



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 41.5/50

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

Commented [H(6): Correct, 1 mark

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

Commented [H(7): Correct, 1 mark

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

Commented [H(8): Correct, 1 mark

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

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)]: Incorrect, the correct response is (e)

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 8/10

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?

Voluntary petition can be initiated by the debtor under any applicable chapter of US Bankruptcy code.

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

Involuntary petition can be initiated by eligible creditors under either chapter 7 or chapter 11 only.

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

Commencement of voluntary petition does not require proof of debtor's insolvency to be established. For commencement of involuntary petition, there needs to be allegation of debtor's insolvency.

Involuntary petition requires minimum number of non-contingent non-insider creditors to apply depending on total number of such creditors. Voluntary petition is made by debtor and has no such requirements.

Question 2.2 (2 marks)

Commented [H(17)]: Total marks 1/2

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

Following are the two potential consequences of violation of the automatic stay

1. Imposition of contempt sanctions which may include payment of debtor's legal fees.
2. Requiring the violator to take actions to undo the effects of its violation.

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

Commented [H(19)]: This is part of the remedies for contempt, but the act's legal status is void or voidable depending on the circuit

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 claim is considered "impaired" unless the restructuring plan leaves the claim holder's "legal, equitable and contractual rights" unaltered. The claim is also considered impaired unless the plan reverses contractual acceleration by curing monetary default and compensating the holder for any damages.

If the restructuring plan proposes zero recovery to a class of claim, the class is deemed to have rejected the plan and not entitled to vote.

All insider creditors are not allowed to vote on the restructuring plan. Unimpaired class of creditors are deemed to have accepted the plan and class of creditors receiving zero recoveries are deemed to have rejected the plan. Thus, only the remaining impaired class of creditors get to vote on the restructuring plan. If the plan is accepted by just one impaired class of creditors it is enforced on all other creditors (cramdown). Voting threshold within a class if 2/3 by value of claim.

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

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

Commented [H(22)]: Correct, 1 mark

Commented [H(23)]: Correct, 1 mark

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?

Preferences

Commented [H(25)]: 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?

Preferences, Actual fraudulent conveyances, constructive fraudulent conveyances

Commented [H(26)]: Incorrect, only preferences require insolvency at the time of the transfer; it may be but is not required to establish a fraudulent conveyance.

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

Actual fraudulent conveyances

Commented [H(27)]: Correct, 1 mark

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

Commented [H(28)]: Total marks 13.5/15

Question 3.1 (3 marks)

Commented [H(29)]: Total marks 2.5/3

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

In USA, the bankruptcy courts derive their powers from Bankruptcy legislation. This is unlike most other federal courts which are established under Article III of the US Constitution. This creates issues related to jurisdiction. Judges not appointed under Article III, such as bankruptcy judges, cannot exercise jurisdiction over matters subject to Article III. To resolve this issue, a distinction between "core" and "non-core" matters was created.

The 1984 amendments to the Bankruptcy code gave authority to bankruptcy courts to issue final orders in core proceedings only. However, in *Stern V Marshall* case in 2011, US Supreme Court ruled that even in core proceedings the bankruptcy court cannot issue final orders that invade the Article III jurisdiction.

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

Commented [H(31)]: Correct, 1 mark

However, subsequent supreme court rulings and amendments to the Bankruptcy rules have clarified the issue further. The Bankruptcy Judges may determine core proceedings over which they lack constitutional authority by issuing a report and recommendation for a review by the district court or with consent of the parties may issue final orders. This is the same procedure as in non-core proceedings. Now the litigants have to state in their pleadings whether they consent to the entry of final orders by bankruptcy court.

Commented [H(32)]: Correct, 1/2 mark, also can enter a final order on a challenge to a petition

Question 3.2 (3 marks)

Commented [H(33)]: Total marks 2/3

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?

A foreign representative in chapter 15 proceedings cannot invoke the avoidance powers provided by the bankruptcy code. These provisions are mainly related to use of bankruptcy code's powers of avoidance of preference and fraudulent conveyances.

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

A foreign representative can invoke avoidance powers in a plenary proceeding such as chapter 7 or 11. Such proceedings may be initiated by debtor or creditors prior to involvement of foreign representative or foreign representative might commence these proceedings post recognition of foreign proceedings under chapter 15.

Commented [H(35)]: Correct, 1 mark, or a foreign representative can bring a claim under analogous foreign or non-bankruptcy US law

Question 3.3 (4 marks)

Commented [H(36)]: Total marks 4/4

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 orders which dispose of all the issues, leaving nothing further to be decided. Final orders may be appealed as of right.

Interlocutory orders are those orders which resolves only some issues or claims. Interlocutory orders may be appealed only with the leave of the appellate court.

Commented [H(37)]: Correct, 1/2 mark

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

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

Commented [H(40)]: Correct, 1/2 mark

Bankruptcy proceedings are generally an aggregation of individual disputes. Thus, a bankruptcy court's order resolving a discrete dispute is considered final order for appeals

purpose. Additionally, the orders extending the period of exclusivity to propose a plan are appealable as of right.

Appeals from bankruptcy courts are heard by

- The district courts
- In some circuits (first, sixth, eighth, ninth, tenth) by Bankruptcy Appellate Panel (BAP) which is convened from the judges of the bankruptcy courts within the circuits. Parties can also request the appeal to be heard by the district court instead.

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Commented [H(42)]: Correct, 1 mark

Appeals from district courts or BAP are heard by the circuit court of appeals. In rare circumstances, the appeals may directly go to Supreme Court where the bankruptcy court or district court certifies either the case raises a question of law or immediate appeal may materially advance the case.

