Overview

A. Introduction
1. Introduction of Squire, Sanders & Dempsey L.L.P.
2. Previous Laws Governing Bankruptcy Procedures
3. The New Enterprise Bankruptcy Law
4. Key Points of the New Law

B. Bankruptcy Procedures
1. Liquidation Procedure
   1.1 Application Procedure - Overview
   1.2 Requirements concerning Bankruptcy
   1.3 Entities Involved
   1.4 Asserting Creditor’s Rights
   1.5 Securing Debtor’s Assets
   1.6 Hierarchy of Liabilities
   1.7 Responsibilities of the Debtor
2. Reorganisation
3. Conciliation
4. Finalizing Bankruptcy Procedure

C. Contact Information
One of the largest international law firms

- 800 lawyers
- 30 locations and 7 associated offices worldwide
  - North America (since 1890) 15 offices
  - Asia (since 1955) 4 offices
  - Europe (since 1990) 12 offices
  - South / Latin America (since 2002) 5 offices
  - Middle East 1 office
## Introduction

### 1. Introduction of SSD

Squire, Sanders & Dempsey Offices Worldwide

<table>
<thead>
<tr>
<th>North America</th>
<th>Europe</th>
<th>Middle East and Africa</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cincinnati</td>
<td>Phoenix</td>
<td>Bratislava</td>
</tr>
<tr>
<td>Cleveland</td>
<td>San Francisco</td>
<td>Brussels</td>
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<tr>
<td>Columbus</td>
<td>Tallahassee</td>
<td>Bucharest*</td>
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<tr>
<td>Houston</td>
<td>Tampa</td>
<td>Budapest</td>
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<tr>
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<td>Tysons Corner</td>
<td>Dublin*</td>
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<tr>
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<td>Frankfurt</td>
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<td>Kyiv*</td>
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<tr>
<td>Palo Alto</td>
<td>West Palm Beach</td>
<td>London</td>
</tr>
</tbody>
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### Asia

- Beijing
- Hong Kong
- Shanghai
- Tokyo

### Latin America

- Buenos Aires*
- Caracas
- Rio de Janeiro
- Santiago*
- Santo Domingo

* = Associated Office
Introduction
1. Introduction of SSD
Squire, Sanders & Dempsey in China

- More than a quarter-century history in China
- One of the first law firms to establish a presence in China
- Received one of the first licenses in the early 1990s
- Established an office in Hong Kong in the late 1990s
- Expanded into Shanghai in 2004
- Home to professionals born and raised in China as well as those who have been actively involved with cross-border China activities for many years
A. Introduction
1. Introduction of SSD
China Practice - Key Areas of Practice

- M&A
- Joint venture formation – particularly in cases involving complicated regulatory and structuring issues
- Restructuring of Companies
- Holding companies
- Litigation, arbitration and anti-counterfeiting
- Intellectual property
- Customs and trade
- Financial Services
A. Introduction

2. Previous Laws Governing Bankruptcy Procedures

  - Applicable to State-owned Enterprises

- Several Issues on Trial of Enterprise Bankruptcy Cases Provisions by the Supreme People's Court (2002)
  - Applicable to all company types

  - Applicable to all non-state owned enterprises
A. Introduction
3. The New Enterprise Bankruptcy Law

- The Enterprise Bankruptcy Law of the People’s Republic of China was promulgated on August 27, 2006 and became effective on June 1, 2007 (the “New Law”)

- The Supreme People's Court has issued several pronouncements:
  - Concerning the Designation of the Administrator (2007)
  - Concerning the Remuneration of the Administrator (2007)
  - Concerning the Application of the New Law on bankruptcy cases pending on the effective date of the New Law (2007)
A. Introduction

