 (incorrect, it is b)**

**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)**

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

[To initiate a formal bankruptcy reorganisation procedure, the petition to the court can be made either by the company or its creditors. Article 2 of the China Enterprise Bankruptcy Law of 2006 states that a voluntary reorganisation petition can be made when the company is not yet bankrupt but is likely to be bankrupt in the near future, which shows that a voluntary reorganisation filing does not require evidence that the company is already bankrupt. This has obviously been done to encourage rescue efforts to be made at as early a stage as possible. However, in the case of a creditor petition under Article 2 of the China Enterprise Bankruptcy Law of 2006, the bankruptcy tests (either cash flow or balance sheet) still apply at a time when the reorganisation petition is presented.

As for the liquidation procedure, under Article 7 of the China Enterprise Bankruptcy Law of 2006, if the company is unable to pay a debt that is due, the creditor can file for liquidation in court. From this it is clear that for creditors a cash-flow bankruptcy test is used before the court will accept a liquidation petition. From the point of view of the company itself, Article 2 of this law allows the debtor to use either the balance-sheet or cash-flow test to convince the court that the commencement of a liquidation procedure is justified. In practice, submitting an audited balance sheet would be enough for the company to prove that it is balance-sheet or factually bankrupt.]

(it is the cash flow test)

**Question 2.2 [maximum 4 marks] (3 points rewarded)**

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

[The two professions in China that dominate Chinese regional bankruptcy administrator lists are lawyers and accounting firms. When a formal bankruptcy procedure is entered into, it is the court that has the exclusive power to appoint a bankruptcy administrator, in most cases an insolvency practitioner firm. Although Article 22 of the China Enterprise Bankruptcy Law of 2006 authorises creditors to request the replacement of the court-appointed administrator by way of a resolution at the creditors' meeting where the incumbent administrator behaves unlawfully or is biased, this generally does not happen in practice.] (the local administrator lists should be noted)

**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.

[The two main types of security available under Chinese law are fixed charge and pledges. A fixed charge can be created upon buildings or the use right of land, and must be registered. A pledge can be made upon assets such as shares, trademarks and patents, but also must be registered at relevant authorities. In regard to pledge registration authorities, these vary considerably and can be quite complex. For trademarks, the registration authority is the China Trademark and Patent Administration Bureau Central Office located in Beijing. A pledge on patents should be registered at the China Intellectual Property Authority Central Office, also located in Beijing. For shares of listed companies, the registration authority is the China Securities Depository and Clearing Corporation Limited, a state-owned company that has offices in Beijing, Shanghai, Shenzhen and Hong Kong. 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 company is incorporated.]

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

**Question 3.1 [maximum 8 marks] (2 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.

[The China Enterprise Bankruptcy Law of 2006 appears on the face of it to be a rescue-oriented bankruptcy statute. However, the greatest challenge is the difficulty of implementing this law in the real world, since every year there are only a small number of court-involved bankruptcy cases. The vast majority of bankrupt companies in China simply continue to exist in the market in an unlawful manner, which jeopardises the interests of creditors.]

(Early rescue, DIP, conversion to rescue, cram down, etc should be discussed)

**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.

[The creditors must approach the reorganisation administrator to prove their claims. Usually, will 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. In the event of a dispute over the legality or the accuracy of the claim, the creditor can litigate before the same court for a judgment, something that occurs regularly in practice.]

**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.

[The China Enterprise Bankruptcy Law provides that a foreign court bankruptcy ruling also binds the company's assets located in China. However, for a foreign court bankruptcy ruling Article 5 adds some restrictions, stating that the foreign bankruptcy court ruling must be recognised by a Chinese court before taking effect in China and that the recognition should be based either on a judicial assistance treaty signed and ratified between China and the requesting country, or on the principle of reciprocity if there no treaty. In the meantime, Article 5 includes some routine public interest reservations, so in this case, the Australian bankruptcy proceeding could be recognised in China, if providing that the recognition of the Australian court bankruptcy ruling not infringe upon the fundamental principles of Chinese law, China's sovereignty, security and public interests and does not disadvantage China's domestic creditors. ( **Reciprocity can be further discussed**)

**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.

[Under Article 70 of the China Enterprise Bankruptcy Law of 2006, in the event of an involuntary bankruptcy liquidation procedure, the debtor (SanLong Limited) or its shareholders holding more than 10% of the company's equity can apply to the court to convert the liquidation to reorganisation and, if agreed, the reorganisation procedure will commence immediately thereafter. Moreover, it is worth emphasising that local government support is critical before any bankruptcy reorganisation filings will be seriously considered by courts.]

**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.

[After being voted and approved on by the creditors (and shareholders, where required), the reorganisation plan must ultimately be confirmed the court before taking effect. The Article 87 provides that the court may cram-down a reorganisation plan that has been voted down by one or more class of creditors or by the shareholders. A reorganisation plan seeking cram-down approval by the court must meet the statutory provisions of Article 87, different of a reorganisation plan that has successfully passed the vote of all classes of stakeholders and that should only be assessed by the court for its procedural legality.

In the case, the CEO of SanLong Limited can ask the Court for cram-down the reorganisation plan, because its been approved by all the classes of creditors but voted down by the shareholders.]

(The fair and equitable test could be mentioned)

38 out of 50 points rewarded

**\* End of Assessment \***