

THE LAW SOCIETY OF HONG KONG
OVERSEAS LAWYERS QUALIFICATION EXAMINATION
2011 SUPPLEMENTARY INFORMATION PACKAGE

HEAD III: COMMERCIAL AND COMPANY LAW

Contents

- 1. Standards, Syllabus and Materials**
- 2. Examiners' Comments on the 2008, 2009 and 2010 Examinations**
- 3. Past Examination Papers (2008 – 2010)**

Important: The test paper for Head III Commercial and Company Law:

- 1. is open book. Candidates may bring in and refer to any book, document or other written material**
- 2. has a duration of 3½ hours**
- 3. has no specific reading time allocated**
- 4. contains FIVE questions. Candidates should answer any FOUR questions only.**

1. Standards, Syllabus and Materials

Overseas Lawyers Qualification Examination

HEAD III: COMMERCIAL AND COMPANY LAW

Standards, Syllabus and Materials

STANDARDS

General Notes to Candidates

The reading list attempts to be as extensive as possible but there is no one particular comprehensive text available. Students should therefore read as widely as possible over these topics. You cannot assume that by reading only a selection of the texts that you will have read in sufficient detail or depth, and it is recommended that you try to look at all the suggested readings.

Where the reading list consists of materials prepared or written not specifically for Hong Kong legislation, you should be aware of any differences in law and principles in such materials which may not be applicable to Hong Kong.

You should also familiarise yourself with the latest legislative changes and legal developments which may have occurred since the publication of those materials.

Candidates will be expected:

- (i) to have a working knowledge of the commercial and company law listed below;
- (ii) to be able to draft and analyze simple documents and forms; and,
- (iii) to be able to perform many of the tasks of a commercial lawyer, including
 - (a) incorporating a new company
 - (b) activating a shelf company

The test paper for this Head of the Examination is set at the standard expected of a newly qualified (day one) solicitor in Hong Kong who has completed a law degree (or its equivalent), the professional training course (PCLL) and a two year traineeship prior to admission.

SYLLABUS

1. Introduction to Business Organizations

- (a) Sole Proprietorship
 - establishment, management, disposal and/or dissolution of business
- (b) Partnership
 - types of partner
 - limited partnerships
 - establishment, management, disposal and/or dissolution of business
- (c) Company
 - newly incorporated or shelf company
- (d) Choice of Business Vehicle
- (e) Business Registration

READING LIST

- *Stott, Hong Kong Company Law (latest edition)*

SYLLABUS

2. Company Practice

- types of company
- incorporation of private company limited by shares
- preparation of memorandum and articles of association
- activation of a company
- registration of an overseas company
- continuing registration requirements for Hong Kong and non-Hong Kong companies
- division of power between members and directors
- members, meetings, resolutions
- directors, procedures, (including meetings and resolutions), fiduciary, common law and statutory duties
- minority protection
- disqualification of directors
- finance, share capital and loan capital, dividends and profits, accounts
- company's repurchase of its own shares
- company's financing the purchase of its own shares
- changing a company's memorandum and articles of association

- disposing of an interest in a company
- transfer and transmission of shares
- sale of company's assets
- voluntary winding-up and distributions in specie

READING LIST

- *Lawton, P., Meetings in Hong Kong: Their Law and Practice (Pitman Publishing latest edition), pp135-294*
- *Stott, Hong Kong Company Law (latest edition)*
- *Tomasic & Tyler, Hong Kong Company Law Legislation and Commentary (Butterworths latest edition)*
- *Hong Kong Company Secretarial Practice Manual (Sweet and Maxwell latest edition), Chapters 1, 2, 4, 5, 6, 7 and 12 (pp 12031-12035)*

SYLLABUS

3. Hong Kong Joint Ventures

- joint venture documentation
- basic provisions of main joint venture agreement
- joint venture articles of association
- minority protection

READING LIST

- Preliminary Note and Precedents on Joint Ventures, Volume 19, The Encyclopaedia of Forms and Precedents (5th ed)

SYLLABUS

4. Acquisition of a Private Company

- (a) **overview of business entities**
- (b) **private company share sale**
 - what the company owns
 - what the shareholders own
 - the difference between legal and beneficial ownership of shares, assets and liabilities

- (c) **taking instructions from the purchaser**
 - what the purchaser wants to buy
 - what the purchaser plans for the company
 - due diligence and investigations of the worth of the company

- (d) **due diligence**
 - the purpose of conducting due diligence and the type of issues to be covered by the due diligence investigation

- (e) **investigations of the company**
 - what to do with the information collected; the nature of the discrepancies and confirmatory information
 - the need for further instructions
 - the effect on the structure and content of the acquisition documents
 - where the information is reflected in the acquisition documents

- (f) **identifying the issues**
 - what to do with the information collected; the nature of the discrepancies and confirmatory information
 - the need for further instructions
 - the effect on the structure and content of the acquisition documents
 - the effect on the purchaser
 - intellectual property issues
 - non-competition and restrictive covenants

- (g) **drafting the acquisition documents**
 - the Share Purchase Agreement
 - the Deed of Indemnity for Tax Liability
 - the Disclosure Letter

- (h) **warranties and representations from seller**

- (i) **information exchange and negotiation**
 - the process of negotiation and settling of the acquisition documents

- (j) **exchange of contracts and completion**
 - which documents are signed
 - the ancillary documents to be prepared
 - the exchange of documents
 - the type of completion: immediate or after conditions precedent satisfied

- (k) **post-completion**
 - attention to post completion tasks: corporate restructurings; filings; stamping; time limits; penalties and consequences of non-compliance
 - the survival of warranties and representations
 - completion agenda

- (l) **cf. sale of business/assets as opposed to share sale**
 - **Transfer of Businesses (Protection of Creditors) Ordinance Cap 49**

READING LIST

- *Tolley*, "Acquisition of Private Companies and Business," in Tolley's Company Law (latest edition)
- Preliminary Note and Precedents on "Part 2: Share Sale Agreements," Volume 11, The Encyclopaedia of Forms and Precedents (5th ed)

SYLLABUS

5. **Charges, Other Forms of Security, and Guarantees**

- company's power to borrow and create security
- debentures
- fixed and floating charges
- charges over book debts
- crystallisation
- practical differences between fixed charges and floating charges
- charges over various types of assets
- registration of charges
- remedies of debenture-holder
- retention of title
- legal nature of guarantees/indemnities
- the types of guarantee
- letters of comfort
- the rights of the guarantor against the principal debtor or borrower
- the rights of the guarantor against the creditor/bank
- discharge of the guarantor's liability
- determination of the guarantee
- other common clauses in a guarantee
- enforcement of the guarantee
- practical tips on the drafting and use of a guarantee

READING LIST

- Please note:
Section 56 A(1) of the Conveyancing and Property Ordinance Cap 219; Section 2(A) of the Land Registration Ordinance Cap 128.
- *Stott, Hong Kong Company Law* (latest edition)
- Precedents - Debenture, Volume 10, The Encyclopaedia of Forms and Precedents (5th ed)
- Continuing Guarantee, Volume 17(2), The Encyclopaedia of Forms and Precedents (5th ed)

