



**SUMMATIVE (FORMAL) ASSESSMENT: MODULE 3B**  
**THE INSOLVENCY SYSTEM OF THE UNITED KINGDOM**  
**(ENGLAND AND WALES)**

This is the **summative (formal) assessment** for **Module 3B** 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 3B.** 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.assessment3B]**. An example would be something along the following lines: 20222-514.assessment3B. **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 3B 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 3B 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 **7 pages**.

## ANSWER ALL THE QUESTIONS

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

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

Please select the **most correct ending** to the following statement:

The Administration (Restrictions on Disposal etc to Connected Persons) Regulations 2021 restrict pre-pack sales which constitute a substantial disposal of the company's property to connected parties where the disposal occurs:

- (a) within 10 weeks of the commencement of the administration.
- (b) **within 8 weeks of the commencement of the administration.**
- (c) within 4 weeks of the commencement of the administration.
- (d) on the day the company enters administration.

#### Question 1.2

What is the **maximum length** of a Moratorium under Part 1A of the Insolvency Act 1986 to which creditors can consent without any application to the court?

- (a) 40 business days.
- (b) One year and 20 business days.
- (c) One year and 40 business days.
- (d) **One year.**

#### Question 1.3

Which of the following **is not** a requirement for a company that wishes to enter into a Restructuring Plan under Part 26A of the Companies Act 2006?

- (a) The company has encountered, or is likely to encounter, financial difficulties that are affecting, or will or may affect, its ability to carry on business as a going concern.
- (b) A compromise or arrangement is proposed between the company and its creditors, or any class of them, or its members, or any class of them.

Commented [WPA1]: 42/50 = 84% a very good effort demonstrating some very good understanding.

Commented [WPA2]: 8/10

- (c) The purpose of the compromise or arrangement is to eliminate, reduce or prevent, or mitigate the effect of, any of the said financial difficulties.
- (d) The company is, or is likely to become, unable to pay their debts, as defined under section 123 of the Insolvency Act 1986.

**Question 1.4**

In cases where the Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021 apply and an independent report from an Evaluator is obtained, the independent report must be obtained by whom?

- (a) The administrator.
- (b) Any secured creditor with the benefit of a qualifying floating charge.
- (c) The purchaser.
- (d) The company's auditor.

**Question 1.5**

Which one of the following **is not** a debtor-in-possession procedure?

- (a) Administration.
- (b) Restructuring Plan.
- (c) Scheme of Arrangement.
- (d) Company Voluntary Arrangement.

Commented [WPA3]: A is correct

**Question 1.6**

A liquidator may pay dividends to small value creditors based upon the information contained within the company's statement of affairs or accounting records. In such circumstances, a creditor is deemed to have proved for the purposes of determination and payment of a dividend where the debt is **no greater than how much**?

- (a) £500
- (b) £750
- (c) £1,000
- (d) £2,000

**Question 1.7**

Which one of the following **is not**, in itself, a separate ground for disqualification of a director under the Company Directors Disqualification Act 1986?

- (a) Wrongful trading.
- (b) Breach of fiduciary duty.

Commented [WPA4]: B is correct

- (c) Being found guilty of an indictable offence in Great Britain.
- (d) Being found guilty of an indictable offence overseas.

**Question 1.8**

The administrator is under a general duty to provide a statement for creditors' consideration setting out proposals for achieving the purpose of administration. He or she must obtain a creditors' decision on whether or not to approve the proposals **within how many weeks** of the date the company entered administration?

- (a) 6
- (b) 8
- (c) **10**
- (d) 12

**Question 1.9**

Which of the following statements is **incorrect**?

- (a) **An insolvency officeholder from an EU Member State will be automatically recognised by the courts in the UK whether the officeholder was appointed before or after Brexit.**
- (b) An insolvency officeholder from an EU Member State is automatically recognised by the courts in the UK if appointed before Brexit.
- (c) An insolvency officeholder from an EU Member State appointed after Brexit may apply to a UK court for recognition under the Cross Border Insolvency Regulations.
- (d) An insolvency officeholder from an EU Member State cannot apply to a UK court for recognition under section 426 of the Insolvency Act 1986.

