



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]: 42 out of 50

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.

Commented [JL3]: d

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]

Commented [JL4]: 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) Under section 423 of the Insolvency Act 1986 (the "Act") the following individuals can bring action:
- the official receiver, liquidator, administrator and (with the leave of the court) any victim of the transaction such as a creditor, where a company is being wound up or is in administration; or
 - where a victim is bound by the Company Voluntary Arrangement, the supervisor of the CVA or any victim of the transaction

- (ii) Under section 6 of the Company Directors Disqualification Act 1986, the liquidator can bring action on behalf of the company to sue a director.

Under section 7, if it appears to the Secretary of State that it is expedient in the public interest that a disqualification order under section 6 should be made against any person, an application for the making of such an order against that person may be made—

- by the Secretary of State, or
- if the Secretary of State so directs in the case of a person who is or has been a director of a company which is being wound up by the court in England and Wales, by the official receiver.

- (iii) Under section 246ZB of the Act, the liquidator can bring an application to the Court (guided by section 214). This is also available to administrator under Small Business, Enterprise and Employment Act 2015.

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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 insolvency practitioner is required to seek a decision from the creditors as to whether or not they approve the administrator's proposal. The decision must be made within 10 weeks of the date the company entered administration, subject to extension as for sending out proposal; decision procedures can either be deemed or qualifying.

There are instances where administrator does not need to seek a decision of the creditors if the statement proposal states that:

- The company has sufficient property to pay all its creditors in full;
- That the company has insufficient property to enable a distribution to be made to unsecured creditors other than by virtue of the prescribed part under section 176A of the Act;
- That neither the rescue nor the better result purpose can be achieved

Rule 15.3 of the Insolvency Rules 2016 lists the five 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 procedures which enables all creditors who are entitled to participate in the making of the decision to participate equally.

Commented [JL6]: 5

The decision date must be not less than 14 days after the date of delivery of the notice. Decision must be sought from the creditors if requested to do so by creditors whose debt is at least 10% of the total debts of the company. Approvals of proposal can be simply by majority in value of the unsecured creditors.

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

Commented [JL7]: 14 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?

During administration, the administrator may need to obtain or retain certain essential suppliers. Contracts that are executory in nature is not automatically terminated upon the appointment of an administrator. Section 233 of the Act deals with suppliers of gas, electricity, water and communication services, inter alia the supply of point of sale terminals, computer hardware and software, data storage and processing and website hosting (paragraph 3A). Paragraph 2 (b) does not permit suppliers to require payment of outstanding debt prior to the date of the appointment of the administrator in exchange for new or continued supply of goods however paragraph 2 (a) provides that suppliers can make it a condition that the administrator personally guarantees the payment of such supplies. Suppliers can request the court to terminate the contract if it can satisfy the court that the continuation of the contract would cause the supplier hardship provided in Section 233A paragraph 4 (b) of the Act.

Section 233B of the Act further provides comfort to administrator that prevents suppliers from terminating a supply upon the administration as well as prevent suppliers from making it a condition of continued supply that pre-administration arrears are paid and from making altering the contract asking for higher payments.

Appointment of an administrator does not automatically terminate any contracts of employment. If employees are kept on for at least 14 days after the administrator's appointment, the employees contract is deemed to be adopted by the administrator. Once the contract of employment is adopted by the administrator, any wages and salary (including holiday pay, sickness pay and contribution to occupational pension schemes) defined in section 99 paragraph 6 in Schedule B1 of the Act.

Commented [JL8]: 5
S 233B extends the provisions to all supplies.

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 liquidator can only distribute funds that are realized from the assets that are owned by the company.

Fixed charge holders can exercise their rights over the assets charged on their debts removing the liquidator's rights over those assets. If the value of the fixed charge is greater than the value of the creditor's claim, the liquidator has rights over the value above the creditor's claim.

Depending on the circumstances, the holder of a qualifying floating charge may choose to enforce its charges by appointing an administrator which will usually prevent a liquidator being appointed until the administration is completed. The floating charge holder may also consent to the appointment of a liquidator rather than an administrator, in which case the liquidator can realize the assets as part of the liquidation.

The first payment deals with "super priority" which is payment to employees when their contract is deemed to be assumed by the administrator. The extent of the payment of the wages and salaries is defined by section 99 of Schedule B1 of the Act.