SYLLABUS

6. Securities and Investor Protection

- licensing of intermediaries and regulation of their activities and operations
- protection of investors
- regulation of public offering of securities and other investment arrangements, and prospectus requirements, including liability for misrepresentation and non-disclosure about securities
- disclosure of interests
- role of the Securities and Futures Commission
- transitional arrangements under the Securities and Futures Ordinance
- corporate governance

READING LIST

- *Stott, Hong Kong Company Law* (latest edition)
- Chapters 1, 2, 3, 6, 7, 8, 14 and 14A, Practice Notes 5, 11 and 21 and Appendix 14 of the Rules Governing The Listing of Securities on The Stock Exchange of Hong Kong Limited
- The following Parts of the Securities and Futures Ordinance:
 - Part I
 - Part II
 - Part IV
 - Part V
 - Part VIII
 - Part XIII
 - Part XIV
 - Part XV and all Schedules relevant to the aforesaid Parts
- Securities and Futures (Stock Market Listing) Rules

SYLLABUS

7. Receiverships

- receiver/receiver & manager
- appointment
- position of receiver
- disqualification for appointment
- effect of appointment
- duties of receiver
- receiver's rights and powers

READING LIST

- *Stott, Hong Kong Company Law* (latest edition)
- *Tomasic and Tyler, Hong Kong Company Law Legislation and Commentary* (Butterworths latest edition)
- *Hong Kong Company Secretarial Practice Manual* (Sweet and Maxwell latest edition) Chapter 12 pp 12011-12021

SYLLABUS

8. Company Liquidations

- how liquidations differ from and are related to receiverships
- types of winding up
 - compulsory liquidation
 - voluntary liquidation (members' voluntary liquidation and creditors' voluntary liquidation)
- differences between various forms of winding up / liquidation
- grounds for winding up
- commencement
- court's powers
- the consequences of commencement
- the consequences of the winding up order
- the stay
- powers and duties of liquidator
- avoidance powers
- effect of winding up on antecedent and other transactions
- directors' disqualification

READING LIST

- *Sherrington*, "Insolvency," Chapter 12 in Trade and Investment Law in Hong Kong (Smart & Halkyard (eds), 1993)
- *Stott*, Hong Kong Company Law (latest edition)

SUMMARY OF MATERIALS

1. Books and articles

As set out in the Reading Lists above

2. Ordinances of Hong Kong

- Business Registration Ordinance, Cap 310
- Companies Ordinance, Cap 32 (including Table A of the First Schedule to the Companies Ordinance) and the Winding Up Rules
- Conveyancing and Property Ordinance Cap 219 s 56A(1)
- Land Registration Ordinance Cap 128 s 2A
- Law Amendment and Reform (Consolidation) Ordinance, Cap 23, ss 9, 13, 14, 15 & 15A
- Limited Partnership Ordinance, Cap 37
- Partnership Ordinance, Cap 38
- Securities and Futures Ordinance, Cap 571
- Stamp Duty Ordinance, Cap 117
- Transfer of Businesses (Protection of Creditors) Ordinance, Cap 49

3. Precedents

- Debenture
- Continuing Guarantee
- Joint Venture/Shareholders' Agreement
- Memorandum and Articles of Association
- Share Sale Agreement
- Business (asset) Sale Agreement

4. Further reading

- Hong Kong Company Law Handbook (Butterworths latest edition)

**2. Examiners' Comments
on the 2008, 2009 and 2010
Examinations**

Examiners' Comments on the 2008 Examination

Head III: Commercial and Company Law

The examination covered a range of questions from the syllabus which required candidates to demonstrate their knowledge and practical understanding of Hong Kong commercial and company law. Some candidates continue to choose to provide pre-prepared answers to questions, thereby simply ignoring the various issues raised by the questions. For example, some candidates provided one unequivocal answer to questions that were designed to invite an analytical discussion of various options available to the client arising from the set of facts presented in the question. When candidates followed this approach, they invariably failed to address many of the issues raised by the question.

In addition, some candidates failed to allocate their time appropriately. They would answer three questions reasonably well and provide a very poor response to last question, which seemed to suggest that the candidate did not have sufficient time to respond to the question.

On the other hand, there was a small proportion of candidates who demonstrated a sound knowledge of the syllabus, producing thoughtful, logical and coherent answers, which were supported by appropriate references to case law and legislation.

Examiners' Comments on the 2009 Examination

Head III: Commercial and Company Law

The examination covered a range of questions from the syllabus which enabled candidates to illustrate their knowledge and practical understanding of Hong Kong commercial and company law. Many candidates still provide one unequivocal answer to questions that are designed to solicit an analytical discussion of the various legal issues raised by a set of facts. These “problem-type” questions are designed to solicit a discussion by candidates of the variable possible options available to the client to whom the candidate is required to provide advice.

Some candidates were not comfortable dealing with questions that required knowledge of recent changes in the law. Overall, major weaknesses were: not directing the answers towards the questions as set; not supporting the answers with adequate reference to legal authorities, and merely citing the rules without sufficient or any analysis. Candidates are expected to demonstrate an ability to analyse the legal issues raised by the questions. In addition, some candidates failed to allocate an appropriate proportion of time - they devoted too much time to the first three questions and neglected the last one.

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Examiners' Comments on the 2010 Examination

Head III: Commercial and Company Law

The examination paper comprised five questions. Candidates were required to answer any four questions only. The questions focused on corporate and commercial problems that solicitors in Hong Kong encounter in practice.

Overall Comments:

Major weaknesses were: producing unequivocal answers to questions without stating the relevant general legal principles; not providing any analysis of the various legal options available to the clients; failing to reach any conclusion; failing to keep the answers organised and coherent; not directing the answers towards the questions as set; not supporting the answers with adequate reference to statutory provisions and case authority. Specific comments regarding individual questions are set out below.

Question 1

The first part of the question required candidates to demonstrate an adequate understanding of issues relating to the powers of the shareholders in general meetings, the powers of the board of directors, and the protection of minority shareholders' interests. Some weaker candidates failed to discuss s 168A as regards unfairly prejudicial conduct.

The second part of the question concerned loans and similar transactions in favour of directors and certain connected persons. On the whole, this question was answered well.

Question 2

Part of this question required candidates to discuss the company's statutory right to increase its share capital, in the light of contradictory provision within the company's articles of association, which stipulated that an increase in share capital would require the unanimous consent of all shareholders. Some candidates identified the key issues and produced a logical analysis but others failed to identify and reconcile the differences between the articles and the Companies legislation. The second part of this question required candidates to analyze the efficacy of a notice convening an AGM. Most candidates dealt with this question reasonably well.

Question 3

The first part of the question invited an analysis of the various options available to a shareholder to recover her loan and equity investment in a joint-venture company. The second part of the question required candidates to address issues regarding unfair preference (s 266B CO). This question was answered reasonably well, although weaker candidates failed to identify the possibility of serving a statutory demand on the company under s 177(1)(d) CO.

Question 4

This question sought to require candidates to demonstrate their knowledge of the principles concerning the issue, content, dating, and registration and vetting of prospectuses. Some candidates, however, omitted to identify and analyse relevant civil and criminal liabilities concerning untrue statements made in a prospectus. Also, not many candidates identified the relevant exceptions regarding the vetting and registration of a prospectus.