4. Key Points of the New Law

- Applicable to all types of companies (including FIE and SOE) but not to individuals
- Introduction of reorganization as legal alternative to liquidation and conciliation for all company types available
- Establishment of a register of professional administrators to assume control of the Debtor
- Acknowledgement and enforcement of foreign verdicts, introducing cross-border insolvencies
  - Bankruptcy proceedings in China have binding effect over assets in foreign territories.
  - The acknowledgement and enforcement of foreign bankruptcy rulings involving assets in China shall be possible.
- Prioritizing Creditors secured claims over other claims, in particular employees’ claims
- Introducing claw-back provisions for certain transactions performed within a certain timeframe prior to the acceptance of the insolvency case
- Establishment of a Creditor’s Committee to supervise the administrator
- Setting civil liability of Debtor’s officials in case of a breach of their obligations of loyalty and diligence
B. Bankruptcy Procedures
Available Procedures

- Liquidation
- Reorganization
- Conciliation
B. Bankruptcy Procedures
1. Liquidation Procedure
1.1 Application Procedure - Overview

Application by

Creditor

People’s Court will notify Debtor within 5 days after receipt of application

The Debtor may file his demurrer within 7 days after receipt of notice

People’s Court will rule whether to accept application for bankruptcy within 10 days after expiration of period

Period may be extended for 15 days upon approval by next higher court People’s Court

Non - Acceptance

People’s Court will serve ruling & reason for denial within 5 days to applicant

Acceptance

Applicant may file appeal within 10 days of service to the People’s Court next higher level

Acceptance

Debtor has to file statements & reports within 15 days hereupon

People’s Court will:
- Notify known creditors within 25 days of the ruling
- Announce decision, detail of first creditors, etc.
- Appointment of the administrator

Court will serve ruling within 5 days to Debtor

Court will serve ruling within 5 days to applicant thereof

Court will serve ruling within 5 days to applicant thereof

Court will serve ruling within 5 days to debtor

People’s Court will rule whether to accept application for bankruptcy within 15 days after receipt
B. Bankruptcy Procedures
1. Liquidation Procedure
1.2 Requirements concerning Bankruptcy

- After the application by either a Creditor or the Debtor for opening bankruptcy procedures, the People’s Court will conduct a Bankruptcy Test.

- The Bankruptcy Test will be a combination of a balance-sheet test and a cash-flow / liquidity test.

- The People’s Court will assume the Debtor to be bankrupt if one of the following two conditions is fulfilled:
  - if the Debtor is unable to discharge its debts when due and its assets are insufficient to discharge its debts in full
    or
  - if the Debtor is unable to pay its debts when due and it obviously lacks the ability to discharge its liabilities, i.e. bankruptcy is evident.
B. Bankruptcy Procedures
1. Liquidation Procedure
1.3 Involved Bodies (i)

- Administrator
- Debtor
- Creditors’ Meeting:
  - A Creditor who has filed a claim will be a member of the Creditors' Meeting with voting rights.
  - A Creditor whose claim is not ascertained cannot exercise voting rights. (The People's Court tentatively may enable it to exercise its voting rights.)
  - A Creditor can attend the Creditors' Meeting and exercise its voting rights by proxy.
  - A representative of the staff and workers and the labor union of the Debtor can attend the Creditors’ Meeting and can express opinions on the relevant matters.
  - The Creditors' Meeting has one chairman, who will be appointed by the People's Court among the Creditors who have voting rights.
B. Bankruptcy Procedures
1. Liquidation Procedure
1.3 Involved Bodies (ii)

- The Creditors' meeting shall exercise the following functions:
  - verifying the claims;
  - applying to the People’s Court for replacement of the Administrator and examining the expenses and remuneration of the Administrator;
  - supervising the Administrator (if existing, done by the Creditor’s Committee);
  - appointing and replacing the members of the Creditors' Committee;
  - deciding to continue or terminate the operations of the Debtor;
  - adopting the reorganization plan;
  - adopting the conciliation agreement;
  - adopting the plan for the management of the Debtor's property;
  - adopting the plan for the realization of the bankruptcy property;
  - adopting the plan for the distribution of the bankruptcy property; and
  - other functions which the People's Court deems necessary to be exercised by the creditors' meeting.
B. Bankruptcy Procedures
1. Liquidation Procedure
1.3 Involved Bodies (iii)

