



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

Commented [JL1]: 41.5 out of 50

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

Commented [JL2]: 10 out of 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

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.

(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.

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.

- (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]

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) Under section 423 of the Insolvency Act, in a CVA if the creditor is bound by the voluntary arrangement the supervisor may take action or against any victim of the transaction. Additionally, where the Company is being wound up or is otherwise in an insolvency process the Liquidator, the Administrator, the Official Receiver and any victim of the transaction so long as they have the permission of the court. Finally, in any other circumstances a victim of the transaction.
- ii) Under section 6 of the CDDA either the Court or the secretary of state has the power to bring action for disqualification.
- iii) Under section 246ZB of the Insolvency Act only an Administrator or Liquidator can bring a claim of wrongful trading to the Court

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Question 2.2 [maximum 5 marks]

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

The five qualifying decision procedures are set out in Rule 15.3 and are:

- i) Correspondence
- ii) Electronic voting
- iii) Virtual meeting
- iv) Physical meeting
- v) Or any method which enables all creditors to participate if they are entitled to do so.

Commented [JL5]: 4.5
Allow creditors to participate equally.

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

Commented [JL6]: 13 out of 15

Question 3.1 [maximum 6 marks]

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?

In respect of certain supplies, the Administrator may compel under section 233 the supplier to continue to provide services without the need to settle any outstanding debts to those suppliers in advance of continuation of service, however, the supplier can stipulate that the Administrator must provide a personal guarantee to the supplier for payment of the continuing services.

The suppliers that must continue to provide services if requested to do so under section 233 are utility providers (such as gas, electric and water) and communication services. Communication services is a relatively broad spectrum of services but in essence is to provide ongoing critical services relating to the Companies technology infrastructure for example software providers, Point of Sale providers, cloud-based services and telephone services which if lost would impede the ability of the Administrator to properly continue business

operations and could see value lost in the business to the detriment of the general body of creditors.

Section 233A and 233B of the Insolvency Act have been implemented to ensure that any insolvency related clauses in service contracts, for the supplies set out above, that note termination on an insolvency event cannot be enforced.

Commented [JL7]: extended to all supplies

Section 233, 233A and 233B apply to Administrations, as well as CVA's and restructuring plans.

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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 priority of payments made by the Liquidator is set out below:

- i. Expenses of the Liquidation including the Liquidators remuneration
- ii. Preferential Creditors
- iii. Prescribed part
- iv. Floating charge holders
- v. Unsecured creditors
- vi. Shareholders

Set out below is an overview of each class of creditor and the rights they are afforded.

- i. Ranking in priority to pre-appointment creditors of any type are the expenses incurred by the Liquidator in conducting an orderly wind down of the company. These expenses can include: the cost of any agents or professionals engaged in support of realizing the assets of the company; the cost of preparing the statement of affairs; any disbursements such as the cost of stationary; remuneration of the Liquidator (subject to the fees estimate regime if paid on a time cost basis) and their staff; and any other appropriate costs of conducting the Liquidation as appropriate e.g. taxes incurred on sales etc.
- ii. Once the costs of the Liquidation have been defrayed in full, the first ranking pre-appointment creditors are those known as preferential creditors. The majority of preferential claims relate to employee claims (at statutory limits) and more recently certain taxes and amounts due to the Crown.
 - a. In terms of employee claims at statutory limits, these include: sums due in respect of outstanding employee and employer pension contributions; sums due in respect of unpaid wages/salary up to £800; any accrued holiday remuneration prior to the date of appointment. Additionally, any sums advanced to employee in respect of the above will also rank as preferential in order to protect lender interest.
 - b. Any qualifying deposits that have been lodged with the company
 - c. Finally, crown preference claims including PAYE, national insurance and VAT payments amongst other deductions from salaries which have not been paid to the Crown.
- iii. The prescribed part is a set aside ringfenced sum of money for the benefit of unsecured creditors in priority to floating charge creditors. The prescribed part applies where there is a floating charge created on or after 15 September 2003 where the company has entered Administration or Liquidation. The prescribed part is calculated based on net property or in other words the surplus monies available to be distributed to creditors after the payment of expenses and preferential claims. The prescribed part is calculated as follows: 50% of

the first £10,000 of net property and 20% of net property thereafter up to a maximum prescribed part of £800,000. The prescribed part can be set aside by the Liquidator where either the prescribed minimum of net property is unavailable or where the Liquidator makes an application to court on the basis that the costs of the prescribed part would exceed the available sum of the prescribed part.

- iv. After the preferential creditors have been repaid in full and the prescribed part has been distributed, the floating creditors are repaid from the net realisations available. Where there is more than one floating charge creditor, they are ranked in priority based on either the date on which the first charge was created or based upon a subordination agreement which dictates priority. As floating charge creditors do have some element of security, they are afforded certain rights which other creditors are not. For example, a floating charge creditor can enforce their security to appoint an Administrator which places a moratorium over the company stopping any action being taken by any other class of creditor to place the company into Liquidation and potential reducing the value available to the floating charge creditor from the realization of the company's assets.
- v. Unsecured creditors do not have any security with which they can take any enforcement action over the company with. These creditors tend to be the day-to-day trade creditors of the company. Unsecured creditors right of recourse is usually to present a statutory demand, which if unpaid or not set aside can be the basis for a winding up petition.
- vi. If after all creditors have been paid in full (as well as any accrued interest) and there are available funds to distribute, a distribution will be made on a pari-passu basis to the shareholders who are paid up.