Once the assets of the company are realized, the liquidator can distribute the fund using the following order under the UK Insolvency Rules 2016:

- 1) Expenses of the winding up, including the liquidator's remuneration:
Under section 115 of the Act, a number of expenses are given priority over the company's preferential creditors, any holders of the floating charge and the company's unsecured creditors. These expenses include the following:
 - Expenses that properly incurred by the liquidator in preserving, realizing or getting in any of the assets of the company (including the conduct of any legal proceedings);
 - The cost of any security provided by the liquidator;
 - Any amount payable to a person to assist in the preparation of the statement of affairs or accounts;
 - Any necessary disbursements by the liquidator in the course of the winding up
 - Remuneration of any person who has been employed by the liquidator to perform any services for the company;
 - Remuneration of the liquidator
 - The amount of any corporation tax on chargeable gains accruing on the realization of the assets of the company; and
 - Any other expenses properly incurred by the liquidator in carrying out the liquidator's functions in the winding up
- 2) Preferential creditors
Section 386, 387 and Schedule 6 provides guidelines on preferential creditors.

Preferential creditors largely comprises of limited claims of employees and some taxation liabilities. There are two classes of preferential creditors: ordinary (priority preferential creditors) and secondary.

- Any sum owed on account on an employee's contribution to an occupational pension scheme, being contributions deducted from earnings of the company's employees paid in the period of four months prior to the commencement of the winding up;
- Any sum owed by the company on account on an employer's contribution to an occupational pension scheme in the period of 12 months before the relevant date;
- Remuneration owed by the company to a person who is or has been an employee of the debtor and is payable in respect of the whole or any part

of the period four months prior to the commencement of the winding up to a maximum total figure which is currently £800;

- Any amounts owed by the company by way of accrued holiday remuneration in respect of any period of employment before the winding up;
- Claims for monies advanced to pay wages or holiday remuneration;
- Levies on the production of coal and steel;
- Claims for so much of any amount which is ordered to be paid by the company under the Reserve Forces (Safeguard of Employment) Act 1985;
- So much of any amount owed by the company in respect of an eligible deposit as does not exceed the compensation that would be payable in respect of the deposit under the Financial Services Compensation Scheme to the person or persons to whom amount is owed;
- So much of any amount owed by the company to one or more eligible persons in respect of an eligible deposit as exceeds any compensation that would be payable in respect of the deposit under the Financial Services Compensation Scheme to the person or those persons;
- An amount owed by the company to one or more eligible persons in respect of a deposit that –
 - Was made through a non-UK branch of a credit institution authorized by the competent authority of the UK, and
 - Would have been an eligible deposit if it had been made through a UK branch of that credit institution.
 - In addition, the UK has reintroduced a form of Crown preference for certain debts owed to the tax authority (Her Majesty's Revenue and Custom).
- PAYE income tax deductions, national insurance deductions, VAT payments, Construction Industry Scheme deductions and student loan repayments.

3) Floating charge holders

After preferential creditors have been paid, the next creditor to be paid will be any floating charge holder. If there are a number of floating charge holders, priority between them is usually based on which the charge was created first.

The liquidator (or administrator) is under a duty to make a "prescribed part" of the company's net property available for the satisfaction of unsecured debts and must not distribute any of those prescribed part to a floating charge holder except insofar as it is in excess of the amount required to satisfy all the unsecured creditors. "Net property" is the amount of the company's property which otherwise would be available for the satisfaction of debts of floating charge holders. It is thus calculated after the liquidation expenses and preferential creditors have been paid.

A floating charge holder, who may have an outstanding unsecured balance owing to it, is not permitted to participate in the distribution of the prescribed part,

4) Unsecured creditors

Creditors with no security, often ordinary trade creditors, are paid out last in the statutory order. Frequently, once the expenses of the liquidation have been paid and distributions have been made to secured and preferential creditors, there is little or nothing left to pay a dividend to unsecured creditors.

5) Shareholders

If there are sufficient funds to pay all the creditors (and interest on their debts) any surplus is distributed amongst the shareholders according to the company's constitution, which will normally permit a distribution pro rata the shareholders' perspective shareholdings.

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

Commented [JL10]: 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;

Corfee Zero Limited ("Corfee"), granted a debenture in favour of Stercus Bank plc ("Stercus"), non-connected person, which contained a floating charge over the whole of the Company's undertaking. This was granted in February 2021, within the 12 months prior to the commencement of the liquidation.

Section 245 of the Act applies to floating charges. It applies to where a company, Corfee, is in liquidation and the provision is aimed at preventing pre-existing unsecured creditors, Stercus, obtaining the security of a floating charge shortly before Corfee enters a formal insolvency procedure. It does not prevent lenders who are providing fresh funding to the

company from taking floating charge to the new funding. In this case, the floating charge was set up on a pre-existing loan.

