



**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 41/50

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

Commented [H(2): Total marks 7/10

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): Incorrect, the correct response is (c)

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

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?

The difference between a voluntary petition for bankruptcy and an involuntary petition for bankruptcy is that a debtor may commence a voluntary proceeding under any applicable chapter by filing a petition, whereas an involuntary petition for bankruptcy is initiated by creditors under either chapter 7 or chapter 11.

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

Another difference between a voluntary petition for bankruptcy and an involuntary petition for bankruptcy is that the former does not require a statement confirming the debtor is insolvent, but in order for a creditor to serve an involuntary petition (under either chapter 7 or chapter 11), the creditor must demonstrate that the debtor is insolvent/cannot pay its debts as and when they fall due.

Question 2.2 (2 marks)

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

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

A violation of the automatic stay constitutes contempt of court. In addition, an act taken in violation of the automatic stay is void or voidable, depending on the circuit in which the bankruptcy is pending. These are two potential consequences of a violation of the automatic stay.

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

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

In instances where the court is concerned that the violator may not act in a prompt manner, it can impose sanctions – for example, paying a daily fine to the court until the stay violation has been rectified.

The violator may also be required to pay the legal costs associated with rectifying the violation and the debtor may be able to commence legal proceedings against the violator in respect of the same.

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?

Section 1124 of Subchapter II (The Plan) of Chapter 11 of the Bankruptcy Code ("s1124") relates to the "impairment of claims or interests". S1124 states the following:

"Except as provided in section 1123(a)(4) of this title, a class of claims or interests is impaired under a plan unless, with respect to each claim or interest of such class, the plan—

- (1) leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interest; or
- (2) notwithstanding any contractual provision or applicable law that entitles the holder of such claim or interest to demand or receive accelerated payment of such claim or interest after the occurrence of a default—
 - (A) cures any such default that occurred before or after the commencement of the case under this title, other than a default of a kind specified in section 365(b)(2) of this title or of a kind that section 365(b)(2) expressly does not require to be cured;
 - (B) reinstates the maturity of such claim or interest as such maturity existed before such default;
 - (C) compensates the holder of such claim or interest for any damages incurred as a result of any reasonable reliance by such holder on such contractual provision or such applicable law;
 - (D) if such claim or such interest arises from any failure to perform a nonmonetary obligation, other than a default arising from failure to operate a nonresidential real property lease subject to section 365(b)(1)(A), compensates the holder of such claim or such interest (other than the debtor or an insider) for any actual pecuniary loss incurred by such holder as a result of such failure; and
 - (E) does not otherwise alter the legal, equitable, or contractual rights to which such claim or interest entitles the holder of such claim or interest."

As such, a claim is considered "impaired" if the holder of the claim is getting less than 100% on the same/what is due in the debtor's proposed repayment plan. A claim is also considered "impaired" if the original debt terms are changed in a negative way, such as reducing the interest rate or lengthening the pay-out period.¹

¹ <https://www.lawyers.com/legal-info/bankruptcy/commercial-bankruptcy/impaired-creditors-and-your-chapter-11-plan.html>

The holder of an impaired claim is not entitled to vote on a proposed plan of reorganisation in instances where it is an "insider", i.e. a connected party.

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

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

Preferences

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

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

Commented [H(22)]: Incorrect, the insiders vote but cannot constitute the impaired consenting class in a cramdown. An impaired class that will receive nothing under the plan does not vote, and is deemed to reject.

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

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

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 conveyances

Commented [H(26)]: Correct, 1 mark

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

Commented [H(27)]: Total marks 14/15

Question 3.1 (3 marks)

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

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

In 2011 (and in the case of *Stern v Marshall*) the US Supreme Court (the "USSC") held that a bankruptcy court could not issue final orders that would contravene Article III jurisdiction, even in core proceedings.

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

By way of background, in the *Stern v Marshall* case, a bankruptcy claim had been filed against Vickie Lynn Marshall (the "Debtor"), to which the Debtor counterclaimed. NB, Section 157 of Chapter 6 of Title 28 of the U.S. Code ("s157") relates to "procedures" and suggests that a counterclaim is considered a "core proceeding" in which a bankruptcy court is able to grant a final order.

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It should also be noted that issues in the counterclaim were subject to court proceedings in a separate state. US law allows for such parallel/simultaneous proceedings, but states that the first judgement issued is binding on both parties.

In this instance, the bankruptcy court issued its judgement first, and awarded the Debtor \$4m. As noted above, issues in the counterclaim were subject to court proceedings in a separate state – such proceedings remained ongoing whilst the bankruptcy judgement was appealed to the district court.