– Subsequent creditors' meeting shall be convened when:
  • the People's Court considers necessary, or
  • when it is proposed to the chairman of the Creditors' Meeting by the Administrator, the Creditors' Committee and the Creditors whose claims account for more than one-fourth of the total amount of the claims

– When the Creditors' Meeting is to be convened, the Administrator shall give 15 days' notice to the known Creditors.

– Resolutions of the Creditors' Meeting are to be adopted by a majority of the attending Creditors who have voting rights and who represent more than one half of the total amount of the unsecured claims.

– If a Creditor believes that a resolution of the Creditors' Meeting is in violation of laws and prejudices its interests, it can within 15 days of the making of the resolution by the Creditors' Meeting request the People's Court to revoke the resolution and order to the Creditors' Meeting to make a new resolution in accordance with the law.
B. Bankruptcy Procedures
1. Liquidation Procedure
1.3 Involved Bodies (iv)

- Creditors' Committee
  - The Creditors' Meeting can decide to form a Creditors' Committee.
  - The Creditors' Committee consists of the representative of the creditors appointed by the Creditors' Meeting and one representative of the staff and workers or the labor union of the debtor.
  - The Creditors' Committee shall not have more than nine members.
  - The members of the Creditors' Committee shall be subject to written confirmation by the People's Court.
  - The Creditors' Committee shall exercise the following functions:
    - supervising the management and disposal of the debtor's property;
    - supervising the distribution of the bankruptcy property;
    - proposing to convene the Creditors' Meeting; and
    - other functions entrusted by the Creditors' Meeting.
B. Bankruptcy Procedures
1. Liquidation Procedure
1.3 Involved Bodies (v)

- The Administrator
  - The post of an Administrator may be assumed by one of the following three categories of persons/organizations:
    - A non-governmental intermediary agency such as a law firm, an accounting firm, or bankruptcy liquidation firm;
    - In cases of minor complexity and relatively centralized Debtor’s properties, an individual from the applicable register of individuals to serve as administrator;
    - Where justified, a liquidation committee formed by members of the government, registered intermediary agencies, financial asset management companies, the People’s Bank, and financial regulatory institutions.
  - The Administrator will be supervised by the Creditor’s Meeting or the Creditor’s Committee, if existing and assigned to the Creditor’s Committee
B. Bankruptcy Procedures
1. Liquidation Procedure
1.3 Involved Bodies (v)

- If a Creditor’s Committee exists, the Administrator has to report when it performs the following acts:
  - transfer of rights and interests in immovable objects such as land and buildings;
  - transfer of other property rights such as mineral exploration rights, mining rights and intellectual property rights;
  - transfer of the whole of inventory or business;
  - borrowing of money;
  - creation of property security;
  - transfer of claims and negotiable securities;
  - performance of contracts which both the debtor and the counterparty have not fully performed;
  - waiver of rights;
  - recovery of security; and
  - other act of property disposal which has a material effect on the interests of the creditors.

- If no Creditors’ Committee exist, the Administrator has to report to the People’s Court.
B. Bankruptcy Procedures
1. Liquidation Procedure
1.4 Declaring Creditor’s Rights

• The term for announcing its claims against the Debtor will be set by the People’s Court. (It is supposed to last between 30 days and a maximum of 3 months)

• A Creditor has to submit the details of his respective claims in written form, also naming any guarantees and other circumstances for the right.

• After the term has ended, a Creditor can only make up his declaration until the final distribution of assets begins.

• The claims will be registered in a registry held by the Administrator, who carries out examination on the filed claims and prepares a schedule of claims.

• This schedule and the claim filing materials will be kept by the Administrator and will be made available for inspection by interested parties.

