

Examiner's report

F4 Corporate & Business Law (CHN)

June 2014



Specific Comments

Question One

This question required the explanation of the conditions for enacting local laws and the conditions for issuing rules and regulations, and stating the hierarchy of effect if there is a conflict. Generally speaking, performance in this question was satisfactory, especially compared with the performance of the previous sessions on the essential system.

In part (a) most of candidates were able to answer the conditions for enacting local laws by the people's congress at the provincial level administration. The key in this part is that the people's congresses and Ministries under the State Council cannot contravene the Constitution, laws adopted by the NPC and the administrative regulations by the State Council in enacting local laws. Some candidates pointed out only the Constitution and laws of the NPC, but omitted the administrative regulations by the State Council.

Part (b) (i) of this question is relevant to the issuance of rules or regulations by Ministries and Commissions under the State Council. Almost all candidates were able to answer this part and obtained satisfactory marks. Part (ii) of this question tested candidates on the knowledge of hierarchy of effect between local laws enacted by the people's congresses at the provincial level and the rules issued by Ministries and Commissions under the State Council, where there is a conflict between these two sets of laws and rules. Since the people's congresses at the provincial level are authorised by the Constitution to enact local laws on the matters specifically relevant to their respective jurisdiction, local laws enacted by the people's congresses at provincial level shall prevail within the same sphere of function. It should be noted that this does not mean there is no precondition. The precondition is that the powers of enacting laws are within the same sphere of function. Some candidates were unable to give a correct answer to this point or unable to point out the precondition for such hierarchy of effect.

Question Two

This question tested the knowledge of the registration of real property and the special provision on the state-owned natural resources, the jurisdiction of such registration and the priority of effect in case a difference between the certificate and the record in register takes place.

Part (a) requires candidates to explain the *registration of the right of real property*. This term refers to a statutory procedure in which the registration organ registers a real right of the right holder, by which a real property in relation to the creation, change, transfer or elimination of the right become effective. Most candidates answered this part correctly.

Part (b) of this question related to state ownership. Under the Property Law, the state owned natural resources need not pursue a registration. A significant number of candidates were not able to give a correct answer to this part. It seems to me that these candidates considered the state owned natural resources to be same as that of the common right of real property.

Part (c) of this question is closely connected with the jurisdiction of registration of a real property. According to the Property Law, the registration of a real property shall be executed by the registration organ of the place where the real property is located. It should be noted that jurisdiction of registration of a real property is different from the jurisdiction of a lawsuit but closely connected to the latter. The general principle is that any jurisdiction over a real property, judicial or administrative, is based on the location of the real property. Therefore, in civil litigation any lawsuit involving a dispute of real property shall be under the jurisdiction of the court where the real property is located. A few candidates were confused the jurisdiction of registration with the jurisdiction of court in litigation and did not obtain marks as expected.

Part (d) of this question is relevant to the principle where the content of the certificate of real property is different from that of the record in the real property register. Since the certificate of a real property is merely the proof of the holder's ownership of real property, where there is any inconsistency, the item recorded in the real property register shall prevail. All candidates answered this part correctly.

Question Three

This question tested the rules with respect to the probation clause in the labour contract. Performance for this question, as a whole, was satisfactory.

Part (a) of this question required candidates to answer under what circumstances a labour contract is not permitted to contain a clause of probation. According to the relevant provision of the Labour Contract Law, a labour contract is not permitted to contain a clause of probation where a labour contract with a term less than three months or a labour contract for the completion of a certain job. Almost all candidates were able to point out these circumstances and received full marks for this part.

Parts (b) and (c) of this question requires candidates to state the various conditions, three items, under which an employer may dissolve a labour contract during the probation period. The relevant provision of the Labour Contract Law stipulates all the conditions that may be the reasons for an employer to dissolve a labour contract during the probation period. In doing so the employer shall give adequate reasons for dissolution. Most candidates were able to state one or two circumstances to be met for an employer to dissolve a labour contract, although few candidates could also state the point as to the reasons to support the dissolution of a labour contract. Some candidates stated that the employer should give one month's notice to the employee. Since the labour contract is dissolved during the probation period, it is not required by the law.

Question Four

This question required candidates to explain *a contract by unauthorised agent*, state the legal effect of a contract by unauthorised agent and the ways to deal with the contract by unauthorised agent.

Part (a) relates to *a contract by an unauthorised agent*. Precisely, it includes a contract concluded under the different situations by an agent, on behalf of the principal, with a third party: the so-called agent having no power of agency, the agent overstepping the power of agency or whose power of agency has expired. As a whole most of candidates were able to understand what a contract by an unauthorised agent is. However, not many candidates were able to explain all the circumstances under which a contract by an unauthorised agent may be concluded.

Part (b) of this question required candidates to state the legal effect of a contract by an unauthorised agent. Almost all candidates were able to give a correct answer to this part.

