



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.**
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- 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

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

Commented [JL2]: 9 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

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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?

Answer:

The following persons can bring an action under section 423 of the Insolvency Act 1986:

- Where the company is being wound-up or is in administration:
 - The official receiver
 - The liquidator
 - The administrator
 - Any victim of the transaction such as a creditor
- Where the victim is bound by a CVA
 - The supervisor of the CVA
 - Any victim of the transaction (whether bound by the CVA or not)
- In any other case
 - The victim of the transaction¹

The following persons can bring an action under section 6 of the Company Directors Disqualification Act 1986:

- The Secretary of State
- The Official Receiver (if the Secretary of State so directs)²
- The court

The following persons can bring an action under section 246ZB of the Insolvency Act 1986:

- The liquidator³
- The administrator⁴

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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.

Answer:

- Correspondence
- Electronic voting
- Virtual meeting
- Physical meeting

¹ Professor Peter A Walton - Foundation Certificate in International Insolvency Law Module 3B Guidance Text - Insolvency System of the United Kingdom (England and Wales) 2021/2022 ("Guidance Text") 5.10.11 p 69 – 70; Section 424 of the Insolvency Act 1986 c. 45 ("Insolvency Act")

² Section 7(1) of the Company Directors Disqualification Act 1986 ("CDDA"); Guidance Text 5.10.5 p 61

³ Guidance Text 5.10.3 p 58; Section 214 of the Insolvency Act

⁴ Guidance Text 5.10.3 p 58; Section 117 of the Small Business, Enterprise and Employment Act 2015

- Any other decision-making procedure which enables all creditors who are entitled to participate in the making of the decision to participate equally.⁵

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

Commented [JL7]: 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?

Answer:

Supply agreements usually contained “*ipso facto*” clauses which automatically terminates the contract should a party to the contract go into administration or other form of insolvency process. Law has since restricted this by operation of section 233 of the Insolvency Act as far as it concerns the supply of gas, electricity, water and communications services (including point of sale terminals, and other information technology hardware, software and support). Suppliers are not permitted to require payment of outstanding debts in order to secure a new or continued supply to the company in administration. A supplier may stipulate that the administrator personally guarantee payment of charges in respect of the supply.⁶

Section 223A of the Insolvency Act expands on section 223 in prohibiting a supplier of services named in section 223 on relying on an “insolvency related term” in a contract of supply to terminate the supply, alter the terms of supply or compel higher payments for continued supply.⁷

Section 223B of the Insolvency Act further expands the operation of section 223 and 223A of the Insolvency Act to apply to any company that enters a formal insolvency procedure, such as liquidation, Part A1 moratorium, provisional liquidation, administration, etc.⁸

Accordingly, yes an administrator can require suppliers of certain goods and service to continue to supply those goods and services during an administration by operation of section 223 and 223A of the Insolvency Act. Note however that the administrator may have to personally guarantee payment of those goods and services. The purpose of this is to allow the company the opportunity to successfully turn itself around in an administration.

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A little explanation of how the new 233B has affected such a scenario would have been helpful.

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.

Answer

Secured creditors with a fixed charge, such as those whose debts contain a hire purchase contract or a retention of title provision will not have those assets subject to

⁵ Guidance Text 5.4.9 p 26

⁶ Section 223 of the Insolvency Act; Guidance Text 5.4.4.4 p 20

⁷ Section 223A of the Insolvency Act, Guidance Text 5.4.4.4 p 20

⁸ Section 223B of the Insolvency Act, Guidance Text 5.4.4.4 p 20

the liquidation, the liquidator has no right to those assets as the assets are not considered to be company property so such creditors will be able to realise those assets without intervention of the liquidator. Note this applies to assets subject to a fixed charge, not those subject to a floating charge, whether crystallised or not.⁹

- Payment of any liabilities to which section 174A of the Insolvency Act applies.¹⁰ This was inserted by operation of the Corporate Insolvency and Governance Act 2020 (c.12). Section 174A sets out the priority of any Moratorium debts under Part A1 of the Insolvency Act.
- Expenses of winding up, including the liquidator's remuneration (section 115)

