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Corporate reorganisation of China's listed companies: Winners and losers

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ABSTRACT
This article is the first empirical study investigating the corporate reorganisation of Chinese domestically-listed companies. Through examining these cases, it challenges the assertion made by most of these corporate reorganisation plans and by Chinese state-run media reports that creditors and general public shareholders were the major beneficiaries. Through an analysis of the data generated from all forth-three such cases, this articles reveals that: First, unsecured creditors could have, on average, received 61.37% more of their claims if the fundamental value distribution principle, the absolute priority norm, could have been complied with in these reorganisations; Second, if the general-public-shareholder-protection scheme issued by the China Supreme People's Court could be rigorously implemented, 85.37% of the shares relinquished by general public shareholders could have been avoided. These two groups were not the winners. Instead, this article argues that it was local governments and controlling shareholders who were the real winners.

Introduction

China's listed companies are probably the most widely studied in China and abroad, largely because of these companies' importance in China's economy, the world's second largest only after the USA at present.[1] Evidently, most existing studies focus on these companies' corporate governance[2] and

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[1]D Barboza, 'China Passes Japan as Second-Largest Economy' *New York Times* (16 August 2010) B1.
[2]E.g. see X Xu and Y Wang, 'Ownership Structure and Corporate Governance in Chinese Stock Companies' (1999) 10 *China Economic Review* 75; D Qi, W Wu and H Zhang, 'Shareholding Structure and Corporate Performance of Partially Privatized Firms: Evidence from Listed Chinese Companies' (2000) 8 *Pacific-Basin Finance Journal* 587; R Tomasic and N Andrews, 'Minority Shareholder Protection in China's Top 100 Listed Companies' (2007) 9 *Australian Journal of Asian Law* 88; G Chen, M Firth, Y Xin and L Xu, 'Control Transfers, Privatization, and Corporate Performance: Efficiency Gains in China's Listed Companies' (2008) 43 *Journal of Financial and Quantitative Analysis* 161; J Fan, T Wong and T Zhang, 'Politically Connected CEOs, Corporate Governance, and Post-IPO Performance of China's Newly Partially Privatized Firms' (2007) 84 *Journal of Financial Economics* 330.

securities regulation issues.[3] But one area of the research seems to remain untouched: the corporate reorganisations of China's listed companies, which are conducted under China's version of Chapter 11[4] enshrined in the newly-enacted PRC Enterprise Bankruptcy Law 2006 (the EBL 2006).[5] This article attempts to address this gap by investigating how the Chinese publicly-traded companies use the new corporate reorganisation law to restructure.

This article brings together data on all 43 of China's domestically-listed company reorganisations which occurred between 1 June 2006 (the time when the China's new reorganisation law came into force) and 31 December 2013 (the date of the most recent cases). In general, the data relied upon here were generated from company annual reports and general announcements, mostly obtained from the official websites of the Shanghai and Shenzhen Stock Exchange, China's only two domestic stock exchanges. In some cases, in the absence of Stock Exchange data, materials for this study had to be obtained from a commercial database, the China Stock Market & Accounting Research Database (CSMAR), which has an archive collection on China's stock markets and the financial statements of China's listed companies. Further, this article also draws upon facts derived from media reports, since most of these cases drew huge press attention because of their impacts on investors, nationwide and beyond.

Through investigating the main characteristics of China's listed company reorganisations, this article seeks to challenge the assertion made in most

[3]E.g. see NC Howson, 'Enforcement without Foundation: Insider Trading and China's Administrative Law Crisis' (2012) 60 *The American Journal of Comparative Law* 955; RH Huang, 'Private Enforcement of Securities Law in China: A Ten-Year Retrospective and Empirical Assessment' (2013) 61 *The American Journal of Comparative Law* 757; GJ Jiang, L Lu and D Zhu, 'The Information Content of Analyst Recommendation Revisions: Evidence from the Chinese Stock Market' (2014) 29 *Pacific-Basin Finance Journal* 1.

[4]Although Chapter 11 is widely quoted, some readers outside the bankruptcy law research might be confused of this definition. In fact, it means Chapter 11 of the USA Bankruptcy Code 1978, which is for bankruptcy reorganisations and has been borrowed by many other jurisdictions. See generally E Warren and JL Westbrook, *The Law of Debtors and Creditors* (6th edn, New York, Wolters Kluwer, 2009) esp ch 8: 'Chapter 11 Reorganization'.

[5]There are journal articles emerging in the past several years shedding light on China's listed company reorganisations. There are: E Lee, 'The Reorganization Process Under China's Corporate Bankruptcy System' (2011) 45 *International Lawyer* 939; Y Ren, 'The "Control Model" in Chinese Bankruptcy Reorganization Law and Practice' (2011) 85 *American Bankruptcy Law Journal* 177; Y Ren, 'Wealth Distribution in Chinese Bankruptcy Reorganization Law and Practice' (2011) 20 *International Insolvency Review* 91. Undoubtedly, Lee and Ren's studies have considerably contributed to China's corporate reorganisation law research. But, two immediate key weaknesses can be spotted. First, their arguments and analysis are based on incomplete data. For various reasons, only some high-profile cases hitting the media's headlines are collected in these articles, and a comprehensive data collection has not been carried out. Second and more importantly, these articles attempt to understand China's corporate reorganisation law and practice through only examining some of China's listed company reorganisations. The second weakness can be very acute, since, in spite of being bound by the same statute, the corporate reorganisations of China's listed companies are, as previously examined by the author, operated in a quite different way from those of non-listed, or ordinary, Chinese companies. Given that the majority of China's corporate reorganisation cases are for ordinary companies, their conclusions can be very contentious.

of these company reorganisation plans as well as in many Chinese state-run news agency reports that unsecured creditors and general public shareholders were the main beneficiaries of these reorganisations. On the contrary, this article uses the data to argue that the real winners in these cases were the Chinese local governments and controlling shareholders. This article also seeks to quantify the losses incurred by unsecured creditors and general public shareholders. More importantly, this article analyses the unique character of the Chinese political economy in which the governments at both local and central levels tend to pursue short-term economic and political gains at the expense of the rule of law.

This article proceeds in six sections. Section A provides a brief overview of China's domestic stock exchanges on which the companies discussed here are listed; this section also seeks to cast light on how China's stock exchange regulators monitor financially-troubled listed companies. Section B describes China's new corporate reorganisation procedure, which is at the heart of the EBL 2006 and has borrowed heavily from Chapter 11 of the USA Bankruptcy Code 1978. Section C discusses the operation of China's listed company reorganisations, and analyses the main features of these cases. Section D illustrates why unsecured creditors and general public shareholders are losers and seeks to quantify these losses. Section E seeks to explain why local governments and controlling shareholders end up being the real beneficiaries. Finally, the final section offers a conclusion and suggests some policy reforms.

Section A: China's stock exchanges and domestic listed companies

China once had well-functioning stock exchanges before. But after the China Communist Party took power in 1949, all stock exchanges were closed down because of the communist ideology. In the 1980s, however, China started its unprecedented economic reform, and one of major reforms was to rebuild its stock exchanges.

1. The Shanghai and Shenzhen stock exchanges and China's listed companies

China's current two stock exchanges, the Shanghai and Shenzhen Stock Exchanges, were established in 1990 and 1991 respectively.[6] In October

[6]See a brief history of China's stock market in recent centuries in Z Chen, 'Capital Freedom in China as Viewed from the Evolution of the Stock Market' (2013) 33 *Cato Journal* 587. See also an article describing the recent development of China's stock market: S Cheng, 'An Analysis of China's Stock Market in the First 10 Years' (2009) 12 *Review of Pacific Basin Financial Markets and Policies* 629.

1992, a ministry-level regulator, the China Securities Regulatory Commission,[7] was created to regulate the stock markets.[8]

The Chinese stock markets have developed rapidly in recent three decades. As shown in Figure 1, the number of listed companies increased from 14 in 1990 to 2,489 by the end of 2013,[9] and, according to the World Bank, the market value of China's domestic listed companies amounted to US$3.7 trillion in the year 2012, the second largest after the USA.[10]

It is noteworthy that one of the Chinese government's main objectives in opening these two stock exchanges is to use them to finance its state owned enterprises (SOEs).[11] Therefore, not surprisingly, the majority of listed companies in China are former SOEs.[12] Though there is a lack of official statistics on the exact proportion, the following figures can give a glimpse on the weight of SOEs on China's stock exchanges.

In 2003, for example, the available data show that 1,265 out of the then 1,300 listed companies (97%) were SOEs.[13] During the recent decade, a growing number of private companies were allowed to be listed, but in 2013 there were still about 80% of China's listed companies transformed from the old SOEs.[14] And, according to a senior Chinese national official in charge of SOEs,[15] by the end of 2012, the state still remained as the controlling shareholder in almost half of China's listed companies.[16]

Thus, it is not an exaggeration to say that China's two domestic stock exchanges are flooded with SOEs, which may cast a shadow to the corporate reorganisation of these companies, due to their connection with governments at various levels.

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[7]The China State Council, 'Introduction of the China Securities Regulatory Commission' <http://www.gov.cn/banshi/2006-11/28/content_455561.htm> accessed 29 September 2014.

[8]See a discussion of the role of the China Securities Regulatory Commission: Y Wei, 'The Development of the Securities Market and Regulation in China' (2005) 27 Loyola of Los Angeles International and Comparative Law Review 479, 493.

[9]The China Securities Regulatory Commission, Statistics as of June 2014 <http://www.csrc.gov.cn/pub/zjhpublic/G00306204/zqscyb/201407/t20140714_257716.htm> accessed 28 September 2014; The World Bank, Data: Listed Domestic Companies, Total <http://data.worldbank.org/indicator/CM.MKT.LDOM.NO> accessed 28 September 2014.

[10]The World Bank, Data, Market Capitalisation of Listed Companies <http://data.worldbank.org/indicator/CM.MKT.LCAP.CD> accessed 29 September 2014.

[11]See Cheng (n 6) 631.

[12]ibid, 597.

[13]D Chen, 'Developing a Stock Market without Institutions: The China Puzzle' (2013) 13 *Journal of Corporate Law Studies* 151, 155.

[14]MP Williams and DW Taylor, 'Corporate Propping through Related-Party Transactions' (2013) 55 *International Journal of Law and Management* 28, 30.

[15]S Huang, 'Strengthen the SOEs Reforms' (2014) 3 *Qiu Shi* 4.

[16]L Tian and S Estrin, 'Retained State Shareholding in Chinese PLCs: Does Government Ownership Always Reduce Corporate Value?' (2008) 36 *Journal of Comparative Economics* 74, 78 (discussing the state ownership in Chinese listed companies).

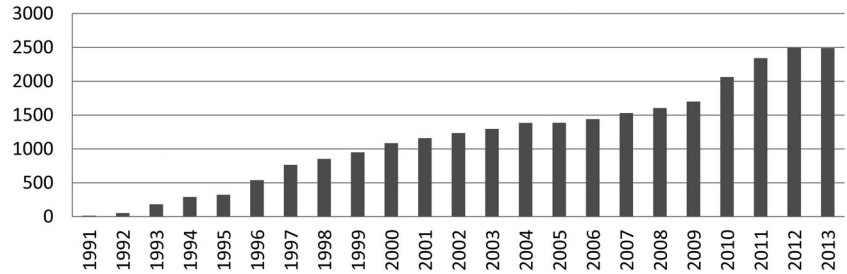

Figure 1. Number of listed companies in China (1991–2013). Source: World Bank.

2. Special treatment of troubled listed companies

Under the listing rules of the Shanghai and Shenzhen Stock Exchanges,[17] a listed company will be placed under Special Treatment (ST) if it reports, among other things, losses over a consecutive two-year period, which is to alert investors that the company may be delisted if it cannot make profits in the following fiscal year. Such a company is classified––and labelled––as an ST company, but the most substantial impact is that the company's daily share price fluctuation is limited to 5%.[18]

In theory, an ST company will be delisted if its financial performance cannot be improved as required afterwards. But as has been well documented,[19] it is very rare for the delisting to be carried out in China. In most cases, these ST companies are brought out of trouble and will continue to float after shaking off the ST status.

Generally, two sources of financing help these ST companies to survive distress. First, given that the majority of China's listed companies have parent SOEs,[20] many ST companies are rescued by their parents who can access cheap loans from China's state-run banks.[21] Second, Chinese governments can also subsidise and revive troubled ST companies for political and

[17]Ch 13 of The Shenzhen Stock Exchanges' Rules Governing Listing of Stock on Shenzhen Stock Exchange (1998) and Ch 13 of the Shanghai Stock Exchanges' Rules Government the Listing of Stocks on Shanghai Stock Exchange (1998) deal with the special treatment of listed companies: The Shanghai Stock Exchanges, 'Rules Governing the Listing of Stocks on Shanghai Stock Exchange' <https://biz.sse.com.cn/sseportal/en/pages/p1075/p1075_content/en_sserule20090408.pdf> accessed 30 September 2014; Shenzhen Stock Exchanges, 'Rules Governing the Listing of Stocks on Shenzhen Stock Exchange' <http://www.szse.cn/main/en/RulesandRegulations/SZSERules/GeneralRules/> accessed 30 September 2014.

[18]See Williams and Taylor (n 14) 30.

[19]See e.g. Chen (n 13) 163–4, and L Tan and J Wang, 'Modelling an Effective Corporate Governance System for China's Listed State-Owned Enterprises: Issues and Challenges in a Transitional Economy' (2007) 7 *Journal of Corporate Law Studies* 143, 155.

[20]Williams and Taylor (n 14) 30.

[21]See Y Cheung, L Ling and T Lu, 'Tunnelling and Propping Up: An Analysis of Related Party Transactions by Chinese Listed Companies' (2009) 17 *Pacific-Basin Finance Journal* 372, 383 (finding that ST companies are usually bailed out by their parent SOEs in China).

economic purposes. For instance, one research reveals that between 1993 and 2003, a 10-year period, the Chinese government subsidies amounted to 14% of the profits made by all China's listed companies as a whole.[22] More strikingly, a recent newspaper article reported that in 2012, one financial year, 94% of China's listed companies were receiving RMB107 billion of government subsidies (approximately US$17.2 billion) in total, on average each of them given some US$7.48 million.[23]

All companies discussed in this article were once ST labelled at some point. Before 2007, some of the ST companies might have resorted to the aforementioned two means to survive, but after China's new corporate reorganisation law came into effect in 2007, some began to use the new law to seek a formal corporate reorganisation solution.

