



**SUMMATIVE (FORMAL) RESIT ASSESSMENT: MODULE 3A**  
**THE INSOLVENCY SYSTEM OF THE UNITED STATES**

This is the **summative (formal) resit assessment** for **Module 3A** of this course and must be completed by all candidates who **qualify for a resit exam for this module**.

**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: **[studentID.assessment3A]**. An example would be something along the following lines: 202122-514.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 "studentID" 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 **28 September 2021**. This assessment must be submitted to [David.Burdette@insol.org](mailto:David.Burdette@insol.org) via e-mail no later than 23:00 (11 pm) on **Tuesday 28 September 2021**.
7. Prior to being populated with your answers, this assessment consists of **8 pages**.

**ANSWER ALL THE QUESTIONS**

Commented [DB1]: 32.5 out of 50 = 65%

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

Commented [DB2]: 7 out of 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**

ABC Corp is filing for bankruptcy under chapter 11. Which of the following **is not** a party in interest in that proceeding?

- (a) A neighboring land owner who has leased equipment to ABC Corp.
- (b) ABC's government regulator.
- (c) A bank that has loaned money to ABC.
- (d) A local advocacy group.**
- (e) All of the above.

**Question 1.2**

Which of the following statements regarding executory contracts is **false**?

- (a) Executory contracts are clearly defined by the bankruptcy code.**
- (b) Chapter 11 debtors have greater flexibility than chapter 7 debtors on when they may assume, assign or reject an executory contract.
- (c) In the most common formulation, executory contracts are defined as those where both sides to a contract have material unperformed obligations.
- (d) A court will generally defer to a debtor's business judgment regarding whether to assume or reject an executory contract.
- (e) Under the hypothetical test, a debtor cannot assume an executory contract if the debtor could not also assign the contract.

**Question 1.3**

In which of the following scenarios does a bankruptcy court have constitutional authority to issue a final order? Assume in each that the counterparty to the dispute has not consented to the bankruptcy court's exercise of jurisdiction.

- (a) A counterclaim against the estate that introduces a question under state law.
- (b) Since the list of core proceedings is non-exhaustive, a bankruptcy court may issue a final determination on any matter that comes before it.

(c) A creditor's claim against an affiliate of the debtor that has guaranteed the debtor's obligation to the creditor

(d) A debtor's motion to dismiss an involuntary bankruptcy petition.

(e) None of the above.

**Question 1.4**

Which of the following statements about "pre-packs" is **false**?

(a) A pre-pack cannot be used if the debtor wishes to reject executory contracts.

(b) Creditors must have sufficient information about the debtor and the plan to make an informed voting decision.

(c) A pre-pack debtor may spend as little as a single day in bankruptcy.

(d) The proposed plan of reorganization is submitted to the bankruptcy court together with the voluntary petition.

(e) Creditors' commitment to vote in favor of the plan may be memorialized in a restructuring support agreement.

**Question 1.5**

Which of the following statements regarding cramdowns is **true**?

(a) If one insider creditor approves of the plan of reorganization, all other impaired classes may be crammed down.

(b) Because cramdowns do not require the consent of all classes, the plan of reorganization may not be fair and equitable to all impaired classes.

(c) Differential treatment of different classes is permitted if there is a reasonable, good faith basis for doing so and such treatment is required for the plan of reorganization to be successful.

(d) Class definition is rarely a battleground when a debtor tries to cramdown classes.

(e) Dissenting creditors are not permitted to challenge the classification of a creditor supporting the cramdown.

**Question 1.6**

Which of the following statements about the plan exclusivity period is **true**?

(a) The exclusivity period is 1 year.

(b) The exclusivity period cannot be extended.

(c) The exclusivity period cannot be shortened.

(d) During the exclusivity period, only a creditor may propose a plan of reorganization.

(e) During the exclusivity period, only the debtor may propose a plan of reorganization.

**Question 1.7**

Which of the following statements about chapter 15 is **false**?