Question 5

The first part of the question concerned the creation of fixed and floating charges over book debts. In the second part of the question, candidates were required to highlight the key differences between a creditors' voluntary liquidation and other applicable modes of liquidation, and to apply the principles to the facts of the question. This question was answered well.

3. Past Examination Papers from 2008 to 2010

2008 OVERSEAS LAWYERS QUALIFICATION EXAMINATION

HEAD III: COMMERCIAL AND COMPANY LAW

Tuesday, 4 November 2008



HEAD III: COMMERCIAL AND COMPANY LAW

TEST PAPER

4 November 2008

Instructions to Candidates :

- 1. The duration of the examination is 3 hours and 30 minutes.**
- 2. This is an open-book examination.**
- 3. There are FIVE questions in this paper.**

ANSWER ANY FOUR QUESTIONS ONLY.

- 4. IF YOU ATTEMPT MORE QUESTIONS THAN YOU HAVE BEEN INSTRUCTED TO ANSWER :**

(a) THE EXAMINERS WILL MARK ALL QUESTIONS THAT HAVE BEEN ATTEMPTED AND NOT DELETED; AND

(b) IN COMPUTING YOUR FINAL MARK, THE EXAMINERS WILL COUNT THE MARKS FOR THE NUMBER OF QUESTIONS THAT YOU WERE INSTRUCTED TO ANSWER TAKING INTO ACCOUNT THE ANSWERS WITH THE LOWEST SCORES.

- 5. Start each question on a separate page of your answer book.**
- 6. Each question has the value noted on the question paper. You are urged to apportion your time in accordance with the relative value of each question. No marks can be awarded to a question for which there is no attempted answer.**
- 7. An examiner will be present for the first 30 minutes of the examination. Any question relating to the paper must be raised in that period. Questions raised after the first 30 minutes will not be entertained.**
- 8. Do not take either this question paper or any answer books with you when you leave the examination room.**

2008 Overseas Lawyers Qualification Examination

Head III: Commercial and Company Law

Question 1 (25 marks)

Titanica Limited (“Titanica”) is a Hong Kong incorporated company which operates a retail computer hardware business in Hong Kong. The shareholders and directors, Moby, Nimo and Poppy, have been friends for more than 10 years. The daily operations of the business are undertaken and conducted by Nimo and Poppy, who are a married couple. Titanica was incorporated in 2005 with an authorized share capital of HK\$10,000 divided into 10,000 shares of HK\$1.00 each. In January 2006, Dick, a friend of Moby, was appointed a non-executive director of Titanica.

The friends had ambitious plans for Titanica, genuinely believing that the business had great potential. However, their hopes were shortlived and Titanica’s business never took off. By July 2008, Titanica experienced serious cash flow difficulties. A meeting of the directors was held on 11 July 2008 to consider whether further funds should be injected into the business. The directors were, however, unable to reach a decision on this issue and so adjourned the meeting for one week. Immediately after the directors’ meeting, Nimo and Poppy, who were also in personal financial difficulty themselves, moved quickly and procured Titanica to enter into an agreement with Fox Limited without the knowledge of Moby or Dick. The directors and shareholders of Fox Limited are Nimo, Poppy and Totem Tam. The terms of the agreement provide that (i) loans amounting to \$2 million, previously advanced to Nimo and Poppy by Titanica, would be assigned to Fox Limited; (ii) Titanica’s principal assets, a shop in Pokfulam and all its inventory, valued at \$1 million, would be transferred to Fox Limited; (iii) Fox Limited would be required to discharge the consideration for the loan assignment and asset transfer on 8 July 2009. Upon discovering the transaction, Moby reported the matter to the police and applied to have Titanica wound up.

(See the next page for a continuation of Question 1)

Question:

Moby consults you to ascertain the following:

- (i) Explain, giving reasons and citing case authority, as appropriate, whether the transaction that Nimo and Poppy caused to be concluded with Fox Limited is liable to be set aside.**

(7 marks)

- (ii) Explain what is meant by tracing and whether the assets disposed of to Fox Limited may be traced.**

(10 marks)

- (iii) Moby discovered that Nimo and Poppy have never prepared audited financial statements or filed any annual returns for Titanica. What, if any, liability are Moby and Dick exposed to?**

(8 marks)

Question 2 (25 marks)

ABB Co. Ltd (“ABB”) is a very successful and well known family business manufacturing and trading in electronic goods. The founder of the business, Bunn, died in 1999 and, since that time, ABB’s board of directors comprised of Bunn’s three sons, namely Alan, Bill and Ben, and Rawson, who is a qualified professional accountant. Alan, Bill and Ben and their step-mother, Annie, each hold 25 per cent of ABB’s issued share capital.

In mid 2007, Rawson came across some paperwork which suggested that some of the hi-fi systems manufactured at ABB’s factory in Guangdong were being delivered to a company called MacS Ltd (“MacS”). Ordinarily the hi-fi systems would either be transported to ABB’s godown in Hong Kong and then distributed to retailers here or sold to wholesalers in the USA. Rawson noticed that MacS’s premises were also in Hong Kong and it thus appeared that ABB was competing with MacS for customers. Rawson then tried to discover the price at which ABB was selling the hi-fi system to MacS but could not find any relevant paperwork or evidence of payment.

Rawson was reluctant to question either Alan, Bill or Ben because he was very well paid and did not want to lose his position as finance director. But he felt uneasy about his findings and sought to discover the scale of the deliveries to MacS and the impact of these activities on ABB’s profits and dividends.

At about the same time Alan, who is the eldest of the three brothers and took on the roles of CEO and chairman of ABB, proposed a massive expansion of ABB’s manufacturing plant in Guangdong. The proposal required ABB to raise more than \$50 million. The board of directors supported the proposal and Rawson was given the task of finding ways to raise the required funds.

Negotiations with various banks, all of which asked for a copy of ABB’s latest audited accounts, resulted in ABB creating a fixed charge over its godown and a floating

(See the next page for a continuation of Question 2)

charge over the stock of electrical goods stored at its godown as security for loans amounting to \$30 million. When Rawson next saw Alan he explained that the banks appeared to be reluctant to lend additional funds largely because of the economic slowdown in the USA. Alan's response was "try asking my step-mother to make up the difference".

Reference to Alan's step-mother, Annie, prompted Rawson to recall his earlier concerns about ABB's relationship with MacS – and the suspicion that Alan, and perhaps his brothers, were diverting ABB's business to another company. Before consulting with Annie, Rawson conducted a search at the Company's Registry, which revealed that the only shareholder of MacS was a company called Scam Ltd ("Scam") and that Alan was the founding member and only shareholder of Scam.

Rawson was so alarmed by this revelation that he arranged a meeting with Annie and explained his concerns. Annie then consulted her lawyer with a view to "stopping the cheating". She had suspected that her step-sons had been cheating her ever since Bunn's death, when the brothers removed her as a director of ABB, but previously she had no evidence.

