



46/50 marks awarded by Zinian

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] (9/10 points awarded)

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, 1 point)

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 (incorrect, the correct one is d)

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, 1 point)

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, 1 point)

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, 1 point)

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, 1 point)

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, 1 point)

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, 1 point)

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, 1 point)

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, 1 point)

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] (2 points awarded)

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

[The filing creditor must convince the court that the debtor is cash-flow insolvent, namely that the debtor is unable to pay a debt that is due.]

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

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

[Large local law and accounting (ie, lawyers and accountants) firms dominate the Chinese regional bankruptcy administrator lists. Although 'qualified' was used by the China Supreme People's Court in its instructions to establish the regional 'qualified' insolvency practitioner list, there are really no 'qualifying' exams or training courses that need to be taken. Provincial supreme courts simply select some local large law and accounting firms to be included in the list.]

Question 2.3 [maximum 4 marks] (3 points awarded)

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

[The first and most widely used form of security is the fixed charge, which can be created over the debtor's assets or the assets of a third party, provided the third party's consent has been obtained in advance. They can be created over both movable and immovable property in favour of a secured creditor. The charge must 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, upon payment of a small fee, at the government agency. For immovable property, the registration authority is the local office of the China Housing Management Authority and, for safety, most secured creditors tend to simultaneously register the charge at the local office of the China Land Management Authority, since the use right of the

land upon which the building stands is part of the property. This is important as land is owned by the state and the right to use the property, which is essentially a lease, can be purchased by private parties. Nonetheless, if there are no building on the land yet, the pure right to use relating to a piece of land can also bear a charge, subject to registration. Occasionally, fixed charges are created over movable properties, which also need to be registered. For vehicles, the registration authority is the local police vehicle management office, whilst for machinery and other equipment, the local office of the China Industries and Commerce Regulation Bureau.]

Pledge should also be included here

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

Question 3.1 [maximum 8 marks] (6 points awarded)

“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* (‘CEBL’) was greatly influenced by Chapter 11 of the *US Bankruptcy Code 1978* on corporate reorganisation. As such, the Chinese bankruptcy law became rescue-oriented by incorporating three substantial bankruptcy option/procedures – reorganisation, composition/settlement and liquidation which is the final option. The way that these options are ordered in the law reflects that the lawmakers expect rescue to be **attempted first**. Moreover, the *CEBL* uses two chapters, Chapters 8 and 9 to highlight corporate rescue; thus, highlighting the lawmakers’ preference towards corporate rescue. Likewise, the rescue-oriented approach is also reflected in specific provisions. For example, in reorganisation proceedings, although the court appoints an administrator in charge of the whole reorganisation process, however, to make a rescue mission more feasible, the *CEBL* allows the debtor to apply for **debtor-in-possession** after the formal reorganisation procedure begins. If approved by the court, the debtor can regain control under the debtor-in-possession model, and the court-appointed administrator only becomes a supervisor. Allowing the debtor to take charge may increase the chances of rescuing the company as the debtor is considered more familiar with the business of the company, and with the moratorium in place, this increases the chances of successfully rescuing the company. Furthermore, even when liquidation proceedings have been commenced, the proceedings can still **be transformed** into a reorganisation proceeding.]

Nonetheless, while the *CEBL* appears on its face to be rescue-oriented, the greatest challenge is the difficulty of implementing this law given the prevailing realities in mainland China. This is shown by the fact that every year, there are only a small number of court-involved bankruptcy cases. There are several reasons why enforcing the rescue-oriented provisions of the *CEBL* is difficult to achieve. For instance, in opening any reorganisation procedure, local government support is critical before such application can be seriously considered by the court. Furthermore, courts are considerably cautious when allowing the commencement of corporate reorganisation. Likewise, many reorganisations end up in liquidation due to the court-appointed administrator’s heavy reliance on finding a buyer to rescue the company. Frequently, no buyer is found. Hence, although the *CEBL* can be considered on its face to be rescue-oriented, the realities and approaches followed in the actual reorganisation procedures show that a successful rescue is a very challenging goal.]

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

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.

[Creditors prove their claims by approaching the reorganisation administrator and filling up a claim form which the latter provides. In many instances, the reorganisation administrator will check the company books and consult the staff from the company's financing unit for verification. If the claim's legality or accuracy is disputed, the creditor can litigate before the same court for a judgment. Notably, many courts arrange for an expedited process to resolve these litigation disputes.]

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

Question 4.1 [maximum 8 marks] (8 points awarded)

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.

[China recognises foreign insolvency proceedings provided there is an existing judicial assistance treaty or reciprocity between China and the origin state of the judgment. This means that for Australian insolvency proceedings to be recognised in China, Australia should have had entered a judicial assistance treaty with China. Unfortunately, Australia has not entered into a judicial assistance treaty with China, and as such, thus, recognition could not be made on this basis.

