



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.**
- 6.1 If 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

Commented [A&O1]: Total marks 35.5/50

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

Commented [A&O2]: Total marks 7/10

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

Commented [A&O3]: Correct, 1 mark

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?

- (a) Yes.
- (b) Yes, if FabCo has fewer than 12 non-contingent, non-insider creditors.
- (c) Yes, if other creditors owed at least US\$5,775 join in the petition.**
- (d) No, because SupplyCo doesn't know whether FabCo is insolvent.
- (e) No, because SupplyCo is not a US company.

Question 1.2

Commented [A&O4]: Incorrect, the correct response is (b)

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?

- (a) The foreign judgment is subject to appeal in the foreign country.**
- (b) The foreign judgment is an injunction.
- (c) The foreign judgment was issued by a court, contrary to the parties' agreement to arbitrate.
- (d) The defendant did not have sufficient notice of the foreign proceeding to put on a defense.
- (e) The foreign judgment is inconsistent with another final judgment on the same subject matter.

Question 1.3

Commented [A&O5]: Correct, 1 mark

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

- (a) A shareholder in ABC Corp, to which XYZ Corp is substantially indebted.
- (b) A journalist writing about XYZ Corp's bankruptcy.
- (c) A shareholder in MNO Corp, which owns all of XYZ Corp's shares.

(d) A retired employee of XYZ Corp who receives payments from the company's pension plan.

(e) A non-profit organization that advocates for companies like XYZ Corp to be held responsible for climate change.

Question 1.4

Commented [A&O6]: Correct, 1 mark

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

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

(e) Both (b) and (c).

Question 1.5

Commented [A&O7]: Incorrect, the correct response is (d)

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

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

Question 1.6

Commented [A&O8]: Correct, 1 mark

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

- (a) Avoidance actions.
- (b) A plan of reorganization.
- (c) DIP financing.
- (d) Lifting the automatic stay.
- (e) Formation of an equity committee.

Question 1.7

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

- (a) Acceptance of the plan by all classes of secured creditors.
- (b) Acceptance of the plan by at least one class of impaired, non-insider creditors.
- (c) The plan is fair and equitable to dissenting classes of creditors.
- (d) The plan does not discriminate unfairly against dissenting classes of creditors.
- (e) The dissenting creditors receive no less than they would under a liquidation scenario.

Commented [A&O9]: Correct, 1 mark

Question 1.8

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

- (a) In a chapter 7 proceeding with consent of the affected senior creditor.
- (b) In a chapter 7 proceeding with consent of the affected junior creditor.
- (c) In a chapter 11 proceeding with consent of the affected senior creditor.
- (d) In a chapter 11 proceeding with consent of the affected junior creditor.
- (e) The absolute priority rule cannot be deviated from.

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Question 1.9

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

- (a) An officer of the debtor if it is a debtor-in-possession in the foreign proceeding.
- (b) The board of directors of the debtor if it is a debtor-in-possession in the foreign proceeding.
- (c) An insolvency professional appointed by the court overseeing the foreign proceeding.
- (d) An insolvency professional appointed by a creditor where the foreign proceeding is an involuntary receivership.
- (e) All of the above.

Commented [A&O11]: Incorrect, the correct response is (d)

Question 1.10

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

- (a) Sale of US property free and clear pursuant to section 363.
- (b) Prosecution of avoidance actions pursuant to section 544 .
- (c) Entrusting the management of US assets to the foreign representative.

Commented [A&O12]: Correct, 1 mark

(d) Application of the automatic stay under section 362 to the debtor's interests in US property.

(e) Discovery about the debtor's assets.

QUESTION 2 (direct questions) [10 marks]

Commented [A&O13]: Total marks 8/10

Question 2.1 [maximum 1 mark]

Commented [A&O14]: Total marks 1/1

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

Pursuant to the US Bankruptcy Code ("the Code"), the following requirements render a corporation to be a debtor under chapter 7 or 11 proceeding, subject to further restrictions on the nature of business:-

(i) The debtor's place of business in the United States; or

Commented [A&O15]: Correct, ½ mark

(ii) Any of the debtor's assets in the United States.