Section B: China's new corporate reorganisation law

Before 2006, China had fragmented legislations on corporate bankruptcy, and there was no formal bankruptcy reorganisation law. In 1986, China enacted its first bankruptcy law, China's Enterprise Bankruptcy Law 1986 (For Trial Implementation) (the EBL 1986), which only applied for SOEs. For non-SOE enterprises, their bankruptcy had to resort to a bankruptcy chapter in China's Civil Procedure Law 1996.[24] In reality, both laws were inadequately implemented, since there were a meagre number of bankruptcy cases every year.[25] In the absence of a vigorous bankruptcy system, most failed enterprises in China exited the market by simply walking away. It is equally fair to say that without a rescue-oriented bankruptcy law some enterprises that only suffered from a sudden illiquidity crisis might have missed the chance to be rehabilitated, as a result of which the going-concern value of these companies was unnecessarily lost.[26]

In 2006, as part of the effort of reforming its commercial law, China promulgated the rescue-friendly EBL 2006 with the aim of establishing an effective corporate bankruptcy system and of helping push forward China's market economy reforms.[27]

The EBL 2006 has three main procedures to deal with companies in trouble––Chapters 8 on reorganisation, 9 on compromise and 10 on

[22]Chen (n 13) 163 (calculating the subsidies to China's listed companies from governments between 1993 and 2003).
[23]J Zhou, 'China's Stock Markets Distorted by Government Subsidies' *Guangming Daily* (24 April 2014) 2.
[24]X Zhang and CD Booth, 'Chinese Bankruptcy Law in an Emerging Market Economy: The Shenzhen Experience' (2001) 15 *Columbia Journal of Asian Law* 1.
[25]See S Li, 'Bankruptcy Law in China: Lessons of the Past Twelve Years' (2006) 2 *Harvard Asia Quarterly* 1.
[26]See W Wang, 'Adopting Corporate Rescue Regimes' (1998) 9 *Australian Journal of Corporate Law* 234.
[27]See CD Booth, 'The 2006 PRC Enterprise Bankruptcy Law: The Wait Is Finally Over' (2008) 20 *Singapore Academy of Law Journal* 275.

liquidation. Many have argued that the EBL 2006 is rescue-oriented;[28] indeed, a number of its pro-rescue mechanisms can be easily identified.

1. Encouraging the use of the corporate reorganisation procedure

First, the EBL 2006 Article 2 allows all companies in distress to file for reorganisation, whatever a small or large company.[29] This is different from neighbouring jurisdictions like Japan and Taiwan where only public companies are eligible for a formal reorganisation procedure.[30]

Second, under EBL 2006 Article 7, both the debtor and its creditors can directly file for reorganisation before a court. And even in the case of an ongoing liquidation procedure filed by a creditor, under EBL 2006 Article 70, the debtor or its shareholders could apply to convert it into a reorganisation procedure.

Third, and more importantly, to promote early rescues, the EBL 2006 Article 2 allows a company which is not bankrupt but is likely to be bankrupt to enter into the reorganisation procedure. This suggests that a Chinese company filing for reorganisation does not need to demonstrate the existence of insolvency, which in turn may considerably encourage early rescue filings.[31]

2. China's debtor-in-possession

Unlike in a liquidation or compromise procedure where it is always a court-appointed administrator in charge of the company's businesses and assets,[32] under EBL 2006 Article 73, the debtor in a reorganisation procedure can request for debtor-in-possession, and if approved by the court, the debtor itself can manage the company and reorganisation affairs afterwards.[33] It is the Chinese version of debtor-in-possession.

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[28]Some articles shed light on China's new rescue-centred Enterprise Bankruptcy Law. E.g. R Parry and H Zhang, 'China's New Corporate Rescue Laws: Perspectives and Principles' (2008) 8 *Journal of Corporate Law Studies* 113; Booth, (n 27); Lee (n 5) 939; Ren, 'The Control Model' (n 5) 177.

[29]Z Jia, 'Issues of China's Enterprise Bankruptcy Bill' (2006) 7 *The China People's Congress Gazette* 575, 577 (noting that the new reorganisation law is open to businesses having the independent legal status).

[30]See T Eisenberg and S Tagashira, 'Should We Abolish Chapter 11? The Evidence from Japan' (1994) 23 *the Journal of Legal Studies* 111; JK Winn, 'Creditors' Rights in Taiwan: A Comparison of Corporate Reorganization Law in the United States and the Republic of China' (1988) *13 North Carolina Journal of International Law and Commercial Regulation* 409.

[31]H Zou, 'China's Corporate Rehabilitation System: Theories and Application' (2007) 25 *Journal of China University of Political Science and Law* 48, 53 (noting that a company which is likely to be bankrupt can file for reorganisation under the EBL 2006); S Li, 'Drafting of New Bankruptcy Law and Credit Culture and Credit System of China' (2005) 1 *The Jurist* 12, 15 (arguing that a company likely to be bankrupt can file for reorganisation under the new bankruptcy law); G McCormack, *Corporate Rescue Law: An Anglo-American Perspective* (Cheltenham, Edward Elgar, 2008) 123 (noting that a company filing for reorganisation in the USA is not required to be insolvent).

[32]EBL 2006 Article 13.

[33]See generally M Falke, 'China's New Law on Enterprise Bankruptcy: A Story with a Happy End?' (2007) 16 *International Insolvency Review* 63.

But China's debtor-in-possession is somewhat different from its counterpart under the US Chapter 11 at least on two aspects.[34] First, China's debtor-in-possession is not automatic or straightforward,[35] since it must be requested by the debtor and approved by the court after a reorganisation procedure has already been commenced. Therefore, literally, if there is no request, or the request is rejected, it is still the court-appointed administrator who stays in control. It is a conditional debtor-in-possession. Second, China's debtor-in-possession, if granted, should be supervised by the previously-court-appointed administrator. Interestingly, such a structure is similar to what appears in the German corporate reorganisation law.[36] Inspired by the German bankruptcy law, China's lawmakers expect to use the supervision of the administrator to curb the potential abuse of debtor-in-possession.[37]

3. Creditor protection in reorganisation plans

Under EBL 2006 Article 79, a reorganisation plan must be proposed within six months, and a three-month extension can be granted by court. To vote on a reorganisation plan, creditors are mandatorily divided into four classes: the secured, employee, tax and unsecured creditor class.[38] The plan is accepted if it has been voted for by both a simple majority in number of creditors and a two-third majority in claims in each class.[39]

To a secured creditor, under EBL 2006 Article 87, its debt will be fully honoured within the value of encumbered assets. Employee claims are given the priority over tax ones after which the residual value will go to unsecured creditors.

To make sure that creditors, especially unsecured creditors, are protected, the EBL 2006 Article 87 requires that the creditor-best-interest test, according to which creditors must be paid not less than in a hypothetical liquidation, must be passed if a non-consensual reorganisation plan seeks the court approval.[40] At the same time, the absolute priority principle, which allows

[34]See a comprehensive discussion of the US Chapter 11 debtor-in-possession in Warren and Lawrence (n 4, esp ch 8.

[35]Ren, 'The Control Model' (n 5) 178–9 (discussing China's version of the debtor-in-possession).

[36]K Kamlah, 'The New German Insolvency Act: Insolvenzordnung' (1996) 70 *American Bankruptcy Law Journal* 417, 432 (noting that in Germany the debtor-in-possession must be monitored by the administrator).

[37]W Wang, 'The Draft of the New Bankruptcy Law and Bankruptcy Corporate Governance' (2005) 2 *The Jurists* 5, 7 (noting that why China's debtor-in-possession is designed to be supervised by an administrator).

[38]EBL 2006 art 82.

[39]EBL 2006 art 84.

[40]X Wang, 'Improving the Corporate Reorganization Regime' (2010) 10 *Journal of Kunming University of Science and Technology* 28, 33 (noting that the creditor-best-interest test must be passed when a non-consensual reorganisation plan seeks court approval, and arguing this test should also be used in a consensual plan submitted for approval).

creditors to be paid before shareholders, must be applied for if a non-consensual reorganisation plan is submitted for court approval.[41]

It can be argued that there are too many similarities between China's new corporate reorganisation law and Chapter 11 of the US Bankruptcy Code 1978, since China heavily borrowed Chapter 11 when making its own corporate rescue law.[42] But the great challenge to China is how to implement the new law in practice.

Section C: corporate reorganisation of China's listed companies

Shortly after the EBL 2006 came into force on 1 June 2007, some listed companies in China began to use this law for restructuring. Before reporting the main characters of these cases, two basic criteria used to selecting them should be clarified.

First, this article only focuses on the reorganisation of China's companies listed on either the Shanghai or Shenzhen Stock Exchange, which means the reorganisation of China's companies listed abroad, in Hong Kong, Singapore and the USA, are not included,[43] since the latter is processed in a somewhat different way. By this benchmark, for instance, the reorganisation of Zhejiang Glass Limited,[44] a Chinese company listed on the Hong Kong Stock Exchange, is not included in this study.

Second, this article investigates the reorganisation of companies which are still listed at the time of reorganisation. This means that the reorganisation of companies which have been delisted before the commencement of the reorganisation procedure is excluded. Take one case for example: the reorganisation of Shenyang Tehuan Limited, which took place in 2011, is excluded, since the company had been delisted from the Shenzhen Stock Exchange since 2004. In fact, up until now, there are only two such cases after the EBL 2006 came into force.[45]

By these two criteria, this article identifies the reorganisations of 43 of China's domestically listed companies, which were accepted by the Chinese courts between 1 June 2007 and 31 December 2013, as demonstrated in Table 1.

Twenty-five of these companies are listed on the Shenzhen Stock Exchange and 18 on the Shanghai Stock Exchange, as demonstrated in Figure 2. Their main characters can be summarised as follows.

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[41] Lee (n 5) 969 (noting that the absolute priority principle must be conformed to in a non-consensual reorganisation plan under EBL 2006 art 87).

[42] See Parry and Zhang (n 28) 113.

[43] See generally China's companies listed abroad at M Humphery-Jenner, 'The Governance and Performance of Chinese Companies Listed Abroad: An Analysis of China's Merits Review Approach to Overseas Listings' (2012) 12 *Journal of Corporate Law Studies* 333–65.

[44] See D Ren, 'Listing Pioneer Zhejiang Glass Faces Bankruptcy' *South China Morning Post* (18 April 2011) <http://www.scmp.com/article/965424/listing-pioneer-zhejiang-glass-faces-bankruptcy> accessed 16 October 2014.

[45] One is the Shenyang Tehuan Ltd, and the second is Liaoning Zhongliao International Ltd.

Table 1. China's listed company reorganisations (Accepted between 1 June 2007 and 31 December 2013).

Company	Court	Accepted on	Listed at
Chaohua	The 2nd Intermediate Court, Chongqing	16 November 2007	Shenzhen
Xingmei	The 3rd Intermediate Court, Chongqing	11 March 2008	Shenzhen
Xiaxing	Xiamen Intermediate Court, Fujian	15 September 2009	Shanghai
Taibai	Jiayuguan Intermediate Court, Gansu	30 November 2011	Shenzhen
Zhonghua	Shenzhen Intermediate Court, Guangdong	12 October 2012	Shenzhen
Chuangzhi	Shenzhen Intermediate Court, Guangdong	12 August 2010	Shenzhen
Hualong	Yangjiang Intermediate Court, Guangdong	10 March 2008	Shanghai
Kejian	Shenzhen Intermediate Court, Guangdong	8 October 2011	Shenzhen
Taifeng	Shenzhen Intermediate Court, Guangdong	10 November 2009	Shenzhen
Shenrun	Shenzhen Intermediate Court, Guangdong	14 April 2010	Shenzhen
Xingtai	Panyu Lower Court, Guangzhou, Guangdong	11 March 2009	Shanghai
Beishen	Beihai Intermediate Court, Guangxi	27 November 2008	Shanghai
Baoshuo	Baoding Intermediate Court, Hebei	3 January 2008	Shanghai
Chuanghua	Chuangzhou Intermediate Court, Hebei	16 November 2007	Shanghai
Dixian	Chende Intermediate Court, Hebei	10 November 2008	Shenzhen
Beiya	Ha'erbin Intermediate Court, Heilongjiang	28 January 2008	Shanghai
Guangming	Yichun Intermediate Court, Heilongjiang	9 November 2009	Shenzhen
Xin'an	Jiaozuo Intermediate Court, Henan	7 November 2008	Shenzhen
Tianfa	Jinzhou Intermediate Court, Hubei	13 August 2007	Shenzhen
Tianyi	Jinzhou Intermediate Court, Hubei	12 August 2007	Shanghai
Deheng	Liaoyuan Intermediate Court, Jilin	13 April 2010	Shanghai
Lanbao	Changchun Intermediate Court, Jilin	16 November 2007	Shenzhen
Shijian	Yanbian Intermediate Court, Jilin	30 December 2011	Shanghai
Danhua	Dandong Intermediate Court, Liaoning	13 May 2009	Shenzhen
Jingchen	Jinzhou Intermediate Court, Liaoning	22 May 2012	Shenzhen
Jinhua	Huludao Intermediate Court, Liaoning	19 March 2010	Shenzhen
Guangxia	Yinchuan Intermediate Court, Ningxia	16 September 2010	Shenzhen
Changling	Baoji Intermediate Court, Shaanxi	14 May 2008	Shenzhen
Pianzhuan	Xianyan Intermediate Court, Shaanxi	25 November 2009	Shenzhen
Qingling	Tongchuan Intermediate Court, Shaanxi	23 August 2009	Shanghai
Jiufa	Yantai Intermediate Court, Shandong	28 September 2008	Shanghai
Hailong	Weifang Intermediate Court, Shandong	18 May 2012	Shenzhen
Hongshen	Xi'an Intermediate Court, Shaanxi	27 October 2011	Shanghai
Huayuan	The Second Intermediate Court, Shanghai	27 September 2008	Shanghai
Yuanfa	The second intermediate court, Shanghai	30 August 2010	Shanghai
Fangxiang	Neijiang Intermediate Court, Sichuan	7 December 2010	Shenzhen
Jingding	Leshan Intermediate Court, Sichuan	23 September 2011	Shanghai
Haina	Hangzhou Intermediate Court, Zhejiang	14 September 2007	Shenzhen
Changhang	Wuhan Intermediate Court, Hubei	26 November 2013	Shenzhen
Zhongda	Wuxi Intermediate Court, Jiangsu	26 April 2013	Shanghai
Xingye	Huludao Intermediate Court, Liaoning	31 January 2013	Shenzhen
Xianchen	Xining Intermediate Court, Qinghai	18 June 2013	Shanghai
Zhongji	The 6th Intermediate Court, Xinjiang Army	19 October 2012	Shenzhen

Source: author's data collection

Figure 2. Reorganisations of Chinese listed companies (2007–2013). Source: author's data collection.

