



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

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

10 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)?

ANSWER

Rules regulate cross-border insolvency law in Germany:

- 1) Cross border insolvency is regulated by section 335 onwards till section 358 of the Insolvenzordnung (InsO)
- 2) European Insolvency Regulation (Recast), 2015/848 governs insolvencies in EU (barring Denmark)
- 3) Annexure A of EIR Recast can be referred for automatic recognition of listed processes commenced in the EU
- 4) Recast Brussels Regulations, European Judgements Regulations or Lugano Convention 2007 for recognition of insolvency processes not listed in Annexure A of EIR Recast as judgements
- 5) Rome I – Regulation 593/2008
- 6) Zivilprozessordnung – German Code of Civil Procedure
- 7) German Civil Code

4, 5, and 7 do not regulate *insolvency law*. And you should mention bi-/multinational agreements.

2 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?

ANSWER

The principle of publication in German law with relation to security rights are rules which ensure that third parties are protected, by being able to gather information on rights which are enforceable against them through an external act of registration. The principle of publicity provides clarity as to who is the owner of a certain thing and indicates the real right (rights in rem). Legal rules for contractual transfer of ownership of assets vary basis the asset being transferred as do the rules for creating security rights on those assets.

Pledge

- The existence of pledge for tangible assets must be made public, by transferring possession to a creditor

Claims

- Claims must be made public by recording them in the insolvency claims schedule maintained by the insolvency administrator, however, assignment of claim does not require publicity except for waterway vessels of a certain size

The insolvency schedule does not show security rights. Pledges on claims need notification of the obligor.

Intellectual Property Rights (IPR)

- For some types of IPRs (patents, utility patents and commercial designs) pledge rights need to be publicized through registration in IPR registers

Receivables, stocks and other direct manufacturing current assets

- Security transfer agreement need not be registered and hence there is no strict publicity requirement

Immovables such as land, ships and planes

- Publicity is guaranteed for real estate assets by registering them in a register e.g. Land Register in the Registry of the local relevant court. This applies to both mortgages as well as land charges

Shares of Limited Liability Company (LLC)

- The assignment of shares of LLC requires a notarized agreement where parties have to appear before a notary public and sign the contract

Shares joint stock Company

- A pledge over shares is completed by transferring the relevant shares to the pledgee and no specific publicity is required except where required by stock exchange listing regulations

3 marks

Question 2.3 [maximum 3 marks]

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

ANSWER

Creditors who intend to participate in an insolvency proceeding must file their claims in writing with the insolvency professional handling the case including the proof, quantum and rationale for the claim.

After collation of all the claims (including request for additional evidence or clarification) against the debtor, claims are then entered into the claims schedule which can be accessed by all participating creditors. After the constitution of the Committee of Creditors (CoC), all registered claims are verified at a verification meeting of creditors called *Prüfungstermin* in accordance with their amount and rank.

Claims in the register are deemed to be final once the claims are not objected by the insolvency administrator or the creditor in the verification meeting and inducted in the insolvency schedule as validated claims. The debtor may argue against inclusion of a claim in the schedule but the debtor’s objection does not have an impact on the insolvency process. If the claim is contested in the validation meeting, then a trial court assesses the veracity of the claim and either allows or disallows the claim. If claim is allowed by the trial court then the claim is added to the claim schedule and the insolvency professional further verifies whether claims added to the schedule are on a pro-rata basis or not.

3 marks

in total: 8 marks

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

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

ANSWER

After determining the financial position of the debtor, the bankruptcy court can order the commencement **opening?** of bankruptcy proceedings where the debtor is insolvent. In the period after commencement of bankruptcy proceedings, the debtor continues operations subject to restrictions and limitations on disposal of assets. **This not correct, cf. § 80 InsO.** There is no moratorium on dues payable to operational creditors after the bankruptcy commencement and the debtor has to pay dues of the suppliers if he chooses to avail their services. **This is not correct either, §§ 80 et seq. InsO.** Hence executory contracts are valid and are binding on the bankruptcy estate, however, their effects are suspended until the insolvency administrator decides to deal with them.

Chapter II of Part III of the InsO lays down the rules that govern fulfilment of legal transactions and executory contracts. The treatment of executory contracts on opening of insolvency, liquidation and corporate rescue proceedings are regulated under section 103–128 of InsO. For specified transactions, the effects of insolvency proceedings are regulated by section 103–118 InsO. InsO does not expressly allow an insolvency administrator or the debtor to reject executory contracts, § 103 InsO? this is subject to section 104 of the InsO. Section 104 InsO, curtails insolvency administrator right's of choice for fixed date transactions and transaction on financial services. This is a very rare exception. Section 103 of InsO, allows the option to the insolvency administrator to either seek fulfilment or reject executory contracts. Indeed.

The insolvency administrator rights under Section 103 of the InsO does not apply to every mutual contract, there is a carve-out in Chapter II, Section 104 InsO also contains specialised provisions and rules to deal with fixed date and financial transaction and also specific types of contracts such as tenancies, lease over immovable objects (section 109 108 InsO) and contracts of employment (section 113 InsO).

