

PCLL CONVERSION EXAMINATION JANUARY 2022

Title of Paper : Business Associations
Date : 12 January 2022
Time : 9:30 a.m. – 9:45 a.m. (Reading Time)
9:45 a.m. – 12:45 p.m.

Instructions

1. Write your **candidate number** on the cover of each answer book. Do **NOT** write your name in the answer book.
2. Start each answer on a separate page of the answer book.
3. Write your answers only in the answer books provided.
4. This is a three-hour examination.
5. This is an open book examination.
6. Reading time for this paper is 15 minutes. Do **NOT** begin writing in your answer books during this period until you are instructed to do so.
7. This paper consists of 3 pages, including Part A and Part B. A total of 300 marks may be awarded.
8. Part A contains two compulsory questions. Candidates must answer **ALL** questions. There is **NO** element of choice. Part A is worth 200 marks.
9. Part B contains two questions. Candidates are only required to answer **ONE** question out of two. Part B is worth 100 marks.
10. The passing mark for this paper is 150 marks.

**DO NOT OPEN THIS QUESTION BOOK
UNTIL YOU ARE TOLD TO DO SO**

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Business Associations

Part A (answer **BOTH** Question 1 and Question 2)

Question 1 (100 marks)

DEF Ltd (“DEF”) is a wholly owned subsidiary of ABC Company Ltd (“ABC”). Both DEF and ABC are private companies incorporated in Hong Kong. ABC was founded by Jones. He is the sole shareholder and director of ABC. He is also the only director of DEF and runs the day-to-day operations of DEF with the assistance of Peter who serves as the general manager of ABC.

DEF operates a restaurant in Central but does not own any substantial assets. ABC owns the property where the restaurant is operated and leased it to DEF. Everyone working at the restaurant (including Peter) is employed by ABC. In addition, any profit made by DEF has been consistently distributed to ABC as dividends. From time to time, DEF also pays the expenses of ABC, such as paying the ABC’s office rent to ABC’s landlord.

- a) Mary visited the restaurant one day and got seriously sick when she found a decomposed snail in her ginger ale. Just when Mary is prepared to sue DEF for negligence, she finds out about DEF’s lack of assets. Can Mary sue ABC instead? **(50 marks)**

- b) More recently, Peter wants to leave ABC and start its own company (“NewCo”). However, in his employment contract with ABC, there is a restrictive covenant prohibiting him from competing with ABC. Peter now plans to get his sister, Carrie, to be the sole shareholder and director of NewCo, though he will still make all the corporate decisions and operate the new business. Can ABC enjoin NewCo from conducting the competing business if Peter carries out his plan? **(50 marks)**

Question 2 (100 marks)

Adrian, Bruce and Cathy founded Best Hotel Limited (“BHL”), a private company incorporated in Hong Kong, in 2015. BHL runs a luxurious hotel in Shatin. Adrian is the majority shareholder, owning 60% of BHL’s shares. Bruce and Cathy each owns 20% of the shares. All of them are directors of BHL. Prior to working in the hotel business, Bruce was a licensed real estate agent who worked on the sale and purchase of commercial properties in Hong Kong for more than ten years.

In 2020, BHL saw a market in budget hotel due to an increase in demand of such hotels driven by the mandatory quarantine requirement for travelers coming to Hong Kong. Bruce was authorized by the Board of Directors to negotiate the purchase of a building in Hung Hom. The plan was to transform it into a new hotel. However, despite Bruce’s experience as a real estate agent, he

substantially overvalued the building and caused BHL to purchase it at a price that was 50% over the market value.

Meanwhile, Sebastian, a prominent investor in Hong Kong, approached Cathy to join him in starting a new online apartment rental business. Without telling Adrian and Bruce, Cathy agreed and started that new business which has proven to be a huge success subsequently.

Advise BHL regarding its potential recourse against Bruce and Cathy under company law.

Part B (answer **EITHER** Question 3 or Question 4)

Question 3 (100 marks)

Trusted One Co. Limited is a private company in Hong Kong and has been running a car rental business since 1988. In 2019, Trusted One entered into an unsecured HK\$50 million loan agreement with Bank Two to finance the opening of multiple new branches in Hong Kong (the “Loan”).

However, the expansion was a failure. When the Loan was due in August 2021, Trusted One failed to pay. Upon further negotiation, Bank Two agreed to extend the repayment date to the end of 2021 on the condition that Trusted One granted a fixed charge over all its core assets in favor of Bank Two. A fixed charge was created on August 31, 2021 and duly registered thereafter.

Trusted One’s business showed no sign of recovery. At the end of 2021, Trusted One failed again to repay the Loan on the extended repayment date. Bank Two petitioned for a compulsory winding up against Trusted One on January 31, 2022.

Yamato Tire is one of the unsecured creditors of Trusted One. However, Trusted One is unlikely to have any assets beyond the charged assets. Is it possible for unsecured creditors like Yamato Tire to improve their potential recovery in Trusted One’s insolvency?

Question 4 (100 marks)

In the judgment of *Waddington Limited v Chan Chun Hoo Thomas*, it is said that “[t]he co-existence of both the statutory and common law regimes... is a source of confusion and complication. It would appear to be appropriate for the statutory regime to replace the common law derivative action altogether”. Critically assess this statement.

~ End of Examination Paper ~