



# Examiners' report

## F4 Corporate & Business Law (CHN)

June 2009

### General Comments

The examination consisted of ten compulsory questions (10 marks each). The examination consisted of two parts, seven knowledge questions plus three questions of case analysis.

The performance of candidates overall was quite satisfactory and above the expectation.

An obvious improvement in this sitting represents that most of candidates followed the requirement that each question started on a new page and indicated which question is being attempted. Even though some candidates still did not follow the discipline and answered two questions on one page.

### Specific Comments

#### Question One

This question required candidates to explain the term *the transfer of jurisdiction*, and *the designation of jurisdiction* by Chinese courts in dealing with civil or commercial disputes. This was a question in relation to the general legal system.

The term *the transfer of jurisdiction* is a form of jurisdiction in the Civil Procedures Law. Under this rule of jurisdiction if a court finds a case it has accepted is not under its jurisdiction, it shall refer the case to the court that shall have a proper jurisdiction over the case. *The designation of jurisdiction* is a special form of jurisdiction which is to deal with the special circumstances, such as the situation of inconvenience to exercise jurisdiction or the situation of concurrent jurisdiction by two or more courts.

The performance for this question varied critically. Overall speaking, the average marks for this question were satisfactory. However, other candidates were unable to give the some key points of the question with respect to the transfer of jurisdiction.

Common errors in this question included:

- Failing to explain the term designation of jurisdiction;
- Confusion of the transfer of jurisdiction and territorial jurisdiction;
- Confusion of the transfer of jurisdiction and jurisdiction by forum levels, and
- Failing to explain the rule under which a court is not allowed to transfer the jurisdiction further to other courts if it accepts the jurisdiction by the form of the transfer of jurisdiction.

#### Question Two

This question required candidates to explain the term *the confirmation of property*, state the means of dispute settlement over the property rights and state the various claims entitled to a right holder if his property rights are infringed by other persons. It is a very important rule under the Property Law of China and provides property holders a useful way to deal with the possible disputes over the property rights. Therefore, this question was intended to test candidates of the basic knowledge as to the property law. To answer this question, candidates should clearly be aware of the differences between the confirmation of property and the dispute arising out of infringement by others. For the former, the core of the question was that the ownership of a particular property was still uncertain. Therefore, parties to the dispute might take any proper procedures so as to confirm the owner of the property in dispute. For the latter, the owner of a property was clear and certain. The dispute came out by the infringement of others. Under such circumstances the legitimate owner of the property might request courts to protect his/her property rights.

Performance of this question was quite satisfactory as most of the candidates understood the meaning of the confirmation of property and the various ways to resolve the disputes over property rights, such as litigation and arbitration, etc. Therefore, the average marks for this knowledge was the highest one in seven general questions.

Errors in Part (a) included:

- Failing to distinguish the disputes over the property rights and the damage of property suffered by illegal activities. This confusion resulted in the incorrect way of dispute resolution.
- Failing to understand the meaning of the confirmation of property.
- Failing to state the possible administrative procedure by property holder to request the relevant governmental department to confirm the owner of the property concerned.

Errors in Part (b) included:

- Failing to state the concrete ways of protection if the property rights of an owner infringed by others, merely stating various measures could be taken.
- Failing to distinguish the ways could be taken to protect the property rights and the legal remedies to the owner if his/her property rights infringed by others.

Errors in Part (c) included:

- Failing to distinguish the difference in nature between the confirmation of property and the protection of property rights.
- Confusion of the ways for the protection of property rights and the legal remedies.

Errors in Part (d) included:

- Confusion of the claim for returning of the original property and the time limit for claiming the right.
- Failing to state the specific way of protection if the movables or immovables of a holder are possessed by a party without an authority.

### Question Three

This question required candidates to explain the term *labour service despatching*, and state the legal relations of the parties and the statutory terms of a labour contract between the entity despatching labour services and the person despatched.

Labour service despatching is a form of business transaction under which an entity despatching labour services, by the conclusion of a contract, despatches the persons (service provider) to another enterprise (the labour service purchaser) to work for a fixed period of time or to provide particular services as agreed in the contract. This form of business transaction has been regulated since the adoption of the Labour Contract Law. Also it has been very popular in the labour market, sometimes it becomes a means of avoiding to enter into a labour contract between an employer and employees. However, candidates have not been familiarised themselves with the relevant rules of law, because of the complicated legal structures among the service provider, labour service purchaser and entity despatching labour services. Overall speaking, the performance in this question was not satisfactory.

Common errors in Part (a) included:

- Failing to understand the meaning of labour despatching service, describing labour despatching services as the labour authorities or labour association to provide labour service for other parties, etc.
- Failing to explain that there are three parties in this form of business transaction.

Common errors in Part (b) included:

- Failing to state the legal relationship between an entity despatching labour services and labour service provider as well as the legal relation between a labour service purchaser and labour provider, especially the legal relationship between the entity despatching labour services and the persons despatched to be the relationship of an employer and employees.

Common errors in Part (c) included:

- Failing to state the statutory requirements by the Labour Contract Law that a fixed-term labour contract for a term of no less than two years.

