



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 6B

GERMANY

This is the **summative (formal) assessment** for **Module 6B** on this course and must be submitted by all candidates who **selected this module as one of their elective modules**.

The mark awarded for this assessment will determine your final mark for Module 6B. 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 **Microsoft Word format**, using a standard A4 size page and an 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: **[studentnumber.assessment5D]**. An example would be something along the following lines: 202021IFU-314.assessment5D. **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. The final submission date for this assessment is **31 July 2021**. The assessment submission portal will close at **23:00 (11 pm) GMT on 31 July 2021**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.
7. Prior to being populated with your answers, this assessment consists of **6 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

How are the competences of a preliminary insolvency practitioner defined?

- (a) By the debtor.
- (b) By the creditors' committee.
- (c) By statute.
- (d) By court decision.**

correct

Question 1.2

Which of the following securities has an accessory nature?

- (a) Suretyship.**
- (b) Transfer of title by way of security.
- (c) Mortgage (*Grundschild*).
- (d) Retention of title.

correct

Question 1.3

Creditors who wish to participate in the insolvency proceedings must file their claims with

- (a) The creditors' committee.
- (b) The creditors' meeting.
- (c) The insolvency practitioner.**
- (d) The court.

correct

Question 1.4

Who has the duty to file for insolvency proceedings?

(a) The directors of a Limited Liability Company (*GmbH*).

(b) All debtors.

(c) Legal persons only.

(d) Entrepreneurs only.

correct

Question 1.5

Wage claims of employees stemming from the period prior to the opening of insolvency proceedings

(a) Enjoy super-priority even ahead of secured creditors.

(b) Qualify as expenses of the proceedings (liabilities of the estate).

(c) Rank as claims of ordinary creditors.

(d) Cannot be recognized in insolvency proceedings at all.

correct

Question 1.6

Who of the following is entitled to submit an insolvency (restructuring) plan?

(a) Every creditor.

(b) The debtor.

(c) The court.

(d) The creditors' committee.

correct

Question 1.7

Which of the following circumstances **is not** relevant for the local jurisdiction of an insolvency court (*Amtsgericht*)?

(a) Registered office.

(b) Location of assets.

(c) Place of residence.

(d) Centre of economic activities.

correct

Question 1.8

The rights of which group **cannot** be affected by an insolvency plan?

- (a) Employees.
- (b) Shareholders.
- (c) Banks.
- (d) Creditors with a right to separation.

Correct was answer (d). Employees are treated like all other ordinary creditors under German law.

Question 1.9

How long is the compliance period (time frame) for discharge of residual debt?

- (a) Seven years.
- (b) Six years.
- (c) Three years.
- (d) One year.

Correct (German law has meanwhile be changed to three years; however, six years is what was still stated in the guidance text).

Question 1.10

How are foreign insolvency proceedings recognised in Germany?

- (a) By decision of the court.
- (b) By the insolvency practitioner.
- (c) By statute (by force of law).
- (d) By a decision of the creditors' meeting.

correct

9 marks

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 3 marks]

Which rules regulate cross-border insolvency law in Germany (only list the norms)?

The rules that regulate cross-border insolvency law in Germany are the following :

- Section 335 et seq InsO (as long as no bi/multilateral agreements apply)
- EU Regulation 2015/848 (concerning other EU Member States).

In German cross-border insolvency, the principle of Universality prescribes the effects of an insolvency proceeding.

3 marks

Question 2.2 [maximum 4 marks]

Explain the principle of publication in German law on security rights: which security rights are made public (and how) and which are not?

The rules on publication of security right sin German law are not codified in one piece of legislation but tend to follow the rules governing the transfer of property of each type of asset, which vary depending on the asset.

Concerning security ownership and assignment, the rule is that an act of publicity is not required. An exception to this rule is for registered inland waterway vessels of a certain size, that requires the creditor to register in a special Ship Register as the new owner.

Concerning pledges, the transfer of possession is considered the necessary act of publicity required. There is no specific publicity required apart form that. However, for claims, the debtor must be notified, in order to be able to pay the right person.

Concerning immovables, a mortgage must be registered in the land register (same for ships and planes). Publicity is therefore guaranteed by this register.

4 marks

Question 2.3 [maximum 3 marks]

What is and what happens at a “verification meeting” (*Prüfungstermin*)?

The verification meeting is a meeting where the amount and ranking of claims that have been lodged are verified.

The insolvency administrator and creditors have the right to dispute any claims which have been lodged.

If the claims are not disputed, then they are deemed “determined”, and give the appropriate voting rights to creditors and the right to participate in any distribution.

If a claim is disputed, the creditor that disputes a claim must instigate proceeding to determine the claim. During the meeting, the insolvency administrator keeps a record of what must be paid to creditors in a distribution register. This register is available at the insolvency court for inspection.

The verification meeting must take place in order for any unsecured creditors to be paid, excepting interim distributions.

3 marks

in total: 10 marks

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

Explain the rules in German insolvency law relating to executory contracts.