As noted previously, whilst s157 suggests that a counterclaim is considered a "core proceeding" in which a bankruptcy court is able to grant a final order, in the matter of *Stern v Marshall*, the USSC held that the issuing of a final order by the bankruptcy court (over a state law claim) was unconstitutional under Article III.

Since the case referred to above, the Bankruptcy Rules have been amended and further USSC rulings have provided additional guidance on the grey area that is bankruptcy court jurisdiction.

As district courts have exclusive jurisdiction to decide upon bankruptcy proceedings, a bankruptcy court may grant a final order on a motion challenging the validity of a bankruptcy petition, providing it has authority from the relevant district court to do so. The USSC held that in proceedings where a bankruptcy judge lacks constitutional authority, said judge may determine a core proceeding by issuing his recommendations together with a report for the district court to review, or, he may issue a final order in instances where he has the relevant parties' consent.

Commented [H(31)]: Correct, 1/2 mark

Commented [H(32)]: Correct, 1/2 mark

NB, finalising a judgement or order as a matter of constitutional authority is different to determining whether or not an order is final for the purposes of an appeal.

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?

Upon the filing of an involuntary/any plenary petition (i.e. one made under any chapter, save for chapter 15), the automatic stay comes into effect without the need for any action by the court. This worldwide automatic stay gives a debtor breathing space to prepare a restructuring plan.

A chapter 15 petition must be filed by a foreign representative. NB, the filing of the petition by a foreign representative does not invoke the automatic stay – this only arises once a petition for recognition of a foreign main proceeding has been granted and the automatic stay applies only to property within the territorial jurisdiction of the United States.

Commented [H(34): The stay can also come into effect on an application for interim relief.

Avoidance powers cannot be invoked by a foreign representative in a chapter 15 proceeding, pursuant to section 1523 of Chapter 15 of Title 11 of the U.S. Code ("s1523") – 'actions to avoid acts detrimental to creditors' – meaning a foreign representative in a chapter 15 proceeding is unable to pursue preferences or fraudulent conveyances (actual or constructive). Whilst not entirely equivalent, a foreign representative can request that pre-petition dispositions/transactions be declared void using either the legislation of the appointing country, or alternative US legislation.

Commented [H(35): Correct, 1 mark

Commented [H(36): Correct, 1 mark, also the foreign representative could commence a plenary proceeding to get access to the avoidance powers

Question 3.3 (4 marks)

Commented [H(37): 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 dispose of all issues (resulting in there being no matters that remain to be decided upon) and have a right to be appealed.

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

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

Interlocutory orders occur within ongoing proceedings and do not dispose of all issues (so only resolve some issues or claims) – these can only be appealed with leave of the appellate court.

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Commented [H(41): Correct, 1/2 mark

Generally speaking, direct appeals from bankruptcy court orders are heard by the district court (for the district in which they sit) – although it should be noted that in some circuits, direct appeals from bankruptcy court orders are heard by a Bankruptcy Appellate Panel ("BAP"). A BAP is made up of a panel of judges from the bankruptcy courts within that circuit.

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Commented [H(43): Correct, 1 mark

Question 3.4 (5 marks)

Commented [H(44): 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 actually insolvent?

Directors of Delaware corporations owe a fiduciary duty of loyalty to the corporation's best interest and owe these duties to the corporation and its shareholders (interestingly, not its creditors).

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Commented [H(46): Correct, 1 mark

Commented [H(47): Correct, 1 mark

UK legislation, namely s214 of the Insolvency Act 1986, covers the concept of "wrongful trading" – unlike this provision, the Delaware Supreme Court has covered the topic of whom are duties owed when the corporation is potentially or actually insolvent and has confirmed that directors do not owe any duties to a corporation's creditors when said corporation is "operating in the zone of insolvency" (i.e. potentially insolvent) or when it is actually insolvent.

Commented [H(48): Correct, 1 mark

NB, directors of Delaware corporations also have a duty of care in educated decision making and, under the business judgement rule, are protected from liability for "errors of judgement", as the business judgement rule presumes that the directors have acted in good faith, on the basis of reasonable information.

Commented [H(49)]: Correct, 1 mark

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

Commented [H(50)]: Total marks 12/15

Question 4.1 [4 marks]

Commented [H(51)]: 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.

A chapter 15 petition must be filed by a foreign representative and the requirements for recognition are minimal: the foreign representative must be able to demonstrate that a foreign court/administrative proceeding (as regards the debtor) is pending and that he is empowered to act by the same.

