



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 38/50

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

Commented [H(2)]: Total marks 8/10

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

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)]: 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)]: Correct, 1 mark

If a debtor rejects an executory trademark license agreement under which it licenses a trademark to its counterparty, which of the following is **true**?

(a) The counterparty has a claim for damages for breach of contract.

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

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

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

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

Question 1.10

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

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

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

QUESTION 2 (direct questions) [10 marks]

Commented [H(13)]: Total marks 6/10

Question 2.1 (2 marks)

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

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

A voluntary petition is when the debtor files a petition under any applicable chapter. An involuntary petition is filed by a creditor against an eligible debtor under chapter 7 or 11.

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

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

A voluntary petition for bankruptcy does not require any allegation of insolvency, whilst an involuntary petition for bankruptcy requires the petitioning creditors to allege that either the debtor is generally not paying its debts as and when they become due (unless the debtor is subject to a bona fide dispute as to liability or amount).

Question 2.2 (2 marks)

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

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

Violation of an automatic stay constitutes a contempt of court and may result in the imposition of contempt sanctions against the stay violator. This may include payment of attorney fees relating to the debtor and requires the violator to take affirmative acts to undo the effect of its violation.

Commented [H(18)]: Correct, 1 mark, also the act itself is void or voidable depending on the circuit

If the court is concerned that the violator of the stay may not act promptly to undo the effect of the violation, it can impose coercive contempt sanctions, which can include a daily fine to be paid to the court until the stay violation has been rectified.

Question 2.3 (3 marks)

Commented [H(19)]: Total marks 1/3

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

A claim is impaired when a creditor is not receiving a 100% return on their claim and their claim or interest is modified (i.e. the creditor's original debt is altered in a negative way such as a delayed in full).

Commented [H(20)]: Correct, 1 mark

A holder of an impaired claim is not entitled to vote if they are insiders; their votes will be disregarded to determine the existence of the accepting impaired class, unless there is no impaired class. In this case, a plan will be 'crammed down' for the dissenting impaired classes in order for it be approved.

Commented [H(21)]: Incorrect, an impaired class that will receive nothing under the plan does not vote and is deemed to reject the plan

Question 2.4 (3 marks)

Commented [H(22)]: Total marks 2/3

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

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

A preference claim applies as the cause of action only where the debtor is paying a creditor for a pre-existing debt.

Commented [H(23)]: 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?

A constructive fraudulent conveyance is the cause of action when the debtor is presumed to be insolvent as the time of transfer and received less than what was reasonably expected of the equivalent value.

Commented [H(24)]: Incorrect, the correct answer is preference. There are circumstances in which a constructive fraudulent transfer may occur without insolvency of the debtor at the time.

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

An actual fraudulent conveyance is the cause of action whereby a debtor transferred/incurred an obligation as an intention to hinder, delay or defraud creditor recoveries.

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

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

Commented [H(26)]: Total marks 13/15

Question 3.1 (3 marks)

Commented [H(27)]: Total marks 2/3

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

Stern v Marshall ("SM") changed the law of bankruptcy court jurisdiction and authority to enter a final order as the US Supreme Court ruled that even in core proceedings, a bankruptcy court cannot issue final orders that invade Article III jurisdiction (i.e. the US Supreme Court has the originating jurisdiction over certain cases meaning that cases can originate at the US Supreme Court and appellate jurisdiction over others).

Commented [H(28)]: Correct, 1 mark

In SM, a bankruptcy claim was filed against the debtor and the debtor responded with a counterclaim, which at the time, there were other issues in relation to the counterclaim and were subject to separate state court proceedings. Under US law, parallel proceedings are permitted in state and federal courts, and the US law states that the first judgment which is

issued becomes binding on the parties. In SM, the bankruptcy court issued its first judgment of US\$400 million to the debtor whilst the state court case continued. As a consequence, the bankruptcy judgment was appealed in the district court.

The verdict made by the jury of the state court was in favour of the claimant's appeal in the district court. Therefore, even though 28 USC § 157 states that a counterclaim is considered a core proceeding which a bankruptcy court can issue a final order, the US Supreme Court held that the final order issued by the bankruptcy court over the state law claim was unconstitutional (per Article III), resulting in the first final judgement being that of the verdict of the state court jury.