Question:

You are Annie's lawyer and she asks you to advise on the following:

(i) whether she has any grounds to petition for ABB Co. Ltd to be wound up by the court and the likelihood of her petition succeeding.

(7 marks)

(ii) whether her step-sons are in breach of their duties as directors, and the powers of the court / liquidator in respect of investigating their activities.

(12 marks)

(iii) the laws, if any, for ensuring that her step-sons cannot be appointed as directors of a company.

(6 marks)

Question 3 (25 marks)

Hydro Company Limited (“Company”) was incorporated in Hong Kong in January 1993. For more than 15 years, the Company has built a reputation for advanced water purification systems. Its customers include major hotels in Hong Kong, Macau and Shenzhen. The Company has only two directors, Peter Yim and his wife, Susan Yim, who are also the Company’s shareholders.

The Company’s business has been expanding ever since the Macau Government encouraged foreign investors to construct up to 25,000 new hotel rooms to meet the growing demand from the city’s booming tourism industry. During the three years ended 2005, the Company’s turnover and net profit achieved a double-digit annual growth rate.

Impressed by the Company’s performance, the Company’s banker, SAR Bank (“Bank”) invited the Company to join its “Premier Overdraft Protection Scheme” in January 2005. Being one of the Bank’s “Preferential Customers”, the Company was granted a pre-approved standby credit limit of up to \$800,000. The interest rate on the amount drawn under this facility is 1% above HSBC’s prime lending rate, with a monthly minimum repayment of 5% of the amount drawn. The Company duly executed the overdraft facility letter on 26 January 2005.

Unfortunately, in June 2006, the Company experienced some serious bad debts when it failed to collect approximately \$5,000,000 from a Shenzhen developer. The combination of bad debts and a previous bad investment in early 2006 produced enormous difficulties for the Company. After prolonged negotiations, the Bank agreed to lend an additional \$1,000,000 to the Company. On 2 January 2008, the Company granted an “all-monies” floating charge over all of its assets, book debts and undertaking in favour of the Bank (“Debenture”). The Debenture secured (1) the

(See the next page for a continuation of Question 3)

previously unsecured loan of \$800,000, being the amount overdrawn on the current account; and (2) a new \$1,000,000 overdraft facility (at 1.75% above HSBC's prime lending rate) established for the Company at the same time as the execution of the Debenture.

Unfortunately, by 31 October 2008, the Company was unable to repay any part of its debts despite repeated written demands. According to a report prepared by the Bank's credit department, the Company's main assets are its book debts, which are estimated to be worth about \$1,100,000. Other pertinent information includes the following:

- The Company's balance sheets began to show a net liability from December 2007;
- The total amount due to unsecured creditors is estimated to be \$700,000. One of the unsecured creditors, Bravo Marble Company Limited ("Bravo"), obtained a summary judgment order against the Company in the amount of \$276,355.
- Desperately trying to help her husband, Susan Yim sold all her diamond rings and gold necklaces in July 2006 and granted an interest-free loan of \$500,000 to the Company. The loan is repayable on 1 July 2009. Susan Yim's sister, Mary Wong, sold her portfolio of shares in July 2006 and granted an interest-free loan of \$300,000 to the Company. This loan is repayable on 1 April 2009.
- On 24 December 2006, the Company made an early loan repayment of \$300,000 to Susan Yim. On 27 June 2008, the Company made an early loan repayment of \$250,000 to Mary Wong.
- The net value of the claims of preferential creditors against the Company is estimated to be \$280,000.

(See over the page for a continuation of Question 3)

- The table below shows recent movements of funds in the Company's overdraft ("OD") facility account with the Bank:

| Date | Deposit (\$) | Withdrawals (\$) | Balance (\$) |
|------------------|--------------|------------------|--------------|
| 3 January 2008 | | | 800,000 OD |
| 12 January 2008 | | 410,000 | 1,210,000 OD |
| 15 February 2008 | 285,000 | | 925,000 OD |
| 28 March 2008 | | 315,000 | 1,240,000 OD |
| 4 April 2008 | 337,000 | | 903,000 OD |
| 27 April 2008 | 178,000 | | 725,000 OD |
| 31 October 2008 | | 275,000 | 1,000,000 OD |

- Bravo issued a statutory demand yesterday threatening to wind up the Company unless the judgment debt (together with interest) is discharged in full within 21 days.

Question:

You are consulted by Mr. Richard Jones, senior manager of the Bank, to advise him of the various scenarios available to the Bank to recover its debt. Prepare a letter of advice to Mr. Jones analyzing the various options (including their advantages and disadvantages) available to the Bank with a view to recommending the most effective option to recover its debt. Your letter of advice should conclude with an outline of a strategic plan for Mr. Jones to consider.

Question 4 (25 marks)

Question 4(a)

- (i) Explain briefly why it is important that the issued share capital of a company is maintained. (2 marks)**
- (ii) Apart from restrictions against financial assistance under the Companies Ordinance, name 4 other means of protection provided under the same Ordinance for the maintenance of capital. (2 marks)**

Jade Limited (“Jade”) agrees to sell all the shares in its wholly-owned subsidiary, Pearl Limited (“Pearl”) to Diamond Limited (“Diamond”). Prior to the sale, Pearl transfers, with the knowledge and agreement of Diamond, certain business assets to Jade, which Jade is to retain and which will not form part of the sale to Diamond. The transfer of these business assets by Pearl is made at below market value.

- (iii) Giving reasons, explain whether the transfer by Pearl is caught by section 47A of the Companies Ordinance. (4 marks)**
- (iv) Are there any alternative strategies which Pearl or Jade could use to transfer the business assets? (2 marks)**

Question 4(b)

John, a colleague in your solicitors’ firm, has been asked by an old client to serve as an independent non-executive director (“INED”) of a company that is listed on the Hong Kong Stock Exchange. John loves the sound systems made by this company and has shares in the company. John is a property lawyer and does not know much about manufacturing. John is not sure if he can accept the appointment. If John accepts the appointment as an INED, he wants to know more about his responsibilities and liabilities. He has heard that the job of an INED is an onerous one and an INED has to serve on different committees.

Prepare a written memorandum of advice for John, dealing with the queries and issues he has raised. (15 marks)

Question 5 (25 marks)

You are consulted by Mr. Lo, who is a director and 40% shareholder of a Hong Kong incorporated company, Xanadu Limited (“Xanadu”), a furniture manufacturer. The remaining shares are held by Mr. Lo’s 3 brothers in equal shares. Mr. Lo tells you that Xanadu has for the past 6 months been experiencing financial difficulty. The company’s main asset is its premises from which it operates in Hong Kong. The value of the property, which is unencumbered, is \$5 million. It is not possible to sell the property as Xanadu’s business is operated from the premises and moving to new leased premises would result in the company incurring significant additional expenditure. Mr. Lo is concerned that Xanadu will, from the end of the current month, not be able to service all its debts, the vast majority of which are debts due to trade creditors. Mr. Lo has calculated that Xanadu will have cash of \$150,000 at the end of the month from which it will need to pay \$500,000 in debts to various trade and other creditors. Although Xanadu has various bank loans, none of them is secured. Xanadu’s total liabilities are \$3 million.