Commented [A&O16]: Correct, ½ mark

Question 2.2 [maximum 2 marks]

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What is an executory contract?

An executory contract is not defined in the Code. But according to a law review article of Professor Vern Countryman in 1973, an executory contract is a contract that there is materially unperformed obligations on both the parties, failure of either to perform would constitute a material breach of the contract.

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Commented [A&O19]: Correct, 1 mark

Commented [A&O20]: Correct, ½ mark

For instance, under a construction contract, construction and payment have been partially completed and settled respectively as the date of bankruptcy petition of the debtor, the contract is an executory contract. Whereas, if only the final payment has not yet settled with the completed construction, this is not an executory contract.

Question 2.3 [maximum 2 marks]

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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 senior or equal to a pre-petition lien on which the estate property is secured for the post-petition financing. By doing so, incentives will be provided to existing creditors to extend further credit to the debtor. The position of those unsecured pre-petition creditors may also be improved by granting facilities in the priming lien.

Commented [A&O22]: Correct, 1 mark

A priming lien may be granted by the court to secure debtor-in-possession financing if the following requirement has been met:-

(i) The interest of the secured creditor being primed is adequately protected;

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(ii) There is no other available source of funds that does not contain such provision; and

Commented [A&O24]: Correct, ½ mark

(iii) There is no substantial additional credit is being made available to the debtor.

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?

Pursuant to section 1126 of the Code, in voting on a plan of reorganization:-

- (i) An unimpaired class of creditors, including those whose acceleration of debt has been reversed, is deemed to accept the plan.
- (ii) The class of creditors that will receive nothing is deemed to reject the plan.
- (iii) The holder of a claim or interest allowed under section 502 of the Code may accept or reject a plan of reorganization. But in view of the above points (i) and (ii), the balance of the decision-making power lies on those impaired classes. To accept a plan, there has to be a simple majority of the given class of creditors, holding at least two-thirds of the value of the claims, vote for it; or in respect of equity interest, two-thirds of the interest have to be voted in favour for the plan.

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Commented [A&O26]: Correct, ½ mark

Commented [A&O27]: Correct, ½ mark

Commented [A&O28]: Specifically, only the class that is impaired and receiving something under the plan may vote.

Commented [A&O29]: Correct, ½ mark

Question 2.5 [maximum 3 marks]

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

Firstly, proceeding under Chapter 15 of the Code is a kind of ancillary proceeding. The foreign representative of the debtor would seek recognition in the United States of the foreign insolvency proceeding under this section. Whereas, proceeding under Chapter 11 of the Code is the plenary proceeding. Broader relief is available to the debtor and creditors.

Secondly, under Chapter 11 of the Code, the automatic stay has effect immediately and worldwide to avoid interference on the estate property upon filing of the plenary petition. Such extraterritorial relief brings more time for the debtor to formulate the reorganization plan, negotiate with the creditors and realise its assets in an orderly process. Whereas, the automatic stay under Chapter 15 of the Code only apply to those debtor's assets within the territory in the United States.

Thirdly, the power of avoidance is also different. Under the automatic stay of Chapter 11 of the Code, the debtor has a full range of avoidance powers. Whereas, under the automatic stay of Chapter 15 of the Code, the foreign representative of the debtor may not avoid the preferential claims and fraudulent conveyance claims raised under non-bankruptcy law.

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Commented [A&O31]: Correct, ½ mark

Commented [A&O32]: Correct, ½ mark

Commented [A&O33]: Correct, ½ mark, also in chapter 15, it comes into effect on recognition of a foreign main proceeding or on order of the court in interim relief or recognition of a foreign non-main proceeding

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

Commented [A&O34]: Total marks 13.5/15

Question 3.1 [maximum 3 marks]

Commented [A&O35]: Total mark 2/3

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?

