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**SUMMATIVE (FORMAL) ASSESSMENT: MODULE 3A**

**THE INSOLVENCY SYSTEM OF THE UNITED STATES**

This is the **summative (formal) assessment** for **Module 3A** of this course and is compulsory for all candidates who **selected this module as one of their compulsory modules from Module 3**. Please read instruction 6.1 on the next page very carefully.

If you selected this module as **one of your elective modules**, please read instruction 6.2 on the next page very carefully.

**The mark awarded for this assessment will determine your final mark for Module 3A**. In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

**INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT**

**Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.**

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.

2. All assessments must be submitted electronically in MS Word format, using a standard A4 size page and a 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way**. **DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.

3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).

4. You must save this document using the following format: **[student number.assessment3A]**. An example would be something along the following lines: 202021IFU-314.assessment3A. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentnumber” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked**.

5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words**.

6.1If you selected Module 3A as one of your **compulsory modules** (see the e-mail that was sent to you when your place on the course was confirmed), the final time and date for the submission of this assessment is **23:00 (11 pm) GMT on 1 March 2021**. The assessment submission portal will close at 23:00 (11 pm) GMT on 1 March 2021. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.

6.2 If you selected Module 3A as one of your **elective modules** (see the e-mail that was sent to you when your place on the course was confirmed), you have a **choice** as to when you may submit this assessment. You may either submit the assessment by **23:00 (11 pm) GMT on 1 March 2021** or by **23:00 (11 pm) BST on 31 July 2021**. If you elect to submit by 1 March 2021, you **may not** submit the assessment again by 31 July 2021 (for example, in order to achieve a higher mark).

7. Prior to being populated with your answers, this assessment consists of **8 pages**.

**ANSWER ALL THE QUESTIONS**

**QUESTION 1 (multiple-choice questions) [10 marks in total]**

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and mark your selection on the answer sheet by highlighting the relevant paragraph **in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

**Question 1.1**

FabCo, based in Utah, owes SupplyCo, based in Mexico, US$10,000 on a past-due invoice. May SupplyCo file an involuntary petition to place FabCo into chapter 11 bankruptcy proceedings?

1. Yes.
2. Yes, if FabCo has fewer than 12 non-contingent, non-insider creditors.
3. Yes, if other creditors owed at least US$5,775 join in the petition.
4. No, because SupplyCo doesn’t know whether FabCo is insolvent.
5. No, because SupplyCo is not a US company.

**Question 1.2**

Which of the following is a *mandatory*, rather than *discretionary*, basis to deny recognition of a foreign judgment under state law based on one of the Uniform Acts?

1. The foreign judgment is subject to appeal in the foreign country.
2. The foreign judgment is an injunction.
3. The foreign judgment was issued by a court, contrary to the parties’ agreement to arbitrate.
4. The defendant did not have sufficient notice of the foreign proceeding to put on a defense.
5. The foreign judgment is inconsistent with another final judgment on the same subject matter.

**Question 1.3**

Which of the following is likely to be a party in interest in the bankruptcy of XYZ Corp?

1. A shareholder in ABC Corp, to which XYZ Corp is substantially indebted.
2. A journalist writing about XYZ Corp’s bankruptcy.
3. A shareholder in MNO Corp, which owns all of XYZ Corp’s shares.
4. A retired employee of XYZ Corp who receives payments from the company’s pension plan.
5. A non-profit organization that advocates for companies like XYZ Corp to be held responsible for climate change.

**Question 1.4**

If a debtor rejects an executory trademark license agreement under which it licenses a trademark to its counterparty, which of the following is true:

1. The counterparty must immediately stop using the trademark.
2. The counterparty can continue using the trademark for the remaining period of the license.
3. The counterparty has a claim for damages for breach of contract.
4. Both (a) and (c).
5. Both (b) and (c).

**Question 1.5**

In which of the following circumstances may a counterparty enforce a contractual *ipso facto* clause?

1. The contract would obligate the counterparty to extend a loan to the debtor.
2. The contract is a lease of real property.
3. The clause is triggered by the bankruptcy filing of a third party, not the debtor.
4. Both (a) and (c).
5. *Ipso facto* clauses are never enforceable against a debtor.

**Question 1.6**

What does a chapter 11 debtor have exclusivity to propose for the first 120 days of proceedings?