Question 3.2 (3 marks)

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

Under a chapter 15 proceeding, the foreign representatives may not invoke the use of avoidance powers (as prescribed under article 23 of the Model Law) provided by the Bankruptcy Code.

The foreign representative can obtain the equivalent relief and invoke the avoidance powers under the Bankruptcy Code in plenary proceedings (i.e. two ways may be via chapter 7 or 11 proceedings) and may choose to commence a plenary proceeding under the Bankruptcy Code after chapter 15 recognition is obtained.

Question 3.3 (4 marks)

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

Final orders dispose of all outstanding issues and leave nothing further to be decided. Interlocutory orders only resolve some issues or claims.

In relation to appeals; final orders are appealed as of right, whereas interlocutory orders are appealed only with leave of the appellate court (i.e. in a court of law that is empowered to hear the appeal).

Appeals from bankruptcy court orders are generally heard by the district court for the district in which they sit. The first appeal will be heard by a randomly assigned judge who will then hear all future appeals from the bankruptcy proceedings.

In certain circuits (i.e. the first, sixth, eighth, ninth and tenth circuits), the bankruptcy court order appeals are heard by a Bankruptcy Appellate Panel, convened from the judges of the bankruptcy courts within the circuit. Within these circuits, a party to the bankruptcy proceedings has the option to request that the appeal be heard by the district court.

Commented [H(29): Correct, 1 mark, following Stern a bankruptcy court can enter a final order on a challenge to a petition or where the parties consent

Commented [H(30): Total marks 2/3

Commented [H(31): Correct, 1 mark

Commented [H(32): Correct, 1 mark, they also may bring claims under applicable foreign or non-bankruptcy US law

Commented [H(33): Total marks 4/4

Commented [H(34): Correct, 1/2 mark

Commented [H(35): Correct, 1/2 mark

Commented [H(36): Correct, 1/2 mark

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

Commented [H(38): Correct, 1 mark

Commented [H(39): Correct, 1 mark

Question 3.4 (5 marks)

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

Director fiduciary duties of Delaware corporations (which are owed to the corporation and its shareholders) include:

- a **duty of loyalty** to the corporation's best interest (including duties of good faith, oversight and disclosure); and
- a **duty of care** in educated decision-making (i.e. requires informed, considered decision-making based on all material information reasonably available).

When the corporation is potentially or actually insolvent, the duties of directors are owed to the **corporation and its shareholders (and not to creditors)**. Further, per *Trenwick AM Litig Trust v Ernst & Young, LL*, 906 A.2d 168 (Del Ch 2006), under Delaware law, there is no obligation of the board of directors of a company that is unable to pay outstanding debts to cease operations and to liquidate, even when insolvent. The board of directors may continue to pursue (In good faith) strategies to maximise the company's value.

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

Question 4.1 [4 marks]

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

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

Firstly, it is not easily ascertainable to determine whether the Centre of Main Interests ("COMI") of Gambling Corp is England. From the facts of the questions, **Gambling Corp's COMI is most likely to be in Greece**, given that it is incorporated and has its principal place of business there (although this is not the only requirements for COMI – i.e. creditors have signed English governed contracts and also operates casinos in England, so COMI may be argued to be England however further information in the question is required i.e. knowledge / understanding of creditors).

Further, various potential proceedings brought against Gambling Corp in **cities such as Las Athens, Vegas, London, and Macau** would be considered foreign non-main proceedings, as Gambling Corp carried out non-transitory economic activities in those places and had places of operation (i.e. casinos and betting parlours) in those cities, which are not Gambling Corp's COMI.

As a result, the English scheme of arrangement would most likely be granted recognition under a US chapter 15 as a foreign non-main proceeding **due to carrying out non-transitory economic activities in London** prior to the commencement of any chapter 15 proceedings and Gambling Corp will be granted certain provisions of the Bankruptcy Code automatically, as well as relief granted on a discretionary basis over its assets, affairs, and property.

