



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] (9 points)

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

Question 1.2 (1 point)

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 (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 (1 point)

Select the correct answer:

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

- (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 (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 (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 (0 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] (9 points)

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?

[For petitions filed by a creditor in China, cash flow test should be met].

Question 2.2 [maximum 4 marks] (3 points)

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

[Lawyers and accountants are the two professions that dominate the regional bankruptcy list. Provincial Supreme Courts merely select some local large law firms and accounting firms to be included in regional qualified insolvency practitioner list, without going through any qualification exams or training courses. The Courts collaborate with local lawyer and accounting associations in making the appointments, but assume that large law and accounting firms are more trustworthy on the basis of financial strength and competence.

Question 2.3 [maximum 4 marks] (4 points)

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 used are fixed charge and pledge. Fixed charges are created over debtor's assets, both movable and immovable property in favour of a secured creditor. A Charge may also be created over the assets of the third parties, where advance consent of such parties were first obtained. To be a valid, Charge must be registered under the China Civil Code of 2020, and thereafter a security certificate is issued on the payment of a small fee. For a Charge over immovable property, registration is carried out at the local office of the China Housing Management Authority, and secured creditors further register the charge at the China Land Management Authority simultaneously.

Registration of pledges depends on whether it is movable tangible assets or intangible assets. For movable tangible assets, no registration is required as the pledge becomes valid once the assets come into the possession of the creditor. In the case of intangible assets,

such as trademarks, patents, shares, and bonds, they must be registered with the relevant registration authority otherwise they are invalid. Trademarks are to be registered with China Industries and Commerce Regulation Bureau Central Office located in Beijing. Shares of a non-listed company is at the local office of the China Companies House where the company is incorporated.

QUESTION 3 (essay-type questions) [15 marks in total] (9 points)

Question 3.1 [maximum 8 marks] (2 points)

“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.

[China Enterprise Bankruptcy Law of 2006 (“the Law”) is for many reasons a rescue-oriented piece of insolvency legislation that emphasis rescue over liquidation. One of such reason is that proof of inability to pay is more relaxed in favour of the debtor company. Article 7 of the Law provides that where a company is unable to pay its debt a creditor can commence liquidation proceeding in court. For the purpose of proving inability to pay debts, the option available to creditor is cash-flow test, since the basis for taking the view that the debtor company is having financial difficulty is the default of the debtor company in its payment obligation to a creditor. However, in the case of the debtor company, Article 2 of the Law allows the debtor to rely on either a cash-flow or balance sheet test to convince the court that commencing a liquidation procedure is justified. This approach is not unrelated to the fact that a company may be technically insolvent by not having cash flow to meet short term payments, but it has assets that far exceed the short- and long-term payments.

Another reason why the Law is rescue oriented is that the debtor company is given time to raise an objection to the liquidation procedure. Article 10 of the Law states that in the event of *an involuntary filling, the company is given seven days to raise an objection*. Giving the company an opportunity to objection helps position the Law as rescue friendly.

Furthermore, the approach of courts to bankruptcy procedures has helped. In China, commencing bankruptcy procedure is difficult, as in most cases the court have been said to simply ignore liquidation petitions without any justification. With the low judicial accountability, the debtor company and its creditor would be compelled to seek informal work out solutions that could entail moratoriums, creditors taking debts haircut and the debtor company remaining operational.

Also, the Law allows debtor company or its shareholders to apply **for conversion** of liquidation to reorganisation. Article 70 of the Law states that in the event of an involuntary liquidation, the debtor or its shareholder holding 10% or more of the company’s equity can apply to court for conversion of the liquidation to reorganisation. Although, this provision is not without its challenges including the fact with the powers of the management ceasing when the administrator is appointed, it is not clear how the board can exercise a conversion request. Having this provision in the Law demonstrates a pro- rescue stance.

In view of the above points, this writer is of the view that the Law is a rescue-oriented piece of insolvency legislation, emphasising rescue over liquidation.

Question 3.2 [maximum 7 marks] (7 points)

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.

[Generally, the process for proof of claims in a reorganisation commences with the reorganisation administrator directing all creditor to submit their claims within a specified number of days through newspaper publications. Within the timelines, the creditors file a claims form provided by the administrator. By reviewing of books of the account and consulting with staff in financing of the company, the administrator is able to verify the claim. In situations where there is a dispute over the veracity or legality of the claim of an individual Creditor, the administrator may file an action in court for an adjudication of the dispute. The judgment from the court reflects the finalized amount that the individual creditor would be entitled to.