Failing to state the special rules as to the minimum wage to be paid for the period when the service providers are out of work.

#### Question Four

This question required candidates to explain the term *subrogate right (right of subrogation)* and state the conditions to be met if a party claims this right under the Contract Law of China.

The rule of subrogate right has been recently introduced as the examinable content. Subrogate right is one of the important rules set up in the Contract Law. Generally speaking, it was a straightforward question requiring candidates merely to give an explanation of the term subrogate right and state the various conditions to be met if a party intends to exercise this right. However, since all the conditions should be satisfied by a party to claim subrogate right, it was difficult for some candidates to state these conditions one by one. It should be noted that these conditions should be fully satisfied, without any exception. To give a full and correct answer to this question, candidates should have a deep understanding of this rule of law.

In terms of the average marks for an individual question, performance of this question was satisfactory.

Common errors of this question included:

- Failing to give a full and clear explanation to the term subrogate right.
- Confusion of subrogate right with the demur right of advance performance.
- Failing to state the conditions to be met for a party to claim this right, such as the legal status of the party in a contract as a creditor; the debtor being reluctant to exercise his creditor's right against a third party resulting in damage to the creditor, etc.

#### Question Five

This question required candidates to state the rules in relation to the purchase of shareholder's equity by a company under the Company Law.

As a general principle of company law a limited liability company is not allowed to purchase the equity (shares) of its shareholders. However, a shareholder may request the company to purchase his/her shares under the special circumstances and within a limited period of time. Candidates should understand the pre-condition if a shareholder intends to make such a request, i.e. the shareholder has voted against the relevant resolutions of a shareholders' meeting. Furthermore, any one of the following circumstances should be met:

- where a company fails to distribute profits to its shareholders for consecutive five years, while the company has been continuously making profit for such five years;
- where the company merges, divides or transfers its substantial assets; or
- where the term of operation of the company expires as stipulated in the articles of association or other events occur for dissolution, but the shareholders' meeting adopts a resolution on revision of the articles of association to make the company continue to exist.

As a whole, the answers to this question were not as good as expected. Candidates should be familiarised with this special rule. However, performance of candidates who did not answer this question satisfactorily demonstrated that there is room to improve in the future.

Common errors of Part (a) included:

- Failing to understand this rule and give no point to this part of question.

- Failing to state the pre-condition for a shareholder to request a limited liability company to purchase his/her shares with a reasonable price.
- Confusion of the pre-condition for requesting the company to purchase the shares of a shareholder and the obligations of a shareholder to make his/her capital contributions or the vote mechanism of a limited liability company.

Common errors of Part (b) included:

- Failing to state any circumstances under which a shareholder may request a company to purchase his/her shares at a reasonable price.

Common errors of Part (c) included:

- Failing to understand there is a time limit for a shareholder to claim this right.
- Failing to point out the 90-day time limit.

### **Question Six**

This question required candidates to state the rules as to convene an extraordinary general shareholders' meeting by a joint stock company. It was not a difficult question, as it required candidates merely to state the various circumstances under which an extraordinary general shareholders' meeting might be held by a joint stock company.

Performances of this question indicated two extremes: some candidates were able to give a quite satisfactory answer to this question; while about some candidates received no or very few marks because they did not state (or stated limited) the circumstances for an extraordinary general shareholders' meeting.

Common reasons for unsatisfactory answers included:

- Confusion of an extraordinary shareholders' meeting with an ordinary shareholders' meeting.
- Failing to state the circumstances under which an extraordinary general shareholders' meeting might be held.

Failing to state the specific period of time within which the extraordinary shareholders' meeting should be held.

### **Question Seven**

This question required candidates to explain the coverage of community liabilities and the order of settlement of bankruptcy expenses and community liabilities under the Enterprise Bankruptcy Law of China.

To answer this question one must have a basic understanding of community liabilities and its difference with the bankruptcy assets. According to the relevant provision of the Enterprise Bankruptcy Law, community liabilities refers to the debts taken place after the court has accepted the application for the bankruptcy of a company. They are different from the bankruptcy expenses that occurred during the bankruptcy process. Furthermore, the order of settlement of bankruptcy expenses and community liabilities is stipulated in the Enterprise Bankruptcy Law, which cannot be changed by any party involved in the bankruptcy process.

The performance of this question was quite satisfactory, as most of candidates were able to answer the key points of this question. Some candidates gained 7-10 marks for this question.

Errors of this question included:

- Confusion of community liabilities with the rule as to the allocation of bankruptcy assets of the company.

Failing to point out the priority of paying off if debtor's assets are not enough to pay off the bankruptcy expenses.

### Question Eight

This question required candidates to determine the lawfulness of the resolutions of the shareholders' meeting, in terms of the replacement of supervisors, the issuance of corporate bonds and the use of the statutory common reserve fund under the Company Law and the Securities Law of China. In general it was a straightforward question as candidates were required to make simple judgements on the relevant matter, without complicated calculation. However, performance of candidates in this question was below the expectation.

