



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]: 30 out of 50

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

Commented [JL2]: 8 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.

Commented [JL3]: b

- (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.**

Commented [JL4]: a

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]

Commented [JL5]: 9 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?

Any of the following persons may bring an action under s. 423 of the Insolvency Act 1986: the Official Receiver, liquidator, administrator, a creditor who is given leave of the court, the supervisor of a CVA or any victim of the transaction designed to defraud creditors.

The Secretary of State and/or the Official Receiver can bring an action under s. 6 of the Company Directors Disqualification Act 1986.

The liquidator can bring an action under section 246ZB of the Insolvency Act 1986.

Commented [JL6]: administrator
4

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.
5. Any other decision-making procedure that enables all creditors who are entitled to participate in decision making to participate on an equal basis.

Commented [JL7]: 5

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

Commented [JL8]: 7 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?

Yes, an administrator has wide-reaching powers and can do anything "necessary or expedient for the management of the affairs, business and property of the company" under paragraph 59(1), Schedule B1 of the Insolvency Act 1986. However, the administrator must perform his or her functions with the first objective of administration in mind, which is to rescue the company so that it can continue trading as a going concern under paragraph 3(1)(a), Schedule B1 of the Insolvency Act 1986. As well as carrying on the company's business, the administrator can sell its assets and trade with suppliers and customers. A creditors' committee is usually appointed, which consults with the administrator on the conduct of the administration.

Commented [JL9]: This question required a discussion of continued supply and executory contracts under s 233, 233A and 233B.
0

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 order of priority of payments in a liquidation is as follows:

1. Fixed charge holders.
2. Liquidators' and administrators' fees and expenses.
3. Preferential creditors.
4. Floating charge holders.
5. Unsecured creditors.
6. Interest incurred on all unsecured debts post-liquidation.
7. Shareholders

1. Fixed charge holders are usually paid first out of any formal insolvency because the fixed charge is attached to a particular asset or class of assets, such as real estate or machinery) that cannot be disposed of without the creditor's consent. These lenders (e.g. banks) have a power of sale over the asset, or the power to appoint a fixed charge receiver to deal with and realise the assets on their behalf. The lenders therefore have a claim over the proceeds of sale in priority to other creditors. They are paid up to the amounts realised from the assets net of the costs involved in realising the assets. If the value of the charged assets is less than the amount of the debt, the fixed charge holder can claim the outstanding balance as an unsecured creditor.
2. Liquidators' and administrators' fees and expenses are paid out ahead of any preferential creditors and floating charge holders. If not, they would be less incentivised to maximise the realisation of assets. Certain expenses incurred by liquidators, such as litigation expenses, must be authorised by floating charge holders, preferential creditors and/or the court.
3. Preferential creditors are paid next. They are mainly employees with employment-related claims, e.g. for unpaid wages and contributions to pension schemes, if provided by employers.

In the case of insolvency of financial institutions only, there are two categories of preferential debts: ordinary preferential debts and secondary preferential debts. The latter are claims for repayment of unprotected deposits held by the financial institution. Since 1 December 2020, UK Revenue and Customs are secondary preferential creditors (behind ordinary preferred creditors) solely for the collection of certain unpaid taxes such as value added tax (VAT), pay as you earn (PAYE) and employee National Insurance contributions.

4. Floating charge holders are paid next, up to the amount realised from the assets covered by the relevant floating charge. A floating charge secures a group of assets that fluctuates over time such as inventory or cash in a trading bank account. Upon the occurrence of specified events set out in the charging instrument, such as events of default, the floating charge crystallises into a fixed charge over the relevant group of assets which remain in the borrower's possession.
5. Unsecured creditors rank next, they are creditors who do not have any security interest in the debtor's assets.
6. Interest incurred on all unsecured debts post-liquidation will be paid next.
7. Lastly, any surplus is paid to the shareholders of the debtor according to the rights attached to their shares.

Commented [JL10]: How does the prescribed part apply here?

Commented [JL11]: 7

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

Commented [JL12]: 6 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;

With regards to the floating charge in favour of Stercus Bank plc (the **Bank**), we are informed that the debenture granted by Corfee Zero Limited (**CZL**) in February 2021 contained a floating charge over the whole of CZL's undertaking. The liquidator should check that the floating charge was registered with Companies House within 21 days of its creation, to be effective. Otherwise, it will be void and the liquidator will not need to take it into account in making distributions to creditors.

