



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] (9)

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 (0)

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] (10)

Question 2.1 [2 marks] (2)

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

[Under Article 7 of the China Enterprise Bankruptcy Law 2006, a bankruptcy petition filed by a creditor in China, the 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. In practice, the petition also require the support of local government, otherwise, there is a good chance the bankruptcy application will be simply ignored, if not rebuffed.]

Question 2.2 [maximum 4 marks] (4)

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

[Insolvency practitioners or bankruptcy administrators in China comprises both individual and companies. They can be lawyer, accountant or none of the 2 professions.]

Lawyers/legal firms and accountants/accounting firms dominate Chinese regional bankruptcy administrator lists. This is because, in 2007, in order to facilitate the implementation of the China Enterprise Bankruptcy Law of 2006, the China Supreme People's Court instructed most provinces to gradually establish their own regional qualified insolvency practitioner lists. Provincial supreme courts simply select some local large law and accounting firms to be included in the lists without going through any qualification exams or training courses. Most provincial courts assume that a large law or accounting firms is more trustworthy both in terms of financial strength and in respect of competence. The provincial supreme people's courts always seek collaboration from local lawyer and accounting associations. These 2 associations are controlled by local government justice and finance departments, respectively. Disgruntled parties seeking to hold insolvency practitioners accountable for any alleged breaches of a bankruptcy administrators' duties, can lodge complaints with the professional organisations to which these insolvency practioners belong.

Article 13 of the China Enterprise Bankruptcy Law of 2006 provides for the simultaneous appointment of the bankruptcy administrator by the court when a liquidation petition is accepted by the court. The Chinese courts generally use the

roster of the locally qualify bankruptcy practitioner list to select the candidate firm and occasionally a bid will be held if the case proves to be complex and large.

Although it seems that the appointed bankruptcy administrator has full control of the bankruptcy process but in reality, they acts under the authrhoruty of the judge overseeing the case.

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 provceedings.]

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.

[There are three types of security available under the China Property Law 2007, namely, fixed charge, pledge and liens. The most widely used type of security is the fixed charge.

In most cases, a charge can be created over both movable and immovable property in favour of a secured creditor, which is usually a bank. A charge can be created over the debtor's asets or even over the assets of a third party with consent obtained from the third party.

A charge must be registered under the China Civil Code of 2020 otherwise the charge is not a valid charge. Invalid charge means that the secured creditor has no priority over the assets. Once the charge has been properly recorded at the government agency, a security certificate is issued to the charge holder. A small fee may apply for the registration of a charge.

All land in China are generally owned by the State because private party is disallowed any ownership of land. Private parties, including individual, can buy and sell the right to use land, essentially a lease. For vacant land, the pure right of use relating to a piece of land can also bear a charge, subject to registration.

For immovable property eg. buildings and the right of use of land, the registration authority is the local office of the China Housing Management Authority. Most secured creditors tend to simultaneously register the charge at the local office of the China Land Management Authority.

For movable property, eg. vehicles and machineries, the registration authority for vehicles is the local police vehicle management office, the registration authority for machinery and other equipment is the local office of the China Industries and commerce Regulation Bureau.]

QUESTION 3 (essay-type questions) [15 marks in total] (12)

Question 3.1 [maximum 8 marks] (5)

“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 of 2006 (“2006 Bankruptcy Law”) comprises three bankruptcy options or procedures, namely, (1) Reorganisation, (2) Composition / settlement and (3) Liquidation. The order of these three bankruptcy options obviously reflects that the lawmakers expect rescue to be attempted first. Since there are two chapters, Chapter 8 and 9, to highlight corporate rescue, i.e. reorganisation and composition/settlement, the intent of the Chinese lawmakers to promote the use of corporate rescue is therefore clearly visible and understood.

For reorganisation filing, there is no requirement to show evidence of bankruptcy. Article 2 of the 2006 Bankruptcy Law states that when the company is likely to become bankrupt in the near future, the company can voluntarily file for reorganisation in court. A voluntary reorganisation filing does not require to pass any bankruptcy tests. Whereas, for liquidation application, Article 7 of the 2006 Bankruptcy Law, states that if the company is unable to pay a debt that is due, the creditor can file for liquidation in court. Creditor has to pass a bankruptcy test. Company may also file for voluntary liquidation but bankruptcy test is also required.

Not only that Liquidation filing requires bankruptcy test, Article 10 of the 2006 Bankruptcy Law allows the company within 7 days of the involuntary liquidation filing, to raise an objection. The court also has absolute discretion to decide whether the liquidation procedure should be formally opened. In reality, it is very difficult to open a bankruptcy procedure in China and in most cases, it requires the support of local government. Even when a liquidation petition is fortunately and finally accepted by the court, after the court accepts the application for bankruptcy and before the debtor is declared bankrupt, Article 70 of the 2006 Bankruptcy Law stipulates 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.

In the case where liquidation is successfully commenced, it is difficult to sell the houses or buildings of the debtors especially when it is occupied or when the company is still in operation. The local government will never support destructive and powerful method of enforcement.

In 2015, the China Supreme People's Court abolished pari passu principle in judgement execution against company debtors. Hence where 2 or more creditor has claim over the assets, the late creditor cannot ensure fairness in sharing the assets.

It is also worth noting that 2006 Bankruptcy Law was a reform from 2 pieces of legislation comprises (1) the Enterprise Bankruptcy Law of 1986 ("1986 Enterprise Bankruptcy Law") which applies only to State-Owned Enterprises ("SOEs") and (2) Chapter 19 of the China Civil Procedure Law of 1991 for non-SOE enterprises. The reform was greatly influenced by Chapter 11 of the US Bankruptcy Code 1978, which is commonly known as a reorganisation bankruptcy law, which encourages reorganisation over liquidation.