In Part (a) candidates were required to determine the lawfulness of the resolution in relation to the replacement of supervisors. The Company Law established several compulsory rules as to the appointment and replacement of supervisors: i.e. directors, senior executives of a company cannot be appointed as supervisors; supervisors as pointed by employees should be decided and appointed by employees themselves, etc. Based on these rules, one could easily make a conclusion that a resolution on this regard was partly in conformity with the Company Law and partly invalid.

Common errors of Part (a) included:

- Failing to point out the lawfulness of the replacement of supervisor for each person respectively, merely a general determination.
- Failing to make a correct determination towards each replacement.

Part (b) of this question was in relation to the issue of corporate bonds. It has been examined several times in the previous sessions. Therefore, candidates should be familiarised with the conditions to issue corporate bonds. However, about half of candidates did not give a satisfactory answer to this part of the question.

Common errors of Part (b) included:

- Failing to understand the statutory requirements of 60 million yuan of net assets and profit-making for three consecutive years.
- Failing to calculate correctly the amount of the net assets of Yuanda Co.
- Failing to give a correct conclusion that the decision to issue corporate bonds being in conformity with the relevant provision of law.

Part (c) of this question was relevant to the use of a company's common reserve fund. According to the Company Law this fund shall be used to make up the company's losses, to expand the operation, or to increase the capital of the company by means of conversion. Hence the resolution concerning the transfer of the statutory common reserve fund to the registered capital was in conformity with law. However, many candidates did not give a correct answer to this part of question.

Common errors of Part (c) included:

- Confusion of the use of the common reserve fund with the rule as to the distribution of profit.
- Failing to understand correctly the voting requirement to adopt a resolution in this matter.

### Question Nine

This question requires candidates to deal with the allocation of the insolvent assets under the Enterprise Bankruptcy Law and Property Law of China. It required candidates to calculate how much City Materials Company was entitled to receive after the necessary deduction. In doing so, candidates should not only have a solid knowledge of both the Enterprise Bankruptcy Law and Property Law, but also carefully do a complicated calculation. Some candidates did not calculate a correct quantity of assets for which City Materials Company was entitled as they had written down the formula correctly. For this reason, they were awarded some marks even though the conclusion was incorrect.

Performance of this question was satisfactory. Many candidates were able to give a correct answer to this question, with reasons to support their answers.

Part (a) of this question required candidates to determine the nature of the mortgage agreement. Common errors of this part included:

- Failing to decide the nature of the mortgage agreement. Under the ordinary condition the mere fact that a mortgage agreement is not registered will not affect the validity of it. In this question, however, Building No. 1, 2 and 3 had been detained by a court order. Therefore, the mortgage agreement was invalid as these buildings were forbidden from disposal by Singen Co.

Part (b) of this question required candidates to determine the nature of City Materials Company as a creditor or the order of priority in allocation of the insolvent assets. The answer to question was very clear that City Materials Co was a common supplier of Singen Co, without any guaranty upon their transactions. Common errors of this part included:

- Misunderstanding of the question by stating that the general order of priority in the allocation of the insolvent assets. However, the question required candidates to determine the order of priority for City Materials Co in the allocation of the insolvent assets.
- Failing to state the reasons why City Materials Co's credit should be the common credit.
- Failing to give a correct determination to this part of question.

Part (c) required candidates to determine the quantity of assets City Materials Co was entitled to receive after the necessary deduction. The correct answer was that City Materials Co should receive RMB 1.5 million yuan for its credit.

- Failing to give a correct answer to this part of question just because of calculation.
- Failing to calculate just because of misunderstanding the order of priority in allocation of insolvent assets.

### **Question Ten**

This question required candidates to deal with the legal issue as to the transfer of a contract under the Contract Law of China.

As a whole, performance of this question was the best one. Most of candidates were able to give a correct answer to both parts of this question.

Part (a) of this question required candidates to determine whether Seller was entitled to refuse to provide the goods. According to the Contract Law a creditor may transfer his contractual rights to a third party if he informs the debtor; otherwise, the transfer will not bind the debtor. Therefore, Seller was not legally bound by such transfer and was entitled to refuse to deliver the goods to the third party in case Buyer did not give a notice.

Part (b) of this question required candidates to determine the validity of the transfer of the contract. This part of question was connected with Part (a). In this case Buyer did not inform Seller and did not receive the consent from Seller, who was a creditor in terms of receiving the price from Buyer, the transfer of contract was invalid.

Common errors of Part (b) included:

Part (b) included:

- Failing to distinguish the transfer of contractual obligation and the transfer of contractual right, stating that any transfer of contract should receive the consent of the other party. According to the Contract Law, the legal effect of the transfer of contractual obligation depends on the

condition that the other party gives his/her consent to such a transaction. This requirement does not apply to the transfer of contractual rights.

- Failing to make a determination as to the validity of the transfer.
- Failing to give a correct determination that the transfer of contract and provide the reasons to support the conclusion, i.e. the transfer was invalid because Buyer, as an obligor and oblige, did not notice the transfer and receive the consent from Seller.