



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: 202223-336.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 "studentID" 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 2023. The assessment submission portal will close at 23:00 (11 pm) BST (GMT +1) on 31 July 2023. 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 9 pages.**

ANSWER ALL THE QUESTIONS

QUESTION 1 (multiple-choice questions) [10 marks in total] (10)

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)

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) Partnerships and sole traders.
- (d) Individuals or sole traders.

Question 1.2 (1)

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)

Select the correct answer:

How is a bankruptcy administrator appointed under the China Enterprise Bankruptcy Law of 2006?

- (a) *The bankruptcy administrator can only be 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 can appoint provisional bankruptcy administrators when filing.*
- (d) *The court can only appoint a bankruptcy administrator after getting consent from both the debtor and the creditors.*

Question 1.4 (1)

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 debtor is allowed to file.*
- (d) *Both creditors and shareholders of the company may file for bankruptcy.*

Question 1.5 (1)

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 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 is automatically selected once a reorganisation procedure is commenced.*

Question 1.6 (1)

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 treated as unsecured creditors in China and are not given preferential treatment.*

Question 1.7 (1)

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 the Chinese courts.*

(c) *If shareholders do not support / approve the reorganisation plan, the plan cannot be crammed-down by the courts.*

(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)

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 from countries which have adopted socialism.

Question 1.9 (1)

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)

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 most?

(a) The United States of America.

(b) Russia.

(c) Poland.

(d) The United Kingdom.

QUESTION 2 (direct questions) [10 marks] (9)

Question 2.1 [2 marks] (2)

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

A creditor filing a bankruptcy petition must show that the company is bankrupt using the cash-flow bankruptcy test. This is because Article 7 of the China Enterprise Bankruptcy Law 2006 states that a creditor must show that the debtor is unable to pay a debt that is due.

Question 2.2 [maximum 4 marks] (3)

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 dominate the bankruptcy lists in China, and are selected primarily by Provisional Courts, who collaborate with local legal and accounting associations (themselves controlled by local government departments). This practice followed the China Supreme People's Court's instruction, 2007, that provinces were to establish regional lists of qualified insolvency practitioners in order to facilitate the implementation and execution of the provisions of the China Enterprise Bankruptcy Law.

In practice, it is not necessarily the case that all insolvency practitioners are 'qualified' as such - and they do not need to pass exams or undertake formal training in insolvency in order to be included on the lists. Rather, the local provincial courts will generally select large, well-known law or accounting firms within the region and appoint their practitioners to the list.

Question 2.3 [maximum 4 marks] (4)

Name the most used type of securities available under Chinese law and explain how and where they are registered.

The most commonly used types of security available in China are fixed charges. Pledges are sometimes also used. Liens and floating charges are provided for by Chinese legislation, but are infrequently used.

Fixed charges

For a fixed charge to be valid, it must have been registered under the China Civil Code 2020. After its proper registration and recording by the relevant government agency, a security certificate will be issued to the charge holder confirming its registration. Charges attaching to immovable property are to be registered at the relevant local China Housing Management Authority branch. In practice, charges attaching to rights of use for land will also be registered at the China Land Management Authority.

Pledges

For pledges attaching to movable, tangible assets, registration of the pledge is not required for it to be effective - possession of the asset is sufficient. However, intangible (or assets which cannot be physically possessed) movable assets (e.g. trademarks and other IP, cash equivalents etc.) must be registered by the relevant authority, depending on the nature of the asset. A list of these is below:

- ***Trademarks - China Industries and Commerce Regulation Bureau Central Office (Beijing)***
- ***Patents - China Intellectual Property Authority Central Office (Beijing)***
- ***Listed entity shares - China Securities Depositor and Clearing Corporation (Beijing, Shanghai, Shenzhen or Hong Kong offices)***
- ***Non-listed entity shares - China Industries and Commercial Regulation Bureau (office local to where the company is incorporated)***

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

Question 3.1 [maximum 8 marks] (6)

“The China Enterprise Bankruptcy Law of 2006 is a rescue-oriented piece of insolvency legislation, emphasising rescue over liquidation.”

Discuss what legal mechanisms in this statute can support this statement.