Nonetheless, China has also recognised foreign judgments on the basis of reciprocity (ie, the foreign state should have given recognition to judgments in favour of a Chinese party *a priori*). This means that there should have been an Australian precedent recognising bankruptcy proceedings or judgment in favour of a Chinese party. Fortunately, Australia is among the countries which adopted the UNCITRAL Model Law on Cross Border Insolvency ('Model Law'), thus, there is a good chance that a Chinese insolvency proceeding has been recognised in an Australian court. Notably, the New South Wales court in *Bao v Qu; Tian (No 2)* [2020] NSWSC 588 has recognised and enforced a Chinese judgment. However, whether this enforcement by an Australian court is sufficient to establish reciprocity is something for the Chinese court to consider. However, one may not be too optimistic if one looks at the existing Chinese record of recognising foreign insolvency proceedings. Up to now, there are only a handful of foreign bankruptcy procedures that have been recognised in China, and none of these include an Australian bankruptcy proceeding.

As such, recognition of the Australian bankruptcy proceeding in China may be pursued by arguing that an Australian court in New South Wales has enforced and recognised a Chinese judgment in *Bao v Qu*. Such application for recognition should be filed in a Chinese local intermediate people's court, where the company assets are located, *i.e.*, Shanghai. However, it remains to be seen whether the Chinese court in Shanghai will give recognition of the Australian bankruptcy proceedings as *Bao v Qu* may not be considered a sufficient precedent. Nonetheless, the applicant may argue that Australia has adopted the Model Law, and therefore its courts would be ready to

recognise Chinese bankruptcy proceedings and judgments. However, again, it would totally depend on the Shanghai court whether to accept this argument.]

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 awarded)

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.

[Article 70 of the *China Enterprise Bankruptcy Law of 2006* ('CEBL') allows the conversion of the liquidation procedure into a reorganisation procedure. Particularly, if there was an involuntary liquidation procedure filed by the creditors, the debtor or its shareholders **holding 10%** or more of the company's equity can petition the court to convert the liquidation procedure into reorganisation. In this instance, since the liquidation of Yangtze Steel Limited was commenced by the Bank of China (Shanghai Branch), the liquidation procedure was an involuntary liquidation procedure. As such, SanLong Limited, as the controlling shareholder of Yangtze Steel Limited holding 32%, can commence the conversion into reorganisation procedure as it complies with the requirement that the conversion process should be commenced by the debtor or shareholders owning 10% or more. Hence, what SanLong Limited needs to do is to file a petition for such conversion before the Shanghai Second Intermediate People's Court by alleging that its petition complies with all the requirements for converting a liquidation procedure into a reorganisation procedure. However, the CEO of SanLong Limited must note that conversions are not frequently used in China, and such rarity might lead to some challenges during the conversion.]

Question 4.2.2 [maximum 3 marks] (3 points awarded)

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 *China Enterprise Bankruptcy Law of 2006* ('CEBL') provides that in cases where the company's equity is affected, adjusted, or cancelled by the reorganisation plan, it should also be voted by the shareholders. Such situation envisaged by Article 85 happened in this situation. In this instance, the reorganisation plan affecting Yangtze Steel Limited proposes that the shares of all previous shareholders be cancelled and what happened afterwards was that SanLong and other shareholders voted against the plan. Under Chinese law, it is unsettled what is the effect of the vote by the shareholders. Some insolvency scholars argue that the vote should be treated as advisory only. In any case, the approval of the reorganisation plan by the creditors still needed to be confirmed by the court. Notably, under article 87, CEBL, the court may **cram-down** a reorganisation plan that has been voted down by one or more class of creditors or by the shareholders. Hence, the court may approve the reorganisation plan even though SanLong and the shareholders have voted down the plan. The court's approval, however, in essence, would depend on whether the reorganisation plan would depend on three tests: (1) **fair and equitable** test (ie, the application of the pari passu principle between creditors in the same class); (2) absolute priority test (ie, shareholders should be paid nothing unless the creditors are paid in full); (3) feasibility test (ie, the reorganisation plan should be achievable). These tests are reflected in article 87 which provides that for the cram-down approval to be exercised by the court, the reorganisation plan must:

- (1) 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);
- (2) Be voted in favour of by the employee and tax authority classes and if not, these two classes must be paid in full;
- (3) 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;
- (4) 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;
- (5) Pays the stakeholders in the same class fairly, with the priority between shareholders and creditors, upheld; and
- (6) Be feasible.

Hence, whether the court would approve the reorganisation plan voted against by SanLong and the other shareholders would depend on the plan's compliance of the specific provisions of article 87 of the CEBL.]

46/50 points/marks awarded

*** End of Assessment ***