English scheme of arrangement ("ESA")

Gambling Corporation's bonds are governed by English law and due to mature in one year. Gambling Corporation is unable to repay or refinance the aforementioned bonds and is therefore considering using an ESA to restructure the same.

Recognition of ESA under US chapter 15 as a foreign main ("FM") or foreign non-main ("FNM") proceedings?

The difference between FM and FNM proceedings is that the FM proceedings are commenced in a debtor's centre of main interest ("COMI").

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

Model Law – COMI

In accordance with Article 16(3) of the Model Law, there is a rebuttable presumption that the place of the registered office of the debtor is the place of its COMI – a key concept and term that is not defined in the Model Law and instead, is set out in paragraphs 157 – 160 of The GEI.

Article 17(2)(a) of the Model Law confirms that the foreign proceedings will be recognised as 'foreign main proceedings' if they take place in the State where the debtor has its COMI – if the Debtor only has an establishment in the foreign State where the foreign proceedings are being opened, then these will be recognised as 'foreign non-main proceedings' in the enacting state, in accordance with Article 17(2)(b) of the Model Law.

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

Whilst the Model Law does not have a definition of COMI, Article 16(3) of the same presumes that, in absence of proof to the contrary, a debtor's registered office (or habitual residence in the case of an individual) is the debtor's COMI.

US Law – COMI

Whilst a COMI is a foreign concept in US law, it is presumed that a debtor's COMI is its place of incorporation – NB, this presumption is rebuttable.

Gambling Corporation's COMI

Gambling Corporation is incorporated and has a principal place of business in Greece. As such, it could be argued that its headquarters, management, and primary assets are also located in Greece – factors that also come into play when analysing a debtor's COMI. In light of the above, it can be assumed that Gambling Corporation's COMI is Greece.

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Given that the ESA is to be commenced in England and not Greece – being Gambling Corporation's COMI – consider that the ESA could be granted recognition under US chapter 15 as a FNM (foreign non-main) proceeding.

Commented [H(54): Correct, 1 mark

Commented [H(55): Specifically, the London casino would satisfy the establishment requirement

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(56): Total marks 5/5

Chapter 11

A debtor (in this case, Oil Corp.) may continue to operate in the ordinary course of business and may liquidate/reorganise during chapter 11 proceedings.

In chapter 11 proceedings, a debtor benefits from a worldwide automatic stay of creditor enforcement proceedings upon a petition for the bankruptcy being filed. In all four of the situations outlined below, Oil Corp. would benefit from this worldwide stay upon commencing a voluntary proceeding/filing a chapter 11 petition.

Commented [H(57): Correct, 1 mark

A violation of the automatic stay constitutes contempt of court. In addition, an act taken in violation of the automatic stay is void or voidable, depending on the circuit in which the bankruptcy is pending. These are two potential consequences of a violation of the automatic stay.

In instances where the court is concerned that the violator may not act in a prompt manner, it can impose sanctions – for example, paying a daily fine to the court until the stay violation has been rectified.

The violator may also be required to pay the legal costs associated with rectifying the violation and the debtor may be able to commence legal proceedings against the violator in respect of the same.

Executory contracts

Per 1.2:

“Chapter 11 debtors have greater flexibility than chapter 7 debtors on when they may assume, assign or reject an executory contract.

In the most common formulation, executory contracts are defined as those where both sides to a contract have material unperformed obligations.

A court will generally defer to a debtor’s business judgment regarding whether to assume or reject an executory contract.

Under the hypothetical test, a debtor cannot assume an executory contract if the debtor could not also assign the contract.”

Situation 1

ShipCo 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.

ShipCo would have a claim against Oil Corp. in the proceedings but would be unable to take any further action as a result of the automatic worldwide stay (upon commencing a voluntary proceeding/filing a chapter 11 petition) as the Bankruptcy Code explicitly prohibits litigation on pre-petition claims.

Commented [H(58)]: Correct, 1 mark

Furthermore, Oil Corp. may continue to operate in the ordinary course of business and may liquidate/reorganise during chapter 11 proceedings.

Situation 2

The US Department of Justice (“DoJ”) is investigating whether Oil Corp illegally purchased oil from countries subject to US sanctions.

Whilst Oil Corp. would be subject to an automatic worldwide stay (upon commencing a voluntary proceeding/filing a chapter 11 petition), regulatory investigations – such as those being conducted by the DoJ – are permitted to continue, as are criminal proceedings.