• The schedule of claims prepared by the Administrator will be submitted to the first Creditors’ Meeting for verification.

• If the Debtor and Creditors have no objection to the claims set out in the schedule, the People's Court will confirm the schedule.

• If the Debtor or a Creditor has objections against any claim set out in the schedule, it may initiate litigation at the People’s Court which has accepted the bankruptcy application.

• Each approved Creditor is automatically a member of the Creditors’ Meeting and enjoys a right to vote therein.
B. Bankruptcy Procedures
1. Liquidation Procedure
1.5 Securing Debtor’s Assets (I)

- **Suspension of actions involving Debtor**
  - the People’s Court can impose a suspension of all civil actions and arbitration proceedings involving the insolvent Debtor.
  - The suspended action may be continued after the Administrator has assumed control of the Debtor’s assets.

- **Performance of contracts involving the Debtor**
  - The Administrator has the power to decide in the best interest of the Debtor if unfulfilled contracts shall be continued or rescinded.
  - If he decides to continue the contract, the other contractual party shall perform its obligations. In return, such party is entitled to demand security for the further performance. Note: The New Law does not specify the extent of such security – like “sufficient” etc.
  - The New Law is not completely clear about the scope of the administrator’s competencies when deciding whether to continue or to rescind a contract, especially in respect of the terms of the contract.
  - The New Law is also unclear whether clauses in contracts upon which a party of a contract would be entitled to an earlier termination of the contract in the event of a bankruptcy application of the other party are void or not, like in other jurisdictions. (In the past, Chinese authorities have accepted such clauses, e.g. in Joint Venture Contracts.)
B. Bankruptcy Procedures
1. Liquidation Procedure
1.5 Securing Debtor’s Assets (II)

- Claw-back provisions

  - Transactions may be revoked which took place within a period 1 year prior to the acceptance of the bankruptcy case (e.g. undervalued or unreasonable transfer of assets, giving security for unsecured debts, repayment of debts in advance and giving up a Creditor claim)
  
  - Any repayment to individual Creditors within a period of 6 months prior to the acceptance of the case may be questioned by the Administrator if the debtor was already bankrupt at that time and still continued to repay Creditors.
  
  - Certain transactions do not require any application to the People's Court in order to be revoked (e.g. the concealing or transfer of assets in order to avoid the debts or the acknowledgement of fraudulent debts)
  
  - The capital contributors of the Debtor have to pay their complete outstanding contribution.
  
  - The Administrator may recover any abnormal income that leading employees of the debtor may have granted themselves.
  
  - The Administrator can prevent Debtors from making distributions to their shareholders.
B. Bankruptcy Procedures
1. Liquidation Procedure
1.5 Securing Debtor’s Assets (III)

• Offsetting against the Debtor’s claim
  – A Creditor may claim for offset against the Administrator after the acceptance of the bankruptcy case if the right to set off against a Debtor’s claim has existed before the acceptance of the case.

Exceptions:  
- If a Creditor’s claim was acquired after the People’s Court's acceptance, or
- if the liabilities were incurred when the Creditor had positive knowledge of the bankruptcy application or
- the Debtor’s inability to pay off its debts.
B. Bankruptcy Procedures
1. Liquidation Procedure
1.6 Hierarchy of Liabilities

• 1. Secured credits
  – For any Creditor whose claim has been guaranteed by particular assets, the New Law provides for priority repayment by the means of those secured assets.
  – Only in case of a shortfall, the remaining claim shall be treated as a common unsecured claim.

• 2. Cost for bankruptcy proceedings and community liabilities
  – Bankrupt expenses and community liabilities are also given precedence over all other Creditors’ claims.
  - The bankrupt expenses include the costs of action on the cases, costs of administration and distributions of debtor’s assets and the administrator’s remuneration.
  - Community liabilities cover among others the cost for the continuance of business operations, liabilities from the damage occurring in connection with the performance of the administrator’s job and liabilities generated from damage due to the debtor’s assets.