Directors of Delaware corporations owe a fiduciary duty of loyalty to the corporation's best interest and a duty of care in educated decision-making ("the Duties") under the law of Delaware, but are protected by the business judgment rule, i.e. no liability from error of judgment.

Commented [A&O36]: Correct, ½ mark

Commented [A&O37]: Correct, ½ mark (understanding this to be a typo for "care")

During the ordinary course of business, even in the situation of potentially insolvent, the directors owe the Duties to the corporation and the shareholders, but not to the creditors.

Commented [A&O38]: Correct, ½ mark

Commented [A&O39]: Correct, ½ mark

When the corporation is operating under the zone of insolvency or indeed actually insolvent, the directors owe the Duties to creditors.

Commented [A&O40]: Incorrect, the duties are always to the corporation and shareholder, even when actually insolvent.

Question 3.2 [maximum 3 marks]

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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.

To make Final Order

In general, a bankruptcy court may enter a final order on those core proceedings. As stipulates under section 157(b)(2), there is a non-exhaustive list of core proceedings, for instance proceedings concerning estate administration, confirmation of plan, counterclaims against the person filing claims against the property.

On the other hand, the bankruptcy court may only hear the non-core proceedings which are satisfactorily related to the bankruptcy proceedings, but no final order can be made. The bankruptcy court would instead submit its proposed findings of fact and conclusion of law for the consideration of the district court, subject to the objection of the interested parties.

Due to complicated nature of the bankruptcy proceedings, there was subsequent rulings of the US Supreme Court and amendments of the Bankruptcy Rules that requiring litigants to state whether they consent to the entry of final order by the bankruptcy court and whether they permit the district court to treat the order of the bankruptcy court as a proposed findings and conclusion of law. In this circumstance, the bankruptcy court may exercise district court's delegated authority to make a final order on a motion challenging the petition validity. As under *Executive Benefits Ins Agency v Arkison*, 134 S. Ct. 2165(2014), the bankruptcy court may make order on a core proceeding which they did not have constitutional authority by issuing a report with their recommendation for review to the district court. A final decision may also be concluded with the consent of the interested parties.

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Commented [A&O43]: Correct, 1 mark

Commented [A&O44]: Correct, ½ mark

Review on the decisions from bankruptcy court orders

In general, appeals on the bankruptcy court's decisions are heard by the district court. In some circuits, such appeals are heard by a Bankruptcy Appellate Panel (BAP), with the discretion of the parties to request be heard before district court instead. Both the district court and BAP will then review on the conclusion of law de novo and on the findings of fact for discretion abuse. Rarely, the appeal from the bankruptcy court's decision may be directly reviewed by the court of appeals at its discretion if there is question of law with no controlling

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Commented [A&O46]: Correct ½ mark

decision of the circuit or the US Supreme Court, or there is conflicting controlling decisions; or such appeal may materially advance the process of the proceeding.

Review on the decisions on non-final order

Appeals on the order from the district court or BAP may be heard to the circuit court de novo of the appeals on the conclusion of law and discretion abuse on findings of fact.

Question 3.3 [maximum 4 marks]

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

The claims for recovery of preferences, fraudulent conveyance and constructive fraudulent conveyance are different in the following four aspects:-

Firstly, in terms of time, recovery of preferences should be a transfer for the debtor's property in a suspect period before petition date pursuant to section 101 of the Code, i.e. 90 days prior to the petition date, one year for transfer to insiders of the corporate debtor. But for claims under fraudulent conveyance and constructive fraudulent conveyance, the related transactions have to be within a two year period prior to the petition date.

Secondly, regarding intention, recovery of preferences and constructive fraudulent conveyance do not need to show any fraudulent intention. But under actual fraudulent conveyance, it has to prove that the debtor is "with actual intent to hinder, delay, or defraud any entity" when making the transfer or incurring the obligations pursuant to section 548 of the Code.