1. Bureaucracy in commencing a listed company reorganisation procedure in China

Under EBL 2006 Article 2, in theory, it is quite simple and straightforward to commence a reorganisation procedure: both the company and its creditors can file for reorganisation before a court if the company is bankrupt or is likely to be bankrupt, as noted before, and the court is liable to accept or reject the filing within 15 days; in the event of rejection, under the EBL 2006 Article 12, an appeal can be made to a higher court. But in reality meeting these terms is not enough to commence a listed company reorganisation procedure, and the following extra requirements must be met.

First, a local court must get the permission of the China Supreme People's Court before accepting a listed company reorganisation filing. Such a restriction only applies for listed companies. Literally, this restriction cannot be found in the EBL 2006.

To identify where this restriction is from, this article managed to find a conference speech made on 30 May 2007 by the then deputy president of the China Supreme People's Court, Mr Xi Xiaoming. Mr Xi stated that local courts must obtain the Supreme Court's permission before accepting a listed company reorganisation filing.[46] Five years later, in 2012, the Supreme Court reiterated this requirement in a judicial notice.[47] But, up until now, there has not been any justification publicly disclosed by the Court.

Little is known about the real intention of the Supreme Court to setting up such a restriction. It is a very high barrier, which may deter reorganisation filings, thereby against the pro-rescue spirits of the EBL 2006.[48] In fact, under EBL 2006 Article 10, whether to accept a reorganisation petition is fully at the discretion of a local court, and the law clearly authorises the local court to assess the merits of petitions and to decide whether the reorganisation procedure can be commenced, regardless of a petition for a listed or a private company.

But in reality, China's local courts are unable––or unwilling––to cite EBL 2006 Article 10 to defend their statutory discretion,[49] and therefore have to

[46]X Xi, 'Enhancing the Roles of Courts in Pursuit of Socialist Harmony' (the National Court Conference on Civil Disputes Adjudication, 30 May 2007, Nanjing, China) <http://wenku.baidu.com/view/de1c054c852458fb770b56ce.html> accessed 17 October 2014.

[47]The China Supreme People's Court, *The Minutes of the Seminar on Listed Company Reorganizations* <http://www.csrc.gov.cn/pub/newsite/flb/flfg/sfjs_8249/201312/t20131205_239353.htm> accessed 19 December 2013.

[48]See generally BL Liebman, 'A Populist Threat to China's Courts?' in MYK Woo and ME Gallagher (eds), *Chinese Justice: Civil Dispute Resolution in Contemporary China* (Cambridge University Press, 2011, 269) .

[49]See T Gong, 'Dependent Judiciary and Unaccountable Judges: Judicial Corruption in Contemporary China' (2004) 4 *The China Review* 33 (arguing the lack of judicial accountability in China's court system); see also L Li, 'The 'Production' of Corruption in China's Courts: Judicial Politics and Decision Making in a One-Party State' (2012) 37 *Law & Social Inquiry* 848 (discussing the institutionalised judicial corruption in China).

seek the permission from the Supreme Court.[50] One of the negative consequences is that it takes too long for these filings to go through the acceptance procedure.

Second, supporting statements in writing from both a local government and the China Securities Regulatory Commission should be presented to the court before the filing can be accepted.[51] Again, this requirement also seems to be unlawful, since its legal basis could not be found on any statutes or official documents. But this unwritten and court-imposed rule matters in reality.

Courts may need support from local governments for a number of reasons. At first, the court needs the local government to tackle potential social stability troubles. More bluntly, this is because the local government is able to deploy police forces, in case of protests caused by disgruntled creditors, employees or individual shareholders in large numbers whose interests may be significantly affected in the reorganisation procedure.[52] In nearly all reorganisation cases in China, there is heavy riot police presence during the creditors' meetings. This reflects the anxiety of China's authorities over the vulnerability of the Chinese society internally.[53]

Also, for the court, a written supporting statement from the local government can serve as a kind of political guarantee, which could shield the court and especially the judges from being negatively assessed by the Communist Party local committee, in the event of a protest launched by affected parties. Social stability appears to be the top worry of China's courts. Judges will be disciplined or at least negatively assessed if a case-related protest happens.[54] This is also why China's courts hesitate to handle cases which involve individuals in large numbers. Without the special support of the local government, the court would be too nervous to accept a listed company reorganisation filing, which always involves a large number of individuals who are employees, shareholders or creditors.[55]

Moreover, for the court, the local government's involvement can make the reorganisation procedure run more efficiently. In particular, the local government can persuade or pressure banks, most of them state-owned and large

[50]See Howson (n 3) 955 (arguing that some government agencies in China tend to use internal notices to replace statutes when regulatory actions are taken).

[51]The Shenzhen Intermediate People's Court, 'The Survey on China's Listed Company Reorganizations' *The People's Court Daily* (3 March 2011) 8.

[52]See CF Minzner, 'Xinfang: An Alternative to Formal Chinese Legal Institutions' (2006) 42 *Stanford Journal of International Law* 103 (discussing Chinese courts' worries about protests launched by litigants).

[53]See generally SL Shirk, *China: Fragile Superpower* (Oxford University Press, 2008).

[54]See CF Minzner, 'Riots and Cover-ups: Counterproductive Control of Local Agents in China' (2009–10) 31 *University of Pennsylvania Journal of International Law* 53 (noting that judges in China are assessed by local governments and the results will determine the former's promotion).

[55]See NC Howson, 'Judicial Independence and the Company Law in the Shanghai Courts in R Peerenboom (ed), *Judicial Independence in China* (Cambridge University Press 2010, 147) (noting that 'even in the context of corporate law application, Chinese courts may be seen acting in the service of state or party policy and in contravention of the law': 148).

creditors, to make concessions and to vote in favour of the government-backed reorganisation plan; thereby the reorganisation procedure can be concluded more quickly.

In many cases, it was quite common for the local government to use the China Banking Regulatory Commission local office to establish an interim bank committee comprising bank creditors. This committee will lead all banks involved to take a coordinated action especially in voting on the reorganisation plan. Securing the local government support largely means having secured the support from large creditors. This can make the court more comfortable in conducting the reorganisation procedure.[56]

Turning to the support of the China Securities Regulatory Commission, because this Commission has, through the two Stock Exchanges, a final say as to whether a listed company reorganisation proposal or plan meets the listing requirements,[57] the courts will have intense communications with the Commission to make sure that the approved reorganisation plans meet the regulatory requirements as well as to avoid embarrassment in case the court-approved reorganisation plans are not recognised by the Commission.

Soliciting the support from these three major public authorities can be quite time-consuming. It should be noted that all the permissions must be substantially requested by the applicant who files for reorganisation rather than by the court. This begs the question which party could afford to do so.

2. Applicants of China's listed company reorganisations

Under EBL 2006 Articles 7 and 70, as noted before, a reorganisation procedure can be entered into through two different routes. Out of all 43 cases, it is found that there were six cases (14%) converted from existing liquidation procedures, three of them requested by the debtor and the other three by the shareholder. The remaining 37 reorganisations (86%) were directly-filed. Out of these 37 directly-filed, 36 of them (97%) were filed by the creditors. Bearing in mind that the six conversion cases were also originally filed by the creditors, hence, in total, as illustrated in Figure 3, 43 out of these 43 reorganisation cases (98%) were initiated by the creditors.

Is this a sign that creditors in China had the initiative in using the new corporate reorganisation law for a rescue outcome? If so, it can be a strong indicator that creditors would be well protected in the subsequent reorganisation

[56]Zhang and Booth (n 24) 11–12 (noting that judges need extra government support in handling corporate bankruptcy cases in China).

[57]See generally G Chen and others, 'Is China's Securities Regulatory Agency a Toothless Tiger? Evidence from Enforcement Actions' (2005) 24 *Journal of Accounting and Public Policy* 451 (describing the relation between China's two stock exchanges and the China Securities Regulatory Commission).

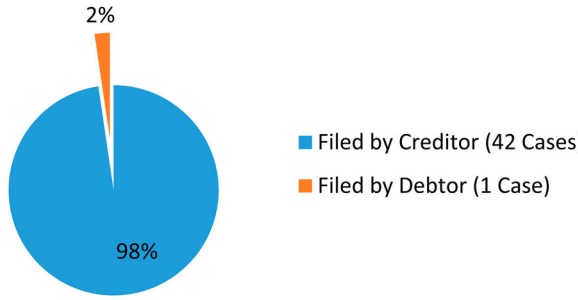

Figure 3. Applicants of China's listed company reorganisations (2007–2013). Source: author's data collection.

procedures. Since this question is firmly related with one of this article's arguments on creditor protection, a closer inspection is needed. Who were these filing creditors?

In spite of the difficulties in unveiling the status of these creditor applicants, the author managed to find that most of them were the related or inside parties. By delving in the debtors' annual reports and the relevant newspaper coverage, the author identifies that at the very least 22 of these 37 filing creditors (61%) were the debtors' subsidiaries, shareholders or connected parties. They were not ordinary creditors. For instance, in the reorganisation case of Xiaxing Electronics Limited, according to the company's disclosed reorganisation materials,[58] it seems that there was no connection between the company and the filing creditor, Xiamen Huoju Group Limited. However, after trawling through the archive of the company's annual reports, it soon transpired that Huoju was in fact one of the company's main shareholders.[59]

To the rest of the filing creditors, their status remains missing. But in view of the barriers in commencing a listed company reorganisation procedure, this article ventures to speculate that most of them were likely to be insiders or connected parties; namely, to ordinary creditors, it appears to be insurmountable to pushing a defaulting listed company into reorganisation in China. This may cast a shadow on creditor protection.

Why did these reorganisations prefer to use the creditors' name to file? There are a number of reasons.

First, filing under the name of a creditor can avoid convening an extraordinary general meeting of shareholders. Under China's Company Law 2005 Article 38, a special resolution must be passed by an extraordinary general meeting of shareholders if the debtor company voluntarily files for

[58]The Administrator of Xiaxing Electronics Ltd, 'The Reorganization Plan of Xiaxing Electronics Limited' <http://www.cninfo.com.cn/> accessed 19 October 2014.
[59]Xiaxing Electronics Ltd, *The 2010 Annual Report* <http://www.cninfo.com.cn/> accessed 19 October 2014.

reorganisation. Given that a listed company usually has tens of thousands of general public shareholders, convening a meeting at such a scale takes time and incurs extra costs (though in practice a small number of them will attend such a meeting). More importantly, the company must face the uncertainties regarding the voting outcome if the meeting is held.

Before this burden, if the debtor can find an alternative to circumvent this, and if there is a creditor that the company can influence or control, undoubtedly the company will choose the creditor to file. The alternative is an easier way to avoid costs as well as uncertainties.

Meanwhile, using a creditor to file for reorganisation can also avoid one of the filing hurdles exclusively imposed on debtors. Under EBL 2006 Article 8, if reorganisation is filed for by the debtor, the debtor is liable to prepare and present a plan explaining how to deal with employee layoffs, potential or real. The court assesses whether the layoff plan is appropriate and will then decide whether to accept or reject the filing. But such an employment protection plan is not required if the reorganisation petition is lodged by a creditor. Hence, for both costs and convenience considerations, the debtor will do whatever it can to find a friendly creditor to give a hand.

Moreover, and more subtly, filing for reorganisation under the name of a creditor can also alleviate the accusation of bankruptcy abuse. This could only be understood in the context of China's bankruptcy system. Although corporate bankruptcy in China has a very short history,[60] it has long been accused of being abused by debtors, especially former SOEs backed by China's local governments.[61] If a bankruptcy procedure is initiated by the debtor, creditors tend to be more sceptical about potential abuse. In other words, a voluntary bankruptcy filing by the debtor is likely to invite accusation. In response, the debtor will try to use a creditor to file, since this can create an impression that the debtor is forced to enter into a bankruptcy procedure rather than proactively seeks to use bankruptcy. Clearly, to this end, the availability of a creditor who the debtor can control would be fit for purpose.

Thus, using a creditor to file for reorganisation does bring the procedural convenience for the debtor, but it may do little to the effectiveness or achievability of reorganisations.

3. Local governments in control of most listed company reorganisations

Under EBL 2006 Article 13, if a reorganisation filing is accepted, an administrator will be simultaneously appointed by the court to replace the debtor and to

[60] See an introduction to the history of China's enterprise bankruptcy law in RW Harmer, 'Insolvency Law and Reform in the People's Republic of China' (1995) 64 *Fordham Law Review* 2563.

[61] See Q Bao, 'Shanghai Has No Bankruptcy Abuse Case' *People's Daily* 22 January 2002, 1 (noting the widespread bankruptcy abuses in China, especially the bankruptcy of SOEs backed by conniving local governments).