Mr. Lo does not believe Xanadu’s cash-flow will improve and estimates that the company will not have sufficient funds to pay its current liabilities for the foreseeable future. He tells you that he is physically and emotionally exhausted and just wants to cease operations as soon as possible although his fellow directors and shareholders want to continue operations for as long as possible without changing the way they operate the business. They are also averse to borrowing further funds from the bank.

Question:

Prepare a detailed letter of advice to Mr. Lo in which you explain the following:-

- (i) whether it is possible to liquidate Xanadu and, if so, what would be the appropriate method(s) of liquidation available to the board to consider? You should also highlight the main differences between the methods of liquidation you outline for Mr. Lo. (10 marks)**

(See the next page for a continuation of Question 5)

- (ii) the procedures (including time periods) that will need to be followed in order to appoint a liquidator by way of a creditors' voluntary liquidation. (8 marks)
- (iii) are there any potential liabilities Mr. Lo and others would be exposed to if the remaining directors refuse to wind-up Xanadu and it continues operating in its current financial predicament? (7 marks)

END OF TEST PAPER

**2009 OVERSEAS LAWYERS
QUALIFICATION EXAMINATION**

**HEAD III: COMMERCIAL
AND COMPANY LAW**

Friday, 6 November 2009



HEAD III: COMMERCIAL AND COMPANY LAW

TEST PAPER

6 November 2009

Instructions to Candidates :

- 1. The duration of the examination is 3 hours and 30 minutes.**
- 2. This is an open-book examination.**
- 3. There are FIVE questions in this paper.**
ANSWER ANY FOUR QUESTIONS ONLY.
- 4. IF YOU ATTEMPT MORE QUESTIONS THAN YOU HAVE BEEN INSTRUCTED TO ANSWER :**
 - (a) THE EXAMINERS WILL MARK ALL QUESTIONS THAT HAVE BEEN ATTEMPTED AND NOT DELETED; AND**
 - (b) IN COMPUTING YOUR FINAL MARK, THE EXAMINERS WILL COUNT THE MARKS FOR THE NUMBER OF QUESTIONS THAT YOU WERE INSTRUCTED TO ANSWER TAKING INTO ACCOUNT THE ANSWERS WITH THE LOWEST SCORES.**
- 5. Start each question on a separate page of your answer book.**
- 6. Each question has the value noted on the question paper. You are urged to apportion your time in accordance with the relative value of each question. No marks can be awarded to a question for which there is no attempted answer.**
- 7. An examiner will be present for the first 30 minutes of the examination. Any questions relating to the paper must be raised in that period. Questions raised after the first 30 minutes will not be entertained.**
- 8. Do not take either this question paper or any answer books with you when you leave the examination room.**

2009 Overseas Lawyers Qualification Examination

Head III: Commercial and Company Law

Question 1 (25 marks)

Question 1(a)

Your client, Henry, has for many years been employed by Winstons Ltd. (“Winstons”), a Hong Kong incorporated trading company. Henry was recently promoted and appointed a director of Winstons.

Because of the global financial crisis, Henry is becoming increasingly concerned about the rising inventory and rapid depletion of cash flow in Winstons. He has also learnt from colleagues in the company’s accounts department that more and more bills are not being settled on time. Many of the company’s creditors are grumbling and some have been sending the company strongly worded payment reminders.

Keith, the chairman of Winstons, is considering securing loan finance for the company as a means to help the company through this difficult time. He realizes that, at a minimum, the company will need to create a floating charge over some of the company’s goods to secure the loan. Keith asks Henry to approach a few of Winstons’ banks to ascertain whether they would be in principle willing to extend a loan to the company.

Question:

Henry is worried about his duties as a director and his personal liability to creditors of Winstons. He asks you to explain to him how one determines whether a company is insolvent and whether there are any circumstances under which he (Henry) could be personally liable to the company’s creditors before and following the possible insolvency of the company, particularly if one of the banks makes a loan, secured by a floating charge, to Winstons.

(15 marks)

(See the next page for a continuation of Question 1)

Question 1(b)

Peter is the chairman of a company, the shares of which are listed on the Hong Kong Stock Exchange. Peter is considering hiring Donald as an independent non-executive director (“INED”) of the company.

Donald is a retired solicitor and Peter thinks Donald’s legal experience will be an asset to the listed company.

Peter will be meeting Donald tomorrow morning and he asks you to write down in point form your suggestions for the contents of an INED’s letter of appointment, which he may then use to prompt him in his discussions with Donald.

Question:

Prepare a note in point form explaining what provisions Peter should include in the letter of appointment of an INED.

(10 marks)

Question 2 (25 marks)

Great Success Holding Limited (“GSHL”) owns the entire issued share capital of each of Strike Rich Limited (“SRL”) and Make Famous Limited (“MFL”). All are private Hong Kong incorporated companies. MFL manufactures microchips and SRL undertakes research and development pertaining to microchips and other related high tech electronic equipment. The ultimate shareholders of GSHL are Henry, Allan and Samuel, who hold 40%, 30% and 30% respectively of the issued share capital of GSHL. Both Allan and Samuel are not actively involved in the business of SRL and MFL and have, since the establishment of the companies, been happy to leave the day-to-day operations to Henry, who is both the Managing Director and Chief Executive Officer of all three companies. Henry is assisted by his sister, Jane, a qualified accountant. She is also a Director of all three companies and attends to the companies’ administration. The companies have achieved moderate success and have a good relationship with The Lion Bank (“Bank”), with which Henry is the main contact.

Without informing Allan and Samuel, Henry established and has been operating a separate company, New Supply Limited (“NSL”), which manufactures microchips. MFL is one of its main customers. Due to the recent expansion of NSL’s plant in China, NSL is on the verge of insolvency. In an attempt to save NSL, Henry arranged for MFL to place a HK\$3 million order to purchase a large consignment of microchips (at greatly inflated prices) from NSL. In order to pay the purchase consideration, Henry arranged for MFL to borrow HK\$3 million from the Bank. In addition to the loan agreement, which Henry signed on behalf of MFL, the Bank required MFL’s repayment obligations to be guaranteed by GSHL. Henry also signed the guarantee on behalf of GSHL and presented to the Bank an extract (certified by Henry to be a true copy of the original) of board resolutions of GSHL and MFL approving the loan and the guarantee, respectively.

(See the next page for a continuation of Question 2)

By the time that Allan and Samuel learnt about what has happened, Henry had disappeared with the proceeds of the loan. After being informed of the situation, the Bank demanded repayment of the loan in full, which it was entitled to do under the loan agreement. The Bank also informed Allan and Samuel that if it did not receive repayment within 3 days, it would enforce its rights under the guarantee.

Question:

Advise Allan and Samuel:

(a) whether The Lion Bank will succeed in its action against MFL on the loan agreement and against GSHL on the corporate guarantee; and

(20 marks)

(b) on any rights which MFL and GSHL may have against Henry.