1. Avoidance actions.
2. A plan of reorganization.
3. DIP financing.
4. Lifting the automatic stay.
5. Formation of an equity committee.

**Question 1.7**

Which of the following is **not** a requirement to confirm a “cramdown” plan?

1. Acceptance of the plan by all classes of secured creditors.
2. Acceptance of the plan by at least one class of impaired, non-insider creditors.
3. The plan is fair and equitable to dissenting classes of creditors.
4. The plan does not discriminate unfairly against dissenting classes of creditors.
5. The dissenting creditors receive no less than they would under a liquidation scenario.

**Question 1.8**

When may distributions to creditors diverge from the absolute priority rule?

1. In a chapter 7 proceeding with consent of the affected senior creditor.
2. In a chapter 7 proceeding with consent of the affected junior creditor.
3. In a chapter 11 proceeding with consent of the affected senior creditor.
4. In a chapter 11 proceeding with consent of the affected junior creditor.
5. The absolute priority rule cannot be deviated from.

**Question 1.9**

Who may serve as a foreign representative to seek recognition of a foreign proceeding under chapter 15?

1. An officer of the debtor if it is a debtor-in-possession in the foreign proceeding.
2. The board of directors of the debtor if it is a debtor-in-possession in the foreign proceeding.
3. An insolvency professional appointed by the court overseeing the foreign proceeding.
4. An insolvency professional appointed by a creditor where the foreign proceeding is an involuntary receivership.
5. All of the above.

**Question 1.10**

Which of the following is *not* available as relief in a chapter 15 proceeding?

1. Sale of US property free and clear pursuant to section 363.
2. Prosecution of avoidance actions pursuant to section 544 .
3. Entrusting the management of US assets to the foreign representative.
4. Application of the automatic stay under section 362 to the debtor’s interests in US property.
5. Discovery about the debtor’s assets.

**QUESTION 2 (direct questions) [10 marks]**

**Question 2.1 [maximum 1 mark]**

What two alternative qualifications render a corporation eligible to be a debtor in a US chapter 7 or 11 proceeding?

To be considered as a debtor under any chapter of the Bankruptcy Code of the US, a minimum requirement has to be met, which can be either the presence of the debtor or its place of business or any of its assets in the US.

As explained in the Guidance Text, there are some exceptions for which certain companies cannot be considered debtors under chapter 7 (railroads, insurance companies, banks and certain other financial institutions), since there are special liquidation procedures for these entities under other state and federal laws.

With respect to article 11, the eligibility is a little broader (railroads and certain types of financial institutions could be considered as debtors under this article). However, stockbrokers and commodity brokers can’t be eligible in chapter 11, while they could be chapter 7 debtors.

**Question 2.2 [maximum 2 marks]**

What is an executory contract?

As it is mentioned in the Guidance Text, the concept of “executory contract” it is not defined by statue, but it has been given meaning through case- law.

For these purposes, the courts have followed the definition established by Professor Vern Countryman of Harvard Law School (known as “*countryman test*”).

Following the “*Countryman test*”, an executory contract is one "*under which the obligations of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performlillce would constitute a material breach excusing the performance of the other*[[1]](#footnote-1)."

The reasoning underlying this power is that the trustee or debtor in possession should be insulated from contracts that impose onerous obligations on the bankruptcy estate, but should also be able to benefit from favorable contracts.

This power to assume or reject executory contracts is especially important in cases of reorganization cases where it is used to relieve the debtor-in-possession of unperformed obligations that otherwise hinder the debtor's opportunity for a fresh start.

**Question 2.3 [maximum 2 marks]**

What is a “priming lien” and what requirements must be met for such a lien to be granted to secure DIP financing?

A priming lien is a concept that operates in the debtor- in- possession sphere and it implies that the court may grant a post- petition credit extension that is senior or equal to a pre- petition lien on state property to secure post- petition financing.

In order for the court to authorize a priming lien, the following requirements must be met:

1. A debtor must show that it is unable to obtain credit otherwise and
2. The existing lienholder’s interest in its collateral is adequately protected notwithstanding the grant of the priming lien.