The China Enterprise Bankruptcy Law provides for three main mechanisms for dealing with distressed or insolvent companies - a reorganisation procedure, composition or settlement procedure, and finally liquidation. The first two of these are rescue-oriented and place the final mechanism, liquidation, as a last-resort. Two entire chapters are dedicated to the rescue procedures - Chapters 8 and 9 of the China Enterprise Bankruptcy Law.

In drafting legislation giving effect to China’s reorganisation procedure, lawmakers took substantial inspiration from the provisions of the US Bankruptcy

code, namely Chapter 11- which provides for a debtor in possession model and aims to promote the continuation of a debtor's business. Perhaps tellingly, the CEB Act deals with reorganisation early and before composition and liquidation procedures. Article 2 stating that a company can voluntarily file for reorganisatioin court, i.e. without passing any bankruptcy tests, when it is likely to become bankrupt in the near future. Further, Article 19 provides for an automatic stay on proceedings against all assets (including by secured creditors and including foreign assets, albeit the effectiveness of this global stay is limited in practice without recognition in the relevant jurisdiction), providing breathing room for the debtor. Article 18 also provides the administrator with room to elect to either continue or discontinue non-completed contracts. It is noted that either a creditor or the debtor can file for reorgnsation under the China Enterprise Bankruptcy Law.

A composition proecure is similar to a reorganisation in that it is rescue-oriented and is aimed ata avoiding liquidation of a debtor and cessation of its business. However, one key difference is that a composition procedure can only be filed by the debtor - i.e. it is always voluntary. Another key difference is in Article 96 of the CEB Act, which states that secured creditors are not affected by a composition procedure - thus lending to this proecure being more creditor-friendly in this respect (balancing the fact that it is necessarily a voluntary procedure). It is noted that a composition procedure does not demarcate creditors into classes with Article 97 providing that for a composition plan to be approved at least 50% of creditors in number and 75% in value must approve the plan.

Question 3.2 [maximum 7 marks] (7)

Briefly explain the process for the proof of claims in a corporate liquidation procedure and the procedure that is followed should the value or existence of a creditor's claim be disputed.

Following the initiationof a liquidation procedure, the liquidation admistrator must advertise in local and national newspapers to call for creditors' claims including providing a date (usually 45 days after the date of the notice's publication) by which time creditors must submit claims or be time-barred from claiming in the liquidation.

A creditor is entitled to set-off any amounts due to the company in liquidation at the date of commencement against its claim, thus reducing its potential claim in the liquidation but generally having a net-positive effect for the creditor (assuming a less-than 100 cents in dollar return). However, mutality between debits and creditors is a pre-requisite for set-off and debts cannot be sold/purchased/assigned between parties.

The adjudication process which follows generally comprises a substantial portion of the aggregate work required of the liquidation administrator, particularly if the amount oexistence of a claim is disputed between the claiming creditor and the

liquidation administrator. In addition to disputes between the administrator and creditor, other creditors are also entitled to object to a claim entered into the register of claims.

If a dispute arises, the matter will be litigated in the same court in which the bankruptcy procedure commenced. Both parties will make submission to the court, and that court's final decision will serve as finality of the value or existence of the claim, and must be adhered to.

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

Question 4.1 [maximum 8 marks] (8)

The bankruptcy liquidator of a Singaporean 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 Singaporean company in China. The liquidator has approached you for advice on how the Singaporean bankruptcy proceeding can be recognised in China. Advise the liquidator.

Chinese bankruptcy law provides for recognition of foreign bankruptcy where there is a judicial assistance treaty with China (establishing reciprocity is an alternative to this - however, this can be difficult in practice as the foreign country is required to initiate reciprocity by previously recognising a judgment in favour of a Chinese party).

In any case, Singapore and China have concluded such a treaty and accordingly the liquidation of the Singaporean company is prima facie entitled to recognition in China. However, it must be noted at the outset that only few foreign bankruptcies have been recognised in China, as the courts have a tendency to take the view that recognising foreign judgments may impede Chinese sovereignty. Accordingly, whilst recognition may be possible in theory, it will likely be difficult to obtain in practice.

Helpfully, there is precedent in China - though not in Shanghai - for the recognition of a Singaporean corporate bankruptcy order. This took place in 2020 in Xiamen, Fujian Province. This case may be useful in having the liquidation recognised..

