



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 out of 50

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

Commented [JL2]: 7 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.

Commented [JL3]: c

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

Commented [JL4]: c

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.

Commented [JL5]: d

QUESTION 2 (direct questions) [10 marks]

Commented [JL6]: 10 out of 10

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) section 423 of the Insolvency Act 1986 deals with fraudulent transactions. Parties that may bring an action under this section include:
 - 1) The official receiver, private liquidator for a company in liquidation or the administrator for a company in administration and with the leave of court any victim of the transaction.
 - 2) The supervisor of a Company Voluntary Arrangement (“CVA”) on behalf of the party who is defrauded who is bound by the CVA or party defrauded.
 - 3) Party who is defrauded in the transaction.
- (ii) section 6 of the Company Directors Disqualification Act 1986 deals with unfit conduct of directors of insolvent firms. A liquidator and / or an administrator would submit a report to the Insolvency Service and the Secretary of State who will make the decision on whether further investigations are needed or sought a disqualification order.
- (iii) section 246ZB of the Insolvency Act 1986 deals with wrongful trading under an administration. The action may be brought by the administrator.

Commented [JL7]: 5

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.

- 1. Correspondence;
- 2. Electronic Voting;
- 3. Virtual Meeting;
- 4. Physical Meeting; or
- 5. Any other decision-making procedure which enables all creditors who are entitled to participate in the making of the decision to participate equally.

Commented [JL8]: 5

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

Commented [JL9]: 15 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?

An administrator may rely on section 233 of the Insolvency Act 1986 (the “Act”) to obtain or retain essential supplies such as utilities, telecommunication services, IT suppliers, etc. It is not allowed for these vendors to demand repayment of amounts due prior to continuation of provision of services or goods. Section 233 of the Act allows the vendor to request that the administrator provide a personal guarantee for the payment of the goods or services provided during the administration.

Section 233A of the act also prohibits a vendor of essential supplies to terminate the provision of such supplies or change the terms of the contract, including charging a higher price.

The Corporate Insolvency and Governance Act 2020 (the “2020 Act”), also introduced a new section 233B which disallows clauses that grants the vendor the ability to terminate or “do any other thing” to the contract if the company enters a formal insolvency procedure such as an administration. The contract may still be ended if the administrator consents to it or on an application to court if the court is satisfied that it would be difficult for the vendor to continue providing such services. Section 233B also further expands the prohibition of termination to all goods and services, not just essential supplies as mentioned above, with the exception of insurers, banks, electronic money institutions, recognised investment exchanges and clearing houses, securitisation companies and international firms with corresponding functions).

Commented [JL10]: 6

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.

If there are assets charged or assigned to a third party (secured creditors), the liquidator only has rights to the assets if there are surplus from the sale of such charged assets e.g., if the outstanding due to the financier is less than the value of the asset pledged, the surplus proceeds after discharging the financier would become part of the assets available for distributions in the liquidation.

If receivables are assigned to a bank or financial institution or assets are on hire purchase or on retention of title contracts, the liquidator may not realise these assets.

Under section 115 of the Insolvency Act 1986 (the “Act”), rules 6.42 and 7.108 of the Insolvency Rules 2016 SI 2016/1024 (the “Rules”), the following expenses have priority over preferential creditors, floating charge creditors and unsecured creditors and must be satisfied in the below order of priority:

1. Expenses incurred by the liquidator to realize assets, including legal expenses incurred to get control and preserve such assets for realization
2. Cost of security that is provided by liquidator
3. Amount due to an individual who prepared the statement of affairs or financial statements
4. Necessary expenses incurred by the liquidator during the liquidation eg. Statutory advertisements, filings, liquidation committee expenses
5. Remuneration of agents contracted by the liquidator to provide services to the company
6. Remuneration of the liquidator, subject to creditors' approval
7. Tax chargeable on gains from realisation of assets
8. Other expenses properly chargeable by the liquidator

Next in line would be the preferential creditors which are split into 2 categories, ordinary preferential creditors, and secondary preferential creditors. Ordinary preferential creditors rank in priority above secondary preferential creditors and needs to be fully satisfied before any payment can be made to secondary preferential creditors. Each ordinary preferential claim rank pari-passu with other ordinary preferential claim and each secondary preferential claim ranks pari-passu with other secondary preferential claim.