(5 marks)

Question 3 (25 marks)

Question 3(a)

Amy and Brian are the directors of Eagle Transport Company Limited (“Eagle”), which is a limited liability company that was incorporated in Hong Kong in June 1996. Eagle has two shareholders, Catherine and David, who each owns 10,000 ordinary shares of HK\$10 each. Eagle adopted the Table A Articles of Association without any amendment. Eagle has only one objects clause in its memorandum which states:

“The company’s object is the carriage of cargo in trucks between such places as the company may from time to time determine and the doing of all such other things as are incidental to or expedient for the furtherance of the company’s objects.”

Two days ago, Eagle expressed its willingness to execute a guarantee to secure a loan to be advanced by Kowloon Bank to Stunning Beauty Salon, a partnership established in 2005 between Catherine and her good friend, Edith.

Question:

- (i) **Advise Kowloon Bank on the following:**
- (a) **the capacity of Eagle to provide the guarantee; (7 marks)**
 - (b) **whether anyone could seek to prevent Eagle from providing the guarantee. (2 marks)**
- (ii) **If the guarantee is given, could anyone associated with the company be held liable for allowing the company to provide the guarantee, and, if so, explain the nature of such liability and the legal basis upon which such liability would arise. (4 marks)**

(See the next page for a continuation of Question 3)

Question 3(b)

Novelty Company Limited (“Novelty”), which is a limited liability company that was incorporated in Hong Kong, was ordered to be wound up by the Hong Kong High Court on 21 October 2009.

Novelty’s current bank account with Kowloon Bank was, in recent years, always overdrawn. Between 12 August 2009 (when the winding up petition was presented) and 21 October 2009 (the date of the winding up order), Kowloon Bank allowed Novelty to continue to withdraw money from, and pay money into, the overdrawn account. During this period Novelty continued to incur losses due to unprofitable trading.

In addition, Novelty sold some of its inventory on 13 August 2009. On 14 August 2009, Novelty paid \$200,000 to one of its suppliers for goods previously supplied (but not paid for) to Novelty on 8 August 2009.

Question:

Advise the liquidator whether the validity of the above transactions and dealings may be challenged and, if so, on what grounds.

(12 marks)

Question 4 (25 marks)

ACBC Ltd (“ACBC”) was incorporated in Hong Kong in the 1990’ s and proved to be a very successful trading business. It was subsequently listed in Hong Kong and its policy of paying a high proportion of its profits as a dividend attracted a large number of investors and drove its share price to more than \$150. ACBC was however badly affected by the Asian financial crisis in 1997 and its earnings, profits and share price all fell significantly.

ACBC did not declare a dividend during the period 2005-07 but during this time attempted to stream-line and consolidate its business. Its share price, although rising slightly, remained very low (\$2.70 to \$3.50) but given a return to profit, a small dividend was declared in June 2008. However, as a consequence of the more recent global economic turmoil, its share price fell more than 30 per cent in the month up to 13 November 2008. In response to this event, its board of directors proposed to privatise ACBC by way of a scheme of arrangement under s 166 of the Companies Ordinance. Trading in its shares was suspended pending the announcement of the Scheme. The closing price of ACBC immediately before trading in its shares was suspended was \$1.20.

The Scheme document, which indicates a cancellation price of \$2.50, gives the reasons for the Scheme and the benefits of the proposal for the shareholders who would be bought out (the “Scheme Shareholders” who together hold 53% of ACBC’s shares) as being:

“The Proposal provides Scheme Shareholders with an opportunity to realise their investment in ACBC for cash during sustained uncertain market conditions and at a significant premium to the market price prevailing on the Last Trading Date.”

(See the next page for a continuation of Question 4)

The meeting to approve the Scheme was scheduled to take place on 1 October 2009. Just 3 days before that meeting it was reported in the press that 500,000 ACBC shares had been given to staff in LL Ltd., a former subsidiary of ACBC, to induce them to vote in favour of the privatisation plan. Two of ACBC's directors are also directors of LL Ltd. The meeting was held and 83% of the number of shares held by the Scheme Shareholders, present and voting, either in person or by proxy, at the meeting, were voted in favour of the Scheme.

ACBC then petitioned the court to approve the Scheme but at the hearing the Securities and Futures Commission ("SFC") applied to intervene. Leave to do so was granted by the court and the SFC was directed to file evidence within 21 days.

Question:

Ardy, a minority shareholder who voted against the Scheme, seeks your advice on the following:

- (a) **What is the role of the court in a scheme of arrangement process ?**
(5 marks)
- (b) **If the SFC finds that (i) the shares given to LL Ltd.'s staff were registered in the names of the staff concerned, (ii) proxy forms were registered in their individual names prior to 1 October 2009 and (iii) they all voted in favour of the Scheme, discuss the implications of these findings in terms of the hearing of the Scheme petition.**
(8 marks)
- (c) **Whether the minority shareholders, who, like himself, opposed the privatisation, would have been better protected if the privatisation had proceeded under either the takeover provisions or the buy-back provisions of The Codes on Takeovers and Mergers and Share Repurchases.**
(7 marks)
- (d) **Besides the SFC findings, are there any other apparent grounds on which the court may not sanction ACBC's proposed Scheme?**
(5 marks)

Question 5 (25 marks)

You are consulted by Mr. Lam, an executive director and the chairman of Sleazy Limited (“Sleazy”), a company which was listed on the Hong Kong Stock Exchange during 2007. Mr. Lam tells you that approximately two weeks ago on 22 October 2009, the company secretary of Sleazy was contacted by the Hong Kong Stock Exchange, which had noted a significant increase in the trading volume of the shares of Sleazy during previous afternoon. The Stock Exchange asked whether or not Sleazy was aware of any reasons for such a sudden and sharp increase.

The company secretary contacted all the directors of Sleazy, including Mr. Lam, and asked whether they were aware of any reasons for the significant increase in the trading volume of the shares the previous day. All directors responded that they were not aware of any reasons for the sudden increase in trading of Sleazy’s shares.

After conveying this information to the Stock Exchange, on 23 October, 2009 Sleazy filed an announcement, in standard form, with the Stock Exchange for publication on the Stock Exchange’s website. The announcement stated in part:

“The Board of directors of Sleazy Limited has noted the increase in trading volume of the shares of Sleazy Limited yesterday and wishes to state that it does not know of any reason for such increase.

Made by the order of the Board of Sleazy Limited, the directors of which individually and jointly accept responsibility for the accuracy of this statement.”

(See the next page for a continuation of Question 5)

Mr. Lam tells you that he now realizes that the reason for the sudden increase in the trading volume of Sleazy's shares on 22 October was the result of a bank, to which Mr. Lam had some 2 years ago pledged 300 million shares in Sleazy, selling those shares on the market to pay down Mr. Lam's loan due to the bank. In fact, Mr. Lam now recalls authorizing the bank approximately two months' earlier to sell as many of the pledged shares as necessary in order to discharge the loan. In reliance on Mr. Lam's authority, the Bank apparently sold 200 million shares on 22 October. However, Mr. Lam tells you that he had forgotten about this arrangement when the Stock Exchange enquired about the sudden increase in trading of Sleazy's shares on 22 October, 2009.