It should be noted that fixed charge creditors essentially sit outside of the priority of payments hierarchy as the debt attaches to pledged property and the rights and remedies of the fixed charge holder are defined in the security instrument (for example the appointment of a Receiver) however where a moratorium is in place the fixed charge holder will need the leave of the office holder to take action under the default remedies. The fixed charge holder can only benefit from the realization of the pledged property and does not benefit from the estate as a whole.

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

Prior to going into compulsory liquidation on 23rd 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 14th 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

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Fixed charges

Commented [JL10]: 9 out of 15

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]

The floating charge in favour of Stercus Bank plc;

Based on the available information, it would appear that the floating charge granted to Stercus Bank was granted without new monies being advanced. Additionally, it was provided during the voidable period of 12 months. Therefore, under section 245, Stercus Bank on this analysis would rank as a wholly unsecured creditor so long as Corfee was insolvent at the time or insolvent as a consequence of the security. Given the statement above that Corfee provided the floating charge security "in order to prevent it [Stercus Bank] from demanding repayment of the company's loans" it can be assumed that they were insolvent on a cashflow basis at the time of the charge being granted per section 123 of the Insolvency Act as they could not repay on demand and had to negotiate an alternate solution.

Stercus may benefit from the prescribed part if there are any other floating charge creditors, which appears unlikely as they were granted a floating charge over all assets with no mention of a junior security or subordination agreement, otherwise they will rank as unsecured creditors only without any ability to enforce under the security they were provided in February 2021. They would however have been able to submit a statutory demand followed by a winding up petition if the statutory demand were not dealt with.

Question 4.2 [maximum 6 marks]

The sale of the coffee roasting machines; and

Under section 238 of the Insolvency Act a transaction can be considered a transaction to defraud creditors and is voidable if the company entered into a transaction which was at the date of the transaction significantly less than the value of consideration paid by the Company.

In this case, the director of the company has paid £10,000 in consideration for items purchased for £25,000 representing a discount of 60% of the original consideration paid by the company. On the face of it, this transaction would appear to meet the criteria of section 238 as the

Commented [JL11]: 4
Applies only to floating charges.

Commented [JL12]: incorrect
238 – Transaction at an undervalue

purchase price is significantly less than the original purchase price. However, consideration should be given to the current market value of the coffee roasting machines and whether market value was paid. This is not addressed in the case study.

The transaction also took place at a time when the company would have known it was having liquidity issues given the security it had to negotiate with Stercus Bank to avoid a repayment demand being issued.

Additionally, the transaction has taken place within the relevant time being within the two years prior to the commencement of the Liquidation.

The above facts would lead a Liquidator to consider the section 238 transaction at undervalue application being made.

However, there are some strong defences here. As the board of the company voted for the sale it could be argued that the transaction was made with the best interests of the company in mind as it was entered into in good faith in order to carry on the company's business. Additionally, without a valuation of the machines as at the date of sale being available it is difficult to confirm that this is a transaction at undervalue.

Therefore, on the basis of the facts set out above a Liquidator would at this stage require further investigation of the transaction be made before taking action.

Question 4.3 [maximum 4 marks]

The payments to Beans and Leaves Ltd.

There are two points of concern with the payments to the supplier.

Firstly, the payment of £8,000 made to the supplier to clear back dated liabilities could be considered a preference transaction under section 239. Under section 239 the company cannot put one of its creditors in a better position than the others by repaying its outstanding debts.

Section 239 requires that the preferred party was a creditor at the time of the transaction; was placed in a better position than if they had been a creditor in the insolvency proceeding; the company had a desire to put the preferred party in a better position and the preference was given at a relevant time.

The supplier at the time of the preference payment was a creditor, was repaid in full rather than being subject to % dividend of their debt in the insolvency process, and the payment was made within 6 months of the winding up order. The company could argue, however, that the preference was not desired as it was influenced solely to continue to trade the business by securing its supplies, though it could equally be argued that the company could have sourced a separate supplier to avoid a preference payment being made, this however then leads into the second point of concern set out below.

The payment in cash of £3,000 and by implication the continued trading of the business is concerning as it is identified as having taken place "A month before the winding up order was made". The company at this stage would have been well aware of the likelihood of the appointment of a Liquidator having been in receipt of a statutory demand and the "creditor's winding up petition issued on 14th October 2021."

Commented [JL13]: 5

Some elements missing – effect of connected party sale.
The structure of the answer could also be improved.
With application questions it is best to follow the following structure:
Identify the issues
State the law
Apply the law
When these steps are done in one go, some elements are often left out.

The facts set out above would leave the directors exposed to action under section 214 of the Insolvency Act on the basis that prior to the winding up order the directors would have reasonably known that the company had no reasonable prospect of avoiding entering liquidation given there appears to be no challenge to winding up petition to set it aside.

Again the directors may argue that this action was taken to reduce losses to the creditors by continuing to trade the business to improve available cash for creditors, though without further information around the company's business it is difficult to make a judgement here. For example if they were attempting to complete on a contract that would have avoided claims from the customer of breach of contract and instead would have seen payments being received for contract completion.

Further investigation from the Liquidator would need to be taken to assess the above potential actions.

Commented [JL14]: 0
Refer to p 64 in the Guidance Text.
This scenario deals with a disposition after the commencement of the company's insolvency proceeding.
Therefore, s 127 and not s 239 applies.

*** End of Assessment ***