Specifically with regards to executory contracts, Article 18 of China Enterprise Bankruptcy Law of 2006 ("the Law"), states that "*the reorganisation administrator is obliged to either assume or reject any uncompleted contracts within two months of the commencement of the reorganisation procedure*". Executory contracts are deemed rejected where the administrator remains mute on the issue for over two months or fails to respond to the claim by the contracting party for over thirty days. Where the executory contracts are assumed, Article 44 of the Law provides that the debts from these contracts become part of reorganisation expenses, in the process giving it priority over all pre-bankruptcy claim.

QUESTION 4 (fact-based application-type question) [15 marks in total] (13 points)

Question 4.1 [maximum 8 marks] (6 points)

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.

[Article 5 of China Enterprise Bankruptcy Law of 2006, provides that a foreign bankruptcy ruling can be recognised if some assets are located in China. In order for the recognition to take place the bankruptcy regulator must confirm whether there is a judicial assistance treaty between China and the foreign county over commercial and civil proceedings. It would appear that Australia is not one of the countries that has treaty with China, therefore recognition should be sought on the basis of reciprocity.

Where there is no treaty in existence, it may be possible to seek recognition on the basis of reciprocity between China and such foreign country. On judicial reciprocity, the Chinese judicial system takes the position that the foreign country must already have a recognition precedent in favour of a Chinese party. If the bankruptcy liquidator of the Australian company can discover cases where Australia courts have decided cases in favour of a Chinese then the foreign proceeding would be recognised in China.

While generally a foreign proceeding may be recognised either on the basis of judicial assistance treaty or reciprocity, however, such foreign proceeding must not infringe on China's sovereignty, fundamental principles of Chinese law, security and public interests for it to be recognised.]

Question 4.2 [maximum 7 marks] (7 points)

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)

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 issue in this question is whether the liquidation procedure commenced against Yangtze Steel Limited by the Bank of China can be converted to a reorganisation procedure on the application of SanLong controlling shareholder holding 32% of the shares. Article 70 of the China Enterprise Bankruptcy Law of 2006 states that *in the event of an involuntary liquidation procedure, the debtor, or its shareholders holding 10% or more of the company's equity can apply to court for a conversion from liquidation to reorganisation*. Given that SanLong is a shareholder that has shares of 32% which is over the statutory limit of 10%, It can apply to court for the liquidation procedure to be converted into a reorganisation procedure.]

Question 4.2.2 [maximum 3 marks] (3 points)

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.

[Generally, shareholders are entitled to vote where the result effect of a reorganisation plan is the cancellation of shares. Thus Article 85 of China Enterprise Bankruptcy Law of 2006 provides that where the equity of a company is affected, adjusted or cancelled by the reorganisation plan it should be voted on by the shareholders. Although from the wording of the statute is appearing that all reorganisations must pass the votes of shareholders, from a practicality perspective it would appear that the intention was for the shareholders to exercise their rights to vote in an advisory capacity. Otherwise, the shareholder would simply either decline to attend the meeting where the votes would be casted or vote down the protest the

plan.

For this reason, the statute gives the courts a wide power to cram down reorganisation plan. Article 87 of China Enterprise Bankruptcy Law of 2006 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). For a court to approve cram-down plan, conditions stated under Article 87 which can be summarized under three tests must be met. The first is the fair and equitable test, which requires *pari passu* participation of creditors in the same class. In the current situation all the classes of creditors have approved the reorganisation plan, it has therefore satisfied this test.

The second test is absolute priority test, in which creditors and preferential creditors are paid in priority to shareholders. Since in the ranking of payments the various categories of creditors rank before shareholders, and they have voted in favour of the reorganisation plan, in this instance the case, the second test has been complied with.

The third test is the feasibility test, which provides that the reorganisation plan should be achievable. The Court may, therefore, still approve the plan without the approval of any of the stakeholders. Upon an assessment of the facts and evidence provided before Shanghai Second Intermediate Court, if it reaches the conclusion that the test(s) have been met, the court can approve reorganisation plan despite the objection of SanLong Limited.

40 out of 50 points awarded

*** End of Assessment ***

Commented [ZZ1]: 40 out of 50 points awarded