The 1986 Enterprise Bankruptcy Law is use to warn underperforming SOEs to operate more efficiently. China government did not expect to use the 1986 Enterprise Bankruptcy Law for fair protection of creditors or for an orderly liquidation of failed SOEs. Its aim was to use it to coerce underperforming SOEs into operating more efficiently.

From the perspective of the debtor and local government, reorganisation proceedings are favoured by all parties above liquidation proceedings, because the operational value of the enterprise and the value of the intangible assets can be maintained.]

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.

Once the liquidator has been appointed, he/she will assume control of the company's assets and business affairs, including the company's books and record. He/she will then advertise the bankruptcy procedure in both local and national newspapers in order to inform all creditors that they should submit their claims. Usually there is a standard claim form for creditors to fill in and submit together with supporting document. Verifying claims is very important as this will enable the liquidators to ascertain the company's total liabilities. Liquidators have to examine the claims and the supporting documents and may seek the assistance of the company's director or finance staff to help verify the claims submitted by creditors. This proof of claims process formed a major part of the liquidators' work.

After the liquidator has realised the company's assets, he can distribute the proceeds under the priority order stated in Article 113 of the China Enterprise Bankruptcy Law of 2006 in the following order and applying the pari passu principle:

- 1. Bankruptcy costs including Liquidator's fees and post bankruptcy expenses;*
- 2. Employees' claims;*
- 3. Tax authorities' claims;*

4. *Unsecured creditors and lastly,*
5. *Shareholders (usually there is insufficient cash to reach this level).*

In the event that there is a dispute on the claim amount, creditor can litigate before the same court for a judgment to adjudicate the dispute. The final result of the litigation serves as the finalised amount of the disputed claim.]

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

Question 4.1 [maximum 8 marks] (6)

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.

[A Singapore company has been placed under liquidation and a Singapore liquidator has been appointed over the company. The legal action undertaken by the Chinese creditors in China court against a company that has been ordered by Singapore Court to wind up is supposed to apply for leave of court to initiate legal action against a bankrupt company because Singapore Insolvency Law allow automatic moratorium which suspends all executions against the company and its assets, meaning no legal actions can be brought against the company without the court's permisison. However, in this case, the China court has already issued an injunction to freeze the assets of the Singaporean company, located in China.

Article 5 of the China Enterprise Bankruptcy Law 2006 stated that a foreign bankruptcy ruling binds the company's assets located in China, provided that the foreign court ruling is recognised by a Chinese court and that it did not infringe upon the fundamental principles of Chinese law, China's sovereignty, security and public interests and does not disadvantage China's domestic creditors.

The recognition of a foreign court ruling should be based on either a judicial assistance treaty signed and ratified between China and the requesting country, or the principle of reciprocity if there is no treaty.

Singapore is one of the 30 countries that has signed a judicial assistance treaty with China. Under Chinese civil procedure law, the party seeking recognition of a foreign bankruptcy judgment would have to do so in a Chinese local intermediate people's court, where the company's assets are located.

So, the Singaporean liquidator should first identify in which province/state/area the company's assets are located then rely on the judicial assistance treaty executed with China and apply for recognition of the Singapore bankruptcy proceeding in the intermediate people's court located in that province/state/area where the assets are

located. The Singaporean liquidators should also be informed that in year 2020, the maritime court in Xiamen, Fujian Province had recognised a corporate bankruptcy order from Singapore.]

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.

[Under Article 70 of the China Enterprise Bankruptcy Law of 2006, in the event of an involuntary bankruptcy liquidation procedure, the debtor or its shareholders holding more than 10% of the company's equity can apply to the court to convert liquidation to reorganisation and, if sanctioned, the reorganisation procedure will commence immediately thereafter.

In this case, Naking Limited being the shareholder with 32% equity in HuangPu Food Limited can apply to the court to convert the liquidation into a reorganisation procedure and present a reorganisation plan to show the court that HuangPu Food Limited has a viable future business, the repayment to its creditors will be better than under liquidation scenario and be given a chance to ride through its financial difficulties via reorganisation instead of being liquidated. The CEO should also be informed that if he can obtain local government's support, the bankruptcy reorganisation filing will have a better chance of success.

Once reorganisation filing is accepted, the court will also appoint a bankruptcy administrator to conduct the reorganisation. However, under Article 73, the company

can apply for debtor-in-possession model to run the reorganosation procedure, meaning the company itself steers the reorganisation operation.]

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.

[Yes, the court can still forceably approve such a plan, making it legally binding on all consenting and dissenting stakeholders by applying the cram-down rule in Article 87.

Under Article 87, a reorganisation plan that has been voted down by one or more class of creditors or by the shareholders, can seek the court to cram-down as long as it meets the following 3 tests:

- (1) Fair and equitable test - by applying the *Pari Passu* principle between creditors in the same class;*
- (2) Absolute priority test - requiring shareholders to be paid nothing unless and until creditors are paid in full and following the priority of payment; and*
- (3) Feasibility test - the reorganisation plan should be achievable.*

The 3 tests must be demonstrated by complying with the following 6 conditions:

- (a) Unless the secured creditors have been fully paid, otherwise, the reorganisation plan must be voted in favour by the secured creditor class;*
- (b) Unless the employee and the tax authority have been fully paid, otherwise, the reorganisation plan must also be voted in favour by both these classes of creditors;*
- (c) The reorganisation plan must be voted in favour 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;*

(d) The reorganisation plan must be voted in favour by the shareholders where their equity is affected by the plan and, if not, the treatment of equity holders is fair and equitable;

(e) The reorganisation plan must ensure fair payment to the stakeholders in the same class, with priority between shareholders and creditors upheld; and

(f) The reorganisation plan must be feasible.]

Final mark: 44/50

*** End of Assessment ***