**Question 2.4 [maximum 2 marks]**

In voting on a plan of reorganization, which class(es) of creditors are (i) deemed to accept the plan, (ii) deemed to reject the plan and (iii) permitted to vote on the plan? What vote is necessary for a class of creditors to accept a plan?

1. An unimpaired class is more likely to accept the plan.
2. However, a class that will receive nothing will deemed to reject the plan.
3. Impaired classes are the only ones entitled to vote on the plan// As explained in the Guidance Text, a specific class of creditors requires a simple majority of the creditors in the class to approve the plan, which hold at least two-thirds of the value of the claims in the class, vote in favour or, for equity interests, if two- thirds in amount of interests vote in favour.

**Question 2.5 [maximum 3 marks]**

How does the automatic stay available in chapter 15 proceedings differ from that available in chapter 11 proceedings?

One of the key points of Chapter 11 is that the voluntary petition is opened immediately, imposing a statutory automatic stay for creditors.

However, in a case under chapter 15, a filing of the petition itself does not automatically imply a stay of the creditor's action. As it is explained in the Guidance text, under this chapter, the stay arises only upon petition for recognition of the grant of a foreign main proceeding and it is limited to the debtor's property within the territorial jurisdiction of the United States. The Bankruptcy Court may grant a stay or other or other relief on an interim basis pending recognition or upon recognition of a non-main proceeding.

The requirements for determining whether or not to grant interim relief are the same as those applicable to request for an injunction. These are:

* Likelihood of success on the merits.
* Risk of irreparable harm.
* Balancing of the equities.
* Public interest.

**QUESTION 3 (essay-type questions) [15 marks in total]**

**Question 3.1** **[maximum 3 marks**]

What fiduciary duties do directors of Delaware corporations owe and to whom are the duties owed in the ordinary course of business? To whom are duties owed when the corporation is potentially or actually insolvent?

As referred to in the guide text, director liability is a matter for state law of the state of incorporation, with Delaware being the preeminent US jurisdiction for corporate law. Under Delaware law, corporate directors have the following duties:

* Fiduciary duty of loyalty to the corporation’s best interest.
* Duty of care in educated decision-making.

These duties are owed to the corporation and its shareholders, but not to creditors, even though where the corporation is potentially insolvent and, thus, the shareholders stand to receive nothing in bankruptcy.

The Delaware Supreme Court has settled any suggestion that directors have obligations to creditors when a company is operating "in the zone of insolvency", or is in fact insolvent.

Specifically, this issue was addressed in *North Am Catholic Educational Programming Foundation, Inc v Gheewalla, 930 A.2d 92, 103 (Del 2007)* case, where the Delaware Supreme Court stated the following:

*“[I]ndividual creditors of an insolvent corporation have no right to assert direct claims for breach of fiduciary duty against corporate directors. Creditors may nonetheless protect their interest by bringing derivative claims on behalf of the insolvent corporation or any other direct nonfiduciary claim....”*

As a result, there is no equivalent under US law of the concept of wrongful trading or deepening insolvency.

**Question 3.2 [maximum 3 marks]**

Describe the circumstances in which a bankruptcy court may enter a final order, who reviews appeals from bankruptcy court orders and how non-final orders are reviewed.

1. **Circumstances in which a bankruptcy court may enter a final order**

The law establishes a distinction between "core" and "non-core" matters, with bankruptcy judges being able to hear and resolve only core proceedings. The statute contains a non-exhaustive list of core proceedings, which include the following:

*“(A) matters concerning the administration of the estate;*

*(B) allowance or disallowance of claims against the estate or exemptions from property of the estate, and*

*estimation of claims or interests for the purposes of confirming a plan under chapter 11, 12, or 13 of title*

*11but not the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death*

*claims against the estate for purposes of distribution in a case under title 11;*

*(C) counterclaims by the estate against persons filing claims against the estate;*

*(D) orders in respect to obtaining credit;*

*(E) orders to turn over property of the estate;*

*(F) proceedings to determine, avoid, or recover preferences;*

*(G) motions to terminate, annul, or modify the automatic stay;*

*(H) proceedings to determine, avoid, or recover fraudulent conveyances;*

*(I) determinations as to the dischargeability of particular debts;*

*(J) objections to discharges;*

*(K) determinations of the validity, extent, or priority of liens;*

*(L) confirmations of plans;*

*(M) orders approving the use or lease of property, including the use of cash collateral;*

*(N) orders approving the sale of property other than property resulting from claims brought by the estate*

*against persons who have not filed claims against the estate;*

*(O) other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtorcreditor*

*or the equity security holder relationship, except personal injury tort or wrongful death claims;*

*and*

*(P) recognition of foreign proceedings and other matters under chapter 15 of title 11.”*

With respect to non-core proceedings, the bankruptcy court may hear these if they are sufficiently related to a bankruptcy proceeding, but it cannot make a final decision.