(a) The automatic stay applies upon the filing of a petition for recognition.

(b) A debtor cannot be subject to an involuntary chapter 15 proceeding.

(c) A chapter 15 petition must be filed by a foreign representative.

(d) The automatic stay applies only to property within the territorial jurisdiction of the United States.

(e) Recognition may be granted to a foreign proceeding as either foreign main or foreign non-main.

**Question 1.8**

Which of the following statements about 363 sales is **false**?

(a) A 363 sale permits a debtor to sell an asset free and clear of encumbrances.

(b) A creditor's lien on assets sold in a 363 sale attaches to the proceeds of the sale.

(c) A 363 sale must be conducted as an auction with a stalking horse bidder.

(d) Purchasers may pay a higher price for assets sold in a 363 sale than in an out-of-court transaction.

(e) Sophisticated parties will insist on a 363 sale if there is any question regarding whether the sale is "in the ordinary course of business".

**Question 1.9**

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 has a claim for damages for breach of contract.

(b) The counterparty must immediately stop using the trademark.

(c) The counterparty can continue using the trademark for the remaining period of the license.

(d) Both (a) and (b).

(e) Both (a) and (c).

### Question 1.10

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

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

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

Commented [DB3]: 8 out of 10

#### Question 2.1 (2 marks)

What is the difference between a voluntary petition for bankruptcy and an involuntary petition for bankruptcy?

A company need not be in default of a debt or insolvent to file a voluntary petition for bankruptcy. An involuntary petition requires the creditors to state and allege that the debtor is not paying its due which is not required for a voluntary petition. An involuntary petition can be question in the event of a bonafide dispute as to the liability or amount. A voluntary petition is commenced by a debtor while creditors commence involuntary proceedings under either Chapter 7 or Chapter 11. In a involuntary petition, the creditors may also seek to appoint an interim trustee to remove the existing management control over the business of the debtor – in the absence of this in both cases the debtor continues to remain in control of the business.

2 marks

#### Question 2.2 (2 marks)

What are two potential consequences of a violation of the automatic stay?

Violation of an automatic stay is treated as contempt of court and the action will be void or voidable depending on the bankruptcy court in which the case is pending. Interested parties may seek to lift the stay and obtain a relief, in the absence of which (i) costs and sanctions may be imposed against the party violating and (ii) directions of affirmatives acts to undo the action violating the stay. A court may further stay the violation and impose daily fines.

2 marks

#### Question 2.3 (3 marks)

In what circumstances is a claim considered "impaired"? When is a holder of an impaired claim not entitled to vote on a proposed plan of reorganization and what happens instead?

The Bankruptcy Code specifies the designation of classes of claims of creditors since the classes are the basis on which voting rights are granted towards a reorgansiation plan of a debtor. A class of creditors is considered to be impaired of the legal, equitable and contractual

rights of the specific class is altered by a plan. Therefore, only an impaired class of creditors have a right to vote on a plan excluding insider votes – unless they are statutory insiders such as shareholders or there is no impaired class. A cramdown on dissenting impaired creditors is imposed to mitigate a holdout problem.

2 marks

#### Question 2.4 (3 marks)

Answer the following questions about preferences, actual fraudulent conveyances and constructive fraudulent conveyances:

- (1) Which cause of action applies only to transfers made on account of antecedent debt?

To establish a preference claim, the transfer must be on account of an antecedent debt. In the event a recipient contemporaneously gave the debtor a new value, a transfer cannot be avoided.

- (2) Which cause of action requires that the debtor be presumed or proven to have been insolvent at the time of the transfer?

Constructive fraudulent conveyance **No, preference**

- (3) Which cause of action requires that the debtor be proven to have intended to frustrate creditors' recoveries?

Actual fraudulent conveyance

2 marks

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

Commented [DB4]: 13 out of 15

#### Question 3.1 (3 marks)

How did *Stern v Marshall* change the law of bankruptcy court jurisdiction and authority to enter a final order?