Paragraph 2 of section 245 states that creation of a floating charge on the company's undertaking or property created at a relevant time (12 months ending with the onset of insolvency per paragraph 3(b)) is invalid except to the extent of the aggregate of —

- a) the value of so much of the consideration for the creation of the charge as consists of money paid, or goods or services supplied, to the company at the same time as, or after, the creation of the charge,
- b) the value of so much of that consideration as consists of the discharge or reduction, at the same time as, or after, the creation of the charge, of any debt of the company, and
- c) the amount of such interest (if any) as is payable on the amount falling within paragraph (a) or (b) in pursuance of any agreement under which the money was so paid, the goods or services were so supplied or the debt was so discharged or reduced.

There is no evidence here that the creation of a floating charge discharged or reduced the debt of Corfee, therefore does not meet the exemption criteria. It was created in order to prevent Stercus from demanding repayment of the company's loan rather than the payment (or reduction) of the loan itself.

Floating charge is invalid therefore the liquidator can write to the Company's house to remove the charge.

Commented [JL11]: 5

Question 4.2 [maximum 6 marks]

The sale of the coffee roasting machines; and

As early February 2021, Corfee experience liquidity issue when it cannot meet its obligations to Stercus.

In July 2021, the case mentioned that the Company continued to suffer cash flow problems. At this point, Corfee can be deemed cash flow insolvent there were evidence that Corfee would be unable to future obligations which would have been payment of Beans and Leaves Ltd ("B&L") as described in section 123 of the Act.

At the time, Corfee is deemed cash flow insolvent, the directors approved the sale of 5 coffee roasting machines to Ann Young (a director) for £10,000 in cash. It is unclear what the motives were for selling the roasting machine; it could be a plan to fund any present obligation in July 2021.

Under section 238 of the Act, the liquidator can take action against Ann Young for the perceived sale at a undervalue. The roasting machines were sold for £10,000 however, the machines were newly bought and costed £25,000 at the time of the purchase. It is unclear what the market value of the coffee machines at the time due to lack of valuation report but the machines would have lifespan more than 1.67 years.

In the director's defence, the court cannot make an order in respect of a transaction at an undervalue if it is satisfied under paragraph 5 of section 238:

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

As mentioned before, it is unclear what the motives were for sale and it could have been for the benefit of the company in a scenario that there was an immediate need for the funding however, it is hard to argue for the director that the sale was for the purpose of carrying on its business. Coffee machines are required to continue a coffee business therefore the disposal of these assets cannot satisfy the first test above.

Under section 212 of the Act, the liquidator may apply to the court to examine into the conduct of the Anne Young (and other directors) and compel her to:

- a) repay, restore or account for the money or property or any part of it, with interest at such rate as the court thinks just, or
- b) contribute such sum to the company's assets by way of compensation in respect of the misfeasance or breach of fiduciary or other duty as the court thinks just.

Question 4.3 [maximum 4 marks]

The payments to Beans and Leaves Ltd.

November 2021, four months after Corfee is deemed insolvent and 1 month after the creditors filed for a winding up petition, the directors of Corfee approved payment to B&L, a key supplier of Corfee, for £8,000 to cover existing liabilities (at the time) and 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 on 23 December 2021. The reason for payment is due to B&L being essential supplier of coffee beans.

As coffee machines have been disposed, continuation of the business is in question therefore obtaining further coffee beans may not have been a sound decision if Corfee is not to continue as a business.

Section 239 of the Act prevent a company to place one of its creditors in a better position than others shortly before entering into a formal insolvency procedure. It prevents such payment in full whether the creditor would have only expected part of the payment through dividend as an unsecured creditor. The preferential treatment is question is within the relevant time under section 240 of the Act (within 6 months prior to the commencement of the liquidation).

Paragraph 4 of section 239 states that a company gives a preference to a person if:

- a) that person is one of the company's creditors or a surety or guarantor for any of the company's debts or other liabilities, and
- b) the company does anything or suffers anything to be done which (in either case) has the effect of putting that person into a position which, in the event of the company going into insolvent liquidation, will be better than the position he would have been in if that thing had not been done.

The person who received the payment was B&L, a creditor of the company therefore the first requirement has been satisfied.

There is a question whether payment made has been put into a better position in comparison to other creditors. Although it is perceived that Corfee is cashflow insolvent, it is not clear whether it is balance sheet insolvent. If Corfee is balance sheet solvent, preferential treat may not be an issue due to the fact that all creditors would be paid out. However, if Corfee is also balance sheet insolvent, the second requirement above would also be satisfied.

Commented [JL12]: Not all of the requirements/ elements of s 238 have been addressed. What about the inability to pay debts and how a connected person sale influences what the office-holder would have to prove?
4

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.

*** End of Assessment ***