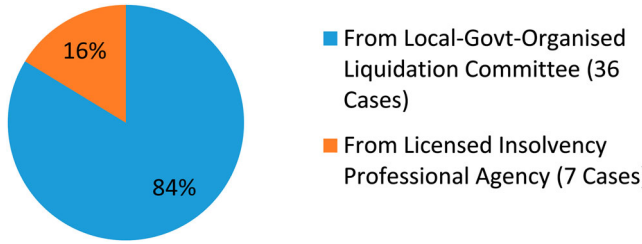

Figure 4. Administrator appointments in China's listed company reorganisations (2007–2013). Source: author's data collection.

take control of the company's businesses and assets. As to administrator candidacy, under Article 24, there are two options: a local-government-organised liquidation committee or a licensed insolvency professional agency, including law or accounting firms.

Regarding the administrator appointments in these 43 cases (as shown in Figure 4), it is found that 36 of them (84%) saw the appointment made from the local-government-organised liquidation committee, and the remaining seven appointments (16%) from the licensed professional agencies. This suggests that the local governments dominated most of these administrator appointments.

As for the composition of the local-government-organised committees, first, without doubt, most individual members were officials from different local government departments. A typical case is the reorganisation of Guangxi Beisheng Pharmaceutical Limited in which 11 out of the 13 committee members were the officials from the nine local government departments, including the legal, auditing, labour, economy, infrastructure, land, business and banking authority.[62]

Second, all these committees were chaired by a local senior official, such as a deputy mayor of the city. For example, in the aforementioned Beisheng case, it was the deputy mayor, Mr Wen Zhen, of the local Baihai City Government, Guangxi Province who headed the liquidation committee. In the case where there was state equity, usually the director or deputy-director of the local state-assets-management authority would chair the committee. In the reorganisation of Xianyan Pianzhuan Limited, for example, it was Mr Wu Lishen, the director of the local Xianyan City State-Assets-Management Authority, who presided at the committee.[63]

[62]The Administrator of Guangxi Beisheng Pharmaceutical Ltd, 'The Public Notice of Being Filed for Reorganization' <http://app.finance.ifeng.com/data/stock/ggzw.php?id=13456333&symbol=600556> accessed 29 August 2013.

[63]Xianyan Pianzhuan Ltd, General Announcement on Reorganization (2009-040) <www.cninfo.com.cn> accessed 1 November 2014.

Third, given that reorganisation always involves legal issues, most of these committees hired lawyers as committee members for advice.[64] For example, in the reorganisation of Jin Hua Group Chloro-Alkali Limited, Mr Yanling Liu, a lawyer from the Beijing-based law firm King&Wood was hired as one of the committee members. [65]

In the rest of these committees where lawyers were not given the membership, it could be easily identified that lawyers were instead hired as legal counsels rather than as committee members in aid of reorganisation affairs. For example, in the reorganisation of Xinjiang Chalkis Limited, the lawyers from a Guangzhou-based law firm were contracted by the liquidation committee to advise the case, although they were not formally appointed as the liquidation committee members.[66] Lawyer service was always needed, though they participated in different ways.

For courts, however, appointing a local-government-organised liquidation committee as the listed company reorganisation administrator remains very controversial in China.

On the one hand, admittedly, EBL 2006 Article 24 does allow the court to appoint such a committee as the administrator. But, as argued by two prominent Chinese bankruptcy scholars, Professors Li Shuguang[67] and Wang Xinxin,[68] who were also the draftsmen of the EBL 2006, the real intention of Article 24 is to reserve such committees only for the bankruptcy of state owned enterprises (SOEs); in other words, for the reorganisation case of a non-SOE company, the court must appoint a licensed professional agency as the administrator. Although most listed companies in China are former SOEs, strictly speaking, they are no longer SOEs after being listed on the stock exchanges. They have become public companies. Therefore, it seems to be against the legislative intention of Article 24 for the court to make such appointments.

On the other hand, in most cases, appointing these committees may also lead to a conflict of interest and allegedly violates EBL 2006 Article 24. To ensure the neutrality of an administrator, Article 24 stipulates that any party who has a direct interest in the reorganisation is proscribed from being

[64]See Booth (n 27) 293 (noting that it was rare for lawyers to be included as government-organised liquidation committee members which dealt with the bankruptcy of SOEs in the past under the EBL 1986 in China)

[65]R Xu, 'Jin Hua Entered into Reorganization Due to the Defaults on RMB 0.9 Billion Debt Payments' *Shanghai Stock Daily*, 22 March 2010 <http://finance.sina.com.cn/stock/s/20100322/01097603768.shtml> accessed 1 November 2014.

[66]The Administrator of Xinjiang Chalkis Ltd, 'The Reorganization Plan of Xinjiang Chalkis Limited' <http://quotes.money.163.com/f10/ggmx_000972_1024455.html> accessed 1 November 2014.

[67]S Li, 'Impacts of the New Enterprise Bankruptcy Law' (2006) 6 *Journal of East China University of Law and Political Science* 110, 111.

[68]X Wang, 'Problems of Enhancing China's Insolvency Practitioner System' (2010) 9 *Legal Research* (Fa Zhi Yan Jiu) 14. See also Parry and Zhang (n 28) 130 (arguing that appointing a local-government-organised liquidation committee was retained for the bankruptcy of SOEs in the EBL 2006).

appointed. However, as noted, most Chinese listed companies have state shares and even half of them are directly equity controlled by the state. In these circumstances, appointing a local-government-organised liquidation committee as the administrator largely means appointing one shareholder to do the job. Clearly, these appointments seem to be unlawful.

Interestingly, although in China it still remains a taboo to specifically criticise authorities in public, the above rampant breaches were immediately pointed out by China's shareholder activists, who accused, on Internet blogs, that it is a breach of EBL 2006 Article 24 for courts to make such appointments.[69] Unfortunately, the key weakness of China's legal system is that many institutions, including government-controlled law courts, do not treat laws seriously,[70] as a result of which these alleged breaches remain widespread in listed company reorganisations.

Despite most cases using a local-government-organised liquidation committee as the administrator, it is not the end of the story, since the debtor-in-possession may, as mentioned previously, in theory, be requested and granted by the court,[71] which means the local government would cede control to the debtor, and this may somewhat alleviate the state dominance. But, in practice, it is another story.

This article finds that, as indicated in Figure 5, out of these 43 reorganisations were there only nine cases (21%) where debtor-in-possession was requested and granted; accordingly, in the majority of the cases (79%), the administrator remained in control. In other words, the landscape of the local government dominance in China's listed company reorganisations has not been substantially changed by the theoretical prospect of debtor-in-possession.

In many cases, the administrator––rather than debtor-in-possession––seems to be the only one realistic option, since at least 16 out of all cases (37%) saw the company's business operation having ceased before the commencement of reorganisation. This suggests that many formal rescues were launched too late, and that it was impractical to rely on the debtor itself to conduct the rescue by granting debtor-in-possession. Terminating the

[69] J Sanhu, 'The Seven-Day Ordeal of Lodging a Petition in Harbin' <http://lzb600705.blog.163.com/blog/static/102776088200982071750660/> accessed 2 November 2014 (describing the insurmountable difficulty of a retail shareholder activist lodging a petition in an effort to revoke the court's appointment of the administrator from the local-government-organised liquidation committee in the reorganisation of Beiya Ltd, in which the state was the controlling shareholder).

[70] See Y Li, 'Misunderstanding and Misuse of China's Corporate Reorganization Regime, A Case of Beiwen in Zhengzhou' (2001) 3 *Financial Law Forum* 11, 17 (arguing that laws are not always treated seriously by many state institutions in China). See also the World Justice Project, *Rule of Law Index 2014* (the World Justice Project 2014) 14–15 (ranking China as low as the 92nd of 99 countries in the world as to constraints on government powers). The weakness of China's legal system can also be understood by reading an excellent article at S Lubman, 'Bird in a Cage: Chinese Law Reform after Twenty Years' (2000) 20 *Northwestern Journal of International Law & Business* 383.

[71] See Ren, 'The Control Model' (n 5) 180 (describing the likelihood of the DIP under China's EBL 2006).

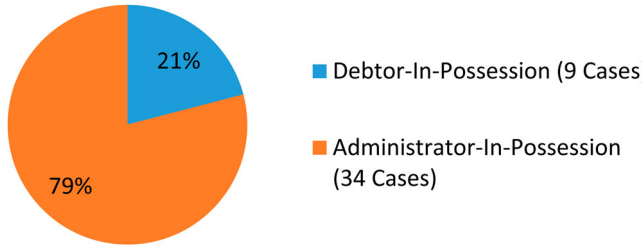

Figure 5. Control models in China's listed company reorganisations (2007–2013). Source: author's data collection.

business operation was largely accompanied by the departure of the key members of the debtor's managing team.

Moreover, bearing in mind that the governments are the major shareholders of most of China's listed companies, for debtor companies, there might be no difference between requesting debtor-in-possession and not. Before the reorganisation procedure, the government controls the listed company as the controlling shareholder, and after the formal rescue procedure commences, the government maintains its control under the name of the administrator. Therefore, to the debtor, it may not be fit for purpose to apply for debtor-in-possession: most of them are continuously controlled by the governments, no matter of being in or out of reorganisation.

Although there were nine cases using debtor-in-possession, they largely existed in name only. That is to say: the debtor-in-possession was granted, but the key decisions were still made by the administrator. For example, in the case of Shaanxi Pianzhuan Ltd,[72] it was the administrator, the government-organised liquidation committee led by the local Xianyang State-Assets-Management Authority, rather than the debtor who made the key decisions about the reorganisation issues, including choosing the company buyer, although the debtor-in-possession was artificially sanctioned.[73] In most cases, with debtor-in-possession granted, instead of being allowed to fully control the company, the debtor was mainly retained to maintain the day-to-day business operation. The control has been lost to the administrator, and it has never really returned.[74]

To sum up, it was overwhelmingly the local government that controls listed company reorganisation in China. This may pose considerable threat to the

[72]Shaanxi Pianzhuan Ltd, 'General Announcement of the Debtor-in-Possession Approved' (2009-042) <http://quotes.money.163.com/f10/ggmx_000697_488151.html> accessed 2 November 2014.

[73]X Zhang, 'The Rocky Road of Shaanxi Lianshi to Buy Pianzhuan' *China Times* (15 May 2010) <http://finance.sina.com.cn/stock/s/20100515/21367942646.shtml> accessed 2 November 2014.

[74]See WJ Woodward, Jr, '"Control" in Reorganization Law and Practice in China and the United States: An Essay on the Study of Contrast' (2008) 22 *Temple International & Comparative Law Journal* 141, 147 (describing the difference of control models in China's and US's bankruptcy reorganisation laws).

protection of creditors and minority shareholders and affect how the value of these companies is equitably distributed.

4. Value distribution in China's listed company reorganisations

With respect to value distribution, at the policy level, China might have the most liberal legal framework on this. Under EBL 2006 Articles 81 and 87, the two fundamental value distribution norms, the *pari passu* and absolute priority principles, which are compulsory in liquidation, are only treated as the default rules in reorganisation.[75] That is to say that affected parties in reorganisation can contract out of these two norms; the other side of the same coin is that if a consensus cannot be reached, under EBL 2006 Article 87, these two norms must be conformed with.

Before reporting how these two value distribution norms were applied, it seems necessary to look at going-concern value preservation at first. The corporate reorganisation regime would be a total failure if going concern value cannot be preserved.[76]

This article measures going-concern value preservation by calculating the debt recovery rate for creditors. Out of all these 43 cases, secured debts were fully honoured within the value of encumbered assets, and two classes of priority creditors––employee and tax authority––were also paid in full. This is a huge success by the Chinese standard, since even secured debt could not be fully paid in an ordinary company liquidation or dissolution case in China, according to the World Bank.[77] Therefore, the recovery rate here is only a matter of unsecured creditors.

Reorganisation is designed to prevent piecemeal liquidation, hence, there was always going-concern value preserved, since liquidation was avoided in all these cases. In particular, zero returns to unsecured creditors have never happened. It is a positive sign of the strength of China's new corporate reorganisation law.

By compiling the unsecured creditors' recovery rate of each case, this article finds that the average recovery rate for unsecured creditors was 25.14%, which means on average unsecured creditors recovered 25.14% of their claims in China's listed company reorganisations. It does reflect a kind of achievement. Specifically, this figure would be more encouraging if compared with the recovery rate for unsecured creditors in China's company liquidations as a whole.

[75]See Ren, 'Wealth Distribution' (n 5) 97 (arguing value distribution in China's corporate reorganisations)

[76]See an excellent article examining going concern value preservation in reorganisation at LM LoPucki, 'The Nature of the Bankrupt Firm: A Response to Baird and Rasmussen's "The End of Bankruptcy"' (2003) 56 *Stanford Law Review* 645.

[77]According to the World Bank data, in an ordinary liquidation case in China, secured creditors on average recoup 36% of their claims. This also means that it is the norm for unsecured creditors to recoup zero in China. See World Bank Group, 'Resolving Insolvency', DoingBusiness.org <http://www.doingbusiness.org/data/exploretopics/resolving-insolvency> accessed 14 January 2015.

According to the existing literature,[78] the average recovery rate for creditors, including secured and unsecured creditors, in China's corporate liquidations is always lower than 10%. It is also widely observed that unsecured creditors get zero returns in most corporate liquidation cases in China.[79] Thus, compared with less than 10%, the 25.14% found here is something which should be celebrated. Such a figure is also somewhat encouraging even if an international comparison is made.

In the UK, according to an article contributed by Professor Armour and others published in 2012, unsecured creditors on average recovered less than 20.20% in randomly selected administrations (reorganisations);[80] in the USA, one study, which examines Chapter 11s conducted in New York and Arizona from 1995 and 2001, finds that American unsecured creditors on average realised 52% of their claims.[81] The comparison between these three jurisdictions is demonstrated in Figure 6, though it should be addressed that such comparison is considerably simplified, since many background factors have not been taken into account.

