



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 6B

GERMANY

This is the **summative (formal) assessment** for **Module 6B** on this course and must be submitted by all candidates who **selected this module as one of their elective modules**.

The mark awarded for this assessment will determine your final mark for Module 6B. 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 **Microsoft Word format**, using a standard A4 size page and an 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.assessment6B]**. An example would be something along the following lines: 202122-336.assessment6B. **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. The final submission date for this assessment is **31 July 2022**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.
7. Prior to being populated with your answers, this assessment consists of **6 pages**.

ANSWER ALL THE QUESTIONS

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

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

Who decides which person should be appointed as Insolvency Practitioner in ordinary liquidation proceedings?

- (a) The debtor.
- (b) The creditors' committee.
- (c) The court.
- (d) **The court, but subject to a diverging decision of the first creditors' meeting.**
correct

Question 1.2

Which of the following securities **does not** have an accessory nature?

- (a) Suretyship.
- (b) **Mortgage (*Grundschild*)**
- (c) Mortgage (*Hypothek*).
- (d) Pledge.
correct

Question 1.3

Which of the following **cannot** be decided by the first creditor' meeting (*Berichtstermin*)?

- (a) **Verification of creditors' claims filed with the insolvency administrator.**
- (b) Shut down of the business.
- (c) Commissioning the insolvency administrator to develop an insolvency plan.
- (d) Election of the final creditors' committee.
correct

Question 1.4

After the occurrence of balance-sheet insolvency (overindebtedness), **how long is the time period** before the directors or obliged to file for insolvency proceedings?

- (a) Three weeks.
- (b) One month.
- (c) **Six weeks.**
- (d) Two months.
correct

Question 1.5

Tax claims stemming from the period prior to the opening of insolvency proceedings:

- (a) enjoy super-priority even ahead of secured creditors.
- (b) qualify as expenses of the proceedings (liabilities of the estate).
- (c) **rank as claims of ordinary creditors.**
- (d) cannot be recognized in insolvency proceedings at all.
correct

Question 1.6

What is the **majority required** for the adoption of a pre-insolvency restructuring plan under the StaRUG?

- (a) 75% in sum regarding the claims of creditors present and voting.
- (b) **75% in sum regarding the claims of all affected creditors.**
- (c) Simple majority in sum regarding the claims of creditors present and voting and simple majority of creditors (head count).
- (d) 75% of all affected creditors (head count).
correct

Question 1.7

Which court has jurisdiction to open insolvency proceedings?

- (a) **Amtsgericht.**
- (b) *Landgericht.*
- (c) *Oberlandesgericht.*

- (d) *Bundesgerichtshof*.
correct

Question 1.8

Which of the following has a **right to separation**?

- (a) Banks.
(b) Pledgees.
(c) Tax authorities with statutory liens on the debtor's assets.
(d) Landlords after termination of the tenancy agreement.
correct

Question 1.9

How long is the compliance period (timeframe) for the discharge of residual debt?

- (a) Seven years.
(b) Six years.
(c) Three years.
(d) One year.
correct

Question 1.10

Which of the following is a general prerequisite for transactions avoidance?

- (a) Substantive insolvency of the debtor.
(b) Disadvantage for the general body of creditors.
(c) Opponent's knowledge of the disadvantage of the general body of creditors.
(d) Opponent is a creditor.
correct

10 marks in total

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 3 marks]

How is "insolvency" defined in the *Insolvenzordnung*?

All insolvency proceedings in Germany are governed by the *Insolvenzordnung* ('InsO'). The InsO indicates three different grounds to for establishing insolvency: (1) inability to pay debts as they fall due, i.e., illiquidity (§17 InsO); (2) imminent illiquidity (§18 InsO); and (3) overindebtedness (§19 InsO).

A debtor is deemed to be 'illiquid' if he is unable to meet his mature obligations to pay. Illiquidity shall be presumed as a rule when a debtor has ceased making payments (§17 (2) InsO).

A debtor is deemed to be 'imminently illiquid' if it is highly probable that he will be unable to meet his existing obligations to pay on the date of their maturity (§18 (2) InsO).

A debtor is to be overindebted if his assets no longer cover his existing obligations to pay, unless it is highly probable that the enterprise will be able to survive for the next twelve months (§19 (2) InsO).

correct (3 marks)

Question 2.2 [maximum 4 marks]

Explain the relationship between pre-insolvency restructuring under the StaRUG and insolvency proceedings under the InsO.

The Gesetz über den Stabilisierungs- und Restrukturierungsrahmen für Unternehmen ('StaRUG'), which was based on Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, entered into force on January 1, 2021. Until then, the only restructuring options available to companies in crisis in Germany were either judicial insolvency proceedings or purely consensual out-of-court restructurings with the consent of all the companies' creditors. The StaRUG now closes that gap between (consensual) pre-insolvency restructuring on the one hand and restructuring via formal and comprehensive (court) insolvency proceedings under the InsO on the other.

