



**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 44.5/50

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

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

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) yA 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**

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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**

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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**

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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) T - 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.

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### 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 petitions for bankruptcy are commenced by a debtor, whereas involuntary petitions are commenced by creditors.

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

Voluntary petitions require no allegation that the debtor is insolvent, whereas involuntary petitions require the petitioning creditor to allege (i) that the debtor is generally not paying their debts when they fall due or (ii) that a custodian has been appointed (without the debtor's authorisation) to take charge of substantially all of the debtor's property in the 120 days before the filing of the involuntary petition.

Voluntary petitions can also be commenced under any applicable chapter of the Bankruptcy Code, whereas involuntary petitions can only be commenced under Chapter 7 or Chapter 11. Unlike voluntary petitions, involuntary petitions can also not be commenced against a farmer, family farmer or not-for profit corporation.

#### Question 2.2 (2 marks)

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

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

1. The party in violation of the stay may be subject to contempt sanctions, such as being ordered to pay the debtors' attorneys' fees. The party in contempt may also be ordered to undo the effect of its violation, along with supportive coercive contempt sanctions (e.g. daily fines applicable while the breach remains existing).
2. The transaction in breach of the automatic stay will be automatically void or voidable (which is dependent on the circuit in which the bankruptcy is pending).

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

#### Question 2.3 (3 marks)

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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 impaired if any legal, equitable or contractual right of the claim holders within its class are altered (s1123 and 1124, Bankruptcy Code). This would include impairments such as reducing the claim holder's level of debt or delaying their payment term.

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While insiders can vote on a plan of reorganisation, its votes will not be counted. Instead, the remaining members of the class must meet the 2/3 requirement (based on claim value) of voting to accept the plan. The holder of the impaired claim could still seek to challenge the plan before the court on the basis it is not fair and reasonable.

Commented [H(22)]: An impaired claim that will receive nothing under the plan do not vote and are deemed to reject the plan.

#### Question 2.4 (3 marks)

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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?

Preference.

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?

Preference.

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 fraudulent conveyance.

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

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##### Question 3.1 (3 marks)

Commented [H(28)]: Total marks 2.5/3

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

Prior to the decision in *Stern v Marshall*, the bankruptcy court's jurisdiction to grant final orders in respect of 'core' matters' (as opposed to 'non-core' matters) was well established. This distinction was established under the referral statute (28 USD §157 and 1334), which also set out a non-exhaustive list of what was considered 'core proceedings', such as proceedings to turn over property of the estate.

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*Stern* changed this position by holding that the bankruptcy court does not have jurisdiction or authority to enter a final order where the relevant matter falls within the jurisdiction of Article III, even if they were 'core' matters under the referral statute. Article III concerns the jurisdiction afforded to federal courts under the US constitution.

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In the *Stern* case, this meant a bankruptcy court's ruling on a debtor's counterclaim against one of its creditors was unconstitutional. Instead, the state court's jury verdict was the final judgment and conclusive of the issues.

This change in law has resulted in changing practises in the courts – including (i) the bankruptcy courts issuing reports and recommendations for review by the district court (as endorsed by the US Supreme Court in *Executive Benefits Ins Agency v Arkison*) and (ii) inviting parties to confirm at the outset of proceedings whether they consent to the bankruptcy court's orders and judgments being entered as final.

Commented [H(31)]: Correct, 1/2 mark, also the bankruptcy court may enter final orders on challenges to a petition

### Question 3.2 (3 marks)

Commented [H(32)]: 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?

A debtor in possession's or trustee's avoidance powers pursuant to the Bankruptcy Code are not available to foreign representatives, having been excluded under 11 USC §1523(a). This has generally been interpreted to be restricted to preventing a foreign representative pursuing preference and fraudulent conveyance transactions, and not to prevent foreign representatives bringing claims under other, non-bankruptcy, foreign laws (*In re Condor Ins Ltd*).

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Foreign representatives can obtain equivalent relief by seeking to undo pre-petition transactions using (i) other applicable US law or (ii) the laws of the country that they were initially appointed in. It may also be open to the foreign representative to open separate plenary proceedings in the US under the Bankruptcy Code – noting the low geographical jurisdictional threshold required to open bankruptcy proceedings in the US.

