



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

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?

- (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

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

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.

Commented [A&O1]: Total marks 35.75/50, note plagiarism in response to 3.1

Note from Course Leader: The marker has detected plagiarism in your answer to question 3.1. Please take note of the course handbook and also instruction 5 of the assessment. No further sanction will be imposed.

Commented [A&O2]: Total marks 9/10

Commented [A&O3]: Incorrect, the correct response is (c)

Commented [A&O4]: Correct, 1 mark

Commented [A&O5]: Correct, 1 mark

(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]: Correct, 1 mark

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.

Commented [A&O10]: Correct, 1 mark

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]: Correct, mark

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 7.75/10

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?

A corporation that has a place of business or property in the United States shall be eligible to be a debtor in a US chapter 7 or 11 proceeding.

Commented [A&O15]: Correct, ½ mark

Commented [A&O16]: Correct, ½ mark

Question 2.2 [maximum 2 marks]

Commented [A&O17]: Total marks 2/2

What is an executory contract?

An executory contract (per the Countryman Test) is a contract under which the obligation of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other.

Commented [A&O18]: Correct, 1 mark

Commented [A&O19]: Correct, ½ mark

Commented [A&O20]: Correct, ½ mark

The US Bankruptcy Code affords the debtor (or the bankruptcy trustee) the right to assume, reject, or assume and assign such executory contracts.

Question 2.3 [maximum 2 marks]

Commented [A&O21]: Total marks 1.75/2

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 referred to as a lien on property senior to or with the same priority as existing liens on the same property.

Commented [A&O22]: Correct, 1 mark

For such a lien to be granted to secure DIP financing under Section 364(d) of the US Bankruptcy Act, it is required that such priming is only available as a last resort when the debtor is unable to obtain any other type of financing (secured only by previously unencumbered assets and a junior lien on already encumbered asset or which may be on account of the debtor having insufficient substantial unencumbered assets that assure potential lenders that all administrative priority claims shall be satisfied,) and either the existing lien holders consent to such prime lien or the debtor demonstrates to such secured creditors that their interest are adequately protected from diminution in value of their collateral as result of the priming lien. In order to secure a priming loan it is therefore required that the DIP Lender's claims is paid prior to the payment of claims by the existing lenders secured by the same collateral, regardless of whether the source of payment is the sale of proceeds of the common collateral.

Commented [A&O23]: Correct, ½ mark

Commented [A&O24]: Partially correct, ¼ mark, it is the court that must be satisfied that the secured creditor's interest is adequately protected

Question 2.4 [maximum 2 marks]

Commented [A&O25]: Total marks 1.5/2

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?

In voting on a plan of reorganisation:

- (i) Each holder of a claim or interest of an unimpaired class of creditors (including those whose debt has been reversed) is deemed to accept the plan under Section 1126(f) of US Bankruptcy Code;
- (ii) class of creditors that will receive nothing under the plan, i.e. the claims or interests of such class do not entitle the holders of such claims or interests to receive or retain any property under the plan on account of such claims or interests is deemed to reject the plan; and
- (iii) The holder of a claim or interest allowed to file a proof under section 502 of Title 11 of the US Bankruptcy Code is allowed to vote on the plan or reorganisation. If the United States is a creditor or equity security holder, the Secretary of the Treasury may accept or reject the plan on behalf of the United States.
- (iv) For a class of creditors to approve a plan or in other words a plan is said to be approved by a given class of creditors if a simple majority of the creditors in the class holding 2/3rd of the claims in the given class or creditors and in case of equity interests, those holding 2/3s in the amount of interest are deemed to voted in favour of the plan.

Commented [A&O26]: Correct, ½ mark

Commented [A&O27]: Correct, ½ mark

Commented [A&O28]: Incorrect, as noted above, certain of these creditors will be deemed to have cast their vote in a certain way. Only impaired creditors who will receive something under the plan have their votes counted.

Commented [A&O29]: Correct, ½ mark

Commented [A&O30]: Total marks 1.5/3

Question 2.5 [maximum 3 marks]

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

The automatic stay available in chapter 15 proceedings differ from that available in chapter 11 proceedings in that:

- (i) while in chapter 11, In terms of Section 362(a) a worldwide stay on creditor actions thereby restricting creditors to possess or exercise control over property (including that located outside United States) of the debtor or of the estate, wherever located and by whomever held, automatically goes into effect when the bankruptcy petition is filed; to its contrary, in chapter 15, the automatic stay of adverse creditor actions and select other actions under Section 1520 of the US Bankruptcy Act is limited to the confines of the territories of United States and to properties located within United States.
- (ii) Further under chapter 11 while the stay applies on the filing of any plenary petition in order to allow the debtor to have an unfettered process of negotiating upon a restructuring plan with its creditors and realise the value of its assets in an orderly process, however the automatic stay in a chapter 15 proceeding is subject to a carveout to permit the filing of a plenary US bankruptcy proceeding even after the recognition of a foreign proceeding.
- (iii) Chapter 15 does not initiate a bankruptcy case and does not create an estate unlike in the case of a Chapter 11 proceeding. Chapter 15 is a proceeding filed by a foreign representative intended to obtain U.S. recognition of a foreign insolvency proceeding. Because an estate is not created, the court's in rem jurisdiction is limited to the United States, which in case of a chapter 11 proceeding is against the world at large.