For example, the UK has a bank-centre corporate financing system, as a result of which many UK companies rely on bank lending secured under various forms of securities including floating charges for financing; in the event of insolvency, the majority of the company value goes to meet the claims of secured creditors, most of them banks, first, which means that little could be left for unsecured creditors. However, the USA has a well-developed equity market, which translates into the fact that many companies use equity markets rather than banks to raise funds, and in the case of bankruptcy because of the application of the absolute priority norm, creditors, especially unsecured ones, are better-positioned. This may explain why unsecured creditors recover at a higher rate in US Chapter 11s than in UK administrations.

China's slightly higher recovery rate for unsecured debt than the UK's counterpart might be because that the Chinese companies studied here are

[78]Zhang and Booth (n 24) 10 (reporting that at least in Shenzhen the return to creditors in bankruptcy is always less than 10%); Li (n 25) 1 (reporting that 'the banks recovered only 10.1% of their loans' in Chinese company liquidations, and in view of the fact that some of bank loans were secured, the recovery rate for unsecured debts would be definitely lower than 10%); X Wang, 'A Character of Market Economy' (1999) 4 *International Trade* 37, 38 (reporting that the average recovery rate for creditors, including secured and unsecured, in China's company liquidations nationwide in 1997 is 6.63%); T Zhou, *China's Financial Sector Problems: Risks Control and Prevention* (Beijing, China Party School Publishing House, 2002) 78 (reporting that in the surveyed bankruptcy cases the banks only recovered 9.30% of their loans in China).

[79]See J Yan, 'An Analysis of the Low Recovery Rate for Creditors in China's Corporate Liquidations' *People's Court Daily* (14 August 2014) <http://www.chinacourt.org/article/detail/2014/08/id/1364746.shtml> accessed 6 November 2014 (reporting that in the Zaozhuang prefecture of Shandong Province it was the norm for creditors [except employees] to get zero returns in company liquidations from 2002 to 2014).

[80]J Armour, A Hsu and A Walters, 'The Costs and Benefits of Secured Creditor Control in Bankruptcy: Evidence from the UK' (2012) 8 *Review of Law and Economics* 101, 116.

[81]A Bris, I Welch and N Zhu, 'The Costs of Bankruptcy: Chapter 7 Liquidation versus Chapter 11 Reorganization' (2006) 61 *The Journal of Finance* 1253, 1289.

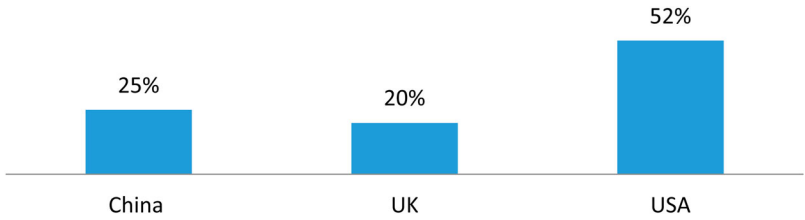

Figure 6. Unsecured debt recovery rates in the UK, USA and China. Source: combined by the author.

all listed companies, which can be financially stronger, whereas the UK companies covered by the aforementioned study are ordinary businesses, most of which are small and medium enterprises and might have no substantial assets at the time of insolvency. Overall, this comparison is only aimed to give a glimpse of unsecured debt recovery rates at the international level, rather than to indicate the superiority of any jurisdictions in using corporate reorganisation law.

Hence, generally speaking, it can be tentatively concluded that China's corporate reorganisation law has functioned well in preserving going concern value at least in these listed company reorganisation cases. But preserving value is one thing; distributing it is another. Now, attention turns back to how the value is allocated.

First, as for the application of the *pari passu* principle, except three reorganisations (Tianfa, Tianyi and Lanbao) which did not publicly disclose the relevant information (as shown in Figure 7) it is found that *pari passu* was applied in 17 out of the remaining 40 cases (42.5%), and in the rest of cases (57.5%) it was relaxed. It is worth repeating that *pari passu* was only a concern of unsecured creditors, since all other creditors––secured, employee and revenue––were fully paid, as noted.

In general, the *pari passu* principle was relaxed in two forms. First, each unsecured claim was broken into several parts, and a variety of recovery rates applied to each of them. It is complex. An example is given to illustrate this. In the case of Xiaxing Electronics Ltd, for instance, each unsecured claim was divided into three parts: the first RMB 10,000, the second between RMB10,000 and RMB100,000, and the third over RMB100,000. The full repayment applied for the first RMB 10,000 of each unsecured claim, the second part got a 50% return, and the third part was 6.15% repaid.[82] Under this plan, if an unsecured creditor only had a claim of less than RMB10,000, it means that this creditor got a full recovery. But for an unsecured creditor having a claim of RMB 1 million, the 100% recovery rate for the first

[82]The Administrator of Xiaxing Electronics Ltd, 'The Reorganization Plan of Xiaxing Electronics Limited' <http://www.cninfo.com.cn/finalpage/2009-11-25/57327719.PDF> accessed 7 November 2014.

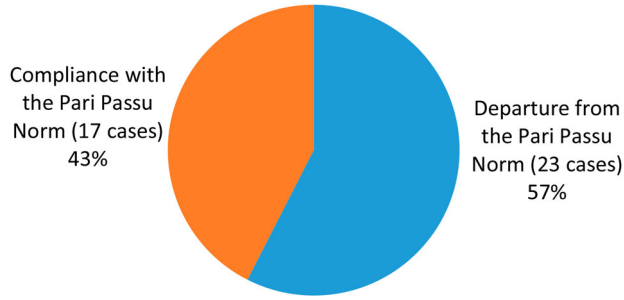

Figure 7. Application of the pari passu principle (2007–2013). Source: author's data collection.

RMB10,000 was substantially negligible, since the majority of its debt was covered by the lower repayment rate of 6.15%. Under this form, obviously, small unsecured creditors benefited; large ones did not.

Unlike the first form, the second was made exclusively in favour of small unsecured creditors. In this situation, unsecured creditors were regrouped according to the amount of their claims, and different recovery rates were made for different groups. The main point was that small creditors got more. For instance, in the case of Hua Yuan Titanium Dioxide Ltd, unsecured creditors were separated into two groups: the first group each of them having the claim of less than RMB 6 million, and the second group each having more than RMB 6 million. The first group was 70% repaid, and the second was 41.69% repaid. Unsecured creditors with relatively smaller claims were particularly favoured.

Whatever the forms of departure, *pari passu* was relaxed in favour of small unsecured creditors. This begs the question why the administrator, who formulated the plan but was not appointed by small unsecured creditors, tried to please this group of creditors. Two factors may offer a partial explanation.

First, the administrator needed the votes of the small unsecured creditors to pass the reorganisation plan. The number of these small creditors matters. As mentioned, the reorganisation plan is not passed unless it is voted for by a majority of affected parties in number of each class. With the favourable recovery rate and even the full repayment provided, it seems unlikely for the small unsecured creditors to vote down the reorganisation plan. This is what the administrator expected to see.[83] Arguably, these creditors were bribed to vote for the administrator-proposed reorganisation plan.

Second, paying small unsecured creditors more was also aimed to prevent protests or at least to make protests less likely. Again, this could only be

[83]See JR Franks, KG Nyborg and WN Torous, 'A Comparison of US, UK, and German Insolvency Codes' (1996) 25 *Financial Management* 86, 94–5 (noting that in Germany occasionally small unsecured creditors are paid in full to secure the approval of the reorganisation plan).

understood in the context of China. Chinese creditors may protest in the court house or directly march to the government if they feel badly treated.[84] This scenario is precisely what the local government and the court are afraid of and will do their best to avoid. Protests are treated seriously as political threats to the one-party regime.[85] Paying some creditors in full or more favourably is clearly a divide-and-conquer strategy, since the creditors who are paid in full will leave, which can in turn reduce the number of potential trouble-makers. The administrator, behind whom are the local government and the court, decided to pay some creditors more to buy peace.

This strategy worked very well in some cases. For example, in the reorganisation of Guangxi Beishen Pharmacy Ltd, under its proposed reorganisation plan, the first RMB50,000 of each unsecured claim was fully repaid, and this meant that 122 out of all 226 unsecured creditors (54%) got full recovery. So, with over half of unsecured creditors financially satisfied entirely, even if there was a protest, at least its scale could be more manageable or containable for both the court and the local government.[86]

But the real concern here is that the local government under the name of the administrator was using the money of large unsecured creditors to pursue its own agenda. And the same tactic was also used in dealing with the absolute priority principle.

Turning to the absolute priority principle, compared with the departure from *pari passu*, which happened in some half of all cases, the departure from absolute priority was the norm rather than the exception in all these cases. Precisely, in all 43 listed company reorganisations, shareholders retained part or whole of their equity in the reorganised company, although creditors, especially unsecured creditors, were not paid in full.

By and large, the departure was operated in two ways. First, the equity of shareholders remained intact, whereas unsecured creditors had to fully shoulder reorganisation costs. This occurred in 9 out of all 43 cases (21%). For example, in the case of Guangdong Hualong Groups Ltd, the equity of all shareholders was untouched, while the unsecured creditors only recovered 13% of claims each.[87] It should be noted that most of such deviations happened in the years 2007 and 2008, when the EBL 2006 was first implemented. As time went on, presumably, it was increasingly realised that this way was excessively unfair to creditors; then the second way emerged later.

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[84]CF Minzner, 'China's Turn Against Law' (2011) 59 *The American Journal of Comparative Law* 935, 946 (noting that in China land seizures and corporate reorganisations of failed enterprises may generate mass citizen discontent or social unrest).

[85]See generally PS Jha, *Managed Chaos: The Fragility of the Chinese Miracle* (Los Angeles, Sage, 2009).

[86]The Administrator of Guangxi Beishen Pharmacy Ltd, 'The Reorganization Plan of Guangxi Beishen Pharmacy Limited' <http://www.cninfo.com.cn/finalpage/2009-02-23/49439063.PDF> accessed 8 November 2014.

[87]Guangdong Hualong Groups Ltd, 'General Announcement of the Reorganization Progress' <http://www.cninfo.com.cn/finalpage/2008-04-26/39207361.PDF> accessed 8 November 2014.

In the second way (taking place in the remaining 79% of cases), instead of being shielded from bearing any costs, shareholders were required to concede part of their equity to increase the unsecured debt recovery rate. For example, in the case of Shenzhen China Bicycle Limited, two controlling shareholders surrendered 10% of their shares, and the rest of shareholders, including the general public shareholders, conceded 8% each; as a result, the returns to the unsecured creditors were increased by 6.31% to 30.67%.[88]

Unlike the departure from absolute priority in US Chapter 11s, China's version of the departure seems to have gone too far. In US listed company Chapter 11s, the departure from absolute priority did happen in many cases, but usually only a less than 5% of the company's value goes to old equity holders in order to reach a desirable consent.[89] In this circumstance, however, the majority of the old equity will be cancelled. On the contrary, in China's listed company reorganisations, the majority of old equity will be retained. This is the key difference between these two jurisdictions.

One may ask the question why the absolute priority principle seemed to be ignored in all these cases. Again, this is because of China's social stability concerns. As early as April 2006, two months before the EBL 2006 took effect, one senior judge of the China Supreme People's Court, Mr Song Xiaoming, gave a presentation in a high-level international conference, the 5th Forum for Asian Insolvency Reform (FAIR), stating that in a listed company reorganisation case 'a certain proportion of stock equities should be reserved for medium and small investors (shareholders)', whether the company is solvent or insolvent, and that this is to 'perform the function to maintain social stability'.[90] In other words, the Supreme Court is of view that in listed company reorganisations the absolute priority principle must be relaxed in the interest of medium and small shareholders. Presumably, Song's speech has been circulated to all Chinese courts, since except this document, there is no legally-binding bylaw which could be identified to justify the widespread departure from absolute priority in China's listed company reorganisations.[91]

But this policy gives rises to two immediate problems. First, it contradicts the EBL 2006 Article 87. Under Article 87, as mentioned before, absolute priority is a default rule. In all reorganisation cases, it can be relaxed subject to consent between creditors and shareholders. But the Supreme Court says

[88]Shenzhen China Bicycle Ltd, 'The Reorganization Plan of Shenzhen China Bicycle Limited' <http://www.cninfo.com.cn/finalpage/2013-11-08/63248707.PDF> accessed 8 November 2014.

[89]LM LoPucki and WG Whitford, 'Bargaining over Equity's Share in the Bankruptcy Reorganization of Large, Publicly Held Companies' (1990) 139 *University of Pennsylvania Law Review* 125, 142–3.

[90]X Song, 'The Courts Role in Enterprise Bankruptcy Proceedings and Restructuring in China' (5th Forum for Asian Insolvency Reform (FAIR), Beijing, China, 27–28 April 2006).

[91]See Howson (n 3) 971 (noting some law enforcement guidelines issued by China's administrative authorities are directly contrary to the statute).

that in listed company reorganisations it must be relaxed regardless of consent reached or not. This policy is controversial,[92] since it is against EBL 2006 Article 87.

Second, this policy has been expansively used and even abused by controlling shareholders at the expense of both unsecured creditors and general public shareholders. According to this policy, it is medium and small investors that are given special protection for the sake of preventing social unrest. In the context of China's securities markets, these investors are the general public who register as investors in Shanghai and Shenzhen Stock Exchanges and become shareholders of certain of listed companies. It seems clear that controlling and institutional shareholders are not on this special protection list. But the reality is that all shareholders used this policy to retain their equity.

To sum up, China's new reorganisation law did show its strength in preserving going-concern value in the listed company reorganisations, since at least it doubled the returns to unsecured creditors by avoiding piecemeal liquidations. But concerns are raised in distributing value, as the two fundamental value distributional norms were often relaxed for political considerations. In some cases, the company's value was distributed quite unfairly. In the event of unfairness, the court is empowered to correct this when approving the reorganisation plan at the last stage.

5. Court approval of reorganisation plans

As noted, there are two different procedures made to approve consensual and non-consensual reorganisation plans respectively. For a consensual one that has been accepted by all classes of affected parties through a vote, under EBL 2006 Article 86, the court will approve it if it generally complies with the EBL 2006. Article 86 does not specify what criteria the reorganisation plan must meet;[93] probably the law is intended to give the full discretion to the court. This is called a normal approval.