Mr. Lam understands that the Securities and Futures Commission ("SFC") is investigating the matter and he understands further that he and Sleazy are likely to be prosecuted for contravening Section 384(1) of the Securities and Futures Ordinance ("SFO"). Mr. Lam has an extract of Section 384(1) of the SFO, which provides:

"(1) Subject to subsection (2), a person commits an offence if-

- (a) He, in purported compliance with a requirement to provide information imposed by or under any of the relevant provisions, provides to a specified recipient any information which is false or misleading in a material particular; and*
- (b) He knows that, or is reckless as to whether, the information is false or misleading in a material particular."*

(See over the page for a continuation of Question 5)

Question:

- (a) Mr. Lam is very concerned about his potential criminal liability under the SFO. However, he understands that the announcement Sleazy filed with the Stock Exchange was not filed with or delivered to the SFC and so he doubts that the SFC will be able to secure a conviction against him or Sleazy under Section 384(1) of the SFO. Citing relevant case authority, prepare a detailed note explaining to Mr. Lam the possible basis upon which both he and the Company could be convicted for contravening Section 384(1) of the SFO. You should also discuss whether the fact that the announcement was not filed with the SFO is or could be relevant. You may ignore any obligations relating to the disclosure of interests to which Mr. Lam, Sleazy and/or the Bank may be subject under the SFO.

(20 marks)

- (b) Briefly explain the difference between an initial public offering (IPO) and a rights issue.

(5 marks)

END OF TEST PAPER

**2010 OVERSEAS LAWYERS
QUALIFICATION EXAMINATION**

**HEAD III: COMMERCIAL
AND COMPANY LAW**

Thursday, 4 November 2010



HEAD III: COMMERCIAL AND COMPANY LAW

TEST PAPER

4 November 2010

Instructions to Candidates:

- 1. The duration of the examination is 3 hours and 30 minutes.**
- 2. This is an open-book examination.**
- 3. There are FIVE questions in this paper.**
ANSWER ANY FOUR QUESTIONS ONLY.
- 4. IF YOU ATTEMPT MORE QUESTIONS THAN YOU HAVE BEEN INSTRUCTED TO ANSWER:**
 - (a) THE EXAMINERS WILL MARK ALL QUESTIONS THAT HAVE BEEN ATTEMPTED AND NOT DELETED; AND**
 - (b) IN COMPUTING YOUR FINAL MARK, THE EXAMINERS WILL COUNT THE MARKS FOR THE NUMBER OF QUESTIONS THAT YOU WERE INSTRUCTED TO ANSWER TAKING INTO ACCOUNT THE ANSWERS WITH THE LOWEST SCORES.**
- 5. Start each question on a separate page of your answer book.**
- 6. Each question has the value noted on the question paper. You are urged to apportion your time in accordance with the relative value of each question. No marks can be awarded to a question for which there is no attempted answer.**
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2010 Overseas Lawyers Qualification Examination

Head III: Commercial and Company Law

Question 1 (25 marks)

Mr. & Mrs. Chan are the only 2 directors of X Ltd. Together, they own 85 per cent of the issued share capital of X Ltd.

X Ltd. is engaged in selling high-end women's fashion through a number of retail stores in Central and Causeway Bay.

Mr. Lee was until 9 months ago a director of X Ltd. but he resigned to devote his time to other business ventures. Mr. Lee owns 15 per cent of the issued share capital of X Ltd.

Mr. Lee has become increasingly unhappy with the way Mr. & Mrs. Chan have been running X Ltd. His complaints include that Mr. & Mrs. Chan no longer consult with him and they have not called any directors' meetings for many months. Also, X Ltd. has started opening retail stores in Guangzhou, China and selling menswear through those outlets. Mr. Lee is convinced that these diversions will cause X Ltd. to lose money and he wants them to focus on the core business of high-end women's fashion.

Mr. Lee has also discovered that Mr. and Mrs. Chan have, for the last 6 months, been drawing \$100,000 from X Ltd.'s bank account. When Mr. Lee confronted the Chan's about this, they told him that these were loans advanced to them by X Ltd.

There is no written shareholders' agreement between the parties.

(See the next page for a continuation of Question 1)

Questions:

- (i) **Advise Mr. Lee whether he is legally justified in complaining that no directors' meetings have been convened for many months and also whether he has any legal entitlement to prevent X Ltd. from selling menswear in China?**

(15 marks)

- (ii) **Advise Mr. Lee whether he may challenge the propriety of the monthly loans or advances from X Ltd. to Mr. & Mrs. Chan. Would your advice differ if Mr. and Mrs. Chan are able to demonstrate that the monthly loans or advances are to reimburse the Chans for expenditure incurred in respect of X Ltd.'s business activities undertaken on behalf of X Ltd. in China?**

(10 marks)

[25 marks in total]

Question 2 (25 marks)

Great Fortune Ltd. (“**Company**”) is a private company that was incorporated in Hong Kong by Allan Au, Billy Bo and Chris Chu in 1995. The authorised share capital of the Company is \$3 million, comprising of 300,000 shares of \$10 each. All shares have been issued fully paid to the shareholders. Allan holds 51% of the issued shares and Billy and Chris hold 25% and 24% of the issued shares, respectively. The three shareholders are also the only directors of the Company.

Things proceeded well after the incorporation of the Company and the three shareholders enjoyed a harmonious working relationship for many years. However, disputes and divisions began arising among the three individuals from September 2009. Allan and Billy are eager to expand the Company’s business into the PRC market. Chris, on the other hand, believes that the Company should focus on its existing business in Hong Kong. If the Company decides to expand its business, it will be necessary to increase its share capital. The Memorandum of Association of the Company contains a set of objects clauses which restricts the Company’s capacity to expand its business. At a recent board meeting, Allan and Billy, outvoting Chris, resolved to convene an extraordinary general meeting (“**EGM**”) of the Company to pass resolutions to:

- (i) increase the share capital of the Company from \$3,000,000 to \$10,000,000 by the creation of 700,000 new shares of \$10 each;
- (ii) delete from the Memorandum of Association of the Company those objects clauses that restrict the Company from expanding its core business.

On 27 September, 2010, Chris received the notice (“**Notice**”) convening the EGM. It stated that the EGM would be held on 12 October, 2010.

(See the next page for a continuation of Question 2)

The Articles of the Company contain the following relevant provisions (Table A is not applicable):

“21. The Company may increase its share capital by such sum, to be divided into shares of such amount as may be determined by all members unanimously...

25. An annual general meeting and a meeting called for the passing of a special resolution shall be called on not less than 21 days' written notice, and a meeting of the Company, other than an annual general meeting or a meeting for the passing of a special resolution, shall be called on not less than 14 days' written notice.”

Questions:

(i) What steps (if any) may Chris take to prevent the proposed resolution to increase the share capital of the Company from being passed in light of Article 21 of the Company's Articles? You must fully explain your answer with reasons (including, where applicable, making reference to relevant legislative provisions and case authority).

(14 marks)

(ii) Giving reasons and making reference to relevant case authority and legislation, explain whether it would be possible for Chris successfully to challenge the holding of the EGM, having regard, in particular, to the Notice convening the EGM.