In addition, Article 5 provides restrictions on the recognition of foreign proceedings. Relevantly, these include that recognition cannot disadvantage China's domestic creditors (which may cause an issue in this case given that a Chinese creditor has already commenced action and obtained relief in respect of certain Chinese assets) and that recognition cannot be of detriment to Chinese public interest. Depending on the nature of the creditor which has taken action - i.e. whether it is a large enterprise or a State-Owned-Enterprise - the public interest restriction could also be enlivened in this case.

However, if recognition is to be sought, notwithstanding the likely limiting factors above, the next step would to apply for recognition in the intermediate people's court local to the area in which the assets are located - in this case, the application should be made to the Shanghai No.1 Intermediate People's Court.

Question 4.2 [maximum 7 marks] (7)

HuangPu Food Limited is a large beverage 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 Fenda Partners, a local law firm included in the local bankruptcy administrator list, as the liquidation administrator.

Shortly after the commencement of the bankruptcy of HuangPu Food Limited, the CEO of Naking Limited, a controlling shareholder holding 32% of the equity of HuangPu Food Limited, approaches you for advice.

Using the facts above, answer the questions that follow.

Question 4.2.1 [maximum 4 marks] (4)

The CEO of Naking Limited tells you that the various businesses of HuangPu Food Limited are still viable and that a piecemeal liquidation of the company will not be in the interests of any of the stakeholders. Since HuangPu Food 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.

Conversation from liquidation to reorganisation is possible in China by law, though in practice it occurs infrequently. The mechanism for conversion is for the debtor or shareholders holding more than 10% of the company's equity may petition the court for conversion into reorganisation. This is under Article 70 of the China Enterprise Bankruptcy Law.

In this case, Naking will be entitled to make this petition given that it holds a 32% stake in HuangPu. The application is to be made to the court in which the liquidation petition was made.

However, whether the petition will be successful is difficult to determine - if the CEO of Naking's suggestion can be shown to be correct, i.e. that a piecemeal liquidation will not be in the best interests of any of its stakeholders (i.e. including its creditors), this would lean towards the conversion petition likely being successful. This is because it is the creditors' interest who are at risk by converting the liquidation into a reorganistaion. But additional facts would be required to be able to form a firm view on this.

It is noted that it remains unclear whether management of HuangPu is actually empowered to file this petition and in what capacity they may do so, given that HuangPu's board will ordinarily have been dissolved on liquidation and replaced by the liquidation administrator.

Question 4.2.2 [maximum 3 marks] (3)

Assuming that the bankruptcy liquidation of HuangPu Food Limited is successfully converted to a reorganisation procedure, a reorganisation plan for HuangPu Food Limited is eventually voted on by the various stakeholders. Due to the fact that HuangPu Food Limited is insolvent, the reorganisation plan *inter alia* proposes that the shares of all previous shareholders be cancelled. Unhappy that its equity in HuangPu Food Limited will be wiped out by the reorganisation plan, Naking 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 Naking Limited as to whether the Court can approve such a plan under the current law in China.

Under Article 87 of the China Enterprise Bankruptcy Law, the court may approve a plan that has been rejected by one or more class of creditors or the shareholders, as has been the case here, subject to a number of conditions. Given that all creditor classes have voted in favour of the plan, and assuming that the plan is feasible and pays stakeholders within the same class fairly, the relevant condition for the court being able to approve the plan under Article 87, in this case, is the condition that the treatment of equity holders must be fair and equitable where equity holders have not voted in favour of a plan affecting their equity. This is a legal question that will be determined with regard to a number of facts, however, on the basis that HuangPu is stated to be insolvent, it would appear likely that the cancellation of shares is not prejudicial to HuangPu's equityholders (as they would be unlikely to have an economic interest in the net assets of HuangPu, i.e. the equity value would be nil). However, it is not clear whether HuangPu is balance sheet or cash-flow insolvent - if only cash-flow insolvent, it is possible that a sale of assets would eventually result in equity being available for shareholders, in which case the cancellation of shares may not be fair and equitable to shareholders. If it can be shown that there is no prospect of this happening, then it is likely that the court would approve the plan notwithstanding the effect on equity holders.

In short, whilst the court may cramdown shareholders by approving the plan under Chinese law, whether it in fact does is complex and will likely be dependent on additional facts not set out in the information provided.

Final mark: 47/50

*** End of Assessment ***