The following expenses are given priority over the company's preferential creditors, any holders of floating charges and the company's unsecured creditors pursuant to Section 115 of the Insolvency Act 1986¹¹:

- Expenses properly incurred in preserving, realising or getting in any of the assets of the company (including legal proceedings);
 - Cost of any security provided by the liquidator
 - Any amounts payable to a person to assist in the preparation of a statement of affairs or accounts
 - Any necessary disbursements by the liquidator in the course of he winding up
 - Remuneration of any person employed by the liquidator to perform any services for the company
 - Remuneration of the liquidator
 - Any corporation tax chargeable gains accruing on the realisation of any assets of the company
 - Any other expenses properly chargeable by the liquidator in carrying out the liquidator's functions in the winding up
- Preferential creditors, as defined in sections 386, 387 and Schedule 6 (section 175).¹²

Ordinary preferential debts rank equally amongst themselves and shall be paid in full, unless the assets are insufficient to meet them, in which case they abate in equal portions.¹³ Secondary preferential debts rank equally among themselves after ordinary preferential debts and shall be paid in full, unless the assets are insufficient to meet them, in which case they abate in equal portions.¹⁴

Schedule 6 of the Insolvency Act lists preferential debts in categories as follows:¹⁵

- Category 1: Debts due to Inland Revenue
- Category 2: Debts due to Customs and Excise
- Category 3: Social Security Contributions

⁹ Guidance Text 5.9.5.1 p 50

¹⁰ Section 115 of the Insolvency Act – inserted by the Corporate Insolvency and Governance Act 2020 (c.12)

¹¹ Guidance Text 5.9.5.2 p 50-51

¹² Guidance Text 5.9.5.3 p 51-52;

¹³ Section 175 (1A) of the Insolvency Act

¹⁴ Section 175 (1B) of the Insolvency Act

¹⁵ Schedule 6 of the Insolvency Act

Category 4: Contributions to Occupational Pension Schemes, etc.
Category 5: Remuneration etc. of employees
Category 6: Levies on coal and steel production
Category 6A: Debts owed to the Financial Services Compensation Scheme
Category 7: Deposits recovered from the Financial Services Compensation Scheme
Category 8: Other deposits

Categories 4 to 6 of Schedule 6 are “ordinary preferential debts” as contemplated in section 386 (1A) of the Insolvency Act. Category 8 of Schedule 6 are considered “secondary preferential debts” as contemplated in section 386 (1B) of the Insolvency Act.¹⁶

Categories 1 to 3 as well as categories 6A to 8 are considered “secondary preferential debts”.¹⁷

- Floating charge holder and “prescribed part”

After the preferential creditors are paid, then any creditor holding a floating charge will get paid next. If there is more than one floating charge holder, the priority between them turns upon which floating charge was created first.

Before any payments can be made to any floating charge holder, the liquidator must consider the application of s176A of the Insolvency Act, which applies to a floating charge created on or after 15 September 2003. This provides for a “prescribed part” of the company’s “net property” to be made available for the unsecured creditors. Where the company’s net property is less than £10,000, the prescribed part is 50% of that property. The Liquidator can determine if making a distribution to unsecured creditors would be disproportionate then the prescribed part does not apply. If the net property exceeds £10,000, the prescribed part is 50% of the first £10,000 in value, plus 20% of the excess value above £10,000 subject to a maximum prescribed part of £800,000. A floating charge holder cannot participate in the distribution of a prescribed part.¹⁸

- Unsecured creditors

There is frequently little or nothing left to pay unsecured creditors, who are typically ordinary trade creditors with no security, once expenses of the liquidation are paid and distributions made to secured and preferential creditors.¹⁹

- Shareholders

If there are surplus funds after paying all the creditors including interest on their debts, the surplus is distributed amongst the shareholders according to the company’s constitution.²⁰

Commented [JL9]: 9

¹⁶ Section 386 of the Insolvency Act.