(11 marks)

[25 marks in total]

Question 3 (25 marks)

Question 3(a)

Andy, Brian and Candy studied computer science together at a university in Canada. After graduating, Candy returned to Hong Kong to take over her family's software business. Andy and Brian commenced their own language-learning software business in Hong Kong under the name "Lingua Frame". In June 2006, Candy agreed to invest funds into Andy's and Brian's business, and a company ("**JV Company**") was formed for this purpose. The JV Company was incorporated in October 2006 and adopted Table A Articles.

On 1 September, 2006, immediately before the incorporation of the JV Company, Andy, Brian and Candy entered into a joint venture agreement ("**Agreement**"). It was agreed, amongst others, that the JV Company would be formed for the purpose of developing and marketing software under the brand-name of "Lingua Frame". Andy, Brian and Candy would be shareholders of the JV Company, holding respectively 30%, 30% and 40% of the issued share capital of the JV Company. The JV Company's issued share capital would be \$1,000 divided into 100 shares of \$10 each.

Pursuant to the Agreement, Candy invested \$2 million into the JV Company by way of an interest-free shareholder's loan. The loan is repayable on demand. Andy and Brian each assigned the intellectual property rights subsisting in the "Lingua Frame" software to the JV Company. It was also a term of the Agreement that Andy, Brian and Candy would act as the JV Company's directors, and that a director could only be removed by way of a special resolution at a general meeting. It was further agreed that Andy and Brian would be chiefly responsible for the day-to-day management of the JV Company, whilst Candy would not play any role in the management of the JV Company, and would be consulted only when major decisions were to be made. The entire sum of Candy's loan was spent on purchasing equipment for the JV Company.

(See the next page for a continuation of Question 3)

To her great surprise, on 1 October, 2010, Candy received a notice issued by Andy and Brian advising her that they intended to remove her as a director of the JV Company pursuant to the Companies Ordinance. They invited Candy to attend a general meeting of the JV Company on 25 October, 2010. Despite Candy's protests at the meeting, Andy and Brian voted in favour of removing Candy as a director of the JV Company by passing an ordinary resolution to this effect.

Candy is very disappointed with both Andy and Brian. Not only does she no longer want to remain a shareholder of the JV Company but she wishes to recover her investment in the JV Company.

Question:

Prepare a letter of advice to Candy, explaining the various options she has to recover her investments - both the shareholder's loan and her equity investment - from the JV Company and/or any other parties.

(18 marks)

Question 3(b)

Candy discovers that in March 2008, Andy advanced by way of loan to the JV Company an amount of \$400,000. The terms of that loan provided that it would be repayable in one lump sum on 1 March, 2011. However, the JV Company repaid \$150,000 to Andy on 2 September, 2008, and a further payment of \$250,000 was made to Andy on 10 January, 2009.

Question:

Discuss the validity of the two repayments to Andy, assuming the JV Company is insolvent as at 31 October, 2010.

(7 marks)

[25 marks in total]

Question 4 (25 marks)

International Bafen Holdings Limited (“**IBHL**”), incorporated in the Cayman Islands, is proposing to list on the Stock Exchange of Hong Kong Ltd. (“**SEHK**”) pursuant to a Global Offering of 280 million shares. The number of public offer shares, subject to adjustment, will be 28 million and the offer price will not be more than \$3.09 (plus fees and levies). The nominal value of the shares will be \$0.10. IBHL’s core business is the manufacture of cotton textiles and the information prepared for inclusion in the prospectus states that growth, in terms of production, was at 10 percent per annum over the last 5 years. The prospectus also forecasts increased growth in each of the next ten years.

Local Company Limited (“**LCL**”), incorporated in Hong Kong, is also proposing to list on the SEHK. The number of public offer shares, subject to adjustment, will be 10 million and the offer price will not be more than \$4.49 (plus fees and levies). The nominal value of the shares will be \$0.10. LCL’s proposal to list is prompted by its invention of a new drug to fight influenza, which is a completely new class of antiviral. The way in which the drug takes effect involves a new concept, which can also be applied to other viruses. The researchers who developed the drug have prepared a detailed report on the drug and its impact on the influenza and other viruses. This report will be included in LCL’s prospectus.

Question:

Your advice is sought with respect to the following questions:

- (i) **IBHL and LCL each ask whether they are required to prepare a full prospectus and if so, which legal provisions will govern the content of such a prospectus and which authorities will vet the prospectuses.**

(6 marks)

(See the next page for a continuation of Question 4)

(ii) IBHL asks whether its growth forecasts may form the basis of any legal action if the forecasts prove to be untrue. You must also explain the requirements, if any, as to forecasts in the Listing Rules.

(5 marks)

(iii) LCL asks you, assuming that its listing is successful, if it is subsequently discovered that the new drug had not previously been tested on humans, only on mice, and is found to have fatal consequences for humans: (i) whether shareholders would be entitled to terminate their purchase contracts; (ii) who may be liable to compensate the shareholders under the Companies Ordinance and/or otherwise; and (iii) whether criminal actions may be brought against anyone and, if so, against whom.

(10 marks)

(iv) To what extent would your answer to (i) above be different if LCL was not proposing to list on the SEHK but to offer 1 million shares for sale to the public?

(4 marks)

[25 marks in total]

Question 5 (25 marks)

Question 5(a)

The in-house lawyer of ABC Bank Ltd. (“**Bank**”) seeks your advice. He explains that the Bank has been approached by a Hong Kong trading company, Golfmagic Ltd. (“**Golfmagic**”), to provide it with a loan facility of up to \$30 million. Golfmagic distributes high-end golf bags to retailers in the U.S.A. It has a number of major blue chip customers in the U.S.A. who have long-term contracts with Golfmagic. The in-house lawyer tells you that Golfmagic has a very good business but that it has no assets other than its customer receivables that it can or will offer up as security for the loan facility. The vast majority of the receivables are the pipeline of regular payments due to Golfmagic from its customers. These receivables are an important source of cash flow to Golfmagic. The Bank is apparently willing to provide the loan facility provided it is able to take a fixed charge over Golfmagic’s receivables.

Question:

Prepare a memorandum of advice to the in-house lawyer of the Bank explaining, with reasons and reference to case authority:

- (i) whether it is possible to create a fixed charge over Golfmagic’s receivables;**
(6 marks)

- (ii) what alternative(s) the Bank has to taking a fixed charge over the receivables and the practical issues the Bank will need to appreciate in connection with such other form(s) of security.**

(7 marks)

(See the next page for a continuation of Question 5)

Question 5(b)

You are consulted by John Uppgive, an executive director of Gameover Limited (“Gameover”), a Hong Kong incorporated company that has been in business for over 20 years. Mr. Uppgive tells you that at a directors’ meeting last week, all the directors, who are also the shareholders of Gameover, made known their desire to wind up Gameover, which has apparently suffered huge losses during the recent global financial crisis. Gameover has debts which far exceed its assets and none of the directors has the motivation to attempt to restore the company to its former profitable state.

Question:

Mr. Uppgive asks you to address a memorandum to the board of directors of Gameover:

- (i) **explaining, with reasons, what is the most appropriate way for the directors to wind up Gameover; and**

(4 marks)

- (ii) **outlining the precise steps and procedures that will need to be followed as part of the winding up process that you have identified in (i) above.**

(8 marks)

[25 marks in total]

END OF TEST PAPER