Assuming the floating charge was registered, the Bank could have chosen to enforce its charge by appointing an administrator, which will usually prevent a liquidator being appointed until the administration is completed. However, as no administrator was appointed, it appears the Bank consented to the liquidator's appointment, in which case the liquidator can realise the charged assets as part of the liquidation and pay the Bank according to its priority.

It may be noted that the floating charge crystallised into a fixed charge attaching to all of CZL's property upon the commencement of the liquidation on 14 October 2021 pursuant to s.129 of the Insolvency Act 1986 (the **Act**). However, the crystallisation of the floating charge does not affect the ranking or priority of the floating charge, which will continue to be treated as a floating

charge for the purposes of insolvency. Under the Act, floating charges rank fourth behind firstly, any debts secured by a mortgage or fixed charge, secondly, liquidator's fees and expenses, and thirdly, any preferential creditors (such as unpaid contributions to occupational pension schemes, arrears of employee wages up to a certain limit, redundancy payments).

Commented [JL13]: this question required a discussion of s 245 as a way to attack a transaction like the giving of a floating charge.

Question 4.2 [maximum 6 marks]

The sale of the coffee roasting machines; and

Under s. 238 of the Act, the factors to be considered by the liquidator in determining whether the coffee roasting machines - sold to Ann Young, a director of CZL, in July 2021 for less than 50% the original purchase price - constitutes a transaction at an undervalue are:

- a. the transaction was entered into for no consideration or for consideration significantly less than market value; and
- b. the transaction was entered into within 2 years before the onset of insolvency (i.e. 14 October 2021, as mentioned above) pursuant to s. 240(1)(a) of the Act.

Applying these factors, the liquidator may be reasonably satisfied that the transaction was at an undervalue because (a) the machines were sold for less than 50% of their market value only 1 year ago; and (b) the sale took place 5 months before the company went into compulsory liquidation in December 2021, i.e. within the "relevant time" of 2 years before the onset of insolvency.

If CZL was insolvent at the "relevant time" or became insolvent as a result of this transaction, the liquidator could bring a claim against Ms Young to set aside the transaction and claw back the GBP10,000 paid for the machines from them.

It is a defence to the set aside action if Ms Young can show that:

- a. CZL entered into the transaction in good faith for the purposes of carrying on its business; and
- b. at the time it did so, there were reasonable grounds for believing that the transaction would benefit CZL.

These factors do not appear to apply because the coffee roasting machines were vital to CZL's business. Selling these relatively new machines meant that CZL may not have had enough machines to carry on its business properly and selling them at a significant discount would not benefit CZL.

The court can set aside the transaction and claw back the GBP10,000 from Ms Young to restore CZL's position to that before the transaction. Further, the court can impose penalties on the directors of CZL who approved the sale, including disqualification from acting as a director for a period of time between 2-15 years, a fine, or imprisonment.

Commented [JL14]: 6

Question 4.3 [maximum 4 marks]

The payments to Beans and Leaves Ltd.

As explained above, on 14 October 2021, the floating charge crystallised into a fixed charge over all of CZL's assets pursuant to s. 129 of the Act. The effect of this crystallisation is that CZL no longer had authority to dispose of or otherwise deal with those assets, including the

payments of GBP8,000 to cover existing liabilities and GBP3,000 to purchase further supplies one month up to the date of the winding up order.

Pursuant to s. 130 of the Act, any disposal of Corfee Zero Ltd's property made after the commencement of the winding up is void, except to the extent ordered by the court.

This transaction could be characterised as a preference as it puts Beans and Leaves Ltd (BLL) in a better position on insolvency that it would otherwise have held, pursuant to s. 239 of the Act.

The liquidator would have to show that CZL's directors were influenced by a desire to prefer BLL. The fact that the payments were made only one month before the winding up order was made and after a petition for winding up had been filed by another creditor, when the directors of CZL had no authority to deal with its assets, should be sufficient evidence. The fact that BLL's email was sent to Ms Young alone, and not the company itself, for an ordinary matter of non-payment for supplies of coffee beans, may be an added factor.

The timing of the payments, being one month before the winding up order, also falls within a "relevant time", being six months prior to the onset of insolvency.

If CZL was insolvent at the "relevant time" or became insolvent as a result of these payments, the liquidator could apply to the court to claw back the cash payments to BLL and for the court to set aside the transactions in order to restore CZL's position to that before the transaction. If the court finds the CZL directors found guilty of a preference, it could impose penalties on them, including disqualification from acting as a director for a period of time between 2-15 years, a fine, or imprisonment.

*** End of Assessment ***

Commented [JL15]: 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.