Commented [A&O31]: Correct, ½ mark

Commented [A&O32]: Correct, ½ mark

Commented [A&O33]: The stay comes into effect in chapter 15 automatically on recognition of a foreign main proceeding or discretionarily on an application for interim relief or recognition of a foreign non-main proceeding.

Commented [A&O34]: Correct, ½ mark

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

Commented [A&O35]: Total marks 11.5/15

Question 3.1 [maximum 3 marks]

Commented [A&O36]: Total marks 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?

Following are the types of duties owed by the directors of Delaware:

(i) **Duty of Care:**

The duty of care requires that directors follow an informed, educated and reasonable deliberative process when making a business decision. This involves, for example, attending meetings, asking questions, reviewing written materials, and otherwise informing themselves of relevant information that is reasonably available to them.

(ii) **Duty of Loyalty:**

The fiduciary duties of directors of a Delaware corporation also include a broad and encompassing duty of loyalty to the corporation and its shareholders. The duty of loyalty imposes on directors with an affirmative duty to protect and act in the best interests of the corporation, and an obligation to refrain from conduct that would injure the corporation and its shareholders, or deprive them of profit or advantage.

The Directors of Delaware corporations owe these fiduciary duties to the corporation's interests and its shareholders in the ordinary course of business and otherwise. The directors are required to eschew any conflict between their duty to the corporation and their self-interest.

The same set of duties continue to be owed to the corporation and its shareholders even in the twilight zone of potential insolvency or actual insolvency of the company and the onus to do the same does not shift towards any other stakeholder, including creditors. This was confirmed and settled by the Delaware Supreme Court in the case of *North Am Catholic Educational Programming Foundation, Inc v Gheewalla*, 930 A.2d 92, 103 (Del 2007)

Commented [A&O37]: This response appears to be copied from an American Bar Association publication: <https://www.americanbar.org/content/dam/aba/publications/blt/2010/09/inside-buslaw-insolvency-201009.authcheckdam.pdf>

Commented [A&O38]: Correct, ½ mark

Commented [A&O39]: Correct, ½ mark

Commented [A&O40]: Correct, ½ mark

Commented [A&O41]: Correct, ½ mark

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.

In terms of Section 157(b)(1), a bankruptcy court may hear and determine, i.e. render final order in:

- (i) all cases under title 11;
- (iii) all "core proceedings" (including but not limited to (a) matters concerning the administration of the estate; (b) counterclaims by the estate against persons filing claims against the estate; (c) orders in respect to obtaining credit etc) arising under title 11 or arising in a case under title 11.

Commented [A&O42]: Total marks 2.5/3

Commented [A&O43]: Correct, ½ mark

Commented [A&O44]: Incorrect, under *Stern v. Marshall*, the bankruptcy court requires consent of the parties even with respect to core matters

Appeals from all final judgments, orders and decrees of a bankruptcy court, as well as discretionary interlocutory appeals, are heard in the district court for the district in which they sit (in terms of Section 158 (a) of US Bankruptcy Act) or in a bankruptcy appellate panel ("BAP") (as in case in certain circuits), in terms of Section 158 (b) of US Bankruptcy Act unless otherwise provided by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA").

Commented [A&O45]: Correct, ½ mark

Commented [A&O46]: Correct, ½ mark

A non-final order being a ruling in a non-core proceeding or the bankruptcy court did not otherwise have the authority to enter a final decree is reviewed by the district court or the BAP

who review such order by reviewing *de novo* all findings on fact and conclusions on law to which the counterparty has an objection to. A new trial is not required and record should be examined without giving deference to proposed factual findings.

Commented [A&O47]: Correct, 1 mark

Question 3.3 [maximum 4 marks]

Commented [A&O48]: Total marks 4/4

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

(i) Fraudulent conveyance:

The provisions of Section 548 of the US Bankruptcy Act allow the bankruptcy trustee to avoid any obligation or transfer of the debtor's interest in property made within two years before filing the bankruptcy petition, if the debtor voluntarily or involuntarily (a) made the transfer or incurred the obligation with actual intent to hinder, delay, or defraud any entity to which the debtor owed a debt; or (b) transferred the property without receiving a reasonably equivalent value, under certain circumstances.

