



**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: 202122-336.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 “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 2022**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. 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] (8 out of 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**

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? (1 point)

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

#### **Question 1.2**

Select the **correct answer**:

Which three bankruptcy options are provided by the China Enterprise Bankruptcy Law of 2006? (0 point)

- (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**

Select the **correct answer**:

How is a bankruptcy administrator appointed under the China Enterprise Bankruptcy Law of 2006? (1 point)

- (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**

Select the correct answer:

Which parties may file for bankruptcy in court under the China Enterprise Bankruptcy Law of 2006? (1 point)

- (a) Directors can file for company bankruptcy in a court.
- (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 (0 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 (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 ( 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 (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 (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 (1 point)**

Select the **correct answer**:

When drafting the corporate reorganisation chapter of 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) Russia.
- (c) Australia.
- (d) The United Kingdom.

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

**Question 2.1 [2 marks] (2 points)**

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

[As per Article 2 of the Enterprise Bankruptcy Law of 2006, the bankruptcy test is applied which means the company should either be cash flow or balance sheet bankrupt when a reorganisation petition is presented. All the companies are entitled to file for bankruptcy if they are deemed to be bankrupt either a cash flow or balance sheet test but under the voluntary recognition process a company need not pass any bankruptcy test. However, under the liquidation procedure under Article 7 of the China Enterprise Bankruptcy Law, 2006, if a liquidation petition is presented by a creditor, the cash flow bankruptcy test is applied before acceptance of the liquidation petition. On the other hand if such petition is presented by the debtor it can be based upon either the balance-sheet or cash-flow test.]

**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.

[In China, Law and Accounting Firms usually dominate the Chinese regional bankruptcy administrators. Bankruptcy administrators are appointed by the Court out of the list of insolvency practitioners and debtors and creditors do not have any say in the matter.

Article 22 of the Law allow creditors to approach the court to replace the administrator on the ground of incompetency, bias or unlawful behaviour by passing a requisite resolution on the creditors.]

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

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

[In China two main securities which are preferred are 'Fixed Charge' and 'Pledge'.

**A fixed charge** is created on the land and building and also on movable assets such as plant and machinery. Since, the land in China is owned by the state, it is the right of use of the land or the leasehold right over the property over which the charge is created.

Such charges are required to be registered under Article 17 the China Civil Code of 2020. Unless it is so registered the charge is not valid. Upon registration of the charge a 'security certificate' is issued. For a charge on immovable property, the registering authority is the regional/local China Housing Management Authority. Charge on movable assets is registered with the China Industries and Commerce Regulation Bureau.

**Pledge of movable tangible** and intangible assets is another preferred mode of creation of security. Since, pledge of tangibles is created with delivery of the assets, no registration of such charges is required. However, as the intangibles have no physical form, the asset comes into existence by way of registration of the right with the relevant authority. Accordingly any change in ownership or creation of charge on such intangibles also need to be registered with the relevant authority.

**Pledge of intellectual property** is required to be registered with the China Intellectual Property Authority, Central Office Beijing. For shares of listed companies, the registration authority is the China Securities Depository and Clearing Corporation Limited and in case of unlisted companies the charge on its shares is registered with the local office of the China Companies House where the company is located.]

**QUESTION 3 (essay-type questions) [15 marks in total] (13 points awarded)**

**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.

[Process under the China Enterprise Bankruptcy Law of 2006 is basically a rescue-oriented legislation on account of four reasons.

**Firstly**, it is broadly based upon and built up on the lines of the concept and provisions of US Chapter 11 process and it is a debtor in control procedure (albeit with the permission of the Court) with overriding powers to the Court to approve a resolution even if it has been rejected by the stakeholders.

**Secondly**, the law prefers rescue over liquidation and opening of liquidation process is mainly driven by the Court and courts retain discretion to allow or not to allow any liquidation process. While there are provisions under Chapter 10 and Article 7 providing for liquidation, but the Company can avoid liquidation by raising objection and submitting that the liquidation will not be in the interest of the stakeholders and that the Company is not a balance sheet bankrupt and it can be revived.

