

PCLL CONVERSION EXAMINATION JANUARY 2021

Title of Paper : Business Associations
Date : 6 January 2021
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 5 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**

PCLL Conversion Examination January 2021

Business Associations

Part A (answer BOTH Question 1 and Question 2)

Question 1 (100 marks)

Jane has been providing private French tutorial lessons on a part time basis since 2015. Recently, Jane is contemplating setting up her own French tutorial school and her best friend, Sandy, is very supportive of Jane's new plan. Sandy owns substantial assets and is considering investing in Jane's new French tutorial school if such school requires additional financing. However, since Sandy is working full time, she does not want to actively participate in the management but would like to join as a passive investor only.

Jane and Sandy are considering which of the following three forms of business vehicle would best suit their business plan namely:

- (a) limited liability company
- (b) general partnership and
- (c) limited partnership.

Consider these three forms of business vehicles and advise Sandy as an investor what is her potential liability in respect of debts of the business and her right to participate in management for each of these three forms of business vehicles.

Question 2 (100 marks)

Kingston Bookstore Limited ("KBL") was incorporated in 2015. KBL runs a book shop in North Point since 2015 on rented premises; however, in the past 2 years, KBL did not do well in business due to high operating costs. The only valuable asset owned by KBL is an office unit in the Western District which is not subject to any mortgage.

In May 2019, KBL obtained a 36-month term loan of HK\$5 million from SAR Bank (the "Bank") on an unsecured basis. KBL managed to repay the monthly instalments to the Bank until March 2020 when it started having cash flow problems.

In April 2020, KBL received a statutory demand from the Bank threatening to resort to winding up proceedings if KBL did not comply with the statutory demand. After several rounds of negotiations between the Bank and the directors, it was clear to the Bank that KBL was not in a position to make any repayment. The outstanding loan owing to the Bank as at 30 April 2020 was HK\$2.5 million. The Bank believed that if KBL was put into liquidation, the Bank might only recover a small portion of the outstanding loan. Thus the Bank agreed to give KBL more time to repay the loan but insisted that KBL should execute a fixed charge (over the office unit in the Western District) in favour of the Bank as security for the repayment of the existing loan. If KBL refused to take this arrangement, the Bank would proceed to present a winding up petition against KBL. As a result, KBL executed the fixed charge on 20 May 2020. This charge was duly registered at the Companies Registry and Land Registry on 31 May 2020.

On 3 June 2020, a creditor of KBL presented a winding up petition against KBL on the ground that it was insolvent and unable to pay its debt. A winding up order was accordingly made on 3 December 2020.

Advise the liquidator whether he can challenge the validity of the fixed charge.

Part B (answer EITHER Question 3 or Question 4)

Question 3 (100 marks)

Fook Yuen Limited (“FYL”) is a private company limited by shares incorporated in Hong Kong. FYL’s main business is investment in commercial buildings for capital appreciation and rental income. FYL owns a number of commercial properties in Kowloon Tong and Shatin.

Simon is the sole shareholder and director of FYL. Simon and Elizabeth recently divorced and Simon was ordered by the Court to pay a substantial sum to Elizabeth. Simon had no money and personal assets to pay such sums. Elizabeth now seeks execution against assets of FYL, arguing that Simon’s liability can be met with FYL’s assets.

Advise whether the Court could lift the corporate veil and order FYL to pay the dues owed by Simon to Elizabeth. What additional information do we need to find out? What are the circumstances in which the corporate veil will be lifted?

Question 4 (100 marks)

Charterhouse Limited (the “Company”) is a Hong Kong private limited company which specializes in the sale of expensive handbags and accessories.

Betty, Melody and Ann are the shareholders of the Company and their respective shareholdings are 40%, 40% and 20%. In addition, Elephant Courier, which is owned by Eddie, is responsible for delivering goods for the Company.

Since Eddie has never entered into any contract, written or oral, with the Company for providing the delivery services for the Company, in order to safeguard Eddie’s interests as well as the shareholders’ interest in the Company, the following clauses were inserted into the Company’s articles:

- (i) Elephant Courier is to be the sole courier for delivering goods for the Company.
- (ii) In the event of a shareholder wishing to leave the Company, such shareholder should first offer her shares to the other shareholders who are bound to purchase the shares at such sum to be determined by the auditors of the Company.

By early 2020, due to a decreasing number of tourists, the Company’s business started to deteriorate. In order to save costs, all shareholders agreed and instructed a cheaper delivery and courier service provider to provide courier services for the Company.

Recently, Ann has opened a retail outlet in Hong Kong selling lady accessories including handbags. Betty is extremely angry about this and she believes that this is the main reason why Ann is no longer interested in the affairs of the Company and blames the deterioration of the Company’s business on Ann.

Betty has since become frustrated with Ann and intends to evict her from the Company. Betty attempts to incorporate into the Company’s articles, a clause that any shareholder who competes with the Company could have her shares acquired by the majority.

Alternatively, Betty wants to quit and sell all her shares in the Company to Ann and Melody. However, both Ann and Melody have refused to take up Betty’s shares.

Advise the parties. (Candidates are not required to discuss any action for unfair prejudice under s724 of the Companies Ordinance (Cap 622))

~ End of Examination Paper ~