**Question 1.10**

Under section 216 of the Insolvency Act 1986, a director of a company which has been wound up insolvent may not, unless an exception applies, be a director of a company that is known by a prohibited name **for what period of time**?

- (a) 6 months.
- (b) 12 months.
- (c) 2 years.
- (d) **5 years.**

**QUESTION 2 (direct questions) [10 marks]**

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**Question 2.1 [maximum 5 marks]**

Commented [WPA6]: 5/5

Who may bring an action under: (i) section 423 of the Insolvency Act 1986; (ii) section 6 of the Company Directors Disqualification Act 1986; and (iii) section 246ZB of the Insolvency Act 1986?

[(i) the following persons have the right to bring an action under section 423 of the Insolvency Act 1986 ("IA"): (1) where the company is in administration or liquidation, the official receiver, liquidator, administrator and (with leave) any victim of the transaction; (2) where a victim is bound by a voluntary administration, the supervisor of the voluntary arrangement or any victim of the transaction; (3) in any other case, a victim of the transaction.

(ii) an action under section 6 of the Company Directors Disqualification Act 1986 may be brought by the Secretary of State, or by the official receiver if the Secretary of State so directs in the case of a person who is or has been a director of a company which is being wound up by the court.

(iii) the administrator may bring an action under section 246ZB of the IA.]

**Question 2.2 [maximum 5 marks]**

Commented [WPA7]: 5/5

List the **five (5)** qualifying decision procedures by which creditors may make decisions in the context of an insolvent company.

[(1) correspondence. If liquidators intend to use the correspondence procedure, he should send each creditor a notice of the decision procedure and a voting form. Creditors may vote by returning the completed voting form.

(2) electronic voting. Liquidators may elect to use an electronic voting system by which creditors can vote at any time without the need to attend at a particular location, for example Outlook voting buttons.

(3) virtual meeting. Liquidators may elect to hold a virtual meeting where creditors are not physically present at the same location but may participate and communicate directly with all the others, and vote at the meeting, for example, Zoom meeting.

(4) physical meeting. Liquidators may elect to hold a physical meeting where creditors may participate in person or by proxy at the location of the meeting, and decisions will be made by creditors at the meeting (in person or by proxy) by voting.

(5) any other decision making procedure which enables all creditors who are entitled to participate in the making of the decision to participate equally.

(r15.3 of the Insolvency (England and Wales) Rules 2016]

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

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**Question 3.1 [maximum 6 marks]**

Commented [WPA9]: 3/6 very good on s 233B but the question also required some consideration of ss 233 and 233A

Can an administrator who wishes to continue to operate the business of the company in administration require suppliers of goods and services to continue to supply those goods and services during the administration?

[Assuming that the exceptions set out in section 233B(10) and Schedule 4ZZA of the of the Insolvency Act 1986 ("IA") do not apply here. The administrator may require suppliers to continue to supply goods and services during the administration under Part VI of the IA.

Section 233B of the IA provides contract clauses which allow suppliers of goods and services to terminate or do any other thing because the company enters administration ceases to have effect when the company is subject to the relevant insolvency procedure (section 233B(3)). It also suspends the exercise of the right by suppliers to terminate or do other thing because of an event occurring before the company entering administration during the period of the administration (section 233B(4)). So even if there is a contract provision which provides the supplier a right to terminate the contract in the event the company enters administration, that provision cannot be enforced. Suppliers may only terminate the supply contract if the administrator consents or on application to the court, the court is satisfied that the continuation of the contract would cause the supplier hardship, and grants permission for termination (section 233B(5)).

Section 233B of the IA also prohibits suppliers from making it a condition of continued supply that pre-insolvency arrears re paid and from making other changes the contract such as increasing prices (section 233B(7)). It means that suppliers cannot impose new conditions such as payment of arrears for its continued supply.]