Rather, it submits proposed findings of fact and conclusions of law to the district court, to which interested parties may object, for final decision by the district court. At the beginning of each motion or pleading, the parties must indicate whether or not the matter at issue is material so that the bankruptcy court can determine the scope of its jurisdiction and its power to enter a final order or judgment.

Besides, as explained in the Guidance text, the referral statute also provides a procedure by which a district court may withdraw the reference of its jurisdiction to bankruptcy court at its discretion. Therefore, this permits matters that have been automatically referred to the bankruptcy court under a general order of reference to be returned to and heard by the district court. If the action raises substantial questions under federal law other than the Bankruptcy Code, the referral must be withdrawn.

The courts have ruled on several occasions on the competence of the bankruptcy courts.

Specifically, in *Stern v Marshall* case the US Supreme Court hold that a bankruptcy court cannot invade Article III jurisdiction even in core proceedings (this case referred to the bankruptcy court’s exercise of final judgment power over a state law claim, which was decided to be unconstitutional under Article III).

1. **Appeals**

The orders that can be appealed are final orders (those that dispose of all issues) and interlocutory orders (those that resolve only dome ussies or claims). Final orders can be appeal as of rights, while interlocutory order may be appealed only with leave of the appellate court. The framework also applies with regard to insolvency proceedings.

Generally speaking, appeals from bankruptcy court decisions are heard by the District Court in their area. In this way, the first appeal of a bankruptcy case will be given to a randomly appointed judge, who will generally hear all future appeals of these bankruptcy proceedings.

However, in some circuit courts, bankruptcy appeals are heard by the Bankruptcy Appeals Panel (BAP), which is convened by bankruptcy court judges in the circuit courts. In these circuits, one of the parties may choose to request that the be heard by the District Court. From the District Court or BAP, there is a further appeal of rights (assuming the original order is an available order to appeal rights).

In rare cases, appeals from the bankruptcy court can be directly submitted to the

Court of appelas, where the bankruptcy court or the district court proves the following:

1. the appeal raises a question of law as to which there is no controlling decision of the circuit or the US Supreme Court, or requires resolving conflicting controlling decisions, or
2. immediate appeal may materially advance the progress of the case.

In these cases the court of appeals has discretion whether to accept it or not.

**Question 3.3 [maximum 4 marks]**

Describe how claims for recovery of preferences, fraudulent conveyance and constructive fraudulent conveyance differ.

1. **Preferences**

The Guidance text provides the following definition of “preferences”:

*“A preference is a transfer of the debtor’s property made in a suspect period before*

*the petition date that must be returned to the estate if it exceeds the amount the*

*recipient would have received in a chapter 7 liquidation had the transfer not been*

*made”.*

The avoidance of this figure aims to treat in a similar way those creditors that are situated in a similar range or position, as well as disincentivize a race to collect from a debtor experiencing economic hardship.

The elements of preferences claims are the following:

1. A transfer if an interest of the debtor in property.
2. To or for the benefit of a creditor.
3. For or on account of an antecedent debt owed by the debtor before such transfer was made.
4. Made while the debtor was insolvent.
5. Made during the suspect period.

* Third parties: 90 days prior to the petition date.
* Insiders: one year prior to the petition date.

1. That enables the creditor to receive more than it would have in a chapter 7 liquidation.
2. **Fraudulent coveyances**

The main difference between preferences and fraudulent conveyance is that a preference is aimed largely at transactions immediately prior to bankruptcy, while fraudulent coveyances is made within two years before the filing of the bankruptcy petition. We can find two types of fraudulent coveyances:

* Actual fraudulent coveyances

The Guidance text provides that:

*An actual fraudulent conveyance**is proven by showing that the debtor made a*

*transfer or incurred an obligation “with actual* ***intent*** *to hinder, delay, or defraud any entity to which the debtor was or became . . .* ***indebted****.”*

The two main elements to pay attention two in this case are the “*actual intent*” and the indebtedness.