Bankruptcy courts are created under the 1978 Bankruptcy Code and consequently several US judgments have held that judges of the bankruptcy courts cannot exercise jurisdiction over matters subjected to Article III. As a consequence of cases such as the Northern Pipeline Construction Co. v. Marathon Pipe Line Co, 458 US 50 (1982), new jurisdictional provisions have been enacted to grant jurisdiction over bankruptcy proceedings to district courts and now the Code distinguishes between **core and non-core matters** allowing bankruptcy courts to examine the same. The non-exhaustive list of core proceedings include: matters concerning administration of estate, counterclaims by the estate against persons filing claims against the estate, motions to terminate, annul or modify the automatic stay, however, in relation to non core proceedings, a final determination cannot be made by the bankruptcy courts. These amendments took place in 1984 that put to rest many questions of jurisdictional conflicts and issues including those related to jury trials with party consent conducted by bankruptcy courts (Langenkamp v. Culp, 498 US 42 (1990)). However in 2011, in the case of Stern v. Marshall, the US Supreme Court held that a bankruptcy court cannot invade Article III jurisdiction even in core proceedings. In this particular case, a first judgment was issued by the bankruptcy court award USD 400 million to the debtor but the parallel state court case continued while the

bankruptcy judgment was appealed to the district court. while counterclaims are listed as core proceedings – on the issue of which a bankruptcy court can issue a final judgment, the US Supreme Court held that the exercise of final judgment power over a state law claim was unconstitutional. The US SC further held that the bankruptcy courts exercise of final judgment power over a state law claim was unconstitutional under Article III. This resulted in amendments to bankruptcy rules and also further rulings of the US SC to clarify certain positions. Presently, the position relying on the cases of *Wellness Int'l Network Ltd. v. Sharif*, 135 S Ct 1932 (2015), Fed R Bankr P 8018.1 and *In re Schulz Mfg Fabricating Co*, 956 F 2d 686 (7<sup>th</sup> Cir 1992) together holds that bankruptcy judges may determine a core proceeding over which they do not have constitutional authority by issuing reports and recommendations that can be reviewed by the district court. in the case of non core proceedings with the consent of the parties, the same procedure can be followed for the issuance of final orders. The amended rules have implanted these rules by requiring a mention in pleadings whether parties consent to final orders or judgment by a bankruptcy court.

Long answer for 3 marks! Not all points covered – 2 marks

### Question 3.2 (3 marks)

What provisions of the Bankruptcy Code may not be invoked by a foreign representative in a chapter 15 proceeding? What are two ways that the foreign representative can obtain equivalent relief?

Chapter 15 excludes the right to use avoidance powers from the powers of the foreign representatives. The provision applies to cases of preference claims and fraudulent conveyances and does not bar the representative to undertake any pre-petition reliefs. A foreign representative may choose to commence plenary proceedings.

Other points for consideration:

1. The power to operate a debtors business in the ordinary course and the power to sell outside the ordinary course subject to court approval, which come into effect upon recognition of a foreign main proceeding do not authorise the foreign representative to return funds collected in the US proceeding to the foreign proceeding for distribution. The grant of such relief is discretionary and requires the foreign representatives to provide that the interest of the creditors are adequately protected.
2. Chapter 15 proceedings cannot be commenced by foreign representatives with respect to: persons who are not subject to chapter 7 proceedings, US citizens or permanent residents eligible to be debtors under Chapter 13 or entities subject to proceedings under the Securities Investor Protection Act.

Not a complete answer – 2 marks

### Question 3.3 (4 marks)

Describe the differences between interlocutory and final orders and how an appeal may be taken from each. Which courts hear direct appeals from bankruptcy court orders?