¹⁷ Guidance text 5.9.5.3 p 53

¹⁸ Guidance Text 5.9.5.4 p 53

¹⁹ Guidance Text 5.9.5.5 p 54

²⁰ Guidance Text 5.9.5.6 p 54

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

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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;

Answer:

Section 245 of the Insolvency Act invalidates a floating charge taken on a company's undertaking or property created at a relevant time. The relevant time for a person not connected with the company is 12 months prior to the onset of insolvency, but only if at the time of the creation of the charge the company was either unable to pay its debts or became unable to do so as a consequence of the transaction.²¹

As the floating charge was taken in February 2021, the floating charge is subject to section 245 of the Insolvency Act. Further the charge was given to prevent Stercus Bank plc from demanding repayment of the Company's loans without any consideration received in exchange for the charge as the debenture contained a floating charge over the whole of the Company's undertaking. Accordingly, the

²¹ Guidance Text 5.10.10 pages 68-69

floating charge would be considered invalid pursuant to section 245 of the Insolvency Act.

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245 applies only to floating charges.

Question 4.2 [maximum 6 marks]

The sale of the coffee roasting machines; and

Answer:

This is a transaction at undervalue as contemplated in section 238 of the Insolvency Act. The Liquidator must show that the Company entered into a transaction with another person for consideration which, in money or money's worth, was, at the date of the transaction, significantly less than the value, in money or money's worth, to the consideration provided by the company.²² Where the company has at the relevant time defined in section 240 of the Insolvency Act entered into a transaction with any person at an undervalue, the office holder may apply to court for an order under section 238 of the Insolvency Act.²³ As this transaction is made with a person who is connected with the Company, section 240(1)(a) of the Insolvency Act defines the relevant time being a period of two years ending with the onset of insolvency. Accordingly the transaction can be attacked.

As the transaction is a sale of equipment for £10,000, which was purchased for £25,000, the practical difficulty is determining if fair value was paid or if the equipment was sold for undervalue as the equipment is considered second hand so it would be prudent to get a valuation to make a determination if the transaction is an undervalue transaction.

If the purchaser purchased the equipment in good faith and for value, the court could rule against an order under section 238 if the Insolvency Act, the respondent can further lead evidence that there are reasonable grounds for believing that the transaction was for the benefit of the Company²⁴ in that it injected cash to the Company when he/she purchased the equipment. From the context of the facts it seems that the director purchased the machines from the company but allowed the company to continue to use the machines, only retaining title, in other words the machines were presumably not removed until the date of liquidation. This could further serve to satisfy the court that the transaction was for the benefit of the Company.

The liquidator will further need to show that the liability under section 238 arises because at the time the transaction was entered into, either the company was unable to pay its debts as and when they become due or because of the transaction the company became unable to pay its debts within the meaning of section 123 of the Insolvency Act.

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Question 4.3 [maximum 4 marks]

The payments to Beans and Leaves Ltd.

²² Guidance Text 5.10.8 p 66

²³ Section 238(2) of the Insolvency Act

²⁴ Guidance Text 5.10.8 p 66

Answer:

Beans and Leaves Ltd enjoyed a preference as contemplated in section 239 of the Insolvency Act. An application under section 239 of the Insolvency act must show that:

- a) the person whom it is alleged has been preferred was, at the time of the transaction, a creditor of the company;
- b) something was done, or suffered to be done, by the company which had the effect of putting that person in a better position, in the event of the company going into insolvent liquidation, than the position he or she would have been in if that thing had not been done;
- c) the company was, in giving the preference, influenced by a desire to produce the effect referred to in (b) above in relation to the person preferred; and
- d) the preference was given at the relevant time.²⁵

In this matter, the preference was given as a result of pressure put on the Company by the creditor in that it threatened to stop supply and insisted in cash on delivery payments. The creditor is not a connected person to the Company so the relevant time is six months prior to the insolvency; in this case, one month prior to the insolvency of the Company falls within the relevant time.

Accordingly the payments to Beans and Leaves Ltd can be recovered as a preference under s239 of the Insolvency Act.

*** End of Assessment ***

Commented [JL13]: 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.

²⁵ Guidance Text 5.10.9 p 67