

**2013 OVERSEAS LAWYERS  
QUALIFICATION EXAMINATION**

**HEAD III: COMMERCIAL  
AND COMPANY LAW**

Friday, 15 November 2013



# HEAD III: COMMERCIAL AND COMPANY LAW

## TEST PAPER

15 November 2013

### Instructions to Candidates:

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

# 2013 Overseas Lawyers Qualification Examination

## Head III: Commercial and Company Law

### Question 1 (25 marks)

For the purpose of this Question, you should:

- (1) assume that the applicable articles of association is the current version of Table A;
- (2) fully explain your answers with reasons for each question (including where applicable the relevant legislative provisions and necessary steps involved).

**Answer the following questions:**

#### Part A

Your principal asked you to review the practice of the Corporate Secretarial Services Department of the firm (the “**Department**”) in which you have been working as a solicitor since September 2013 upon completion of your traineeship with the firm. You discovered that the amount of the authorised capital of most of the shelf companies set up by the Department is as low as HK\$10,000. Very often, a purchaser of a shelf company needs to increase the share capital immediately upon the purchase. You raised this with a senior executive of the Department but she was unable to tell you the reason.

- (a) Do you think the Department should continue with this practice?

(10 marks)

*(See over the page for a continuation of Question 1)*

## **Part B**

Oriental Gourmet Ltd. (the “**Company**”) is a private company incorporated in Hong Kong in 1996 by Mr. Chan and Mr. Wong. The authorised share capital of the Company is HK\$10,000,000 divided into 1,000,000 shares of HK\$10 each. All shares have been issued to Mr. Chan (60%) and Mr. Wong (40%) respectively. The two shareholders are also the only directors of the Company which operates three up-market Chinese restaurants in town.

In recent years, the profit margin of these restaurants has decreased significantly due to high rental and food costs and a weak economy. Mr. Chan believes that the Hong Kong market is somehow saturated and the Company should seek business opportunities in mainland China. He has formulated an initial business plan which involves the need to raise more share capital for the Company.

Two weeks ago, he proposed to convene a board meeting to increase the amount of the authorised capital of the Company to HK\$20,000,000 and to allot all new shares (the 1 million shares created by the increase of the share capital) to existing shareholders in the following manner:

Mr. Chan: 800,000 shares;

Mr. Wong: 200,000 shares.

After the allotment, Mr. Chan will hold 70% of the issued shares of the Company and Mr. Wong will become a 30% shareholder. The board meeting was held yesterday and Mr. Wong supported both the increase of the share capital and the allotment of new shares.

- (b) Advise Mr. Chan and Mr. Wong whether they can proceed to increase the share capital and allot the new shares on the basis of the board meeting.**

**(15 marks)**

**[25 marks in total]**

## Question 2 (25 marks)

Answer all parts of the following questions:

### Part A

- (a) Explain the major differences between a members' voluntary winding-up and a creditors' voluntary winding-up.

(6 marks)

### Part B

In January 2011, Kowloon Land Limited (“Landlord”) and SCTD Limited (“Tenant”) entered into a 5-year fixed-term lease of an office unit in Causeway Bay. The monthly rent is HK\$320,000. Since July 2012, the Tenant had persistently failed or neglected to pay rents until forced to do so. Seven warning letters have been issued by the Landlord’s solicitors. Evidence shows that the Tenant had been persistently paying the rents at the last possible moment (i.e. shortly before a writ was about to be issued) by recourse to loans made to it by others, including its directors, the directors’ spouses, and (occasionally) its subsidiary companies.

- (b) This morning the Landlord wrote to your firm: “...the Tenant has missed their rent payment again! The series of defaults by the Tenant are completely intolerable. Please investigate and advise whether we can push the Tenant into liquidation as soon as possible.” Discuss.

(7 marks)

*(See over the page for a continuation of Question 2)*

### **Part C**

During January to July 2012, the OLQE Bank Limited (“**Bank**”) advanced HK\$1m to Fido Company Limited (“**Fido**”) under an unsecured overdraft facility. On 10 August 2012, Fido executed a debenture containing a fixed charge over its book debts in favour of the Bank (“**Debenture**”).