The answer to part (c) covers several points. First, the counterparty to the contract may urge the principal to ratify the contract within one month. Second, the counterparty keeping silent shall be deemed as a refusal of ratification to a contract by an unauthorised agent. Thirdly, a *bona fide* counterparty has also the right to cancel the contract before the contract is ratified. Some candidates were able to state one or two points, focusing on the first two points, but failed to state the *bona fide* counterparty's right of cancellation.

Question Five

This question required candidates to explain the term *actual controller*, state the statutory voting requirement to provide a guarantee to company shareholders or actual controller as well as the rule as to inconsistency between the articles of association and the law in relation to the voting requirement.

As a whole, performance to this question was satisfactory. Except for the misunderstanding by some candidates to part (a) with respect to the term actual controller, most candidates were able to give correct and precise answers to parts (b) and (c).

In part (a) candidates were required to explain the term *actual controller*. It refers to any person who is not a shareholder of a company but can control the company's acts through an investment relationship, agreement or other arrangements with the company. Therefore, the actual controller must not be a shareholder of a company but can control the company through various indirect ways other than the equity shares of the company. Some candidates, however, failed to distinguish the meanings of an actual controller and the majority shareholder.

Parts (b) and (c) of this question relate to the voting requirement for a limited liability company to provide guarantee for its shareholder or actual controller. Most candidates were able to pick up the key points in this part, i.e. the restriction on the participation of the shareholders' meeting by the shareholder obtaining the guarantee or the shareholder controlled by the actual controller as well as the special voting requirement for a resolution on the matters to provide such a guarantee. Candidates also correctly gave the answer relating to the compulsory nature of this requirement and its effect on the articles of association of a company.

Question Six

This question required candidates to explain the circumstances in which *community liabilities* will take place, state when community liabilities can be cleared and at least TWO items that should be regarded as community liabilities. Generally speaking, it is not an easy question, requiring candidates to understand precisely the knowledge of bankruptcy law and correctly pick out TWO items to be deemed as the community liabilities.

Part (a) of this question covers several key points. First, such liabilities are generated from the failure or acts by the debtor, the bankruptcy administrator or the relevant persons. Second, these liabilities exist for all the creditors, not for a single creditor. Thirdly, such liabilities will be generated in the period of time from date of the bankruptcy liquidation application being accepted and before the allocation of debtors' assets. Though performance for this part is satisfactory, only few candidates were able to pick up all three points.

Part (b) of this question is to test the knowledge of the clearance of the common liabilities. According to the Enterprise Bankruptcy Law, the community liabilities can be cleared through the debtor's assets at any time during the process of bankruptcy liquidation. Performance for this part was unsatisfactory, as many candidates confused the clearance of common liabilities with the order of allocation of debtor's assets at the end of the liquidation process.

Part (c) of this question is relates to liabilities that shall be deemed as community liabilities. Generally speaking, it is a comparatively complicated question. Since the common liabilities include various liabilities that may be generated during the entire period of the liquidation process and from different causes. Therefore, it requires candidates to have a solid understanding of the common liabilities and the liabilities that can be deemed as common liabilities. According to the Enterprise Bankruptcy Law, common liabilities will be generated from the following activities:

- (i) a contract, the performance of which both parties fail to fulfil, upon the performance request by the bankruptcy administrator or debtors against the opposite party;
- (ii) the negotiorum gestio of the debtor's assets;
- (iii) the liabilities as generated from the ill-gotten gains;
- (iv) the labour costs and social insurance for the continuance of business operation, as well as other liabilities as incurred therefrom;
- (v) the damage that occurs in the performance of functions and duties by a bankruptcy administrator or other relevant personnel, and
- (vi) any damage caused by the debtor's property.

One can understand that common liabilities are for the common interests of all creditors and are necessary for the completion of the liquidation procedures. Furthermore, some liabilities shall be settled immediately at the time the liabilities fall due. That is the particular reason why these liabilities shall be cleared at any time before the settlement of the debtor's assets. Performance for this part of question was unsatisfactory, since many candidates failed to understand the meaning of common liabilities or confused them with the order of settlement of debtor's assets.

Question Seven

This question required candidates to explain the *doctrine of independent legal entity of a company* and the *system of disregard of corporate personality*, and state the forms of liabilities for abuse of the independent legal entity. As a whole performance for this question was satisfactory, since the doctrine of independent legal entity of a company constitutes the legal basis of the company system. Candidates should have knowledge of this doctrine and should know the system of disregard of corporate personality.

Part (a) is relates to the meaning of the doctrine which means a company being a separate legal entity, having the independent properties of a legal person and enjoying the right to such properties. Shareholders of a company shall assume liability towards the company to the extent of the amount of capital contributions subscribed by each of them respectively. A company shall be liable for its debts to the extent of all its assets. The key points of this doctrine include three aspects: independent properties of a company, shareholders' liability for the debts of the company and the liability of a company. The limited liability of the shareholders toward a company is the substantive difference from the partners of a partnership. Most candidates could pick up some contents of the answer, but failed to give a full answer covering all the key points.