Appeal from circuit court of appeals will go to Supreme Court.

Question 3.4 (5 marks)

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

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 insolvent?

Directors of Delaware corporate owe a fiduciary duty of loyalty to the corporation's best interest and a duty of care in educated decision making (business judgement).

Directors owe these duties to the corporation and its shareholders in all scenario i.e. both in ordinary course of business as well as when the corporation is potentially or actually insolvent. Directors do NOT owe these duties to the creditors of the corporation.

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

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

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

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

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

The supreme court of Delaware has given a clear judgment in North American Catholic Educational Programming Foundation, Inc. v. Gheewalla. The Supreme Court of Delaware concluded that creditors of corporation, which is in the "zone of insolvency," could not assert a direct claim for breach of a fiduciary duty against the corporate directors.

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

Commented [H(49)]: Total marks 11/15

Question 4.1 [4 marks]

Commented [H(50)]: Total marks 3/4

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 bankruptcy court can recognize a foreign bankruptcy proceeding as either a "foreign main proceeding" or a "foreign nonmain proceeding."

The Bankruptcy Code defines a foreign main proceeding as "a foreign proceeding pending in the country where the debtor has the center of its main interests (COMI). The Bankruptcy Code does not define the COMI. Relevant factors to be considered for COMI analysis are

1. Location of Headquarters – Gambling Corporation is incorporated and has a principal place of business in Greece.

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

2. Location of Management – It can be assumed the management is location in its principal place of business i.e. Greece.
3. Location of Primary Assets – Gambling corporations have casinos and parlours in many international locations including Greece
4. Location of Majority of debtor's creditors or majority of creditors that will be affected by the action – This information is not provided.
5. Jurisdiction whose law will apply – Bonds are governed by English Bonds.

However, we do not know if bond holders are the only creditors of the company.

Thus, the COMI of Gambling Corporations should be considered as Greece and Greek Insolvency proceedings can be considered as the Foreign Main Proceedings under chapter 15 of US Bankruptcy code.

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

Commented [H(52): Correct, 1 mark

Commented [H(53): Correct, 1 mark, the London casino would be the necessary establishment in the jurisdiction

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?

Commented [H(54): Total marks 5/5

On filing of a chapter 11 petition, an automatic worldwide stay comes into effect immediately. The scope of the stay is covered in 11 U.S. Code clause 362. The impact of this stay on the four situation is as follows -

Commented [H(55): Correct, 1 mark

1. Breach of contract Lawsuit by ShipCo (customer) – USD 1bn damages

The code prohibits initiation, continuation, or enforcement of any pre-petition claims on the debtor or its property. This this lawsuit will be stayed.

Commented [H(56): Correct, 1 mark

2. US DoJ investigation on illegal oil purchase –

This stay does not extend to criminal investigation or proceedings. This US DoJ investigation on whether Oil Corp illegally purchased oil from countries subject to US sanctions will continue.

Commented [H(57): Correct, 1 mark

3. USA Bank Foreclose OilCorp refinery location in Philippines –

The code prohibits enforcement of any security by creditors on pre-petition claim. Hence this action by USA Bank will have to be stayed.

Commented [H(58): Correct, 1 mark

4. Landlord Eviction for non-payment of commercial lease -

This stay does not stop eviction of debtor-tenant from non-residential property where lease is expired or terminated by the expiration of the stated term of the lease.

Commented [H(59): Correct, 1 mark, but here there is no evidence the lease had expired

Question 4.3 [6 marks]

Commented [H(60): Total marks 3/6

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?

Reference Clause 365 (Executory contracts and unexpired leases)

(i) **Assume and assign the trademark license**

Trademark (Interconnect) is owned by Plastic Corp (executory contract). While the bankruptcy law abrogates contractual restrictions on assignment to enable debtor to achieve higher value of its assets, counterparty consent is required in case of Intellectual property licensing law. Thus, Oil Corp will require consent from Plastic Corp to assign the trademark license to the Purchaser.

Commented [H(61)]: Correct, 1 mark

Commented [H(62)]: Correct, 1 mark

Oil Corp does not require any consent from USA Bank for this goal.

(ii) **Reject the patent licenses so the purchaser has the exclusive right to use the patents**

Oil Corp owns patented process it has licensed to Plastic Corp (executory contract). If Oil Corp terminates this executory contract, the licensee (i.e. Plastic Corp) may choose to enforce its rights as per the terms of contract and as per non-bankruptcy law including damages. Hence the propose course of action depends on the terms contract between Oil Corp and Plastic Corp.

Commented [H(63)]: Incorrect, contractual limitations are not enforceable in bankruptcy, but the Bankruptcy Code's section 365(n) protects licensees of patents and therefore consent would be required

Oil Corp does not require any consent from USA Bank for this goal.

(iii) **Sell the manufacturing facility free and clear of the USA Bank lien**
Reference Clause 363 (Use, sale, or lease of property)

Oil Corp can sell this manufacturing facility under 363 sale process and free and clear of USA Bank lien. Since this facility is lien marked to USA bank, its consent is required for the sale along with the consent of the court. USA bank will have priority on the proceeds from its sale.

Commented [H(64)]: Incorrect, the property can sold without USA Bank consent where the value of the assets exceed the amount of the loan

Consent of Plastic Corp is not required for sale of this manufacturing facility.

Commented [H(65)]: Correct, 1 mark, the lien will transfer to the proceeds of sale

*** End of Assessment ***