Section 115 (Expiry of Mandates), Section 116 (Expiry of Management Contracts) and Section 117 (Expiry of Proxies), all deal with automatic termination of contracts that are of personal service and related to specific named individual in the contract. Contracts for lease and employment continue to exist and bind the insolvency estate.

Section 119 of the InsO, states agreements that exclude or limit application of section 103-108 (dealing with executory contracts) are invalid (Ipso facto clauses) and section 279 extends this to a scenario where debtor is in possession and is being monitored by insolvency monitor. Law in Germany hasn't been crystallised for termination under ipso facto clauses and it remains a contentious issue. Restricting enforcement of such a clause forces the counterparty to continue unviable contract with the debtor, which contravenes the sanctity of enforcing contractual remedies. Contractual termination, close-out netting or set-off provisions under executory contracts continue to survive insolvency.

InsO or Section 103 does not specify or impose a time limit for assuming or rejecting executory contracts. It is left to the reasonable commercial judgement of the insolvency administrator and requires no court interventions. Under the InsO, the counter-party can always request the administrator to expedite decision making stating that any delay in the matter could have a detrimental effect on the business of the counter-party and then the insolvency administrator would need to decide about the disposition of executory contract within a reasonable time frame else it would be deemed that the contract has been rejected and legal consequences would follow.

Once the insolvency administrator seeks fulfilment of the executory contract, then expenses related to the contract are considered as administrative expenses and have payment priority over other financial creditors as specified under section 55(1) sub-paragraph 2 of the InsO. However, if the contract is rejected by the insolvency administrator then the debtor is deemed to have breached the contract, giving the counter party an unsecured pre-bankruptcy claim (under section 103(2)) for damages (unless it is secured) and all the respective obligations expire. If the insolvency administrator breaches a contract after commencement of bankruptcy proceedings, the claim for damages arises and is treated as an administrative expenses of the estate.

Protecting supplies to the debtor for business continuity and maintaining going concern status:

Operating creditors are prohibited from terminating supply contracts merely on the count that the debtor has entered the insolvency. Termination is allowed specifically in cases where there is non-payment of dues for services provided after the debtor has entered into insolvency process. Operating creditors are allowed to exercise termination rights only when undue financial hardship can be demonstrated, following which the court will thoroughly examine the

cost of creditor's hardship versus the hardship faced by the debtor during the rescue plan period before assenting to such a termination.

10 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.

ANSWER

The various legal positions related to the fact base case are as follows:

Policy laid down under section 129 InsO for claw-back or avoidance transactions made prior to the opening insolvency proceedings and putting creditors to a disadvantage may be contested by the insolvency administrator under sections 130 to 146 of the InsO.

The insolvency administrator can void or impeach certain contracts and disposition of assets made by the debtor prior to the opening of the insolvency process or transactions taking place after the filing of the insolvency petition. Transactions which are to the detriment of the debtor are generally voided. Transaction such as preferential transactions, undervalue transactions, fraudulent transactions and extortionate credit transactions with related parties and others are generally reversed or reclaimed at the application of the insolvency administrator.

Generally, the claw-back period is 3 months prior to filing of the insolvency petition. However, this period is extended backwards from date of filing of the insolvency petition up to 10 years in certain suspect cases. The claw back period is determined as per section 140 of the InsO and it states that "*a transaction shall be deemed performed on the date when its legal effects become existent*" viz, conditions for legal effectiveness are met or when transaction is perfected.

Section 130 (Congruent Coverage), provides for reinstatement of assets that have left the insolvency estate, where they have been disposed-off 3 months prior to filing of the insolvency petition and the creditor was aware of the debtor's insolvency. In case of congruent coverage, the creditor receives a claim satisfaction which is equal to the amount due to it as per the loan agreement.

Section 131 (Incongruent Coverage), similar to section 130; provides for reinstatement of assets that have left the insolvency estate, when they have been disposed-off 3 months prior

to filing of the insolvency petition and the creditor was aware of the debtor's insolvency. This can be challenged during the last month prior to the request to open insolvency proceedings without demonstrating that the debtor was illiquid at that moment. In case of incongruent cover, the creditor receives an out of turn payment or perfection of security than otherwise due contractually or which is inconsistent with the contract.

Section 130 and section 131 deal with specific creditor preference transactions which disadvantage the creditor class as a whole and hence need to be challenged by the insolvency administrator. Additionally, connected parties are presumed to have known about the debtor's illiquidity or of the filing of the insolvency petition drawing suspicion of the insolvency administrator.

Under section 132 InsO (Transactions immediately disadvantaging the Insolvency Creditors), the insolvency administrator can choose to challenge transactions which directly prejudice the interests of creditors (fraudulent transactions). For voiding a transaction under this section, the transaction should cause direct detriment to the creditor not only as a consequence of the transaction but continuing also at the time of executing the transaction. The suspect period coverage under section 132 is a look back of 3 months prior to filing of the insolvency petition and the creditor was aware of the debtor's impending insolvency. Section 132 InsO not applicable in cases where section 130 & section 131 have been triggered. Provisions related to connected parties are the same as set out section 131 InsO.