Commented [A&O49]: Correct, 1 mark

Commented [A&O50]: Correct, ½ mark

The trustee is also authorised to avoid transfers of property made within ten years before filing of the petition in certain circumstances.

Fraudulent transfers under Section 548 have two different categories: Transfers involving actual fraud which requires proving of intention, and transfers involving constructive fraud which does not require a fraudulent intent to be proved. Since proving the debtor's state of mind is difficult, courts look to specific "badges of fraud" to demonstrate the required intent. Those badges include evidence that:

- (a) The debtor absconded with the proceeds immediately following receipt;
- (b) The transfer involved lack of consideration (value), when both the debtor and transferee know that creditors will not be paid as a result;
- (c) There is a significant disparity between the value of the property transferred and the payment made for the property;
- (d) The transferee is an officer, or agent or creditor of an officer, of a corporate debtor;
- (e) The debtor was insolvent; or
- (f) A special relationship existed between the debtor and the transferee.

(ii) Constructive fraudulent conveyance

A constructive fraudulent conveyance does not require proof of the debtor's fraudulent intent or state of mind. A transfer is said to be constructively fraudulent if the debtor which received less than reasonably equivalent value:

- (a) Was insolvent on the date of the transfer or became insolvent as a result of the transfer;
- (b) Engaged in or was about engage in a business transaction for which the debtor's remaining property constituted unreasonably small capital;
- (c) Intended to incur or believed that he or she would incur debts beyond the his or her ability to pay as the debt matured; or
- (d) Made the transfer or incurred the obligation to or for the benefit of an insider under an employment contract and not in the ordinary course of business.

Badges of constructive fraud generally looked into by courts include:

- (a) Value of the transferred property, including whether it is equal to the value received by the debtor;

- (b) Actual market value of the property transferred and received;
- (c) Nature of the transaction, checking whether it was an arm's-length transaction; and
- (d) Presence (or absence) of good faith of the transferee of the property.

(iii) Preference:

Section 547(b) of the Bankruptcy Code permits a debtor or trustee to recover "preferences." These "preferential" payments allow the recipients to receive more than they would have received if the payment had not been made and the debtor's assets were divided equally among all creditors. There is no requirement to prove intention to prefer for such a transaction to be able to be applied for avoidance by the trustee. It therefore generally entails a transfer of an interest of the debtor in property made to or for the benefit of a creditor and which was made for or on account of an antecedent debt owed by the debtor (before such transfer was made) at a time when the debtor was insolvent and 90 days before the date of the filing of the bankruptcy petition (extended to one year if the transfer was made to an insider), as a result of which the creditor received more than it would have received if the case were a Chapter 7 liquidation.

Commented [A&O51]: Correct, ½ mark

Commented [A&O52]: Correct, ½ mark

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Question 3.4 [maximum 5 marks]

Commented [A&O56]: Total marks 3/5

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

In the event a US court recognises a foreign insolvency proceeding, the same should be recognised as 'main' or 'non-main' proceeding as the same would determine the reliefs that will follow and be available to the debtor post recognition.

The court while making such a decision will usually determine as to whether the country in which the foreign proceeding is pending and is ought to be recognised is the one in which the debtor has its "centre of main interests" (COMI). A proceeding is non-main if it is pending in a country where the debtor merely has an establishment. Therefore, if a foreign proceeding is not recognised as a main proceeding, it must receive recognition as non-main if the proceeding is from a country where the debtor has an "establishment". Chapter 15 defines an "establishment" as any place where the debtor "carries out a non-transitory economic activity".

Commented [A&O57]: Correct, 1 mark, conversely, a main proceeding is one pending in the debtor's COMI. Also, COMI is assessed as of the date of commencement of the US proceedings.

While COMI has not been defined under the statute, it is usually presumed to be the place of incorporation of the debtor company or the place of registered office as prescribed under Section 1516 (c) of the Bankruptcy Act. Other indicators (as propounded by case laws) include – (i) locations of headquarters; (ii) location of management; (iii) location of primary assets; (iv) location of a majority of debtor's creditors or creditors that will be affected by the relief requested by foreign representative or officeholder; and (v) jurisdiction whose law will apply to most disputes. It is the one which should be ascertainable by creditors and third parties on the basis of an objective analysis and evidence. Cue is also drawn to the definition of COMI provided under EU's Regulations on Cross-Border Insolvencies which defines it to be the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties". Adopting this rule, the US court has held that the proceeding in the country where the debtor had its principal office and primary concentration of employees was the COMI of the debtor (*In re Tri-Continental Exchange Ltd.*, 349 B.R. 627 (Bankr. E.D. Calif. 2006)

Commented [A&O58]: Correct, ½ mark

Commented [A&O59]: Correct, 1 mark

Commented [A&O60]: Correct, ½ mark

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

Commented [A&O61]: Total marks 7.5/15

Question 4.1 [maximum 5 marks]

Commented [A&O62]: Total marks 3.5/5

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?

