



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: **[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.**
- 6.1 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 2022**. The assessment submission portal will close at 23:00 (11 pm) GMT on 1 March 2022. 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 2022** or by **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. If you elect to submit by 1 March 2022, you **may not** submit the assessment again by 31 July 2022 (for example, in order to achieve a higher mark).
7. Prior to being populated with your answers, this assessment consists of **8 pages**.

ANSWER ALL THE QUESTIONS

Commented [H(1): Total marks 36/50

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

Commented [H(2): Total marks 9/10

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and **mark your selection on the answer sheet by highlighting the relevant paragraph in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

Question 1.1

Commented [H(3): Correct, 1 mark

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

Commented [H(4): Correct, 1 mark

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

Commented [H(5): Correct, 1 mark

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.

Commented [H(6): Incorrect, the correct response is (a). The shortest pre-packs have been less than 24 hours.

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.

Commented [H(7): Correct, 1 mark

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.

Commented [H(8): Correct, 1 mark

(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

Commented [H(9)]: Correct, 1 mark

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

Commented [H(10)]: Correct, 1 mark

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

Commented [H(11)]: 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 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.

Commented [H(12)]: Correct, 1 mark

QUESTION 2 (direct questions) [10 marks]

Commented [H(13)]: Total marks 7.5/10

Question 2.1 (2 marks)

Commented [H(14)]: Total marks 2/2

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

A voluntary petition can be made by the debtor, whereas an involuntary petition is made by a petitioning creditor subject to satisfying the financial threshold of US\$15,775, and who is making a legitimate claim that the company is unable to pay its debts or a liability that is due.

Commented [H(15)]: Correct, 1 mark

Commented [H(16)]: Correct, 1 mark

Question 2.2 (2 marks)

Commented [H(17)]: Total marks 2/2

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

Acts taken in violation of the automatic stay are considered void or voidable as an act in contempt of court. Relief from the automatic stay can be obtained, but if such an act takes place, and/or relief has not been sought, the act can result in imposition of contempt actions such as paying the debtors attorney fees and taking affirmative action to undo the act.

Commented [H(18)]: Correct, 1 mark

Commented [H(19)]: Correct, 1 mark

Question 2.3 (3 marks)

Commented [H(20)]: Total marks 1/3

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?

A claim is considered impaired if its legal, equitable or contractual rights have been altered and they are unlikely to receive their claim in full. If an impaired claim will become unimpaired as a result of the plan, thus curing any default or loss, then they are not entitled to vote and they will be recognised within a separate class of unimpaired creditors.

Commented [H(21)]: Correct, 1 mark

Commented [H(22)]: An impaired claim that will receive nothing under the plan doesn't vote and is deemed to reject the plan.

Question 2.4 (3 marks)

Commented [H(23)]: Total marks 2.5/3

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?

A preference claim arises where a payment is made by a debtor to a creditor for a pre-existing debt. The date of the transfer if (for a non-insider) is 90 days prior to the petition date.

Commented [H(24)]: Correct, 1 mark

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

Debtors are presumed to have been insolvent 90 days prior to the petition date and thus any payments made to creditors outside of ordinary business to a creditor could be subject to a cause of action for a preference claim for antecedent debts.

Commented [H(25)]: Correct, 1 mark

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

Actual and Constructive fraudulent conveyances are causes of actions which requires that the debtor intended to frustrate creditors recoveries.

Commented [H(26)]: Partially correct, 1/2 mark, only actual fraudulent conveyance requires actual intent

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

Commented [H(27)]: Total marks 13.5/15

Question 3.1 (3 marks)

Commented [H(28)]: Total marks 2/3

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

Stern v. Marshall was a United States Supreme Court case in which the Court held that a bankruptcy court lacked constitutional authority under Article III of the United States Constitution to enter a final judgment on a state law counterclaim that is not yet resolved even though prior to the decision, Congress appeared to grant such statutory authority. It was decided that as the Bankruptcy Court's decision was a non-core matter, it could not enter a final judgement on it. As such, bankruptcy courts lack the constitutional authority to enter a final judgment on certain state-law claims submitted by a debtor as a counterclaim to a proof of debt. Thus bankruptcy courts now may enter a final judgment only over counterclaims that either arise directly out of bankruptcy law or are so intertwined with the proof of debt claim that they would have to be resolved in the claims adjudication process.