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

### Question 3.3 (4 marks)

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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?

Interlocutory orders resolve only some issues or claims in proceedings (which generally means the proceedings can/will continue after they are made). Whereas final orders dispose of all issues and therefore leave nothing further to decide.

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

Given the collective nature of bankruptcy as a remedy, the US Supreme court has held that an order resolving a discrete dispute in insolvency proceedings is a final order for appeals purposes. This means that insolvency proceedings remaining open after a court order does not preclude its from being considered final.

Final orders can be appealed as of right, whereas interlocutory orders can only be made with the leave of the appellate court.

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

The court that hears the appeal from the bankruptcy court will depend on the circuit within which the bankruptcy court sits. In most circuits, the appeal will be to the district court of that circuit. In certain other circuits, the appeal may be referred to the Bankruptcy Appellate Panel (albeit a party has the option to request that it be heard by the district court instead).

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

### Question 3.4 (5 marks)

Commented [H(43)]: Total marks 4/5

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 actually insolvent?



In Delaware, directors owe duties to the corporation they are a director of and not its shareholders. This duty is owed at all times. Unlike other jurisdictions, directors do not owe any duty to the company's creditors – even in circumstances where the company is or is potentially insolvent, despite the shareholders therefore having little to no financial interest in any ultimate bankruptcy (*North AM Catholic Educational Programming Foundation, Inc v Gheewalla*).

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Commented [H(45)]: Incorrect, the duties are also owed to and enforceable by the shareholders

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

The fiduciary duties directors of Delaware corporations owe to the corporation and its shareholders include (i) a duty of loyalty to the corporation's best interests and (ii) a duty of care in educated decision making.

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

The directors are, however, entitled to rely on the 'business judgment' rule to protect them from liability for breaches of fiduciary duties arising from errors of judgment. The business judgment rule provides that a board is presumed to have acted in good faith and based on reasonable information, albeit that presumption can be rebutted. Unless the presumption of acting in good faith and based on reasonable information is rebutted, a director cannot be held liable for breaching his duties to the corporation/shareholders in the absence of gross negligence.

The business judgment rule does not apply where the board is not disinterested and independent, or where a controlling shareholder is on both sides of a transaction concerning the corporation.

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

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##### Question 4.1 [4 marks]

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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.

An English scheme of arrangement is capable of being granted recognition in the US under chapter 15 as it satisfies the requirement of being "a collective judicial or administrative proceeding in a foreign country" under a law relating to adjustment of debt in which the assets and affairs of the debtor are subject to the supervision of a foreign court for the purposes of reorganisation. Gambling Corporation's scheme therefore could be recognised in the US.

An application for such recognition may be refused if the scheme itself is manifestly contrary to US public policy. This is a very narrow restriction so, if the scheme has been scrutinised and sanctioned by the English High court is unlikely to be triggered.

Whether the English scheme is granted recognition as foreign main or foreign non-main is dependent on whether Gambling Corporation's centre of main interest is located in England and Wales.

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Based on the information available, Gambling Corporation is likely to be Greece on the basis it is incorporated there and it has its principal place of business there. However, the presumption that a COMI is in a corporation's place of incorporation is rebuttable and the assessment of COMI is based on considering and balancing various factors such as the

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location of the headquarters, management, primary assets etc. There may therefore be arguments to argue Greece is not the COMI.

Assuming, based on the information available, England & Wales is not Gambling Corporation's COMI, the US would categorise the English scheme of arrangement as foreign non-proceedings. This means the scope of relief available under the US recognition is more limited and will only be available subject to the discretion of the court (as opposed to being available automatically). In order to obtain such relief, the English foreign representative will need to satisfy the court that it is appropriate in the circumstances for the assets in question to be administered in the English scheme.

**Commented [H(53):** Correct, 1 mark, the London casino would qualify as the necessary establishment

#### Question 4.2 [5 marks]

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

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?