### Question 3.2 [maximum 9 marks]

Explain the order of priority of payments in a liquidation and explain the nature of the rights enjoyed by each class of creditor or expense.

[the distribution of assets in liquidation follows the following order:

#### (1) payment of expenses of the winding up

All fees, costs and other expenses incurred in the course of the winding up are expense of the winding up. The main categories of winding up expenses are listed below and they are usually paid in the following order:

- expenses properly incurred by the liquidator in preserving, realising or getting in any of the assets of the company (including the conduct of any legal proceedings),
- costs of any security provided by the liquidator,
- Any amount payable to a person to assist in the preparation of a statement of affairs or accounts,
- Any necessary disbursements by the liquidators in the course of the winding up,
- remuneration of any person employed by the liquidator and the liquidator,
- remuneration of the liquidator,
- The amount of any corporate tax on chargeable gains accruing on the realisation of any assets of the company,
- Any other expenses properly chargeable by the liquidator in carrying out his functions.

#### (2) payment of preferential debt

Preferential debts generally include certain debts owed to employees and certain tax liabilities.

**Commented [WPA10]:** 7/9 a good answer but more detail is needed in places e.g. around s 176A. Also, the position of fixed charge holders required some explanation.

There are two categories of preferential debts, ordinary and secondary. Ordinary preferential debt is paid before secondary preferential debts, but in their respective classes, debts rank equally amongst themselves.

Ordinary preferential debts include contributions to pension schemes, wages and salaries and holiday pay to employees. Secondary debts generally consist of debts owed to HMRC such as VAT, PAYE.

(3) payment to floating charge holders (other than the prescribed part of the company's net property)

Floating charge holders are paid before unsecured creditors, and amongst themselves, priority generally turns on time of creation.

The liquidator is under a duty to make a prescribed part of the company's net asset available for the unsecured creditors, and therefore, only property in excess of the prescribed part will be distributed to floating charge holders.

Floating charge holders are not allowed to participate in distribution of the prescribed part, even if their debts are not paid in full. The balance of the floating charge may be paid after the payment prescribed part.

(4) payment to unsecured creditors

Creditors with no securities (and not preferential creditors) are unsecured creditors. They are usually trade creditors.

If creditors entered into subordination agreements, the order of priority as between them will follow the agreement, and therefore the above orders regarding creditors may be altered by subordination agreements.

(5) payment to shareholders

If there are sufficient funds to pay all creditors, the surplus will be distributed amongst the shareholders in accordance with the company's constitution or shareholders agreement.]

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

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Prior to going into compulsory liquidation on 23<sup>rd</sup> December 2021, under pressure from its bank, Stercus Bank plc, and in order to prevent it from demanding repayment of the company's loans, Corfee Zero Limited ("the Company"), granted a debenture in favour of Stercus Bank plc in February 2021. The debenture contained a floating charge over the whole of the Company's undertaking.

The winding up order followed a creditor's winding up petition issued on 14<sup>th</sup> October 2021.

In July 2021, as the Company continued to suffer cash flow problems, the directors approved the sale of 5 coffee roasting machines to Ann Young (a director) for £10,000 in cash. The machines had been bought for £25,000 a year before.



A month before the winding up order was made, Ann Young received an email from Beans and Leaves Ltd, one of the Company's key suppliers. The supplier demanded immediate payment of all sums owing to it and informed the Company that further supplies would only be made on a cash on delivery basis. As the continued supply of coffee beans was seen as essential by the Company, the board authorised a payment of £8,000 to cover existing liabilities and agreed to further payments, on a cash on delivery basis, for further supplies which amounted to further payment of £3,000 up to the date of the winding up order.

The liquidator has asked for advice whether any action may be taken in respect of the floating charge in favour of Stercus Bank plc and the two subsequent transactions.

**Using the facts above, answer the questions that follow.**

**Identify the relevant issues and statutory provisions and consider whether the liquidator may take any action in relation to:**

**Question 4.1 [maximum 5 marks]**

Commented [WPA12]: 5/5

The floating charge in favour of Stercus Bank plc;

[The floating charge may be avoided under section 245 (floating charges) of the Insolvency Act 1986 ("IA").