• 3. Repayment sequence for liquidated insolvent assets
  – After the deduction of bankrupt expenses and community liabilities, the liquidated assets will be distributed first with regard to employee-related claims (employments wages, medical benefits and pension premiums).
B. Bankruptcy Procedures
1. Liquidation Procedure
1.7 Responsibilities of the Debtor

- Responsibilities of the Debtor’s management and employees during
  the insolvency procedure:
  - Applicable to legal representatives of the enterprise and, subject to the
decision of the People's Court, the financial management personnel and
  other business management personnel of the Debtor.
  - Such personal shall:
    - Safe keep the property, seals and information such as accounting
      books and documents;
    - Shall carry out work as required by the People’s Court and the
      Administrator
    - Shall give truthful answers to the questions addressed to them;
    - Shall attend the Creditors’ Meeting and giving truthful answers to the
      questions of the Creditors;
    - Shall not leave their places of domicile without the permission
      of the People's Court (Note: Very important for expatriate
      personnel), and
    - Shall not accept new appointments as director, supervisor or
      senior management personnel in other enterprises (Note: Also
      very important for expatriate personnel).
B. Bankruptcy Procedures
2. Reorganization (i)

- It is one of the major innovations of the New Law
- Reorganization is aimed at giving still viable but temporarily encumbered enterprises a break from Creditors’ claims in order to recover and set up a concept for sustainable success in the future.
- Any Creditor as well as the Debtor may apply for reorganization directly with the People’s Court.
- The Debtor or its capital contributor may apply for reorganization even after the People’s Court has already accepted a Creditor’s application for bankruptcy and not announced the debtor to be bankrupt, yet.
- Similar to the “debtor-in-possession” concept allowing the Debtor to continue to manage his business under the supervision of a court-appointed administrator and exercise the functions assigned to the Administrator
- During the reorganization period, the exercise of control over secured rights is basically suspended unless a damage or reduction in value of the secured property threatens to take place.
B. Bankruptcy Procedures
2. Reorganization (ii)

- If the reorganization proceedings no longer seem to have the chance of success or the cooperation between Debtor and Administrator is impaired, the Administrator or any interested party may apply with the People’s Court to declare the Debtor bankrupt.

- Reorganization proceedings
  - To begin reorganization proceedings, the debtor or the Administrator have to propose a sustainable rectification plan upon which the People’s Court will hold a Creditors’ meeting within 30 days in order to negotiate and vote on the plan.
  - Once the reorganization plan is approved by the People’s Court the rectification plan that will be implemented has binding force for the Debtor and all Creditors.
B. Bankruptcy Procedures
3. Conciliation

• Debtor and Creditors can agree on a compromise and settlement of debts other than stipulated by the New Law.

• Accordingly, a Debtor may apply for compromise with the People’s Court by submitting a draft of the conciliation agreement unless he has already been declared bankrupt. In such case the draft is discussed, negotiated and eventually approved by the Creditors’ Meeting.

• In case of disagreement, the People’s Court may cancel the conciliation proceedings and declare the debtor bankrupt;

• In the event that the proposal is adopted and confirmed by the People’s Court, the Administrator will hand over the assets and business operations back to the Debtor.

• The conciliation agreement has binding force on all parties involved once it is confirmed by the People's Court.
B. Bankruptcy Procedures
4. Finalizing Bankruptcy Procedure

• In the event that the People’s Court decides to declare the Debtor bankrupt, it will serve its decision to the debtor and all known Creditors having declared their claims according to the requirements of the New Law.

• The announcement of bankruptcy shall not happen if a third party guarantees or pays for the debtors assets or if the debtor pays off all the due debts.

• The bankruptcy assets shall be distributed according to the above mentioned hierarchy.

• The Administrator is supposed to establish a distribution plan that has to be approved by the Creditors’ Meeting.
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