Once Oil Corp files a petition for chapter 11 relief, it benefits from the automatic worldwide stay. This stay allows it with time to formulate and negotiate a restructuring plan within the initial 120 day exclusivity period.

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In relation to each of the four scenarios:

1. ShipCo's claim against Oil Corp constitutes litigation on a pre-petition claim. It will therefore be subject to the stay and therefore will not be capable of being continued. Oil Corp should provide written notice to the court and the other parties of its petition, which will likely result in the claim being stayed. Instead, Ship Co's will claim will fall to be dealt with in the chapter 11 process. This may require a separate process to establish the quantum of ShipCo's damages claim and, assuming it will be impaired, to verify the quantum of its voting power in respect of any reorganization.
2. The US Department of Justice can continue investigating Oil Corp for illegally purchasing oil from countries subject to US sanctions as it constitutes a regulatory investigation that is not subject to the worldwide stay.
3. Any foreclosure action taken by the USA Bank would constitute an act to obtain possession or control of the property of Oil Co. As the filing of the Chapter 11 petition gives rise a worldwide automatic stay, the USA Bank should not proceed with the foreclosure. If the debtor has no equity in the property in the Philippines and it is not necessary for the restructuring, or if the Bank considered the filing was to delay, hinder or defraud its creditors, it could make an application to lift the stay. If not, assuming it's claim is being impaired, it will be entitled to vote on any reorganization plan put forward.
4. Assuming the lease of the Houston property has not expired, eviction would constitute an act to obtain possession or control of the property of Oil Co and therefore be in breach of the stay. The landlord therefore cannot take eviction action. Any claim for

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**Commented [H(57):** Correct, 1 mark

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**Commented [H(59):** Correct, 1 mark

arrears (assuming they are to be impaired) will allow the landlord to vote on any reorganization plan put forward.

Where any breach of the stay occurs, the breaching party risks being found in contempt of court.

**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?

Each of the contracts concerned appear to be executory contracts. In the case of the two IP contracts with Plastic Corp, it is assumed the licence term has not expired and there are outstanding payment obligations on the licensee side. In the case of USA Bank, it is understood the facility remains outstanding and repayment obligations are due.

1. Oil Corp (or its trustee) requires the consent of Plastic Corp to assume and assign the trademark license. It therefore cannot achieve its first goal unilaterally. This is because trademark licenses are generally not assignable absent licensor (i.e. Plastic Corp.) under Federal Law (confirmed in *Re Trump Entertainment Resorts, Inc*). This is in contrast to the majority of executory contracts (i.e. contracts with unperformed obligations on both sides), which can be assigned absent counterparty consent in bankruptcy pursuant to the Bankruptcy Code.
2. Whether Oil Corp (or its trustee) can reject the patent license and thereby achieve its second goal without consent of Plastic Corp is dependent on what type of bankruptcy process it has filed for. If it has filed for chapter 11, it may not reject the license for the purpose of selling it to another party pursuant to 11 USC §365(n) and 1107(a) (confirmed in *Jaffe v Samsung Electronics Co, Ltd*), unless it obtains permission to terminate from the court. Conversely, Oil Corp could reject the patent license if it was in Chapter 7 (and will be automatically deemed to do so if no decision is made by the trustee in 60 days of the petition date). If rejected, Plastic Corp would have a claim in damages against Oil Corp.
3. Whether Oil Corp (or its trustee) can sell the manufacturing facility free and clear of the USA Bank lien will depend on the value of the property. If the property value exceeds the level of the debt secured against it, the facility can be sold without the USA Bank's consent pursuant to section 363(f) of the Bankruptcy Code. The USA Bank will then have a lien over the proceeds of sale of the facility and be paid those in priority to other creditors. Otherwise, if the property is in negative equity (i.e. if the USA Bank's debt exceeds its security), the USA Bank's consent to the sale is necessary.

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

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

Commented [H(63)]: Correct, 1 mark

Commented [H(64)]: While technically the license could be rejected, Plastic Corp would retain the ability to use the patent for the duration of the license term under 365(n)

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**\* End of Assessment \***