It seems Stercus Bank is not connected with the company (they are not controlled by the same person or persons who are associated within the meaning of section 249 and 435 of the IA).

Avoidance of certain floating charges

Section 245 of the IA provides that where a floating charge on the company's undertaking or property was granted to a person not connected with the company at a time within the period of 12 months prior to the onset of insolvency, and at the time of creation of the floating charge the company was unable to pay its debts as they fell due within the meaning of section 123 of the IA (cash flow insolvency), or became unable to pay its debts in consequence of the transaction under which the charge was created, such charge is invalid unless new consideration was provided to the company.

The company was ordered by the court to be wound up. In such a case, the onset of insolvency was the commencement of the winding up (section 245(5) of the IA). The commencement of the winding up is the date of the presentation of the winding up petition (section 129(2) of the IA), which is 14 October 2021. So the onset of insolvency in this case is 14 October 2021. The charge was created in February 2021, within 12 months of the onset of insolvency.

It is not clear whether the company was cash flow insolvent or became cash flow insolvent because of this transaction concerning the floating charge. If the company was not insolvent or became insolvent in February 2021, the floating charge cannot be avoided under section 245 of the IA. The liquidators need to investigate the solvency of the company in February 2021.

It seems that no new consideration was made to the company. The promise not to make demand is not a new consideration for purpose of section 245 of the IA. If there was any consideration (for

example reduction of any debt of the company), the floating charge cannot be invalidated under section 245 of the IA.

#### Avoidance of preference

Section 239 of the IA prevents a company, before entering into an insolvency procedure, from placing any creditors in a better position than others. By giving Stercus Bank a floating charge shortly before it went into insolvent liquidation, the company may have put Stercus Bank in a better than other creditors.

To succeed on an application under section 239, the liquidators need to establish (1) the bank was a creditor of the company at the time the floating charge was created, (2) by granting the floating charge to the bank, the bank was put in a better position than it would have been in in the event of an insolvent liquidation had the floating charge not have been granted, (3) the company, in giving the preference, was influenced by a desire to prefer the bank, (4) the preference was given within the period of 6 months prior to the onset of insolvency, and at the time the preference was given, the company was unable to pay its debts as they fell due within the meaning of section 123 of the IA (cash flow insolvency), or became unable to pay its debts in consequence of the transaction (section 240 of the IA).

At the time of the transaction, the bank was a creditor of the company, and the granting of the floating charge put the bank in a better position than it would have been in without the floating charge in the event that the company went into an insolvent liquidation, because with the floating charge, the bank ranks ahead of all unsecured creditors and had a better chance of recovery in an insolvent liquidation.

The onset of insolvency, as explained above is 14 October 2021. The floating charge was granted in February 2021. So it seems that the floating charge was granted outside of the 6 month time period stipulated in section 239 of the IA and therefore, cannot be invalidated under section 239 of the IA.

Even if the floating charge was granted within the relevant time, the liquidators may not be able to establish that the company was influenced by a desire to prefer the bank. Desire is subjectively determined (Re MC Bacon Ltd [1990] BCC 78). It seems from the facts that the company granted the floating charge for purpose of preventing the bank to make demands, and not influenced by a desire to prefer the bank.]

#### **Question 4.2 [maximum 6 marks]**

##### **The sale of the coffee roasting machines; and**

[The sale of five coffee roasting machines may be challenged under section 238 (transaction undervalue) and/or section 423 (transactions defrauding creditors) of the IA.

#### Transaction under value

To succeed in an application under section 238 of the IA, the liquidator must establish that (1) the transaction was made for a consideration which, at the date of the transaction, significantly less than the value of the consideration provided by the company, (2) the transaction took place at a relevant time.

Commented [WPA13]: 6/6

The company sold the machines purchased for £25,000 a year ago for £10,000. It seems that the transaction was made for a consideration significantly less than the value of the consideration provided by the company.