The rules applying to executory contracts are §103 and following of the InsO :

“Section 103 – Insolvency Administrator’s Right of Choice (1) If a reciprocal contract has not been performed or has not been fully performed by the debtor and the other party at the time when insolvency proceedings are commenced, the insolvency administrator may perform the contract in place of the debtor and demand performance from the other party. (2) If the administrator refuses to perform the contract, the other party may assert a claim for non-performance only as an insolvency creditor. If the other party requests that the insolvency administrator exercise his/her right of choice, the administrator must declare without delay whether or not he/she wishes to demand performance of the contract. If he/she fails to do so, he/she cannot insist on performance.”

According to this text, an executory contract is considered to be a contract where contractual obligations remain unfulfilled on both sides, or not fully performed.

The debtor in possession or insolvency administrator has the choice to fulfil an executory contract. The party to a contract that the insolvency practitioner has chosen to fulfil must perform outstanding contractual obligations if the administrator chooses to opt for the fulfilment of the contract. As a consequence, any outstanding claim gets elevated in rank subsequently as an administrative claim. If the administrator chooses fulfilment, the debtor too must fulfil their obligations.

If the administrator decided to not fulfil the contractual terms, then the contracting partner can use the non-performance of the insolvency administrator to register a claim that is satisfied on a pro rata basis.

The contractual partner can try and force this decision to be taken, by demanding that the insolvency administrator pronounces their intention to fulfil the contract or not. If the insolvency administrator does not opt immediately for fulfilment, this does not automatically wind up the contract, but the insolvency administrator can no longer use their power of demanding fulfilment from the contractual party.

If a contractual partner has a claim against the debtor or fulfilled the contractual obligation before the opening of insolvency proceedings, the claim can be satisfied by the insolvency administrator on a pro rata basis.

Section 105 provides for the issue of divisible performance : *“If the performance owed under a contract is divisible and the other party has already partially provided the performance due by it at the time of commencement of insolvency proceedings, this party is an insolvency creditor for the amount of its claim to counter-performance corresponding to the partial performance, even if the insolvency administrator demands performance in relation to the performance still outstanding. The other party is not entitled to claim the return of any partial performance that passed into the debtor’s assets prior to commencement of proceedings from the insolvency estate on the grounds of non-performance of its claim to counter-performance.”*

This provision covers executory contracts that are stretched out over a period of time, such as supply contracts. The return obligation must be satisfied in full for services performed after the opening of the insolvency proceedings. However, those performed prior to the opening of the insolvency proceeding are satisfied as a pre insolvency claim on a pro rata basis.

Ipso facto clauses are neutralised / not effective with the opening of insolvency, and material adverse change clauses are in theory also not effective, unless the conditions in these clauses

do not relate to the insolvency proceedings themselves. Therefore, the general rule is that a creditor cannot just rupture contractual relations with the debtor solely because of the opening of insolvency proceedings.

Some contracts have special rules attached to them (Section 104 et Seq InsO) such as contracts for financial services, leases (Sections 109-112 InsO) and Service contracts (Section 113 InsO) and employment contracts (Section 120 InsO). For most of these contracts, the debtor in possession or the insolvency administrator has a special right to termination following a three-month notice period.

15 marks

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

In January 2018, Bank (B) has granted debtor (D) a loan of EUR 50,000. Since B asked for security, D has transferred legal title over a lorry by way of security and has assigned all current and future receivables against her customers by way of security. Sixteen (16) months later, in May 2019, D is unable to pay her debts when they fall due. On 3 July 2019, B, being aware of D's substantive insolvency, terminates the loan contract and sells the lorry for EUR 20,000 to W. On 5 July 2019, B reveals the assignment to all customers of B and receives EUR 15,000 from X, who bought goods from D on 1 July 2019 and who pays B the money he owes to D. On 1 August 2019, D applies for insolvency proceedings. B receives another payment of EUR 10,000 from Y who bought goods from D on 10 September 2019. Five days later, the court opens insolvency proceedings and appoints I as insolvency administrator. I maintains B's business and sells goods to Z for EUR 5,000. Z is a regular customer of B, knows about the assignment and pays EUR 5,000 upon delivery to B. I claims EUR 50,000 from B, arguing that the sale of the lorry and the payments of X, Y and Z are subject to transaction avoidance (§§129 *et seq* InsO).

What are the various legal positions? Test this based on the norms.

Section 129 of InsO tells us that certain transactions can be considered if :

- They are considered disadvantageous for the creditors,
- and that can be reasonably thought to have a reason to contest them.

A transaction that has reduced the amount that creditors can receive in distribution can be considered disadvantageous of the creditors. Indeed, a transaction at an undervalue, preferences to certain creditors, creation of new security rights before the opening of insolvency proceedings etc. can all be considered transactions that might have grounds to be contested if they have reduced the value of the estate which in itself has a negative impact on any creditor distribution.

Section 130 et seq InsO lists reasons to contest these transactions.

In the case at hand, the insolvency administrator appointed, I, argues that the sale of the lorry by B and they payments of X, Y and Z are subject to avoidance transactions. It is therefore necessary to analyse these transactions separately, in order to lay down the legal positions and norms for each transaction.