Thirdly, the recipient under preferences is the creditor who exists prior to the transfer, and such transfer will enable such creditor improving its position when compared to liquidation without such transfer happened. But the recipients under the fraudulent conveyance and constructive fraudulent conveyance need not to be a creditor of the debtor.

Last but not least, the retention of property by the recipient under the avoidance actions between the above three categories are different. Under the recovery of preference, the recipient creditor may suffer no penalty, but he has to return the transfer with potential prejudgment interest from the transfer date. Whereas, the recipient of an actual or constructive fraudulent conveyance may retain the property or enforce the obligation incurred with consideration provided in good faith pursuant to section 548 of the Code.

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?

Foreign main proceedings are those proceedings that commenced in the debtor's centre of main interests (COMI). It is presumed under section 1516(c) of the Code that the place of incorporation of the company is its COMI, subject to rebuttal. For those proceedings commenced in the jurisdiction other than the COMI where the debtor has an establishment in the jurisdiction, it is recognized as foreign non-main proceedings.

When determining whether the presumption of incorporation place is the COMI of the debtor is rebuttable, the following factors will be considered:-

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Commented [A&O48]: Correct, ½ mark

Commented [A&O49]: Correct, ½ mark

Commented [A&O50]: Correct, 1 mark

Commented [A&O51]: Correct, ½ mark

Commented [A&O52]: Correct, ½ mark

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Commented [A&O54]: Total marks 4.5/5

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Commented [A&O56]: Correct, ½ mark

Commented [A&O57]: Correct, 1 mark

- (i) Domicile of the debtor;
- (ii) Principle place of business;
- (iii) Location of assets, especially primary assets;
- (iv) Location of headquarters;
- (v) Location of management;
- (vi) Location of majority of the creditors, especially those will be affected by the relief requested by the foreign representative;
- (vii) Applicable jurisdiction for most disputes.

Commented [A&O58]: Correct, 1 mark, also a debtor's COMI should be ascertainable by its creditors or other third parties on the basis of objective evidence.

The above factors were assessed as of the date of the US petition commenced as a result of *the Bear Stearns case 374 BR 122*. But as the referencing Model Law has been revised by the UNCITRAL Working Group which specifies the COMI test is to be tested as of the commencement date of the foreign proceeding. The Code is proposed to be amended by the National Bankruptcy Council accordingly. Furthermore, in case the US bankruptcy court finds that the COMI was manipulated in bad faith, the US bankruptcy court may deny the recognition according to existing case law.

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

Commented [A&O60]: Total marks 7/15

Question 4.1 [maximum 5 marks]

Commented [A&O61]: Total marks 3/5

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?

By filing a voluntary petition under Chapter 11 of the Code, automatic stay is invoked for Rental Corporation. Automatic stay commenced immediately upon the filing of any plenary petition. Such automatic stay applies to the property of the estate all over the world. The following will discuss the specific effect on various stakeholders:-

Commented [A&O62]: Correct, 1 mark

- (i) Regarding the DOJ investigation, it will not be subject to the automatic stay due to the statutory exceptions. Pursuant to section 362 of the Code, regulatory investigation is one of the exceptions which are not subject to the automatic stay.
- (ii) Regarding the securities class action litigation, the secured creditor may request a lift-stay or relief from stay pursuant to section 362 of the Code. The secured creditor has to prove that they are suffering from lack of adequate protection. In other words, the value of the property may decline during the proceedings and the secured creditor may recover less than the full recovery. Analysis has to be conducted on the value of the property and also the value of the secured creditor's claim by applicable non-bankruptcy law so as to determine whether such relief should be granted.
- (iii) Regarding the delinquent leases, the lease may be a kind of executory contract. Pursuant to section 365 of the Code, Rental Corporation has an election to assign or reject an unexpired lease of non-residential property within 120 dates of the relief order. According to section 365(d)(4), a further extension of 90 days for a cause may be

Commented [A&O63]: Correct, 1 mark

Commented [A&O64]: Incorrect, the securities class action is stayed as pre-petition litigation. The word "securities" refers to the fact that the plaintiffs own stock in the defendant corporation and assert claims under the securities law.