Section 133 InsO (Wilful Disadvantage), any transaction entered in the claw back period of ten years leading up to the filing of the insolvency petition or in the period subsequent to the petition with an intent to prejudice creditors may be challenged by the insolvency administrator, if the counter-party was aware of debtor's intent on the date of the transaction. Onerous contracts with connected parties may be challenged as causing wilful disadvantage, if it was transacted within two years of the commencement of the insolvency proceedings. Any transaction out-side the suspect period of two years and where it is observed that the related party was not aware at the date of the transaction cannot be covered under section 133 InsO.

Section 134 InsO (Gratuitous Benefit), a gratuitous benefit granted is voidable under this section, if was granted in the suspect period of four years prior to the filing of the insolvency petition.

Section 135 InsO (Loans replacing Equity Capital) is not applicable for this case study since there is no mention of conversion of equity into loan or shareholder providing security or guarantee in lieu of third party loans and hence is not discussed.

Section 142 InsO (Cash Transactions) "Payments on the part of the debtor in return for which his property benefited directly from an equitable consideration may only be contested under the conditions of section 133 sub-section (1)". This covers transactions causing wilful disadvantage or those having incongruent transactions.

Case study testing:

Tabulated facts summarised for testing transaction avoidance under 129 *et seq* InsO.

Timelines	Particulars
January 2018	Date of Loan and transfer of security Bank (B) has granted debtor (D) a loan of EUR 50,000 and 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.
May 2019 Illiquidity/ D's substantive insolvency	Sixteen (16) months later D is unable to pay her debts when they fall due.
1 July 2019	X bought goods from D.
3 July 2019 Awareness of debtor insolvency	B, being aware of D's substantive insolvency, terminates the loan contract and sells the lorry for EUR 20,000 to W.
5 July 2019	B reveals the assignment to all customers of B and receives EUR 15,000 from X.
1 August 2019 Application for insolvency	D applies for insolvency proceedings.
10 September 2019	B receives another payment of EUR 10,000 from Y who bought goods from D.
15 September 2019 Appointment of insolvency administrator	Court opens insolvency proceedings and appoints I as insolvency administrator.
Post insolvency petition period business and sales	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.

You could have started with the following.

Bank (B) has granted debtor (D) a loan of EUR 50,000 and I (insolvency administrator) claims EUR 50,000 from B. Prima facie, avoidance transactions in the case study should get covered under section 130 (Congruent Coverage) InsO since it is specific creditor preference transactions which disadvantages other creditors of D and "Awareness of circumstances pointing directly to insolvency or to a request to open insolvency proceedings shall be considered equivalent to awareness of insolvency or of the request to open insolvency" (Section 130(2) InsO).

Application to open insolvency is filed on 1 August 2019, hence the claw-back period for vulnerable transactions starts from 1 August 2019 till 1 May 2019 where three months suspect period is applicable.

- Sale of lorry to W for EUR 20,000 on 3 July 2019

Lorry is sold to W on 3 July 2019. This transaction can be challenged under section 130(1) InsO because it is within the three month look-back period ending 1 May 2019 from filing of insolvency petition and the creditor B was aware of D's substantive insolvency.

This is not correct, since B had an unchallengeable security right and the realisation of this right does not cause new disadvantage for the general body of creditors.

- Receipt EUR 15,000 from X on 1 July 2019

B received EUR 15,000 from X on 1 July 2019, this transaction can be challenged under section 130(1)No.1 InsO because it is within the three month look-back period ending 1 May 2019 from filing of insolvency petition and the creditor B was aware of D's substantive insolvency.

Actually, decisive is not the payment of X but the establishment of the claim.

- Receipt of EUR 10,000 from Y on 10 September 2019

This can be challenged under section 130(1)(2) InsO which states that "A transaction granting or facilitating an insolvency creditor of security or satisfaction may be contested if it was made after the request to open insolvency proceedings, and if the creditor was aware of the debtor's insolvency on the date of the transaction, or of the request to open insolvency proceedings".

B received payment of EUR 10,000 from Y on 10 September 2019 which is after 1 August 2019, viz, the date request to open insolvency proceedings and B was aware of the D's insolvency on the date of the transaction.

correct

- Z pays EUR 5,000 to B

Again this can be challenged under section 130(1)(2) InsO, B received payment of EUR 50,000 from Y which is after 1 August 2019, viz, the date request to open insolvency proceedings and B, after 15 September 2019, which is date of appointment of I as insolvency administrator (I sold goods since he maintained business as an administrator) and since Z is a regular customer of D, it can be safely deduced that Z was aware of the D's insolvency on the date of the transaction.

This is not correct. B did not acquire this claim, since it came into existence after the opening of the proceedings (§ 91 InsO).

6 marks

*** End of Assessment ***

in total: 34 marks