By contrast, where there is a non-consensual reorganisation plan that has been voted down by one or more than one class of affected parties, EBL 2006 Article 87 provides a list of conditions for the plan to meet. If the plan fails to meet one of them, the court will reject the plan and force the company into liquidation. This article summarises these

[92]Mr Xiaohong Chen, director of The China State Council Enterprise Research Centre, expresses his view that the absolute priority principle must be complied with in listed company reorganisations: see M Chaoyan and A Zhen, 'Reorganization Following Bankruptcy, A New Path of Rehabilitation Created by Lan Bao' *Huaxia Daily* (29 December 2007) <http://business.sohu.com/20080102/n254421868.shtml> accessed 18 January 2015.

[93]X Wang, 'Theories and Practices of Corporate Reorganization' (2012) 11 *Journal of Law Application* (Fa Lv Shi Yun) 10, 15 (noting that the EBL 2006 is silent on the criteria which a court can use to approve a consensual reorganisation plan).

conditions as the four tests, which are very similar to those in the US Chapter 11s.[94]

The first is the creditor-best-interest test, which requires that creditors be paid not less than in a hypothetical liquidation; the second is the *pari passu* test, which stipulates that creditors within the same class (mainly unsecured creditor class) must be paid *pro rata*; the third is the absolute priority test, which indicates that absolute priority must be complied with;[95] the final is the feasibility test, which, as demonstrated by its name, means that the plan must be feasible.[96] If all of these four tests are passed, the court may approve––and force dissenting parties to accept––the reorganisation plan. In the language of the corporate reorganisation law, it is called a cram-down approval.

In these 43 cases, all reorganisation plans were approved by the courts; no rejection has been found. In other words, the court confirmation of reorganisation plans seemed to be guaranteed in China. In particular, the normal approval was used in 31 cases (72%), and the cram-down approval was seen in the remaining 12 cases (28%).

As for the normal approval in these 31 cases, at first glance, the court seemed to have done the right things, since all classes of affected parties had voted for the proposed plan. But great unfairness might be hidden, and this is mainly because of the oversimplified, deeply-flawed EBL 2006 Article 82 on how to form the class of unsecured creditors.[97]

Under Article 82, creditors are divided into four classes––secured, employee, tax and unsecured––to vote on a reorganisation plan. But the key problem of this Article is that it is silent on whether an unsecured creditor who is an insider should abstain from voting as an ordinary unsecured creditor, or whether a new class should be formed to accommodate these insider parties.[98] Without categorising unsecured creditors further, the majority rule is artificially followed, but in substance, the voting outcome might be manipulated by the insiders under the guise of the ordinary unsecured creditors. The China Supreme People's Court knows this, but no any policy action has been

[94]Warren and Westbrook (n 4) esp ch 8.

[95]Wang (n 93) 18 (noting that absolute priority must be complied with in the case of a cram-down approval under EBL 2006 Article 87).

[96]These tests are probably directly borrowed from the Chapter 11 of the US Bankruptcy Code 1978. See 11 USC Sec 1129, and detailed discussion of this in KN Klee, 'All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code' (1979) 53 *American Bankruptcy Law Journal* 133, 136–7 (describing the similar tests used by American bankruptcy courts to assess reorganisation plans).

[97]See Falke (n 33) 74 (noting that many gaps are left in the EBL 2006 and may lead to difficulties in the implementation of this law).

[98]See DC Cohn, 'Subordinated Claims: Their Classification and Voting under Chapter 11 of the Bankruptcy Code' (1982) 56 *American Bankruptcy Law Journal* 293, 295–301 (discussing claim subordinations in Chapter 11s).

made until now.[99] Realistically, although China has no formal claim-subordination rules, courts can use the general principle of equity embedded in China's Civil Law 1986 Article 4 to restrict insiders from voting as ordinary unsecured creditors.

A typical case can demonstrate the potential inequity caused by not excluding insiders from the class of unsecured creditors. In the case of Shenzhen China Bicycle Ltd,[100] the largest unsecured creditor, Shenzhen Guoshen Energy Ltd, holding the RMB 0.46 billion debt representing 26% of the unsecured claims, was included in the class of unsecured creditors to vote, but Guoshen was also the company's controlling shareholder.[101] With debtor-in-possession granted in this case, it means that the reorganisation plan was made by Guoshen and then was substantially approved by itself but under a different name as an ordinary unsecured creditor. Inevitably, the voting result had been considerably affected, if not manipulated, by Guoshen. For the purpose of equity, ideally, Guoshen should be barred at least from voting as an ordinary unsecured creditor.

Regarding the cram-down approval in the remaining 12 cases, unfortunately, they are the real negative examples of China's version of the rule of law.[102] As mentioned before, under EBL 2006 Article 87, a cram-down approval cannot be sanctioned if the absolute priority test is not passed. But, given the automatic departure from absolute priority in all China's listed company reorganisations, clearly, all cram-downs here violated the EBL 2006, because they failed in passing the absolute priority test.[103] The most serious concern is that some cram-downs were in fact supported and agreed with by the China Supreme People's Court, according to Professor Li Shuguang, a leading Chinese bankruptcy scholar.[104]

Moreover, in these 12 cram-downs, at least there were six cases where the *pari passu* principle was also relaxed; again, it was a violation of EBL2006 Article 87, since they failed in passing the *pari passu* test noted above.

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[99]M Liu and H Chi, 'Cram-downs in Chinese Company Reorganization' (2011) 10 *Journal of Law Application* 81, 85 (the author Min Liu is a judge in China's Supreme Court, and he noticed the widespread abuses made by insiders as unsecured creditors when voting on the reorganisation plan).

[100]Shenzhen China Bicycle Ltd, 'Announcement on the Voting Result of the Second Creditors Meeting' <http://finance.ifeng.com/a/20130823/10504488_0.shtml> accessed 10 November 2014.

[101]Z Zhen, 'We Must Proscribe the Zhonghua Reorganization Scandal from Being Repeated' *China Stock Daily* (24 October 2013) <http://www.cs.com.cn/ssgs/gsxw/201310/t20131024_4180435.html> accessed 10 November 2014 (mentioning that Guoshen held the RMB 0.46 billion unsecured claim in the Zhonghua [China] reorganisation case).

[102]See generally R Peerenboom, 'What Have We Learned about Law and Development? Describing, Predicting, and Assessing Legal Reforms in China' (2005) 27 *Michigan Journal of International Law* 823 (describing the development of China's rule of law).

[103]See BL Liebman, 'A Return to Populist Legality? Historical Legacies and Legal Reform' in S Heilmann and EJ Perry (eds), *Mao's Invisible Hand, The Political Foundations of Adaptive Governance in China* (Cambridge, Harvard University Asian Centre, 2011) 177 (noting that China's judges sometimes ignore legal rules entirely when adjudicating cases).

[104]Y Liu and Y Gao, 'Corporate Reorganization of Hai Ji Lv Jian' *China Stock Market Weekly* (27 April 2009) <http://stock.jrj.com.cn/2009/04/2711394859465.shtml> accessed 15 January 2015.

With respect of the creditor-best-interest test, it seems that this test was passed in all cram-down cases. In all reorganisations, there was a routine assets valuation procedure. Licensed auditors were hired to evaluate the liquidation value of the companies. At least from reading these reorganisation plans, unsecured creditors were always paid more than in liquidation. For example, the unsecured creditors of Hebei Baoshuo Limited recovered 13% of their claims each, whereas according to the assets evaluation report, they could only recover 10.12% if the company was liquidated.[105]

As for the feasibility test, since it is considerably subjective in nature, most courts seemed to be unable to make a real judgement. In reality, it was more a kind of formality for judges to insert a brief statement in the reorganisation approval document that 'the court is of view that the plan is feasible'. In fact, no substantial assessment was made. Professor Zou Hailin, another leading Chinese bankruptcy scholar, argued that assessing the feasibility of a reorganisation plan involves business judgement and is beyond what judges as legal professionals can do.[106] Very few judges are business-minded, which means the feasibility test is largely not used in practice.

After approving the reorganisation plan, the court will close the judicial reorganisation procedure, and the debtor is liable to execute the reorganisation plan.[107] Under EBL 2006 Article 90, the administrator supervises the plan's execution.

To summarise, several main characters of the implementation of China's listed company reorganisations can be learnt. First, most of these cases were politically driven,[108] since local governments played the key role in supporting the commencement of these cases and in controlling these companies in the reorganisation process under the name of bankruptcy administrators. Second, these cases reflected the less-developed rule of law in China, since many statutory rules were not respected by public authorities including law courts. Third, the corporate reorganisation law itself did show its strength in preserving going concern value by preventing piece-meal liquidations, since the debt recovery rate was considerably increased compared with in liquidations. But great unfairness lied in distributing the preserved value. The following parts turn to the questions who are winners and losers.

Section D: are unsecured creditors and general public shareholders winners?

The answer looks to be affirmative. To unsecured creditors, on the one hand, bearing in mind the creditor-best-interest test, all of them were paid more

[105]The Administrator of Hebei Baoshuo Ltd, 'The Reorganization Plan'.
[106]H Zou, 'Uncertainties of Cram-Downs' (2012) 11 *Journal of Law Application* 24, 25.
[107]EBL 2006 art 89.
[108]See an insightful discussion of this in JM Marsden and S Mui, 'Local Concerns Outweigh Offshore Creditors' Interests in Chinese Restructurings' (2014) 9 *Journal of Corporate Renewal* 23.

than in liquidation, as reported above. On the other hand, on average, they recovered 25.14% of their claims, whereas their counterparts in liquidations could only recoup less than 10%. To general public shareholders (retail investors), the majority of their equity was retained, and they were only in some cases required to sacrifice a small portion of their equity to pacify unsecured creditors, but they would have lost everything if these companies had been liquidated. Thus, on the face of it, both unsecured creditors and general public shareholders seemed to be the winners or beneficiaries, but this article points to the contrary.

1. *Unsecured creditors were losers*

An early study shows that the average unsecured creditors' recovery rate in Chinese corporate reorganisations as a whole, including both listed and private company reorganisations, amounts to 33.67%.[109] In view of the two different recovery rates, one question arises: why do the unsecured creditors in listed company reorganisations recover 25.14%, but the national average for both listed and private company reorganisations is 33.67%? Listed companies are supposed to financially stronger, because in China only the very healthy companies are selected to be listed, and because the performance of these companies is constantly monitored by the regulators to ensure adequate protection of investors.[110] In turn the unsecured creditors' recovery rate is supposed to be higher instead?

One of the causes is soon spotted: unsecured creditors in these cases were served with a low recovery rate partly because the absolute priority principle was routinely circumvented.

As noted, for political considerations, the China Supreme People's Court does not acknowledge absolute priority as a default rule in listed company reorganisations.[111] Instead, the Court makes clear that the absolute priority principle must give way to maintaining social stability, thereby this fundamental value distribution norm is put upside down. Inevitably, unsecured creditors bear the brunt of the Court's decision.

This article finds that if the absolute priority principle could have had been complied with, the average unsecured debt recovery rate could be increased from the current 25.14% to 86.51%, and in 25 out of all 43 cases (61%) the unsecured creditors could get the full recovery. How are these figures generated?

To count how much more the unsecured creditors could get, it is vital to determine the share price when the company is in the process of reorganisation. This article mainly refers to the price-measuring methods used in the existing reorganisation cases.

[109]Z Zhang, 'Corporate Reorganization under the Enterprise Bankruptcy Law of the People's Republic of China: The Relevance of Anglo-American Models for China' (PhD thesis, Durham University 2014) 127.
[110]See generally Fan, Wong and Zhang (n 2) 330.
[111]EBL 2006 art 87.

Following this approach, if the share price is set in the reorganisation plan, this article simply uses it to calculate the equity value of the company. In the case where the share price is not shown in the reorganisation plan, this article uses either the closing price at the date when trading was suspended by the Exchange or the opening price at the date when the company resumed trading, depending on which price is publicly available. In addition, in some cases, the share price was generated from the average price traded during the period of twenty market days prior to its suspension. Choosing these methods is also because they were used and preferred by many administrators in calculating share prices in other reorganisation plans; in general, there is not a uniform method to do so.

In addition, using the above share prices is also intended to make this article's argument more conservative and robust, since in most cases the share prices soared after the conclusion of the reorganisation procedure; if the post-reorganisation share price, which is always far higher than the aforementioned depressed prices, is selected to calculate how much should go to creditors, the vast majority of these cases may see the full repayment to all unsecured creditors; but this cannot be quite reliable due to the volatility of share prices in the equity market. For the sake of being conservative, this article uses the above methods to count what unsecure creditors are entitled, which are obviously less controversial. The counting methods are very complex, and they are listed in detail in Appendix 1.

By such methods, for example, in the case of Beishen Pharmacy Ltd, the share price was fixed at RMB3.00 per share in the reorganisation plan. Each shareholder was required to surrender 23% of the shares to increase the recoveries for unsecured creditors. As a result, unsecured creditors got a 50.44% recovery. But the real problem is that if the absolute priority principle could be conformed to, the equity value of RMB911 million retained in the hands of the old shareholders could be enough to pay the cancelled unsecured debt of RMB515 million. In other words, in the Beishen case, the unsecured debt recovery rate should be 100% rather than the current 50.44% if the absolute priority principle was complied with.

After obtaining all assumed recovery rates in these cases, this article reaches the estimated figure that the average unsecured recovery rate should be at 86.51% rather than the present 25.14%. Unsecured creditors were not winners; instead they might be the largest losers.

Some may ask a firmly-related question why the company's equity was still valuable after the company had been financially bankrupt. At this point, equity is presumed to be worth nothing. It is strange indeed. Such a phenomenon does, however, exist in China; or it reflects the Chinese characters of its

socialist market economy.[112] In substance, the company's equity value is mainly because of its license to float on the stock exchange, which is called the shell value.[113] Being allowed to float on either the Shenzhen or Shanghai Stock Exchange is more like a permanent membership. With delistings rarely taking place, the equity of these companies were still highly valuable.