Commented [A&O65]: Incorrect, the lessor is stayed from pursuing eviction proceedings because the leases were in payment default but did not terminate prior to the petition date

granted. Any further extension needs to obtain the consent from the lessor or landlords of the premises.

- (iv) Regarding the credit facility, because of the automatic stay, this class of creditor is prohibited to litigate on the pre-petition claims, enforce any pre-petition judgment against Rental Corporation and its property, obtain possession or control of Rental Corporation's property, create or enforce any lien against the property of Rental Corporation, collect on the pre-petition claims or set-off the pre-petition debt against any pre-petition claim as stipulated in section 362(a) of the Code.

Commented [A&O66]: Correct, 1 mark

Question 4.2 [maximum 5 marks]

Commented [A&O67]: Total marks 2/5

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

The lessors of office space to Rental Corporation may request a lift-stay or relief from stay pursuant to section 362(b) of the Code. The lessors have to prove that they do not have adequate protection if prohibited their action against Rental Corporation. Again, valuation is a crucial element to prove that the value of its interest in the property exceeds the value of the property. That Rental Corporation has no equity in the property and it is not necessary for the concerned property be part of the reorganization plan.

Commented [A&O68]: Giving you credit here for noting above the 120 day deadline to assume or reject (1 mark) and the potential 90 day extension (1 mark). Also, Rental Corporation must pay rent as an administrative expense for the period prior to rejection of a lease, if it assumes and subsequently rejects a lease it must pay two years rent as an administrative priority, and lessors have a claim for the unpaid pre-petition rent.

The court, upon reviewing the particular situation of the lessors with cause shown, may terminate, annul, modify the automatic stay or continue the stay with condition protecting the interests of the affected party.

Rental Corporation may avoid the lift-stay by allowing the lessors to pursue remedies of "indubitable equivalent" of the lost value, for instance periodic cash payments or grant of replacement liens on the unencumbered estate property pursuant to section 361 and 362(d) of the Code. If the court satisfied that there is insufficient protection to the lessors, administrative expense priority will be given.

Question 4.3 [maximum 5 marks]

Commented [A&O69]: Total marks 2/5

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?

The debtor can assign an executory contract under section 364 of the Code. It can transfer its interests in key contracts which are required for the operation of the business. Pursuant to section 363 of the Code, a debtor can, with court approval, sell its property free and clear of creditor interests.

Commented [A&O70]: Correct, 1 mark

Under section 365(n), it protects the licensees of patents and copyrights owned by the debtor by not to terminate the licenses in connection with the sale of the intellectual property without their consent. In other words, Paint Corporation is allowed to transfer its proprietary

Commented [A&O71]: Correct, 1 mark, also, in a 363 sale, the purchaser could take less than all of Paint Corporation's assets and liabilities; this could generate a higher price for payment of clean-up costs than if the business was sold as a whole outside of bankruptcy. Home Corporation would also have the certainty of knowing that its purchase could not be overturned on appeal

and patented recipes to Home Corporation without terminating the distribution contracts with the home improvement stores.

Nevertheless, the licensee, i.e. the home improvement stores, may have options to the debtor's decision on rejecting to enforce the executory contracts. Pursuant to section 365(n) of the Code, the licensee may choose to treat the distribution contracts as it is terminated by such the rejection of the debtor equals to the breach on the contract; or the licensee may retain its right as if the license continues.

If the licensee, i.e. the home improvement stores in this case, chose to retain its right, they should be allowed to exercise its rights to sell the patented house paint as such those rights existed before the sale to Home Corporation in the during of the distribution contracts and any extended period under applicable non-bankruptcy law. On the other hand, the licensee has to make all royalty payments due under those distribution contracts. In the meantime, the licensee is deemed to waive any right of setoff in relation to those distribution contracts and any claim allowable under section 503 of the Code.

*** End of Assessment ***