Final orders are those that close all issues relating to a case, i.e., no further adjudication on the matter whereas interlocutory orders resolve only a few issues or part claims. While final orders of courts can be appealed till the designated final court of appeal, interlocutory orders may only be appealed with the permission of the appellate court. in practice, the first appeal from a bankruptcy case will go to a randomly assigned judge who will then proceed to hear future appeals from the bankruptcy proceedings and presently there are Bankruptcy Appellate Panels who review all bankruptcy appeals. While the distinction between interlocutory and final orders has not been concretely established and is considered on a case to case basis, however the US Supreme Court in *Bullard v. Blue Hills Bank*, 135 S Ct 1686 (2015) has held that a *bankruptcy order resolving a discrete dispute is a final order for the purposes of an*



*appeal.* Appeals from bankruptcy courts are generally heard and reviewed by the relevant district courts but in certain circuits the bankruptcy appellate panel hears the case.

Good answer – 4 marks

#### Question 3.4 (5 marks)

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

In general, while director liability is a subject matter of state law, i.e. where the company is incorporated, Delaware is a leading state in business and most corporate laws are modelled on the laws of Delaware, as is the case in relation to director liability. The prevailing rule in relation to director liability is the business judgment rule, where directors are protected from errors in judgment. In an ordinary course of business directors owe a fiduciary duty of loyalty to the corporations best interest and a duty of care in decision making in relation to the corporation. In this context, it is presumed that the board of directors have acted in good faith and on the basis of reasonable information. A transaction is void unless a fairness standard is satisfied, example in cases where an independent or a controlling shareholder is on both sides of a transaction. Even when a company is insolvency, the board of directors of the company may pursue good faith strategies to maximise the value of the firm (*Trenwick Am Litig Trust v. Ernst & Young LLP*, 906 A.2d 168 (Del Ch 2006)). Moreover, while creditors can protect their interest by bringing derivative claims, individual creditors of an insolvent corporation do not have a right to assert direct claims on grounds of fiduciary duty violations against directors (*North Am Catholic Educational Programming Foundation, Inc v. Gheewala*, 930 A.2d 92, 103 (Del 2007)).

During the bankruptcy proceedings, directors continue to owe duties to the corporation and shareholders. Directors do not owe any duty to creditors in accordance with the *Trenwick* precedent.

Good answer – 5 marks

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

Commented [DB5]: 4.5 out of 15

#### Question 4.1 [4 marks]

Gambling Corporation is incorporated and has a principal place of business in Greece and it operates casinos and betting parlors in many international cities, including Athens, Las Vegas, London and Macau. Gambling Corp's bonds (governed by English law) are due to mature in one (1) year, but it is unable to repay or refinance them. Gambling Corp is considering using an English scheme of arrangement to restructure the bonds.

Discuss whether the English scheme of arrangement could be granted recognition under US chapter 15 as a foreign main or foreign non-main proceeding.

Yes, the English Scheme of Arrangement could be granted recognition under Chapter 15. A foreign representative must establish that a foreign court or administrative proceeding with respect to the debtor is pending and that the foreign representative is empowered to act by the proceeding. Under the definition of the foreign proceeding (Section/ Title 101 (23)) which includes foreign court reorganisations, Gambling Corp would be granted recognition unless a public policy defence can be successfully argued before the relevant US court. In terms of the second part of the question, the determination of the centre of main interest is the basis for characterising proceedings as foreign main or non main proceedings. The debtors COMI

presumed to be its place of incorporation is a rebuttable presumption and therefore factors of location of assets, management, headquarters, majority of debtors creditors and jurisdiction whose law will apply to most disputes become a subject matter of determination of a COMI – on the basis of which the type of recognition is granted by the US court. The case of Morning Mist Holdings Ltd. v. Krys (also known as In re Fairfield Sentry Ltd), 714 F. 3d 127 becomes relevant here which discussed the determination of COMI for filing a Chapter 15 proceeding. In the present instance, given valuable assets are in London and the governing law of contract of the bonds is English – despite the establishment being Greece; and also that no other proceedings have been opened in any other jurisdictions, the US courts may recognise the proceedings are foreign main proceedings – with a specific emphasis on the applicable law towards the refinancing arrangements proposed.