For the above purposes, a debtor may expect to become “**indebted**”, when it anticipates liability under a money judgment, settlement, penalty or similar obligation arising from violation of state or federal securities laws or fraud, deceit, or manipulation in the sale of a registered security.

Intent may be proven circumstantially, by reference to “badges of fraud” developed in state fraudulent transfer law, which are the following:

* 1. *the transfer or obligation was to an insider;*
  2. *the debtor retained possession or control of the property transferred after the transfer;*
  3. *the transfer or obligation was disclosed or concealed;*
  4. *before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit;*
  5. *the transfer was of substantially all the debtor’s assets;*
  6. *the debtor absconded;*
  7. *the debtor removed or concealed assets;*
  8. *the value of the consideration received by the debtor was not reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred;*
  9. *the debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred;*
  10. *the transfer occurred shortly before or shortly after a substantial debt was incurred; and*
  11. *the debtor transferred the essential assets of the business to a lienor that transferred the assets to an insider of the debtor.*
* Constructive fraudulent conveyance

While the actual fraudulent conveyance involves the intent to defraud creditors, the constructive fraudulent conveyance involves a transfer, which is made in exchange for manifiestly inadequate consideration.

In accordance with the above, a constructive fraudulent conveyance is proven by showing that the debtor received less than reasonably equivalent value in exchange for a transfer or

incurrence of obligation. In addition, one of the following additional factors was present:

* + - the debtor was insolvent at the time of or became insolvent as a result of the transaction;
    - the debtor was unreasonably undercapitalized for the business or transactions it was engaged in or planned to engage in;
    - the debtor intended to or believe it would incur debts beyond its ability to pay on maturity; or
    - the transfer was made to or for the benefit of an insider, or the debtor incurred an obligation under an employment contract with an insider outside the ordinary course of business.

**Question 3.4 [maximum 5 marks]**

How does a US bankruptcy court determine whether a foreign proceeding is a main or non-main proceeding under chapter 15?

Whether a proceeding is a main or non-main under Chapter 15 is determined by where the company's centre of main interests ins based.

To these effects, foreign main proceedings will be those that are commenced in the debtor’s center of main interests (COMI).

As it is explained in the Guidance Text, COMI is a concept foreign to US law, which as usually uses the concepts of domicile, principal place of business, and location of assets in determining jurisdiction and venue.

In relation to the foregoing, the court has ruled in Morning Mist Holdings Ltd v Krys case, stating the following:

“*In a nutshell: for a proceeding to be recognized as a “foreign main proceeding,” it must be “pending in the country where the debtor has the center of its main interests.” 11 U.S.C. § 1517(b)(1). That determination is based on a debtor’s COMI at the time the Chapter 15 petition is filed. A court may look at the period between the commencement of the foreign proceeding and the filing of the Chapter 15 petition to ensure that a debtor has not manipulated its COMI in bad faith, but there is no support for Morning Mist’s contention that a debtor’s entire operational history should be considered. The factors that a court may consider in this analysis are not limited and may include the debtor’s liquidation activities.”*

Thus, a debtor’s COMI is presumed to be its place of incorporation, but this is rebuttable. The most relevant factors in the COMI analysis are:

* location of headquarters;
* location of management;
* location of primary assets;
* location of a majority of debtor’s creditors or a majority of the creditors that will
* be affected by the relief requested by the foreign representative; and
* jurisdiction whose law will apply to most disputes.

A debtor’s COMI should be ascertainable by its creditors or other third parties on the basis of objective evidence. At this point it is relevant *In re SPhinX, Ltd* case, where the judge confirmed this need for the COMI to be ascertaible for third parties on the basis of the EU regulation.

On the other hand, proceedings in a jurisdiction other than the debtor’s COMI can be recognized as foreign non-main proceedings ONLY if the debtor had an establishment in the jurisdiction (a place where it carried out non-transitory economic activity) prior to the commencement of chapter 15 proceedings.

In relation to the above, the guidance text presents the Bear Stearns case, where the US bankruptcy court held that the Cayman Islands could not be the COMI for a Cayman-incorporated hedge fund because the fund was an “exempt” company, licensed on the basis that it would not have operations in the Cayman Islands.