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

The directors of Oil Corp. owe a fiduciary duty of loyalty to the corporation’s best interest and owe these duties to the corporation and its shareholders (interestingly, not its creditors). NB, the directors of Oil Corp. also have a duty of care in educated decision making and, under the business judgement rule, are protected from liability for “errors of judgement”, as the business judgement rule presumes that the directors have acted in good faith, on the basis of reasonable information. If the DoJ can prove that the directors of Oil Corp. have not acted in good faith (on the basis of reasonable information), despite commencing a voluntary proceeding/filing a chapter 11 petition, the directors may still be found personally liable for any potential misconduct.

Situation 3

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.

USA Bank would have a claim against Oil Corp. in the proceedings but would be unable to foreclose on an Oil Corp. refinery located in the Philippines as a result of the automatic

worldwide stay (upon commencing a voluntary proceeding/filing a chapter 11 petition) as the Bankruptcy Code explicitly prohibits enforcement of pre-petition judgements against the debtor or property of the estate and any act to obtain possession or control of property of the estate.

Commented [H(60)]: Correct, 1 mark

Furthermore, Oil Corp. may continue to operate in the ordinary course of business and may liquidate/reorganise during chapter 11 proceedings.

Situation 4

Oil Corp has forgotten to pay rent on its Houston, Texas office space and its landlord is threatening to evict it.

NB, Oil Corp. has "forgotten" to pay rent on its Houston, Texas office space, as opposed to being unable to.

Its landlord would have a claim against Oil Corp. in the proceedings but would be unable to evict it as a result of the automatic worldwide stay (upon commencing a voluntary proceeding/filing a chapter 11 petition) as the Bankruptcy Code explicitly prohibits enforcement of pre-petition judgements against the debtor or property of the estate and any act to obtain possession or control of property of the estate.

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

Furthermore, Oil Corp. may continue to operate in the ordinary course of business and may liquidate/reorganise during chapter 11 proceedings.

Question 4.3 [6 marks]

Commented [H(62)]: Total marks 4/6

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?

Oil Corp. has filed for bankruptcy

Oil Corp. has commenced a voluntary proceeding by filing a chapter 11 petition and is considered a "debtor in possession". It may continue to operate in the ordinary course of business and may liquidate/reorganise during chapter 11 proceedings.

As noted above, in light of petition for the bankruptcy being filed, Oil Corp. will benefit from a worldwide automatic stay of creditor enforcement proceedings.

Executory contracts

Per 1.2:

“Chapter 11 debtors have greater flexibility than chapter 7 debtors on when they may assume, assign or reject an executory contract.

In the most common formulation, executory contracts are defined as those where both sides to a contract have material unperformed obligations.

A court will generally defer to a debtor’s business judgment regarding whether to assume or reject an executory contract.

Under the hypothetical test, a debtor cannot assume an executory contract if the debtor could not also assign the contract.”

363 sale

As a debtor in possession and as regards a 363 sale, Oil Corp. is able to sell its property free and clear of creditor interests with approval of the court.

- (i) assume and assign the trademark license

I note that Oil Corp 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.

Trademark licenses are not assignable without consent of the licensor. Given that the trademark “Interconnect” is licensed from Plastic Corp, Oil Corp cannot achieve goal (i) without the consent of Plastic Corp.

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

Commented [H(64)]: Correct, 1 mark

- (ii) reject the patent licenses so the purchaser has the exclusive right to use the patents

I note that Oil Corp. has invented several patented processes for plastic manufacturing, which it licenses to Plastic Corp.

Licenses (in this case, Plastic Corp.) of patents owned by a debtor (in this case, Oil Corp.) are protected insofar as their licenses are unable to be terminated in connection with a sale without their consent. To this end, Oil Corp cannot achieve goal (ii) without the consent of Plastic Corp.

Commented [H(65)]: Correct, 1 mark

Commented [H(66)]: Correct, 1 mark

- (iii) (iii) sell the manufacturing facility free and clear of the USA Bank lien

I note that 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. As a result, USA Bank’s claim in the proceedings is a secured claim and it therefore has the benefit of being protected when Oil Corp. proposes to sell the facility subject to the lien. In this scenario, Oil Corp could not achieve goal (iii) without the consent of USA Bank.

Commented [H(67)]: If the value of the property exceeds the secured claim, it may be sold without creditor consent and the creditor’s lien applies to the proceeds of the sale.

Alternatively, it could be interpreted that USA Bank would have a claim against Oil Corp. in the proceedings but would be unable to take any further action as a result of the automatic worldwide stay (upon commencing a voluntary proceeding/filing a chapter 11 petition) as the Bankruptcy Code explicitly prohibits enforcement of a lien against property of the estate on account of a pre-petition claim. Should this interpretation be correct, Oil Corp could achieve goal (iii) without the consent of USA Bank.

*** End of Assessment ***