The automatic stay in effect when a Chapter 11 proceedings is filed does not operate as a stay—

Commented [A&O63]: Correct, 1 mark

(i) In case of the commencement or continuation of a criminal action or proceeding against the debtor as per the terms of section 362 (b) of the US Bankruptcy Act.

- Accordingly, DOJ investigation which is in the nature of a criminal investigations shall not stayed or impacted and may continue against Rental Corporation despite the filing of the Chapter 11 petition by itself.

Commented [A&O64]: Correct, 1 mark

(ii) In case of the commencement or continuation of an investigation or action by a securities self-regulatory organization to enforce such organization's regulatory power as per the terms of section 362 (b) (25) of the US Bankruptcy Act.

- Accordingly, actions by SEC which is a securities regulatory body shall not be stayed and may continue against Rental Corporation despite the filing of the Chapter 11 petition by itself.

Commented [A&O65]: Here the securities class action is a private suit by a group of shareholders in the company, which would be stayed as pre-petition litigation.

(iii) Lessors are unsecured creditors of Rental Corporation who is required to check for inclusion of it claims in the schedule of debt prepared by Rental Corporation. If its claim is not scheduled (i.e., listed by the debtor on the debtor's schedules) or is scheduled as disputed, contingent, or unliquidated, it can file a proof of claim (and attach evidence documenting the claim) in order to be treated as a creditor for purposes of voting on the plan and distribution under it.

Commented [A&O66]: Correct, ½ mark, though also note that the stay would bar commencement of an eviction proceeding because the lease hadn't expired pre-petition.

(iv) Credit facility – while the loan contract cannot be terminated merely on ground of a chapter 11 proceeding petition having been filed by Rental Corporation, however, the lender shall not be obligated to continue disbursing facility or extend the loan under the facility agreement. Further, the credit facility provider being creditors of Rental Corporation is required to check for inclusion of it claims in the schedule of debt prepared by Rental Corporation. If its claim is not scheduled (i.e., listed by the debtor on the debtor's schedules) or is scheduled as disputed, contingent, or unliquidated, it can file a proof of claim (and attach evidence documenting the claim) in order to be treated as a creditor for purposes of voting on the plan and distribution under it.

Commented [A&O67]: Correct, 1 mark

Question 4.2 [maximum 5 marks]

Commented [A&O68]: 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 following protection and rights are afforded to lessors of office spaces of Rental Corporation:

- (i) Motion for relief from the automatic stay – the lessors may insist on immediate payment of administrative rent by either a reorganizing debtor or bankruptcy trustee. This motion is recommended in every case where the tenant is in default on the petition date. All such motions must be filed separately from any other motion.
- (ii) Motion for adequate protection (adequate assurances of performance of both the duty to pay administrative rent, maintain insurance, security and other operating concerns).
- (iii) Proof of Claim- The lessor's claim should be filed in every case where there is a loss. The written proof of claim must be filed within 90 days after the first date set for the meeting of creditors in the case. The proof of claim form is a standard form, and should include all three types of claims

Commented [A&O69]: Correct, 1 mark, also the debtor has 120 days to assume or reject leases of commercial real estate, subject to a 90 day extension for cause. If the debtor assumes and then rejects a lease, it must pay 2 years rent as an administrative expense

Commented [A&O70]: Correct, 1 mark

Question 4.3 [maximum 5 marks]

Commented [A&O71]: 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?

A sale under Section 363 of the Bankruptcy Code may address the issues as identified under the problem in that it inter alia provides the following mechanism to ensure adequate protection to any proposed sale of a property under the section:

- (i) Section 363(g) of the Bankruptcy Act allows the trustee, notwithstanding anything contained in Section 3636(f) of the Bankruptcy Act, to sell the property free and clear of any vested or contingent right in the nature of dower or curtesy.
- (ii) Subject to the provisions of section 365, Section 363(l) of the Bankruptcy Act allows the trustee to sell, or lease property under this section, notwithstanding any provision in a contract, a lease, or applicable law that is conditioned on the insolvency or financial condition of the Paint Corporation, on the commencement of a case under this title concerning the debtor, or on the appointment of or the taking possession by a trustee in a case under this title or a custodian, and that effects, or gives an option to effect, a forfeiture, modification, or termination of the debtor's interest in such property.
- (iii) The reversal or modification on appeal of an authorization of a sale or lease of property does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and such sale or lease were stayed pending appeal.

Commented [A&O72]: Correct, 1 mark. Home Corp. could buy just the assets it is interested in and leave behind the property and contamination claims. This could yield a higher purchase price. The distribution contracts could be assumed and assigned in connection with the sale without the counterparties' consent.

Commented [A&O73]: Correct, 1 mark

*** End of Assessment ***