The second question is why unsecured creditors were so disadvantaged. A number of reasons can explain this. At first, as mentioned before, all these cases were substantially initiated by the debtors themselves. Creditors, especially unsecured creditors, were quite passive as to whether or when the reorganisation procedure could be launched. In other words, it was the intention and the initiative of the debtor to use the reorganisation procedure, thus naturally it was unlikely for the debtor-initiated reorganisation procedure to be pursued in favour of creditors.

Second, the reorganisation process was largely out of the creditors' control, which made them quite vulnerable. As noted, in most of the existing cases it was the local-government-organised liquidation committee staying in charge as the administrator. Creditors, including unsecured ones, did not have a say on the appointment.[114] Even the Chinese courts were unable to refuse to appoint such committees, since courts are also somewhat controlled by the governments. Some Chinese judges also complain about this.[115] Admittedly, in theory creditors could request the court to replace the incumbent administrator, but this has never happened in reality. The situation would be worsened by the connection between local government and debtor, since in most cases the local government was exactly the controlling shareholder.[116] Arguably, it was a game played by and for the debtor.

Third, as a consequence of being unable to control the reorganisation procedure, information for creditors was scarce; even when certain of the company's information was available eventually, but it usually reached creditors too late. Without having information of the company, creditors

[112]China's status of market economy is still not recognised by the EU and USA, so this article calls it a self-styled market economy. See M Dalton, 'Malmstrom: No Automatic Market Economy Status for China in 2016' *Wall Street Journal* (11 December 2014) <http://blogs.wsj.com/brussels/2014/12/11/malmstrom-no-automatic-market-economy-status-for-china-in-2016/> accessed 17 January 2014.

[113]See X Chen, C Jevons Lee and J Li, 'Chinese Tango: Government Assisted Earnings Management' Working Paper, Tulane University, New Orleans, USA, December 2003 <http://www.bm.ust.hk/~acct/Incubator_Research_Camp/ChineseTango.pdf> accessed 18 January 2015.

[114]EBL 2006 art 22.

[115]X Jiang, 'The Role of Administrators in Corporate Reorganization' in X Wang and Z Yi (eds), *The 2nd National Bankruptcy Conference Collection* (Beijing, Law Press, 2010, 176) (the judge author argues that sometimes courts are pressured by governments to appoint the latter as administrators). See also Shenzhen People's Intermediate Court, *Report on Handling Corporate Bankruptcy Cases* <http://www.szcourt.gov.cn/shenwu/view.aspx?id=4207> accessed 22 September 2012 (the court is of view that courts must resist the pressure from local governments by not appointing the government-organised liquidation committees as administrators in bankruptcy).

[116]See Q Qiang, 'Corporate Governance and State-Owned Shares in China Listed Companies' (2003) 14 *Journal of Asian Economics* 771 (noting the firm control connection between China's local government and listed company).

were easy to be manipulated. Under EBL 2006 Article 61, the administrator is liable to provide an audited report of the company's assets to the meeting of creditors, but usually such a report was too skeletal for creditors to know how many assets the company really had. For example, in the case of Hebei Dixian Ltd, the company had 3,000 hectares of land but only admitted 324 hectares in its assets report; it seemed to be impossible for ordinary creditors to verify such information.[117] This was made public thanks to a whistleblower, one of the company's senior managers, who reported this to the China Securities Regulation Commission years after the reorganisation procedure; both creditors and shareholders were shocked by what this manager had made public.

The audited reports might lack details, but another problem is that they always reached creditors too late. In practice, creditors were given a bundle of reports only at the time when the meeting of creditors commenced. Without having sufficient time to digest these reports, usually one or two hours later, they were required to vote on the reorganisation plan. Creditors were angry, but they were, in extreme cases, revenged with violence after they voted down a local-government supported reorganisation plan.[118] To some extent, it can be argued that creditors had no choice but to vote in favour of a government-supported reorganisation plan.

In addition, the disadvantaged position of the unsecured creditors could also be attributed to the weakness of the Chinese courts. Courts are supposed to be the ultimate defenders of law. However, as argued by Professor Howson, 'Chinese courts may be seen acting in the service of state or party policy and in contravention of the law'.[119] As reported earlier, at the very least, all cram-down approvals issued by the courts were illegal, since these reorganisation plans failed to pass the absolute priority test under the EBL 2006. Unfortunately, the Chinese courts, including the Supreme Court, are unable, or unwilling, to act as the defender of law. The vulnerability of the courts in turn makes the creditors more vulnerable.

2. *General public shareholders were not winners either*

Like unsecured creditors, general public shareholders were not well protected also because of the lack of representation.

To a large extent, most of the losses of general public shareholders are made by controlling shareholders before reorganisation. As has been

[117]Q Wang, 'Ex-Manager of Dixian Reports Business Irregularities to the National Regulator' *Shenzhen Business News* (8 December 2011) <http://finance.sina.com.cn/stock/s/20111208/070010955299.shtml> accessed 18 January 2015.

[118]X Qin, 'Lawyer Assaulted in the Debtor-Controlled Hongshen Reorganization' *Shanghai Stock Daily* (17 April 2012) <http://finance.sina.com.cn/stock/s/20120417/012511839312.shtml> accessed 18 January 2015.

[119]Howson (n 55) 138.

complained repeatedly by shareholder activists,[120] if the company was not abused by the controlling shareholders, the company would not go bankrupt and did not need to resort to bankruptcy reorganisation for survival. For example, in the case of Shandong Jiufa Food Ltd, the company's financial illiquidity was mainly because its controlling shareholder, Jiufa Group Ltd, took away the company's RMB0.79 billion cash illegally (tunnelling), as a result of which the company collapsed eventually in 2008.[121] Although the Chinese securities regulator has started to crackdown such abuses from years ago, it seems that it has not gone far enough.[122]

Turning to the general public shareholders, as mentioned, the company's equity was kept entirely intact in 11 cases. Thus, it seems at least in these cases, shareholders, especially general public shareholders, were not victimised by reorganisation. But, in the remaining 32 cases, which are the focus of this section, the general public shareholders surrendered part of their equity to support the rescue efforts, and this article finds that most of these surrendered shares should not be conceded if the policy intention of the China Supreme People's Court could be faithfully materialised.

As analysed, the Supreme Court requires that the absolute priority principle should be relaxed in favour of general public shareholders, not for controlling and institutional ones. Again as reported above, this controversial policy was expansively used, since both controlling and institutional shareholders took advantage of this policy at the expense of both unsecured creditors and general public shareholders.

This article finds that in 20 cases the general public shareholders did not need to concede a single share if the absolute priority principle could have applied to the controlling and institutional shareholders (see Appendix 2). In these cases, if all of the controlling and institutional shares were surrendered, these shares would be enough to pay unsecured creditors at the same level, without forcing general public shareholders to concede anything.

For example, in the case of Shenzhen China Bicycle Ltd, the general public shareholders were asked to give up 35 million shares to pay the unsecured creditors, and the controlling and institutional shareholders relinquished 11 million shares but retained 98 million shares. It seems clear: if the 98 million shares still possessed by the latter could be conceded according to the absolute priority principle, as a result, the general public shareholders in this case did not need to concede anything.

[120] C Wang, 'ST Chuangzhi: 140 Million Still in the Hands of the Controlling Shareholder' *21st Economy News* (27 January 2010) <http://finance.sina.com.cn/stock/s/20100127/02157314622.shtml> accessed 18 January 2015.

[121] X Liu, 'ST Jiufa: Creditors in Danger' *China Commercial Review* (11 May 2011) <http://finance.qq.com/a/20110511/004883.htm> accessed 18 January 2015.

[122] See Q Liu and Z Lu, 'Corporate Governance and Earnings Management in the Chinese Listed Companies: A Tunneling Perspective' (2007) 13 *Journal of Corporate Finance* 881 (discussing the widespread tunnelling in Chinese listed companies).

By this method, with the current unsecured creditor recovery rate remaining unchanged, this article concludes that, in these 32 cases where general public shareholders were required to concede shares, 85.37% of these conceded shares (relinquished shares) could be prevented if the Supreme Court's aforementioned policy intention could be fully implemented. Put it in a different way, general public shareholders paid 85.37% more than they were required. They were not winners either.

Why were general public shareholders disadvantaged? They encountered similar situations faced by unsecured creditors, as analysed before. Even worse, unlike unsecured creditors, general public shareholders have another more acute problem: the collective action dilemma,[123] since they are considerably dispersed. It is quite difficult to coordinate the vast number of these individuals, as it is quite common for a Chinese listed company to have over 40,000 general public shareholders.[124] Coordinating these shareholders is not easy. For example, in the case of Heilongjiang Beiya Ltd, only the shareholders representing 426 million shares voted on the reorganisation plan, and the remaining shareholders holding 538 million shares, the vast majority of whom were general public shareholders, were absent from the meeting, notwithstanding the online voting system was also available.[125]

In a nutshell, the unsecured creditors and general public shareholders were not winners in China's listed company reorganisations.

Section E: who were winners?

To a large extent, local governments and controlling shareholders were the main beneficiaries of these reorganisations. Unlike controlling shareholders, local governments benefited from these cases in a subtle and indirect way.

1. Local governments as winners

Local governments were likely to be the main winners, since reorganising these companies served both their political and economic interests.

This should be understood against the background of China's political economy. China has 32 provincial governments, 333 prefecture governments and 2,861 county governments in the hierarchy.[126] The most active local

[123]See C Xi, 'Institutional Shareholder Activism in China: Law and Practice' (2006) 17 *International Company and Commercial Law Review* 251, 287.

[124]E.g. the reorganised company, Xiamen Xiaxin Electronic Ltd, had 54,192 shareholders, most of them general public. See H An and B Ye, 'Rehabilitation of Xiaxin through the Reorganization Procedure' *People's Court Daily* (30 August 2011) 3.

[125]Heilongjiang Beiya Ltd, 'General Announcement on the Meeting of the Shareholders' (Harbin Heilongjiang China, 22 April 2008).

[126]Xinhua News Agency, 'Statistics of China's Administrations above County Level' *Xinhua Net* (31 December 2003) <http://news.xinhuanet.com/ziliao/2004-10/29/content_2154078.htm> accessed 19 January 2015.

governments in these cases are at the prefecture level. With only 2,489 domestically listed companies in China, as noted before, this means in theory each prefecture can only have fewer than eight listed companies. But given the imbalanced economy of China, in fact some prefectures have fewer. For example, by the end of 2013, the Shenzhen prefecture in the well-developed Guangdong province had 260 listed companies,[127] the Luoyan prefecture in the less-developed Henan province had 10,[128] and the Lu'an prefecture in another less-developed Anhui province had only one.[129] Thus, in practice, there is fierce competition between regions in China to fight for more IPOs and for having more listed companies.

First, on top of what the local government sought to gain was the political image. Under China's current political climate, the local government, especially its senior political leaders, will lose face if a local company is delisted. To save face, the local government will do whatever it can to maintain the listing of a local company.[130] This may partially explain why the delisting is a very rare phenomenon on China's stock exchanges.[131] Rescuing a local listed company is a serious political mission. For example, when Guangming Furniture Ltd was ready to enter reorganisation in 2010, an official in the Yichun Prefecture Government explicitly told a newspaper: 'since Guangming is the only one listed company in Yichun, our major government leaders are very serious to rescuing it and will ensure its success by whatever means.'[132] This is also echoed by a recent research,[133] which finds that local senior politicians are more likely to be promoted if there are more listed companies in the region. In all these cases, for the local government, its political goal was achieved, since all companies remained the listing status after going through reorganisation.

Second, by rescuing these companies, the local governments were to maintain their own tax bases. In China, taxes are charged and shared

[127]L Zhu, 'The Number of Listed Companies from Shenzhen Reached 260' *Shenzhen Business Daily* (16 September 2011) <http://www.szsmb.gov.cn/content.asp?id=53396> accessed 19 January 2015.

[128]The Financial Office of the Luoyang Prefecture Government, 'Latest Development of Local Companies Seeking to Float' <http://www.henanjr.gov.cn/portal/jrfw/zbsc/webinfo/2012/09/1348104660380154.htm> accessed 19 January 2015.

[129]X Zhou, 'Tongfeng Electronics Merged by Tieniu Group' *Anhui Business Daily* (17 June 2007) <http://ah.anhuinews.com/system/2007/06/17/001769151.shtml> accessed 19 January 2015.

[130]See S Li and Z Wang, 'An Empirical Study on Implementing China's Enterprise Bankruptcy Law during the First Three Years' (2011) 22 *The Journal of China University of Political Science and Law* 58 (noting that a local listed company reflects the political image of the local government).

[131]See Y Wang and M Campbell, 'Business Failure Prediction for Publicly Listed Companies' (2010) 16 *Journal of Business and Management* 75, 79 (reporting that from 2000 to 2008 there were only 42 delistings from the Shanghai Stock Exchange).

[132]Y Wang, 'ST Guangming Ready for Reorganization and Visible Intervention of Yichun Government' *21st Century Business News* (7 January 2010) <http://finance.sina.com.cn/stock/s/20100107/03077205091.shtml> accessed 19 January 2015.

[133]JD Piotroski and T Zhang, 'Politicians and the IPO Decision: The Impact of Impending Political Promotions on IPO Activity in China' (2014) 111 *Journal of Financial Economics* 111.

between the central and local governments.[134] The central government may pay little attention on where a listed company is located, but local governments do. To this end, this is why the local government will rescue the local listed company at any costs. This is also why in many cases the local government help the listed company to remain balance-sheet healthy through generous subsidies. In all these 43 cases, it is found that only four companies (Shenrun, Deheng, Danhua and Yuanfa) removed the registered headquarter to where its main business operation took place. It means that the vast majority of them (91%) stayed and continued to contribute taxes to the local governments. As for these four dislocation cases, it remains unknown what kind of deals have been reached between two local governments behind closed doors.