Under Schedule 6 of the Act, the following claims are preferential:

Ordinary preferential creditors

1. Sums owed on employee's contribution to work pension fund for the period of four months before appointment of liquidators
2. Sums owed on employer's contribution to work pension fund for the period of 12 months before appointment of liquidators
3. Remuneration owed to an employee for the period of four months before appointment of liquidators, up to GBP800.
4. Amounts owed for accrued holiday leaves for any period before appointment of liquidators
5. Funds advanced to pay salaries
6. Levies on steel and coal productions as stated in article 49 and 50 of the European Coal and Steel Community Treaty
7. Amount ordered to be paid to the company under the Reserve Force (Safeguard of Employment) Act 1985 and any default made by the company in discharging its obligations under the Act
8. Amount owed by the company for an eligible deposit less than the consideration payable for the deposit under the Financial Services Compensation Scheme to the individual

Secondary preferential creditors

9. Amount owed by the company to one or more eligible individuals for an eligible deposit that is more than the consideration payable for the deposit under the Financial Services Compensation Scheme to that individual
10. Amount owed to one or more eligible individuals for a deposit that
 - a. Was made through a non-UK branch of a bank authorised by UK, and
 - b. Would have been an eligible deposit if made through a UK branch of the bank
11. Crown preference for debts owed to the tax authority, PAYE income tax deductions, national insurance deductions, VAT payments, Construction Industry Scheme deductions, and student loan repayments

Once all preferential creditors are satisfied, a floating charge holder is next in priority. If there are more than one floating charges, the priority is given to the charge that was created first. Pursuant to section 176A of the Act, for any company with a floating charge created on or after 15 September 2003 and the company has gone into liquidation, the liquidator will have to make a "prescribed part" of the net assets available for distribution to the unsecured creditors. Net assets are the amount of assets available after satisfaction of liquidation expenses and preferential creditors.

Where the net assets are less than GBP10,000, the prescribed part is 50%. If the liquidator is of the view that a distribution of the net asset (being less than GBP10,000) would likely be more costly than beneficial to unsecured creditors, the liquidator would not have such duty to make the payment of the prescribed part.

Where the net assets are more than GBP10,000, the prescribed part is 50% of the first GBP10,000 and 20% of any amount above GBP10,000, with total amount of the prescribed part capped at GBP800,000.

If the floating charge holder, after receiving the distribution of the net assets, is still not fully satisfied, they are not allowed to receive a payment under the prescribed part as an unsecured creditor.

Unsecured creditors are paid out last in the order of priority.

If all creditors are fully paid, the balance of proceeds will be distributed to Shareholders on a pro rata basis based on their percentage shareholding.

Commented [JL11]: 9

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

Commented [JL12]: 9 out of 15

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 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;

The liquidator may consider rely on Section 245 of the Insolvency Act 1986 (the "Act") to invalidate the floating charge in favour of Stercus Bank PLC. There are a few things that the liquidator will need to consider.

Firstly, is Stercus Bank PLC a connected person? If no, then the relevant period is 12 months prior to the appointment of liquidator. If yes, then the relevant period is 2 years. Given that the charge was granted in February 2021, within 12 months prior to the appointment of liquidator, it falls within the relevant period. Given that the winding up petition was issued on 14 October 2021, the liquidator is deemed to have commenced on 14 October 2021 despite the court order only being granted on 23 December 2021.

The next issue to consider is whether at the time of creation of the charge the Company was unable to pay its debts pursuant to the definitions set out in Section 123 of the Act or as a result of the charge is no longer able to do so. Given that the charge was only created to avoid Stercus Bank from demanding repayment, it could be argued that the Company was already insolvent at that point. It is also further noted that the cashflow issues continued through the months of July 2021 and till the winding up order was made.

Finally, the liquidator should also consider whether there is fresh consideration that is being provided for the floating charge. Given the facts of the case, it does not appear that any fresh consideration provided by the bank and it could be said that it is likely for the liquidator to be able to successfully rely on Section 245 of the Act to invalidate the floating charge in favour of Stercus Bank PLC.

Commented [JL13]: 4
Applies only to floating charges.

Question 4.2 [maximum 6 marks]

The sale of the coffee roasting machines; and

The liquidator may consider applying under Section 218 of the Insolvency Act 1986 (the "Act") to reverse this sale of the coffee roasting machines if there is a case of a sale at undervalue.