**No, recognition as foreign main proceeding not possible. COMI is Greece. May only recognise as foreign non-main proceedings.  
0 marks**

#### **Question 4.2 [5 marks]**

Oil Corporation is incorporated in Delaware and has its principal place of business in Texas. Oil Corp is facing a number of challenges to its business. First, ShipCo, one of its key customers, has filed a breach of contract lawsuit in Texas state court alleging that Oil Corp sold it contaminated oil that caused USD 1 billion in damage to ShipCo's container ships. Second, the US Department of Justice is investigating whether Oil Corp illegally purchased oil from countries subject to US sanctions. Third, Oil Corp. has missed a payment on its secured loan from USA Bank, and USA Bank is threatening to foreclose on an Oil Corp refinery located in the Philippines. Fourth, because of all these distractions, Oil Corp has forgotten to pay rent on its Houston, Texas office space and its landlord is threatening to evict it. What would be the effect of Oil Corp filing a chapter 11 petition on each of these four situations?

The contracts of Oil Corp and corresponding consequences of Chapter 11 proceedings are as follows:

1. ShipCo lawsuit in Texas = USD 1 billion: the initiation of the chapter 11 **will be stayed** on account of the legitimacy of the dispute in the event a voluntary petition is initiated. However, the initiation of Chapter 11 proceedings would result in the stay in the proceedings based on the stage on which the dispute is at.
2. DoJ Investigation on illegal purchase = criminal sanctions: initiation of chapter 11 proceedings **does not impose any automatic stay** over criminal proceedings hence the DoJ investigation can continue so long as it does not impact the assets of the corporation in Chapter 11
3. USA Bank secured loan = foreclosure in Philippines: initiation of Chapter 11 proceedings results in a worldwide **automatic stay** over the assets of the debtor in this case – Oil Corp, therefore USA Bank cannot initiate any new proceedings.
4. Rental agreement in Texas = eviction: The landlord cannot evict, pending chapter 11 proceedings since essential services of the debtor will continue pending bankruptcy since Chapter 11 will allow for the reorganisation of the debt. **Only half mark**

**3.5 marks**

#### **Question 4.3 [6 marks]**

Oil Corp has filed for bankruptcy and is planning to sell its plastic manufacturing business through a 363 sale. The plastic manufacturing business operates under the trademark "Interconnect", which is licensed from Plastic Corp. Oil Corp has invented several patented processes for plastic manufacturing, which it licenses to Plastic Corp. The main manufacturing facility for the plastic business is in Dallas, and Oil Corp has granted a lien on the facility to USA Bank to secure its USD 500 million loan.

Oil Corp thinks it will get the highest return for the plastics manufacturing business if it can (i) assume and assign the trademark license; (ii) reject the patent licenses so the purchaser has the exclusive right to use the patents; and (iii) sell the manufacturing facility free and clear of the USA Bank lien. Can Oil Corp achieve each of these goals without the consent of Plastic Corp and USA Bank? Why or why not?

- (i) The trademark license belongs to Plastic Corp, so Oil Corp needs permission to assume and assign the trademark license in the first scenario. This assignment can be done without permission from USA Bank unless barred by the security contract to USA Bank / requiring prior permission. The lien is on the business and not the intellectual property. **Yes**
- (ii) In the second instance Oil Corp does not need the permission of USA Bank or Plastic Corp since the patent licenses are assets owned by Oil Corp and therefore does not need any prior permissions from either USA Bank or Plastic Corp. **No**
- (iii) Oil Corp cannot sell the facility without the permission of USA Bank since a charge is created and it must either set off the amounts prior to sale or close the account. Oil Corp does not need the permission of Plastic Corp prior to sale of the manufacturing facility. **No**

363 sales allow OilCorp to retain control of the business.

**1 mark – you must provide reasons for your answers!**

**\* End of Assessment \***