Under the Debenture, Fido must deposit all the proceeds of the collected book debts into a designated account controlled by the Bank. On the first business day of each calendar month, Fido is allowed to transfer a maximum of HK\$300,000 (or 20% of the total amount of proceeds kept in the designated account, whichever is lesser) from the designated account to Fido’s general trading account. However, such right will be terminated immediately upon the occurrence of any event of default stipulated in the Debenture. The term “Secured Indebtedness” is defined as: “All amounts which may at any time in the future be or become due or owing, actually or contingently, from time to time to the Bank by Fido.”

On 1 September 2012, the Bank advanced HK\$2,000,000 to Fido. On 20 May 2013, the Bank appointed a receiver under the Debenture due to Fido’s failure to pay interest on the due date. Fido went into liquidation on 21 June 2013 upon the petition filed by an unsecured creditor. Evidence shows that between 20 May 2013 and 20 June 2013, the Bank’s receiver recovered HK\$900,000. Evidence also shows that Fido was solvent on 10 August 2012.

- (c) **Advise the Bank regarding the validity of the Debenture, and the proceeds collected by the receiver before Fido's liquidation.**

**(12 marks)**

**[25 marks in total]**

### **Question 3 (25 marks)**

**Answer the following questions:**

#### **Part A**

- (a) What are the regulatory objectives and functions of the Securities and Futures Commission (the “SFC”)?** (5 marks)

#### **Part B**

- (b) What activities carried on by a “licensed corporation” (as defined under the Securities & Futures Ordinance (“SFO”)) are regulated by the SFC?** (5 marks)

#### **Part C**

X is a “responsible officer” (as defined under the SFO), Y and Z are licensed representatives (Section 120 of the SFO) of a licensed corporation (Company XYZ) registered with the SFC to carry on the regulated activity of asset management. Upon the instruction of X, Y distributes advertisements to the general public in Hong Kong to offer to enter into an agreement to acquire securities.

- (c) Is this in breach of any provisions of the SFO?** (5 marks)

#### **Part D**

Z conducts trading activities on the shares of a company listed on the Stock Exchange of Hong Kong, by repeatedly cancelling his bid orders and re-inputting them at the same prices, thereby artificially inflating the share price by his fake bid orders. He then disposes of his entire shareholding in the company.

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

**(d) Is this in breach of any provisions of the SFO? If so, which provisions and what sanctions may be imposed against Z?**

**(5 marks)**

**Part E**

In order for Company XYZ to distribute investment funds to its customers, its employees should obtain information on the financial situation, investment experience and investment objectives of customers by performing an investor risk assessment questionnaire for each customer. However, some of the customers have not completed such questionnaire and some of the information obtained is either incomplete or outdated for at least 12 months.

**(e) Set out actions the SFC may take against Company XYZ.**

**(5 marks)**

**[25 marks in total]**



## Question 4 (25 marks)

### Part A

Godfrey's Wines Limited (the "Company") is a small company incorporated in Hong Kong, specialising in importing and distributing wines and spirits. It operates from a warehouse in Aberdeen and has two retail outlets, one in Kennedy Town and one in Sheung Wan. James and Godfrey are the two shareholders, owning 50% of the total shares each (each holding 50 shares of HK\$1 each). They are also directors. Approximately two years ago, James and Godfrey approached Esther to see if she was interested in joining the Company. Her wine knowledge and experience, together with her contacts with vineyards in Europe were attractive, and hiring Esther would give the Company the opportunity to expand its portfolio of wines. She agreed to join the Company only if she was offered a directorship and if she had a one-year notice period. Accordingly, Esther was duly appointed as a director, and her contract of employment contains a term to the effect that her employment and directorship could not be terminated by the Company on less than 12 months' notice.

Since Esther was taken on, the Company has shown moderate growth. However, the Company cannot grow further without more capital, since it cannot finance opening more retail outlets and expanding its portfolio of wines since most vineyards have minimum order requirements and each new line ties up significant amounts of working capital.

James and Godfrey have recently been approached by Grapes and Vines Limited, which is a large private company based in England. Grapes and Vines Limited is interested in acquiring a majority stake in the Company, by offering to buy some existing shares held by James and Godfrey and by subscribing for new shares and injecting subscription proceeds into the Company. In addition, Grapes and Vines Limited has access to many lines of wine which can be imported into Hong Kong but without the minimum order requirements imposed by vineyards.

*(See over the page for a continuation of Question 4)*

James and Godfrey told Esther of the approach by Grapes and Vines Limited and were excited to share this news. Esther's reaction though surprised them both. She said that she had worked at Grapes and Vines Limited many years ago and that she hates its management personnel. She said that, as a director of the Company, she would not allow a deal to go through in any circumstances.