Commented [JL14]: 238

The liquidator will need to show the following:

- 1) The company made a gift to another person; or
- 2) Entered into a transaction with another person on terms that provided for the company to receive no consideration; or
- 3) Entered into a transaction with another person for a consideration which, in money or money's worth, was at the date of the sale less than the consideration provided.

For this to apply, the sale must be made within 2 years prior to the appointment of liquidators. Given that the sale happened in July 2021, this falls squarely in the relevant period.

The next issue to consider is whether there is indeed an undervalue or if the consideration provided by the director (£10,000) was not a fair value for the coffee machines. As the coffee machines were bought a year ago for £25,000 it could be argued that their value should not have decreased substantially but ultimately it is a practical issue in terms of valuing the coffee machines and whether it is worth the time for the liquidator to pursue the directors for a somewhat small claim (possibly in the region of £10,000). If it would incur significant costs, then the benefits to creditors would be marginal and practically speaking not a viable avenue for the liquidator to pursue.

If the courts hold that there is a transaction at undervalue, the court will likely order the reversal of the transaction and the liquidator will then have control over the asset and may seek to realise the coffee machines, given the liquidation status, it might be the case that the value of the coffee machines are even less than £10,000.

As the sale is to a connected person (a director), it is presumed that the company has been insolvent or because of this sale became insolvent. It will be up to the directors to prove otherwise.

Continuing from the above, a case could be made that the directors are liable for wrongful trading pursuant to Section 214 of the Act. The court must be satisfied of the following:

- 1) The company has been placed into insolvent winding up;

- 2) Prior to the liquidation, the person ought to have known that it is not possible for the company to avoid being placed into an insolvent winding up; and
- 3) At the relevant time, where the conclusion ought to have been made, the person was a director.

The defence for the directors would be that they have taken every step to minimise loss to creditors. The liquidator will have to prove that the directors knew or ought to have known that it was not possible for the company to avoid an insolvent liquidation.

The Anti-deprivation rule may also apply in this case as the sale of the coffee machine to the directors would have presumably made the company insolvent. The sale would have deprived the creditors of the asset which would have been available for the benefit of the creditors. The defence for the director will be to argue that the transaction was entered in good faith and not for the purposes of depriving creditors of the coffee machines.

Commented [JL15]: 5
Defence to s 238?

Question 4.3 [maximum 4 marks]

The payments to Beans and Leaves Ltd.

The liquidator may apply under Section 239 of the Insolvency Act 1986 (the "Act") to have preferences avoided by the court. In this case, it could be argued that the payment to Beans and Leaves Ltd would have put Beans and Leaves Ltd in a better position than others.

The court must be satisfied of the following:

1. Beans and Leaves Ltd is a creditor of the company;
2. Something was done (payment to Beans and Leaves Ltd) to put Beans and Leaves Ltd in a better position if the company was put into liquidation (in this case Beans and Leaves was paid in full);
3. The company was influenced by a desire to prefer Beans and Leaves; and
4. The preference was given at a relevant time.

As points 1 and 2 are easily satisfied, the issue is on proving points 3 and 4.

For point 4, the relevant period, given that Beans and Leaves Ltd is not a connected person, is 6 months prior to the appointment of liquidators. Given that the payment was made 1 month before the order was made, it falls squarely in the relevant periods.

The only contentious point is whether there is a desire to prefer Beans and Leaves Ltd. Even though the payment does prefer Beans and Leaves Ltd, it does not automatically amount to a desire to prefer. Given that the coffee beans were seen as an essential supply to ensure continued trading of the business, it may be difficult to prove that there is a desire to prefer as the case of it being a commercial consideration is much stronger.

Like the above, a case could be made that the directors are liable for wrongful trading pursuant to Section 214 of the Act. The court must be satisfied of the following:

- 1) The company has been placed into insolvent winding up;
- 2) Prior to the liquidation, the person ought to have known that it is not possible for the company to avoid being placed into an insolvent winding up; and
- 3) At the relevant time, where the conclusion ought to have been made, the person was a director.

The defence for the directors would be that they have taken every step to minimise loss to creditors. The liquidator will have to prove that the directors knew or ought to have known that it was not possible for the company to avoid an insolvent liquidation.

Should the court hold that there is a case of wrongful trading, the court will order the directors to compensate the company in an amount in line with the increase in liabilities during the same period.

*** End of Assessment ***

Commented [JL16]: 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.