1) The sale of the lorry

It is reminded that in January 2018, D transferred the title of the lorry over to B, to offer security for a new loan that B granted to D of 50.000 euros.

In May 2019, D was confronted to cash flow insolvency, as she became unable to pay her debts as they fell due.

On the 3rd of July 2019, B became aware of this fact, according to the case facts. B terminated the loan contract and sold the lorry for 20.000 euros to W.

In this case, the termination of the contract and the sale of the lorry was indeed after insolvency occurred, but before any petition had been filed by D to the Court to open insolvency proceedings.

It is necessary to distinguish in this case the transfer of title by way of security, and the sale of the lorry.

The transfer of title by way of security was in January 2018, to offer security for a new loan. We do not know the value of the lorry at that time, but a little over a year later it sold for 20.000 euros. We can also note that the transfer of title of the lorry was not deemed sufficient security by the lender B to cover the 50.000 euros loan.

A transfer of title by way of security in a non-accessory security right. Indeed, B effectively held the title to the ownership of the asset in a fiduciary capacity. This means full ownership is transferred.

Presuming that this transfer of title was regularly accomplished, a contractual agreement must have been drafted between B and D on the transfer of property, and a separate security agreement. If the debtor remained in possession of the collateral (Section 930 BGB), then B could have had a constructive possession over the object, which suffices to establish the legal transfer of ownership, and can be noted in the agreement of the parties.

Therefore, B was the legal owner of the lorry since January 2018. The enforcement of any security rights can be done before the opening of insolvency proceedings, and even during preliminary insolvency proceedings, unless the court says otherwise.

New security was not granted just before the opening of the insolvency proceedings, in the three-month period prior to the opening of insolvency proceedings (Section 130 et 131 of InsO), but back in January 2018, and the general balance of the operation back in January 2018 seems established (new security, for a new loan). Therefore, this operation does not seem to be a contestable transaction in the terms of the relative InsO articles cited above.

However, it needs to be underlined that the case facts are not very clear in that if I is asking B to pay 50.000 euros (amount of the loan), then this implies that B might have not delivered the loan, or have, by terminating the contract, obtained full satisfaction for the claim. It might be interesting to see if this payment on the principal of the loan could not be clawed back as a preferential payment of a creditor, without discussing the validity of the enforcement of security rights. Indeed, the transfer of title as mentioned before does not have an accessory nature.

You could be more precise (and shorter): The sale of the lorry is the realization of an unchallengeable security right. This does not cause any additional disadvantage to the general body of creditors.

2) Payments of X, Y and Z

i) Payment of X

B revealed the assignment of receivables to the contractual partners of D on the 5th of July 2019. D applied for insolvency on 1st August 2019. If the relative legal requirements for the assignment of receivables were respected (proper notification of the debtor, in this case, to X), then B could have justifiably received payment from X (sections 398 and 413 of InsO).

In the case at hand, we do not know the date of the obligation created for the future receivables (X). It is necessary to know if the obligation was created in a three-month period prior to insolvency (see above for relative articles).

The facts are clear: X's claim was created through the contract with D 1 July 2019 and thus within the relevant suspect period. However, you should give reason why the assignment in January 2018 is not the relevant point in time.

If that is the case, then it is possible that the payment could be avoided under Section 130 of InsO, as it would be situated in the three-month suspect period before the opening of insolvency (and especially as B was aware of the situation of insolvency of D).

It could therefore be a contestable transaction that placed B in a better situation than it would have been in the insolvency proceedings, and reduced the distribution amounts available to other creditors.

ii) Payment of Z

Claims created after the opening of the insolvency procedure are not covered by the security right, as section 91 of InsO hinders the improvement of a creditor's position after the opening of proceedings.

So, all receivables created at this point are part of the insolvency estate and not the security right.

Therefore, I who has sold goods to Z for 5.000 euros was the correct debtor to pay, and not B. This obligation did not enter the security right but belonged to the insolvency estate. I could therefore claw-back this amount from B.

correct

iii) Payment of Y

The payment of Y must follow a mixed reasoning of the two payments aforementioned. Indeed, in order to decide whether Y could be avoided, it would be necessary to ask the following questions:

- When was the obligation was created,
- Can a creditor enforce assignment of receivables in "preliminary" insolvency proceedings, subject to the date of creation of the obligation, as the payment of Y happened before the opening of insolvency proceedings but after the petition had been filed at the Court by D.

In principle, on the second point, it could be possible for a creditor to enforce security rights in this preliminary period of insolvency proceedings, as long as all the legal requirements and subjects concerning avoidance transactions are respected (InsO 21(2)).

However, relating to the first point, it seems likely, in view of the facts of the case (sale of goods), that the obligation was created in the suspect period three months prior to the insolvency proceedings. Therefore, in this case, as in the payment of X, if the obligation was created in the three months prior to insolvency proceedings, the correct debtor to pay could have been D, not B, and the payment could be subject to a claw back by I.

The claim was created after the application for and prior to the opening of insolvency proceedings and is thus challengeable under § 130 (1)No.2 InsO.

12 marks

*** End of Assessment ***

in total: 46 marks