The Bankruptcy Court also ruled that the Cayman Islands liquidation proceedings did not qualify as foreign nonmain proceedings, based on the conclusion that the Funds do not have an "establishment" in the Cayman Islands within the meaning of Chapter 15.

**QUESTION 4 (fact-based application-type question) [15 marks in total]**

**Question 4.1 [maximum 5 marks]**

Rental Corporation is a publicly-traded company that leases office space from office building owners and sublets the space to small businesses. It has recently announced that it is being investigated by the US Department of Justice Fraud Division (DOJ) regarding allegedly fraudulent misstatements of revenues; shortly after the announcement, a securities class action litigation was filed against Rental Corporation in New York federal court. Due to the increase in the numbers of businesses operating remotely, Rental Corporation has suffered a decline in revenues. As a result, it has failed to pay rent on some of its office space leases and it has just defaulted on its quarterly payment on its credit facility. What would be the effect of a chapter 11 petition being filed by Rental Corporation on each of (i) the DOJ investigation, (ii) the securities class action litigation; (iii) the delinquent leases and (iv) the credit facility?

* + - 1. DOJ Investigation: this is one of the exemptions to which the automatic stay is subjected, so the automatic stay wouldn’t apply.
      2. Securities class action litigation: the litigation on pre- pretition claims is subjected to the automatic stay. However, Nevertheless, the exercise of rights under security contract is another of the statutory exceptions provided.
      3. Delinquent leases: the automatic stay would apply.
      4. Credit facility: in this case, the lender may pursue payment from Rental Corporation. As it has been explained in the Guidance Text, *ipso facto* clauses are given no effect only where they are asserted against a debtor with respect to its own filing or financial condition. The issuer of an unconditional guarantee cannot assert the debtor’s own defences to the debt.

**Question 4.2 [maximum 5 marks]**

Considering the facts set forth in Question 4.1, what protections does the Bankruptcy Code provide to lessors of office space to Rental Corporation?

1. In this case, the Bankruptcy Code provides for a relief from the stay through a lift-stay or relief from stay motion if a lack of protection is proved. This circumstance may occur if the value of the property may decrease during the proceedings with the consequence that the creditor does not recover the full amount of the claim.
2. The debtor has no equity in the property and it is not necessary for reorganization. As mention above, it will be necessary for the creditor to prove that his interest is greater than the value of the property.

In addition to these, as explained in the Guidance Text, the court may terminate the automatic stay as of a given future date, annul the stay retrospectively, modify the stay to permit specific act (a given example of this is to file a lawsuit against the debtor to avoid lapsing of statute of limitations) or condition the continuance of the stay on the debtor’s compliance with a condition to protect the affected party’s interest in the property (in this case, the lessor), in each case for cause shown.

**Question 4.3 [maximum 5 marks]**

Paint Corporation formulates house paint according to proprietary and patented recipes at its factory in the United States, which it sells to home improvement stores under a number of distribution contracts. The US Environmental Protection Agency is investigating whether Paint Corporation’s operations are causing harmful chemicals to contaminate a nearby river. Paint Corporation is concerned it cannot afford the clean-up that may be required and is seeking to sell its business. Home Corporation is interested in buying the business, but does not want the potentially contaminated property (it can manufacture paint at its own factory) and is concerned about obtaining consent from all the home improvement stores to assign the distribution contracts. How would a sale under section 363 of the Bankruptcy Code address these issues?

Through a 363 sale, the debtor can sell its property in the ordinary court of business without court or creditor interference and he also can sell it free and clear of creditor interests with court approval.

Regarding obtaining the consent from the home improvement stores to assign the distribution contracts, we have to bear in mind that the debtor can transfer its interests in key contracts that are required to operate the business, even where they obtain contractual restrictions on assignment or purport to terminate upon bankruptcy filing. One exception to this are licenses of patents and copyrights owned by the debtor, which are protected so that licenses can’t be terminated in connection with the sale of the intellectual property without their consent.

**\* End of Assessment \***

1. <https://scholarlycommons.law.hofstra.edu/cgi/viewcontent.cgi?article=1998&context=faculty_scholarship> [↑](#footnote-ref-1)