Commented [H(29)]: Correct, 1 mark

Commented [H(30)]: Correct, 1 mark

Commented [H(31)]: Incorrect, the counterclaim was a core matter but nonetheless the court held that the bankruptcy court lacked jurisdiction to enter a final order

Commented [H(32)]: Incorrect, the bankruptcy court can enter a final order on a challenge to a petition or when the parties consent

Question 3.2 (3 marks)

Commented [H(33)]: Total marks 3/3

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 rights for avoidance powers and fraudulent conveyances, despite it closely following the Model Law in many other respects. If a foreign representative seeks to obtain these powers, s/he can do so via a plenary proceeding under the Bankruptcy Code after Chapter 15 recognition is obtained. The scope will then be limited to the debtors assets in the US. Alternatively s/he can seek recovery actions under any other applicable US law subject to limitations issues.

Commented [H(34)]: Correct, 1 mark

Commented [H(35)]: Correct, 1 mark

Commented [H(36)]: Correct, 1 mark, foreign laws may also be invoked if applicable

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?

A final order is one that “disposes of all issues” leaving nothing to be decided, whereas an interlocutory order resolves only some issues or claims.

An appeal from a final bankruptcy order can be heard by the district court or BAP (Bankruptcy Appellate Panel – made up of Bankruptcy Judges in the State) filed and appealed at the same, whereas an appeal of an interlocutory bankruptcy court order may only be taken with the leave of the district court.

Normally issues of core proceedings are dealt with by the Bankruptcy Court and the US Supreme Court has held that a bankruptcy order resolving a discrete point is a final order for appeals purposes.

Commented [H(37)]: Total marks 3.5/4

Commented [H(38)]: Correct, 1/2 mark

Commented [H(39)]: Correct, 1/2 mark

Commented [H(40)]: Correct, 1 mark

Commented [H(41)]: Correct, 1 mark

Commented [H(42)]: Correct, 1/2 mark, whereas a final order is appealable of right

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?

Directors of Delaware corporations are subject to the fiduciary duties of a) care and b) loyalty (which include the subsidiary duties of good faith, oversight and disclosure). These can be described as a) having informed, deliberative decision-making based on all material information reasonably available and b) acting on a disinterested and independent basis, in good faith.

Being disinterested is considered has being free of any material financial or other benefit from the matter under consideration and not having a relationship with any interested party that would or could influence the director in his/her decision making.

Directors are expected to have sufficient board level attention to risk management issues eg compliance with the law and business regulations, however Delaware law will apply the “Business Judgement Rule” which is a presumption that directors are acting in accordance with their fiduciary duties, and thus, any rebuttal of that presumption and the burden of proof in that rebuttal lies with the plaintiff. The Business Judgement Rule not applicable only when Board decisions are made with the majority of the board being non-independent or disinterested, or when a controlling shareholder sits on both sides of a transaction. In those circumstances they will be considered void unless the “entire fairness” is satisfied.

This is enforced further with confirmation that a director is entitled to rely in good faith on company records and on information presented to the board by the company’s officers, employees or board committees, or indeed by whomever the director can reasonably believe or assert the information was within their sphere of professional or expert competence.

In addition, Delaware corporations may include in their certificates of incorporation (COI) an exculpation provision for the benefit of directors, which prohibits the personal liability of a director to the corporation or its stockholders for monetary damages for breaches of the duty of care (but not, among other things, breaches of the duty of loyalty).

Commented [H(43)]: Total marks 5/5

Commented [H(44)]: Correct, 1 mark

Commented [H(45)]: Correct, 1 mark

All of the above is demonstrative of the fact that Delaware law has “put to rest” any theory that Directors have a duty to creditors; Directors of Delaware companies owe their duties to the corporation and to its shareholders, and not to creditors even in circumstances of potential or actual insolvency.

Commented [H(46)]: Correct, 1 mark

Commented [H(47)]: Correct, 1 mark

Commented [H(48)]: Correct, 1 mark

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

Commented [H(49)]: Total marks 6/15

Question 4.1 [4 marks]

Commented [H(50)]: Total marks 4/4

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.