By contrast to these four dislocation cases, there are 12 cases in which the company's main business operation was in fact removed to the different province,[135] which means that in principle their registered headquarters should follow, but it was not the case. This further convinces this article's assertion that the local governments were winners, since these companies must pay taxes to the authorities where their registered offices are.[136]

Third, in many cases, local governments were the controlling shareholders. This may also explain why the local courts remained silent when the aforementioned Supreme Court's general-public-shareholder protection policy was misused by the controlling shareholders. The controlling shareholder was the local governments, thus keeping a blind eye seemed to be the best strategy for the courts.

In addition, the local governments' gains were also reflected at maintaining social stability by using unsecured creditors' money to bribe the general public shareholders as well as the small unsecured creditors, as mentioned before. And in the existing cases, inevitably, there were still some protests occurring. For example, on 12 December 2011, some general public shareholders of Yinchuan Guangxi Ltd travelled to Beijing and protested before the China Securities Regulatory Commission, and the protestors even blocked the main gate of the Commission's building.[137] According to the present political practice in China, it is the local government which is responsible to bring, either by force or by persuasion, these protestors back to their hometown. This involves costs. Such costs are usually passed to the company ultimately. Though it seems impossible to unfold the size of these costs

[134]See K Tsui and Y Wang, 'Between Separate Stoves and a Single Menu: Fiscal Decentralization in China' (2004) 177 *The China Quarterly* 71.

[135]These companies are Chaohua, Hualong, Kejian, Beiya, Guangming, Xing'an, Tianfa, Tianyi, Lanbao, Pianzhuan, Jiufa and Huayuan.

[136]Wang (n 132) (reporting that one of the local government's aims in reorganisation is to make the company's registered office remained unchanged for tax purposes).

[137]M Li, 'A Wave of General Public Shareholder Protests' <http://t.hexun.com/wdqhgtq/12576158_d.html> accessed 2 April 2015.

in each case, this article does find a staggering figure which may give a glimpse.

According to its 2012 annual report,[138] Sichuan Jinding Ltd had to pay the local government RMB26,210,000 (approximately GBP2.621 million) for the latter's social stability expenditure during the company's reorganisation process; presumably, the local Leshan City government used this money to cover all costs incurred from its social stability activities.

2. Controlling shareholders as winners

The controlling shareholders were the winners, mainly because they exploited the Supreme Court's policy by circumventing the absolute priority principle.

First, most of the controlling shareholders' gains were exactly the losses of unsecured creditors. In other words, the former sought to retain the bulk of their equity at the expense of the latter. In principle, according to the absolute priority principle, shareholders should be the first line to bear the consequences of the company's bankruptcy; they are not allowed to receive anything unless creditors, especially unsecured creditors, are fully paid. This principle is also upheld by both China's bankruptcy and company law, but controlling shareholders backed by local governments misused the controversial policy of the China Supreme People's Court and transferred almost all costs of reorganisations to unsecured creditors.

As has been calculated, the unsecured debt recovery rate could have been increased from the present 25.14 to 86.51% if the absolute priority principle could be faithfully complied with. Unsecured creditors' losses were mainly because what they were legally entitled had been grabbed by controlling shareholders. Admittedly, all shareholders, including general public and controlling shareholders, joined the feast, but controlling shareholders took the lion's share.

Second, on the side of shareholders, controlling shareholders also used their positions to force general public shareholders to unnecessarily bear the costs of reorganisations. As noted before, in many cases, the general public shareholders did not need to concede a single share if the controlling shareholders were subject to the absolute priority principle in the first place; as a result, the relinquished shares by general public shareholders in these cases were their losses, which should be instead born by the controlling shareholders.

It should be noted that the losses and gains are inter-conditional between general public shareholders, controlling shareholders and unsecured creditors. If a metaphor of a food chain could be used, at the top are the controlling

[138]Sichuan Jinding Ltd, *2012 Annual Report*, 15 <http://www.cninfo.com.cn/finalpage/2013-01-29/62078578.PDF> accessed 2 April 2015.

shareholders, followed by the general public shareholders, with the unsecured creditors at the bottom.

Conclusions

This article has provided an in-depth investigation of how China's listed companies use the new corporate reorganisation law for restructuring and has answered who are the winners and losers.

One point should be particularly addressed: enacting and implementing a Chapter 11-style corporate reorganisation law in China has been proved to be a step in the right direction, since an enormous amount of going-concern value has been preserved, as reflected in the increased unsecured debt recovery rate. This has been achieved mainly through using reorganisation to avoid piecemeal liquidation. But concerns are raised especially on creditor protection.

To better protect creditors, first, to solve short-term problems, it seems urgent for Chinese courts to stop appointing local-government-organised liquidation committees as administrators in listed company reorganisations. As investigated in this article, most of the local governments are the controlling shareholders, thereby it seems natural for them to place their own interests ahead of creditors. The current imbalance between debtor and creditor could be alleviated by not making such appointments. And, as analysed above, appointing these committees is also against the spirit of the EBL 2006. Ideally, the China Supreme People's Court could issue a judicial notice correcting the current practice. Meanwhile, creditors should be given a strong voice on the administrator appointment, as the current situation of creditors can largely be attributed to the little control of creditors in Chinese listed company reorganisations.

Second, to solve the problems in the long run, China may strengthen its rule of law. Many problems of creditor protection reported in this article are in fact caused by the less-developed rule of law in China. Many creditor protection rules are clearly written in the EBL 2006, but in reality the public authorities, including law courts, violate them without being held accountable. This cannot be easy.[139]

Overall, China's listed company reorganisations also reflect the widely-held observation that China's current commercial law reform is still 'in a two-steps forward, one step backward' process.[140]

[139]See E Piles, *China's Human Rights Lawyers: Advocacy and Resistance* (Oxford, Routledge, 2014) 62.
[140]R Peerenboom, 'Conclusion, Law, Wealth and Power in China' in J Garrick (ed), *Law, Wealth and Power in China* (Oxford, Routledge, 2011, 272, 273) .

Appendices

Appendix 1. Assumed payment increase to the unsecured creditors: June 2007 to 31 December 2013.

Company	Share Price Applied	Absolute-Priority-Principle-Bound Increase of the Unsecured Debt Recovery Rate	Final Recovery Rate for Unsecured Debts
Chaohua	¥2.72 a share (the average price during the 60 days before being suspended)	83.94%	93.94%
Xingmei	¥5.00 a share (the price set in its reorganisation plan)	70%	100%
Xiaxing	¥3.71 a share (the price set in its reorganisation plan)	34.19%	55.96%
Taibai	¥3.3 a share (priced according to a share deal in the reorganisation plan)	58.31%	100%
Zhonghua	¥2.875 a share (generated from averaging the A and B shares priced in the plan)	69.33%	100%
Chuangzhi	¥4.68 a share (the price set in the reorganisation plan)	84.42%	100%
Hualong	¥3.65 a share (the price referred in a recent share deal)	Missing	Missing
Kejian	¥11.25 a share (priced in its reorganisation plan)	47.03%	82.28%
Taifeng	¥8.64 a share (priced in its reorganisation plan)	79.67%	100%
Shenrun	¥8.535 a share (generated by averaging the A and B shares priced in its reorganisation plan)	69.95%	100%
Xingtai	¥6.9 a share (the price generated from an auction, later the market price was speculated to ¥15.58 a share)	78.23%	100%
Beishen	¥3.00 a share (set in its reorganisation plan)	49.56%	100%
Baoshuo	¥6.00 a share (priced in its 2008 reorganisation plan)	31.46%	44.46%
Chuanghua	¥5 a share (priced in its reorganisation plan)	38.15%	49.59%
Dixian	¥2.1 a share (the market price shortly after the reorganisation)	98%	100%
Beiya	¥3.5 a share (the average price during the three months before being suspended)	81%	100%
Guangming	¥12.52 a share (generated from a share transaction during the reorganisation)	82%	100%
Xin'an	¥2.92 a publicly circular share, and ¥1.28 a non-circular share	36.78%	53.83%
Tianfa	¥4.445 a share (the average price during the twenty days before being suspended)	82.27%	100%

(*Continued*)

Appendix 1. Continued.

Company	Share Price Applied	Absolute-Priority-Principle-Bound Increase of the Unsecured Debt Recovery Rate	Final Recovery Rate for Unsecured Debts
Tianyi	¥4.33 (the average price during the twenty days before being suspended)	70.82%	80.89%
Deheng	¥5.28 a share (the price of the shares sold to the strategic investor)	58.15%	100%
Lanbao	¥0.88 a share (the average price during the twenty days before being suspended)	12.27%	34.27%
Shijian	¥3.03 a share (the concluding price on the day of opening the reorganisation procedure)	83.24%	93.24%
Danhua	¥3.64 a share (priced in its reorganisation plan)	78.7%	100%
Jingchen	¥6.16 a share (the closing price on the day of being suspended)	95%	100%
Jinhua	¥3.9 a share (the starting price set in a subsequent auction by the company)	95%	100%
Guangxia	¥7 a share (the closing price on the day of being suspended)	50%	100%
Changling	¥6.34 a share (priced in its reorganisation plan)	82%	100%
Pianzhuan	N/A (already fully paid)	N/A	N/A
Qingling	¥5.78 a share (priced in its reorganisation plan)	50%	100%
Jiufa	¥2.15 a share (priced in its reorganisation plan)	15.08%	35.56%
Hailong	¥2.93 a share (the closing price on the day of entering reorganisation)	36.12%	76.12%
Hongshen	¥4.32 a share (priced in its reorganisation plan)	88%	100%
Huayuan	¥4.37 a share (priced in its reorganisation plan)	69.49%	83.91%
Yuanfa	¥6.92 a share (priced in its reorganisation plan, and also the average price during the twenty days before being suspended)	24.06%	100%
Fangxiang	¥3.82 a share (priced in its reorganisation plan, also the closing price on the day of being suspended)	55.49%	75.17%
Jingding	¥3.8 a share (priced in its reorganisation plan)	82%	100%
Haina	¥7.2 a share (the closing price on the day of being suspended by the stock exchange)	74.65%	100%
Changhang	¥2.53 a share (priced in its reorganisation plan, also the closing price on the day of being suspended by the stock exchange)	37.32%	48.96%

(*Continued*)

Appendix 1. Continued.

Company	Share Price Applied	Absolute-Priority-Principle-Bound Increase of the Unsecured Debt Recovery Rate	Final Recovery Rate for Unsecured Debts
Zhongda	¥2.1 a share (priced in its reorganisation plan)	70.4%	100%
Xingye	¥2.41 a share (the closing price on the day of opening the reorganisation)	44.13%	49.13%
Xianchen	¥8.00 a share (the price of the shares sold to an investor by the administrator later)	97%	100%
Zhongji (中基实业)	¥2.5 a share (evaluated by an official evaluating firm)	35.58%	89.44%
Average		62.90%	86.51% (in 25 out of 41 (61%) cases, unsecured creditors could have been fully paid)

Appendix 2. Assumed advantages to the general public shareholders: June 2007 to 31 December 2013

Company	Shares Conceded by the General Public Shareholders (shares)	The Remaining Shares Possessed by the Controlling and Non-Circular Shareholders (shares)	The Remaining Shares Possessed by Controlling and Non-Circular Shareholders out of the Shares Conceded by General Public Shareholders (%) (the preventable loss of the general public shareholders)
Chaohua	N/A	N/A	N/A
Xingmei	N/A	N/A	N/A
Xiaxing	24,463,037	139,672,203	More than 100%
Taibai	N/A	N/A	N/A
Zhonghua	35,370,070	98,299,817	More than 100%
Chuangzhi	57,994,320	39,611,130	68.30%
Hualong	N/A	N/A	N/A
Kejian	26,784,163	38,768,400	More than 100%
Taifeng	18,849,303	144,021,257	More than 100%
Shenrun	10,945,500	39,685,143	More than 100%
Xingtai	4,867,215	115,624,761	More than 100%
Beishen	71,588,733	64,324,528	89.85%
Baoshuo	40,295,784	83,996,769	More than 100%
Chuanghua	6,813,915	210,998,483	More than 100%
Dixian	N/A	N/A	N/A
Beiya	N/A	N/A	N/A
Guangming	2,008,600	89,318,325	More than 100%
Xin'an	7,375,679	26,442,772	More than 100%
Tianfa	N/A	N/A	N/A
Tianyi	N/A	N/A	N/A
Deheng	29,426,283	11,122,180	37.80%
Lanbao	N/A	N/A	N/A
Shijian	60,386,904	70,002,146	More than 100%
Danhua	50,700,000	86,529,867	More than 100%
Jingchen	54,891,780	27,755,280	50.56%

(*Continued*)

Appendix 2. Continued.

Company	Shares Conceded by the General Public Shareholders (shares)	The Remaining Shares Possessed by the Controlling and Non-Circular Shareholders (shares)	The Remaining Shares Possessed by Controlling and Non-Circular Shareholders out of the Shares Conceded by General Public Shareholders (%) (the preventable loss of the general public shareholders)
Jinhua	89,923,200	266,179,200	More than 100%
Guangxia	82,968,977	7,483,400	9.02%
Changling	24,206,332	41,754,520	More than 100%
Pianzhuan	N/A	N/A	N/A
Qingling	104,345,643	93,427,425	89.54%
Jiufa	43,245,467	31,837,607	73.62%
Hailong	126,403,439	176,684,732	More than 100%
Hongshen	23,790,543	33,589,968	More than 100%
Huayuan	85,410,900	15,105,870	17.69%
Yuanfa	97,627,600	151,510,400	More than 100%
Fangxiang	43,980,444	113,109,955	More than 100%
Jingding	64,219,577	53,717,587	83.65%
Haina	N/A	N/A	N/A
Changhang	247,218,252	180,285,800	72.93%
Zhongda	153,989,758	227,466,836	More than 100%
Xingye	274,010,858	332,607,048	More than 100%
Xianchen	22,414,589	10,683,725	47.66%
Zhongji	186,813,818	170,695,084	91.37% (continued)
Average			Except the eleven reorganisations where all previous shares remained intact, the general public shareholders had, on average, 85.37% preventable losses in the remaining thirty-two cases if the policy of the China Supreme People's Court could be adequately implemented. In particular, in twenty out of these thirty-two cases (62.5%), the losses of the general public shareholders could have been one hundred per cent avoided.