**Thirdly**, another factor which shows that China Enterprise Bankruptcy Law of 2006 is rescue oriented piece of insolvency legislation is that initiation of resolution process is not dependent upon the company passing of a bankruptcy test, the process can be initiated under Article 2 of the Law even in cases where the Company is likely to enter bankruptcy in future.

**Fourthly**, the law is also backed by another alternative mechanism in the form of 'composition/settlement'. Under Article 95 of the China Enterprise Bankruptcy Law of 2006, a company has option to file for composition. On admission of the process, the Court direct voting on the proposal/plan and such plan gets through if voted in favour by half or more of attending creditors in number holding two-third or more of the total claim.

Even under reorganisation plan, various options are available to rescue a company by way of debt forgiveness, or debt restructuring, equity adjustment etc. Under Article 81 of the China Enterprise Bankruptcy Law of 2006, the plan should also include a business restructuring sub-plan as the main aim of the process is to revive and an alternative plan would ensure that the company is not pushed into liquidation and every alternative is used to ensure rescue and revival of the Company. ]

**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.

[Under the China Enterprise Bankruptcy Law of 2006, on admission of the application, Court appoints a Bankruptcy Administrator, to manage the process. The Administrator takes control of the debtor's property, manage its affairs, inviting claims and formation of Committee of the Creditors and performs such other functions that may be required by the court.

Court while passing order for initiation of the bankruptcy process also directs filing of claims by Creditors and the time frame and forms and manner of filing of claim by creditor. The period for filing of claims (Article 45) 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 may file claims in respect of following debts:

- ◆ Debts that are due at the time of the court's acceptance of the application for bankruptcy, this may be crystallised or uncrystallised debt or a conditional debts or debts subject to time limits.
- ◆ Claim can also be filed in respect of which litigation or arbitration process is pending.
- ◆ Claim can also be filed in respect of indemnity obligations owed to a guarantor of the debtor or to another joint debtor who has discharged a debt on the behalf of the debtor.
- ◆ Party affected by termination of contract by the Administrator can also filed claim under the provisions of the Bankruptcy Law.

A creditor is entitled to attend and vote at the creditors' meeting. However, secured creditors cannot vote on the plan unless they have waived their right to priority. A creditor whose claim has not been determined may not exercise voting rights except with approval of the Court.

Under Article 58 of the China Enterprise Bankruptcy Law of 2006, first list of claims received by the Administrator is placed before the creditors meeting for verification. In case of disagreement or contest from the debtor and creditors, the matter is decided by the People's Court. Where there is dispute over claims list by a debtor or creditor, complaint could be brought before the People's Court accepting the case.]



**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.

[For the purpose of the above question, since the Chinese creditor has taken legal action in a local court in China, therefore, it is presumed that it is not an insolvency or bankruptcy proceedings. Similarly, as regards the Australian company, it is not specifically stated where are bankruptcy proceedings initiated. Since, the company is referred to as Australian company, so it is presumed that the proceedings too have been initiated in Australia. It is also noted that China and Australia have no existing treaty on recognition of foreign judgement.

The issue has cross border implications on account of bankruptcy proceedings of the Australian Company.

Article 5 of the China Enterprise Bankruptcy Law of 2006, provides that if insolvency procedure is commenced in China, it would cover all the assets of the debtor both within and outside China. At the same time, it also provides that where a verdict or ruling entered by foreign court involving the debtor's property within Chinese territory and if the foreign creditor or the administrator wants to enforce it in China, then such Creditor or the Administrator shall have to move a petition to that effect in the relevant court in China for acceptance and execution.

Such petition are considered by the Courts in China if there exist international agreements between China and the Country of foreign proceedings or if the Court is satisfied that the foreign verdict or ruling is based on mutual reciprocity principle and that there is no violation of basic principles of the Chinese Laws, and there is no detriment to state sovereignty, security and social public interests, and no harm would be caused to the legitimate rights and interests of creditors in China.