Under Chapter 15, a foreign proceeding or foreign non-main proceeding will be determined based upon where the debtor has its center of main interest (or COMI). Whilst COMI is not defined within Chapter 15, it is presumed generally as the location of the company’s incorporation or registered office. That said, COMI can be challenged if it is truly said to be where it is headquartered and where the majority of business and operational decisions are made, or in other words where its “nerve centre” is located, and/or where the location of its assets are.

A foreign non-main proceeding is where the debtor may have an establishment, or where the company has “any place of operations where the debtor carries out a non transitory economic activity”.

Therefore in this example, the English scheme of arrangement, could be granted recognition under US Chapter 15 as a foreign non-main proceeding because: it is incorporated and has its principle place of business in Greece, but has an establishment in London (amongst other locations) and, the bonds in which it is seeking to restructure is being undertaken through English proceedings.

Commented [H(51)]: Correct, 1 mark

Commented [H(52)]: Correct, 1 mark

Commented [H(53)]: Correct, 1 mark

If it was being restructured via insolvency proceedings in Greece, it would have been considered a foreign main proceeding.

Commented [H(54)]: Correct, 1 mark

Question 4.2 [5 marks]

Commented [H(55)]: Total marks 2/5

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?

Breach of contract

If Oil Corp chose to file a Chapter 11 petition, then the breach of contract claim by ShipCo will be considered a pre-petition action (as it was taken prior to any decision to file a petition to restructure) and as such it is likely to be decided before a state court as a non-core proceeding.

Commented [H(56): The automatic stay would come into effect on the filing of the petition.

If ShipCo filed a proof of claim then the judge may decide that the creditor voluntarily subjected itself to the bankruptcy court's jurisdiction, but if not, then the State court will be the likely forum, the result of which is that the damages if awarded, will still be payable and the reorganisation plan would need to consider the ability to pay a potential award. Nevertheless, a stay on all pre-petition litigation is made pending the outcome of any reorganization plan, which may give Oil Corp some breathing space and potential room for negotiation.

Commented [H(57): Correct, 1 mark

The risk to Oil Corp is that Ship Co may seek to transfer the appropriate jurisdiction for the insolvency proceeding as into Texas, based upon its principle place of business, and where litigation is ongoing, rather than the assumed filing by Oil Corp in Delaware, which is a far friendlier state for directors and their duties owed.

Sanctions breaches

Any investigation being undertaken by a law enforcement agency would be subject to the criminal law, including breach of US sanctions law. The filing of a Chapter 11 application will not negate this possibility. Instead, it is likely that the US Trustee may also investigate criminal, fraudulent, or abusive conduct for possible civil or criminal prosecution would pursue the matter and if required, refer the matter for criminal prosecution.

Commented [H(58): Correct, 1 mark, this is an exception to the stay

Missed payment on secure loan

Under Chapter 11, Oil Corp could seek to restructure the debt by lowering the interest rate on the loan, extending its maturity, or both. In certain circumstances, the amount of secured debt can be written down to the value of the creditor's collateral.

The potential difficulties for USA bank to foreclose in an overseas jurisdiction may provide for better negotiating terms for Oil Corp.

Commented [H(59): Incorrect, the stay has worldwide effect so would bar foreclosure in the Philippines

Missed rent payment – office space

In a Chapter 11 bankruptcy filing, unexpired leases (non residential leases) become property of the bankruptcy estate. This allows the debtor to decide whether to assume the lease, or reject the lease. Moreover, a tenant automatically gets four months to decide whether to assume or reject a lease. If Oil Corp decide to reject the lease, it is automatically deemed in breach of the lease agreement and the landlord can therefore terminate the lease accordingly and surrender the property. The landlord is then left with a claim for damages. If Oil Corp decides to assume the lease, it must cure all monetary defaults or provide adequate assurance that such defaults will be promptly cured, as well as provide adequate assurance of its future payments.

Commented [H(60): As an unexpired lease, the automatic stay bars eviction proceedings

Question 4.3 [6 marks]

Commented [H(61): Total marks 0/6

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?

A

*** End of Assessment ***