Parts (b) and (c) of this question required candidates to explain the meaning of disregard of corporate personality and liability for abuse. This system is an exception to the doctrine of independent legal entity. As a general principle, shareholders shall not be liable for the debts or civil liabilities of company. However, where the shareholders damage the interests of the company by abusing the doctrine of independent legal entity and conducting fraudulent behaviour, they shall be liable for damages without considering the general principle as to shareholders' limited liability toward the company.

Question Eight

This question requires candidates to deal with the legal issues relevant to the lost-and-found object under the Property Law. As a whole, most of candidates were able to give a correct answer to each part of question, and therefore obtained satisfactory marks.

Part (a) required candidates to determine whether Mr Ding could request the reward from Ms Liang for returning the lost-and-found handbag. According to the Property Law a lost-and-found object shall be returned to the right holder. However, the Property Law does not stipulate that a person is entitled to request a reward for finding the lost object. Most candidates were able to give a correct conclusion on this part, but only a few of them were able to state the reason to support their conclusion.

Part (b) of this question is relates to the reward offered by the right holder. Under the Property Law, where the right holder publicly offers a reward for the lost object, he or she shall keep the promise when claiming the lost-and-found object. An offer of reward for the lost object is an offer to a non-specific offeree and a unilateral act. Whenever the offer takes effect the offeror is bound by such an expression. A few candidates failed to give a correct conclusion, or failed to provide reasons to support their correct conclusion.

Part (c) of this question required candidates to state how to deal with the lost-and-found object in case nobody comes to claim after the expiration of the particular period of time. According to the Property Law, such object shall become state owned property after the expiration of 6 months for claiming the right of property if such



object has been submitted to the police. Most candidates were able to state that the lost-and-found object shall be owned by the State, but some failed to give the specific period of time for claiming the property.

Question Nine

This question required candidates to deal with the legal issues in relation to the transfer of contractual obligations. Although the scenario seems to be more complicated, the rule as stipulated in the Contract Law is clear and direct. Generally speaking, performance for this question was unsatisfactory. Most candidates were able to give correct conclusions to any one or two parts of this question, but others failed to answer one of the two parts. Furthermore, in giving reasoning to support their conclusions, there is room for improvement.

Part (a) of this question requires candidates to determine whether the transfer agreement is a valid one. According to the law, the creditor's consent is required if a debtor transfers the contractual obligation in whole or in part to a third party. In this case Shenhua was a debtor and wanted to transfer the debts to the third party. Generally, the transfer of debts would not be binding upon Kangyi Chemicals if Shenhua failed to give a notice and receive consent from Kangyi Chemicals. However, Kangyi Chemicals has acknowledged the transfer and held Shenhua Holdings as its counterparty by filing a lawsuit against Shenhua Holdings. Under such circumstances, the transfer agreement should be regarded as a valid one. Some candidates failed to note the fact that Kangyi Chemicals has already acknowledged the transfer of debts and held Shenhua Holdings, the third party, to be its counterparty and merely focused on the requirement of notice and consent. Of course the conclusion would be totally different. Any party's consent may be expressed by different ways: oral, written or through actions. The relevant provision of the Contract Law does not stipulate that consent must be in written form. Several candidates failed to give a correct judgement merely because Kangyi Chemical did not give a written consent to the transfer.

Part (b) is closely connected with part (a). In case the debtor lawfully transfers the contractual obligations, the relevant rights subordinated to such a transfer would automatically transfer to the new debtor. Hence where the creditor files a lawsuit against the new debtor, it should have the same right of defence as that of the original debtor.

Question Ten

This question required candidates to deal with the legal issue of the conditions for the public issue of corporate bonds. This form of scenario question has been given in several sessions and must be familiarised by candidates. The correct answer to this question required candidates to have knowledge of the relevant rule. As a whole, performance for this question was satisfactory.

Part (a) of this question tested the knowledge of the legitimate form of the public issue of corporate bonds. According to the Securities Law, securities to be offered to unspecific investors with a total face value exceeding RMB 50 million yuan shall be underwritten by an underwriting syndicate, a group of underwriters but not a sole underwriter. Therefore, the proposed public issue of corporate bonds was not in conformity with the law, although the proposal was to entrust an underwriter for the issue. Several candidates did not give a correct answer because they failed to notice the requirement of an underwriting syndicate by the law.

Most of candidates were able to give a correct answer to this part (b) that the maximum period for public issue of securities shall be 90 days.

Most of candidates were able to state that the proposed interest rate for the corporate bonds was in conformity with the law and the reason for such a conclusion was the interest rate of saving deposit as the basis.

Part (d) of this question tested the knowledge as to the use of corporate bonds. According to the Securities Law, funds raised through the issue of corporate bonds must be used for the purpose approved and shall not be used



to make up the losses of the company or for non-production expenditure. Most of candidates answered this part quite well, not only giving a conclusion, but also giving some reasons to support such a conclusion.