James and Godfrey come to see you for advice. Putting aside the approach by Grapes and Vines Limited, they are now not comfortable in Esther being present at board meetings of the Company in which strategies, budgets, business plans and other confidential matters are discussed and decided upon.

The applicable articles of association is the current version of Table A.

**Answer the following questions:**

- (a) Can Esther prevent a deal with Grapes and Vines Limited, assuming that she remains a director of the Company? Explain your reasoning.**

**(2 marks)**

- (b) James and Godfrey want Esther to be removed from the board, but are concerned that they need to wait at least a year given the term in her employment contract. Describe to them in detail the procedure which they would need to follow to remove her as a director, and advise on the earliest possible time by which she can be removed from the board. Can they do this without having any meetings which involve Esther?**

**(8 marks)**

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

## **Part B**

Before entering into detailed discussions with Grapes and Vines Limited, James and Godfrey want to be paid a dividend. The last time they were paid a dividend was in March 2013. This dividend was by reference to the audited accounts for the financial year ended 31 December 2012, and they received the maximum possible amount the Company could lawfully pay. They now want to receive the maximum amount possible by reference to the trading period up to 30 September 2013.

**Answer the following questions:**

**(a) How is dividend that the Company can lawfully pay calculated?**

**(2 marks)**

**(b) Explain the procedure which needs to be followed in order for the Company to pay a dividend by reference to the trading period up to 30 September 2013.**

**(3 marks)**

## **Part C**

Grapes and Vines Limited has proposed a deal to James and Godfrey, which they have accepted. James and Godfrey will each sell 30 of their shares in the Company to Grapes and Vines Limited for a consideration of HK\$6,000,000 each. In addition, in order to finance further expansion of the Company, Grapes and Vines Limited will subscribe for a further 100 shares of HK\$1 each for a total subscription price of HK\$20,000,000. Grapes and Vines Limited will appoint 3 directors with effect from the date of completion of the deal. Grapes and Vines Limited has stated that, on the basis that it is financing expansion through its subscription for new shares, it is important to Grapes and Vines Limited that it has effective control over “operational” issues and decisions affecting the Company (e.g. hiring new staff, opening new retail outlets etc.). James and Godfrey agree to this. (Assume for the purposes of this Part that Esther is no longer a director and that James and Godfrey are the only two directors.)

*(See over the page for a continuation of Question 4)*

**Answer the following questions:**

- (a) Advise James and Godfrey what rights they will have as shareholders owning 20% of the total shares which would be in issue.**

**(3 marks)**

- (b) Advise James and Godfrey what protection they should look for in a shareholders' agreement (assuming James' and Godfrey's agreement to Grapes and Vines Limited having control over "operational" issues).**

**(7 marks)**

**[25 marks in total]**

## Question 5 (25 marks)

**Answer the following questions:**

Quinn Property Development Limited (“**Listco**”), a company whose shares are listed on the Hong Kong Stock Exchange, has entered into an agreement to sell Navarone Tower (the “**Property**”) which Listco holds through a wholly-owned subsidiary called Quayle Investment Holding Limited (“**Subco**”) for HK\$200 million.

Listco’s CEO has sent you the following information about Listco and Subco.

With regard to Listco –

- Consolidated total assets: HK\$5 billion (5,000,000,000)
- Issued share capital: 2 billion shares
- Average closing price: HK\$4.00
- Revenue: HK\$3 billion
- Profits: HK\$300 million

With regard to Subco –

- Total assets: HK\$200 million
- Book value of Property: HK\$90 million
- Revenue: HK\$200 million
- Profits: HK\$20 million

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

**Questions:**

**Listco's CEO wishes to know whether the sale of Subco is a notifiable transaction under the Listing Rules and, if yes, which type? In providing your advice:**

- (a) Give a brief description of the different types of notifiable transactions under the Listing Rules.**

**(5 marks)**

- (b) Set out the different tests and ratios in determining the different types of notifiable transactions.**

**(5 marks)**

- (c) Using the above information, make calculations under each test to determine whether the sale of Subco is a notifiable transaction under the Listing Rules and, if yes, which type?**

**(10 marks)**

- (d) Once you have determined what type of notifiable transaction the proposed sale of Subco falls into, advise what procedural requirements Listco needs to follow.**

**(5 marks)**

**[25 marks in total]**

**END OF TEST PAPER**