In this regard, the Chinese Court system heavily rely upon two factors (1) existence of judicial assistance treaty between the two countries and/ or (2) prior favourable recognition in the interest of a Chinese party. In the absence of a bilateral treaty, as in the present case China and Australia have no such treaty, establishment of reciprocity between the two countries is must. Going by the practice, up till now very few cases have been recognised in China and even in such cases, the status of foreign liquidator must be recognised by the Chinese Courts before the foreign liquidator could attempt to sell assets of the relevant company which are located in China. However, despite such challenges involved in seeking recognition of foreign judgement in China, since assets of the Australian Company which are in China and the same are under threat on account of civil proceedings initiated in China, the Liquidator of Australian Company is advised as follows:

- ◆ Liquidator of Australian Company shall check whether there are any instances of Australian Court having afforded and provided assistance in respect of the order from Chinese court.
- ◆ If such instance exists, then based on such prior recognition by Australian Court, an application should be moved under Article 282 of the China Civil Procedure Law of 2007, in a Chinese local intermediate people's court where the assets are located;

- ◆ If no such instance exist, then also an application should be moved under Article 282 of the China Civil Procedure Law of 2007, In such an application it needs to pleaded that Australian bankruptcy order does not violate basic principles of the Chinese Laws, and that there is no detriment to state sovereignty, security and social public interests, and that no harm would be caused to the legitimate rights and interests of creditors in China. Thus, in the absence of reciprocal treaty or existence of prior recognition of order of Chines Courts in Australia, the Australian Liquidator shall have to cede to the priority of the local creditors in China so that the Chines Court are convinced that any such recognition of the foreign order shall not in any way prejudicial of to the interest of Chinese law and Chinese creditors whose interest shall be fully protected.

**Question 4.2 [maximum 7 marks] (6 points awarded)**

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.

[Under Article 70 of the China Enterprise Bankruptcy Law, 2006, where the creditor files the liquidation application, the debtor or capital contributor holding more than one tenth of 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. If the Court is satisfied that the application for reorganization satisfies the requirement of the law, it may order re-organisation of the Company under Article 71.

Further, under Article 73 of the China Enterprise Bankruptcy Law, 2006, debtor can move application and the Court can pass order for the debtor to manage the affairs of the Company under supervision of the Administrator. Once the debtor in possession order is passed the functions and duties of the administrator are performed by the debtor.

On more advantage that accrues in such an event is that on order of reorganisation, the debtor gets exclusive right, under Article 79, to submit reorganization plan. Additionally, it is noted that Article 87 of the China Enterprise Bankruptcy Law, 2006, provides that in the event reorganization plan has been voted down by either the meeting of creditors or of shareholders or both, it may still be forcibly approved by the court if certain statutory conditions are satisfied.

So, if 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, it will be open to Yangtze Steel Limited or to its shareholders as mentioned above, holding more than ten per cent of the company's equity, to apply to the court to convert liquidation into reorganization.

Once such a request is allowed, Yangtze Steel Limited can engage with the creditors and work out a reorganisation plan building upon the strength of the business of the Company which are viable. A reorganization plan needs to contain proposal on reorganisation of the company's business operation and also on restructure the company's debts. It would also be advisable to the Company to seek active support of the creditor so that approval of the reorganisation is not jeopardise.]

**Question 4.2.2 [maximum 3 marks] (2 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 the China Enterprise Bankruptcy Law, 2006, lay down that the investors of the debtor may attend as non-voting group creditors' meeting where reorganization draft plan is discussed. It further provides that where the reorganization plan draft involves adjustment of investor's equities, then a separate group for investors it to be set up for the purpose of voting on the draft plan. Further, Article 86 of the China Enterprise Bankruptcy Law, 2006 requires that the plan must be adopted by each voting group and that the adjustment of investor equities involved in the reorganization plan should be fair and impartial or the investor group adopts the draft plan.

Thus, under the circumstances as mentioned in the above problem, the proposal and the plan would require consensus of shareholders. In view of the above, as the plan in this case proposes that the shares of all previous shareholders be cancelled and SanLong Limited has voted against the plan, this plan can be challenged by the Sanlong Limited and as such rejected by the court on non-compliance with the mandatory requirement of provisions of Article 86 of the China Enterprise Bankruptcy Law, 2006.]

45 out of 50 points awarded

✳ End of Assessment \*

Commented [ZZ1]: 45 out of 50 points awarded