Commented [H(40)]: Total marks 5/5

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

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

Commented [H(43)]: Correct, 1 mark

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

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

Commented [H(46)]: Total marks 11/15

Commented [H(47)]: Total marks 3/4

Commented [H(48)]: Correct, 1 mark, and therefore foreign main recognition would not be appropriate for English proceedings

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

Commented [H(50)]: Correct, 1 mark

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(51): Total marks 4/5

Upon filing for chapter 11, Oil Corp is granted an automatic stay which is effective upon the filing of the petition.

Commented [H(52): Correct, 1 mark

Once an unsecured creditor committee ("UCC") is formed via the 20 largest creditors of Oil Corp, it would be granted an exclusivity period for 120 days from the petition date to negotiate with the UCC and other creditor groups to attempt to develop a plan. In relation to the facts of this case, creditors in the UCC would most likely include ShipCo (US\$1 billion claim), USA Bank (secured loan – unknown amount), and the landlord of the Houston, Texas office space (unknown amount).

In relation to the first creditor, ShipCo; the effect of a chapter 11 filing would not bar ShipCo from continuing their lawsuit in the Texas state court whilst parallel proceedings are carried on in district court (i.e. the chapter 11 bankruptcy proceedings). The US Supreme Court upheld in 2011 that a bankruptcy court cannot issue final orders that invade Article III jurisdiction and therefore, any order stemming from the bankruptcy proceedings would not interfere from a judgment handed to ShipCo in the Texas state court.

Commented [H(53): Incorrect, the stay would apply to the litigation, though the stay could be lifted or the case could be transferred to the bankruptcy court with the consent of the parties

Regarding the US Department of Justice ("DoJ") investigation, the automatic stay granted to Oil Corp via the chapter 11 is subject to certain exceptions such as criminal proceedings or regulatory investigations. The DoJ investigation would fall under this list of exceptions and permitted to continue as a continuation of a criminal action against Oil Corp.

Commented [H(54): Correct, 1 mark

Regarding the USA Bank foreclosure; USA Bank would have a claim, or a legal or equitable right, against Oil Corp with special protection should Oil Corp propose to use or sell the collateral as a part of its bankruptcy plan. Any act to obtain possession or control of the Oil Corp refinery would be prohibited under the automatic stay granted under chapter 11.

Commented [H(55): Correct, 1 mark

Finally, in the case of outstanding rent due on the Houston, Texas office space; The landlord will have a claim into the bankruptcy estate due to Oil Corp's lack of payment of rent on its office space. Any attempt by the landlord to collect on the claim would be prohibited under the automatic stay under the chapter 11. Should the claim be substantial enough to be admitted into the UCC, the Landlord would be allowed a seat at the negotiating table to form a plan with the Oil Corp to reorganise its debts.

Commented [H(56): Correct, 1 mark, it may only pursue eviction if the lease expired prior to the bankruptcy

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 intended goals of Oil Corp are stated and answered below:

(i) assume and assign the trademark license;

This goal is not achievable. As the trademark 'Interconnect' is licenced from Plastic Corp, Oil Corp cannot assume and assign the trademark licence unless consent is obtained from Plastic Corp. If consent is achieved, then this goal is achievable.

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

This goal is also not achievable: the licences provided by Oil Corp to Plastic Corp are protected such that the patent licenses may not be terminated in connection with the proposed sale and requires the consent of Plastic Corp. If consent is achieved, then this goal is achievable.

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

This goal is achievable and does not require the consent of USA Bank. In a 363 sale, Oil Corp can sell the manufacturing facility in the ordinary course of business without court or creditor interference and can sell its property free and clear of creditor interests, subject to court approval. Further, A good faith purchaser may retain the manufacturing facility notwithstanding a subsequent reversal of court approval for the sale on appeal.

It is noted that USA Bank may however make a bid to buy the manufacturing facility subject to the secured lien it has provided Oil Corp via a "credit bid" by offsetting a portion of the purchase price against the amount of the secured lien (US\$500 million).

*** End of Assessment ***

Commented [H(57)]: Total marks 4/6

Commented [H(58)]: Correct, 1 mark, this is because trademark law permits Plastic Corp to refuse performance from an assignee

Commented [H(59)]: Correct, 1 mark, this is due to Bankruptcy Code 365(n)

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

Commented [H(61)]: Correct, 1 mark, and the lien attaches to the proceeds of the sale