The machines were sold to a director, a person connected with the company under section 249 of the IA. In such circumstances, relevant time for purpose of section 238 means within a period of two years prior to the commencement of liquidation, and at a time the company was insolvent (i.e. unable to pay its debts as they fell due or became unable to pay its debts in consequence of the transaction) (section 240 of the IA). The commencement of liquidation is 14 October 2021 and the transaction occurred in July 2021, within the two year period. Because the transaction was made with a connected person, it is presumed that the company was insolvent at the time of the transaction (section 240(2) of the IA).

It seems that the liquidators can establish all elements required under section 238. However, if the transaction was entered into in good faith and for the purpose of carrying on its business, and at the time it did so there were reasonable grounds for believing that the transaction would benefit the company, the court would not make the order under section 238. So the liquidators need to investigate the purpose and fairness of the transaction, for example, whether the transaction was necessary to raise needed capital for continuing operation of the business, whether the sale price is fair considering the market condition and the urgency of the sale, and whether the directors approved the transaction in good faith for the benefits of the creditors as a whole.

#### Transaction defrauding creditors

Section 423 of the IA prevents a company entering into a transaction undervalue with an intention to defraud creditors. It is similar to the requirements in section 238. However, it does not have a time limit during which a transaction must have occurred, and it requires the liquidators to establish intention to defraud creditors. From the facts, it seems that the transaction can be challenged under section 238, in such a case, it is better to make an application under section 238 because it does not require proof of intention.]

### **Question 4.3 [maximum 4 marks]**

#### **The payments to Beans and Leaves Ltd.**

[Payments to Beans and Leaves may be challenged under section 214 of the IA (wrongful trading) or section 127 of the IA (avoidance of property disposition).

#### Avoidance of property disposition

Section 127 of the IA provides that any disposition of the company's property, and any transfer of shares, or alteration in the status of the company's members, made after the commencement of the winding up is, unless the court otherwise orders, void. As stated above, the commencement of the winding up is 14 October 2021 (the date of presentation of the winding up petition under section 129(2)). The payment to Bean and Leaves was made in November 2021, after the commencement of winding up. So the transaction may be void under section 127.

The court has a discretion whether to declare the disposition void. If the transaction was made in the ordinary course of business in the benefit of unsecured creditors, the court will be unlikely to invalidate this transaction. Supply of coffee beans is essential to the business. It seems that the transaction was made in the ordinary course of business. It may be argued

**Commented [WPA14]:** 3/4 there is more that could be said about the s 127 application – pre existing debt? The 214 proposal is misconceived as the cut off date for such an action is the winding up. A director cannot be sued for WT due to actions taken after the commencement of the winding up.

that the transaction was made in an attempt to rescue the company and to minimise loss to creditors, and therefore in the benefit of unsecured creditors. If the court is so persuaded, it may not invalidate the transaction under section 127 of the IA.

#### Wrongful trading

Section 214 provides that the court may order directors of a company, which went into insolvent liquidation, to make contribution to the company's assets if the directors allow the company to continue to trade when they knew or ought to have known that there was no reasonable prospect of avoiding insolvent liquidation.

In order to succeed, the liquidator need to establish that the directors knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation. In assessing whether a director ought to have made such conclusion, the court will look at the general knowledge, skill and experience that may reasonably be expected of a director carrying out the same functions (objective standard), and the general knowledge, skill and experience that the particular director has (subjective standard). (section 214(4) of the IA). It seems that the company had cash flow problems and the directors knew about it. The liquidators need to investigate whether, given the background of the company's cash flow problems, the directors knew or ought to have known the company cannot trade out of insolvency.

However, the court will not make such order if it is satisfied that the directors took every step with a view to minimising the potential loss to the company's creditors as he ought to have taken (section 214(3) of the IA). Supply of coffee beans is essential to the business. Therefore, it may be argued that the directors approved the transactions in a view to rescue the company and to minimise loss to creditors. If this argument is successfully made out, the court may not order the directors to make contribution under section 214 of the IA.

**\* End of Assessment \***