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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?

When a creditor files a bankruptcy petition, the bankruptcy tests that would be applied and have to be proven are cash flow or balance sheet insolvency.
(cash flow 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.

In China, the two professions that dominate Chinese regional bankruptcy administrator lists are lawyers and accountants. The lists are compiled by the provincial Supreme People's Courts upon the direction of the China Supreme People's Court.

A bankruptcy administrator can only be appointed on a bankruptcy matter by either the provincial Supreme People's Court or the local Intermediate People's Court, as selected directly from the list or sometimes through a tender for complex cases.

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 charges and pledges.

A fixed charge is registered under the China Property Law of 2007 with the China Housing Management Authority and the China Land Management Authority (for immovable property), the local police vehicle management office (for vehicles) and the China Industries and Commerce Regulation Bureau (for machinery and equipment).

In contrast, a pledge over tangible moveable property is not required to be registered however pledges over certain intangible assets need to be registered, such as trademarks

with the China Industries and Commerce Regulation Bureau, patents with the China Intellectual Property Authority, listed company shares with China Securities Depository and Clearing Corporation Limited and non-listed shares with the China Companies House located where the company in question is incorporated.

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

Question 3.1 [maximum 8 marks] (7 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 three principal options under the China Enterprise Bankruptcy Law of 2006 are reorganisation, settlement and liquidation. The **first two options** clearly indicate that the China Enterprise Bankruptcy Law of 2006 is a rescue-orientated piece of insolvency legislation, since it provides more options to rescue than for liquidation.

The conceptual elements for reorganisation under the China Enterprise Bankruptcy Law of 2006 are predominantly adopted from Chapter 11 in the US which is a voluntary procedure **without having** to satisfy any bankruptcy tests when filing for reorganisation.

Similar to Chapter 11, **reorganisation under the China Enterprise Bankruptcy Law of 2006 is based on a debtor-in-possession** structure for the process. However unlike Chapter 11, debtor-in-possession is not the default opening position for reorganisation in China, since an application needs to be made to court following the appointment of the court administrator, for reorganisation to be based on debtor-in-possession. Nevertheless, the emphasis and orientation for rescue is apparent, albeit under the supervision of the court and any court appointed administrators.

Reorganisations are voted on by four types of creditors namely secured, unsecured, employees and tax authorities. The threshold for voting is majority but representing two thirds in value for each type of creditor that attends the vote. Despite this, the China Enterprise Bankruptcy Law of 2006 allows a court to force through a reorganisation plan if not approved by the creditors vote, which in effect allows for a **cram down** of the reorganisation plan in a manner similar to Chapter 11.

Settlement under the China Enterprise Bankruptcy Law of 2006 is also a voluntary procedure and also involves voting by creditors on a settlement plan presented to court. This further cements the legislators intent for the China Enterprise Bankruptcy Law of 2006 as rescue minded legislation.

(conversion to rescue from liquidation 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.

In the process of having a reorganisation plan accepted under the China Enterprise Bankruptcy Law of 2006, creditors need to be able to prove their claims which form part of the reorganisation plan. For creditors to do so, they need to approach the administrator of

the company undergoing reorganisation and provide details of their claims as per the form supplied to them by the administrator.

This will then give the administrator the opportunity to investigate the creditors claim by inspecting the company's accounts, operations and speaking with the company's employees in order to verify the creditors claim.

If there is a disparity in the creditors' alleged claim, and the administrator's findings, there may be a dispute which the creditor can seek to resolve by applying to the same court where the reorganisation is being supervised in order to seek a judgment of the court which confirms the legal basis or factual details of the creditors claim.

The court expects such creditor applications for judgements on proving their claims (given that it regularly happens in reorganisations) and therefore the court seeks to implement expedited procedures for these creditor applications.

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

Question 4.1 [maximum 8 marks] (8 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.

Assuming the bankruptcy liquidator is in possession of a final and conclusive judgment, the China Civil Procedure Law of 1991 allows the bankruptcy liquidator to apply directly for its recognition to the local Intermediate People's Court relevant to the location of the Australian company's assets in China.

However in order for the judgment held by the bankruptcy liquidator to be recognised, the China Civil Procedure Law of 1991 requires that a judicial assistance treaty is in place between China and Australia, or otherwise that the courts of Australia have taken the first step in recognising a judgment of a Chinese court, thereby allowing for the Intermediate People's Court to reciprocate recognition. At present, it would appear that there is neither a judicial assistance treaty nor reciprocity with Australia or Australian courts.

The above assumes that the judgment sought to be recognised is not contrary to Chinese law, sovereignty, security or public interest. This situation may be better if the bankruptcy liquidator seeks to recognise a foreign arbitration, however again a judicial assistance treaty or reciprocity with the relevant country is required.

Notwithstanding the above, the recognition of foreign judgments is particularly difficult and challenging in practice, with very few precedent cases (involving Italy, France and Germany), therefore making such instances rare. Ultimately the bankruptcy liquidator may be best to consider unfreezing and recovery of the Australian company's assets in China through the Chinese courts.

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.

The liquidation of Yangtze Steel Limited appears to be involuntary. In this case, the CEO of SanLong Limited can consider applying to court for conversion of the liquidation procedure into a reorganisation procedure, on the basis of his shareholding of 32% in Yangtze Steel Limited, since the minimum equity threshold under Article 70 of the China Enterprise Bankruptcy Law of 2006 to make such an application is a shareholding of 10%.

The application would then have to be approved by the court and may be difficult to achieve given that liquidation to have been accepted by the Chinese court would suggest that Yangtze Steel Limited has already passed the applicable bankruptcy tests. It is also unclear how the Bank of China (Shanghai Branch) would respond to such an application in seeking to protect its interests.

Question 4.2.2 [maximum 3 marks] (3 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 85 of the China Enterprise Bankruptcy Law of 2006 requires that the vote of shareholders be taken when their shareholding is to be cancelled pursuant to and in order to approve a reorganisation plan. Nevertheless, the court must approve the reorganisation plan, however the vote proceeds, and pursuant to Article 87 of the China Enterprise Bankruptcy Law of 2006, a court may **cram down** the reorganisation plan even if voted down by SanLong Limited as the shareholder.

Article 87 of the China Enterprise Bankruptcy Law of 2006 sets out statutory requirements in order for a cram down to be successful, which relate to each type of stakeholder, but when it comes to shareholders the requirement is that shareholders have voted in favour, or their treatment has been **fair and equitable**.

In addition, the court will seek to ensure that creditors receive full payment from the reorganisation plan before shareholders, such that shareholders be left with nothing given creditors should receive priority.

Based on precedents, a quarter of all reorganisation plans have been crammed down by the Chinese courts.

47 out of 50 points rewarded

*** End of Assessment ***