The StaRUG establishes a statutory pre-insolvency restructuring framework (and thus is not a insolvency statute) to avert probable insolvency. It contains several new pre-insolvency restructuring procedures, including a new preventive restructuring plan and corresponding protection of minority creditors. It is an alternative to formal bankruptcy or liquidation proceedings, and governs the restructuring of imminently illiquid entrepreneurs outside of insolvency proceedings. The StaRUG offers a tool-box for pre-insolvency rescue (which must be distinguished from corporate rescue in insolvency proceedings under the InsO), and more in particular enables entrepreneurs to implement restructuring measures (e.g., a moratorium) with the involvement of creditors, even against the will of the creditors ('a cross-class cram-down'), and without having to open formal proceedings – as is the case with insolvency. The key restructuring tool under the StaRUG is the restructuring plan which is put to vote across separate classes of creditors.

Although many provisions are similar and may be applied in the same way (even though the circumstances prior to insolvency proceedings in imminent illiquidity scenarios are different), it is worth highlighting that some restructuring instruments (e.g., rules on executory contracts: §§103 et. seq. InsO) and measures (e.g., transactions avoidance; §§129 et. seq. InsO) available within insolvency proceedings are not available in pre-insolvency restructuring proceedings.

Moreover, the InsO is the only statute in Germany which applies to all kinds of debtors and is applicable to liquidation as well as the restructuring of insolvent debtors.

This is not an exact answer to the question. The difference concerns the reasons to open such proceedings (imminent illiquidity for StaRUG necessary, actual liquidity an obstacle): 2 marks

Question 2.3 [maximum 3 marks]

Explain the special rules on tenancy agreements for real estate compared to the general rules on executory contracts?

The treatment of executory contracts upon insolvency is for every insolvency proceeding (bankruptcy, liquidation and corporate rescue) regulated by §§103 et. seq. InsO. It should be noted that pre-insolvency proceedings do not per se affect the existing contracts and have no direct implications for termination. The opening of the insolvency proceeding itself does also not wound up such contract. §103 InsO contains a general rule for the execution of mutual contracts, which grants the insolvency administrator a right of choice with regard the fulfilment of certain contracts.

As a general rule for the execution of executory contracts, §103 InsO grants the insolvency administrator a right of choice with regard the fulfilment of certain contracts if a reciprocal contract was not or not performed in full by the debtor and the other party (the creditor) prior to the opening of the insolvency proceedings. In that case the insolvency administrator can choose between assuming and fulfilling such contract instead of the debtor and claim a fulfilment or performance from the other party (in which case the claim of the other party must be satisfied in full) or refusing to fulfil or perform such contract (in which case the claim of the other party by reason of the non-fulfilment or non-performance will only be satisfied on a *pro rata* basis). If the other party requests the insolvency administrator to exercise his right of choice, insolvency the administrator must declare without delay whether or not he wants the fulfilment or the performance of the contract. If the insolvency administrator omits to make such a declaration, he will no longer be able to ask for fulfilment (§103 InsO). Depending on his choice, the creditor's respective claim is either preferential (§55(1) (No 2) (alternative 1) InsO) or a mere insolvency claim (§103(2) (sentence 1) InsO).

The InsO does not provide for a general right of the insolvency administrator to reject executory contracts, except in the case of some types of contracts, such as a contract for the tenancy of immovables. §§108 and 109 InsO contain special rules for tenancy agreements for real estate.

In general, such agreements remain in place, but with effect for the insolvency estate. However, only the insolvency administrator is empowered to act for an on behalf of the insolvent debtor (tenant). §108 InsO especially encompass a special right for the insolvency administrator at his own discretion to terminate such agreement (concluded by the debtor as tenant), subject to a three-month notice period. If the insolvency administrator does not exercise his right to terminate, payment and other obligations under the tenancy agreement remain unaffected and enjoy priority over the claims.

correct (3 marks)

8 marks in total

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

Explain the rules in German insolvency law relating to transactions avoidance.

German insolvency law has extensive so-called 'claw back provisions' allowing the insolvency practitioner to challenge transactions which occurred within the relevant suspect periods before the opening of insolvency proceedings.

Under German law, transactions can be contested by the insolvency practitioner under §§129 et seq. InsO if (1) they were made prior to the request to open insolvency proceedings, (2) they place the creditors at a disadvantage, and (3) the insolvency practitioner demonstrates that he has reason to contest the transaction and he thus provides evidence of an avoidance ground (these avoidance grounds are listed in §§130 et seq. InsO).

A transaction is assumed to place the general body of creditors at a disadvantage where the assets or the amount of proceeds that are meant to satisfy or pay the ordinary creditors are reduced. The term 'transaction' includes any action which has a legal effect (e.g., payments, creation of security rights, waiver of claims). A 'disadvantage' can be established in case of a decrease in assets, an increase of liabilities, a delay of enforceability, etc. A typical example is the sale of an asset below value. The burden of proof for any placement of the creditors at a disadvantage is with the insolvency practitioner.

However, the InsO provides for certain presumptions, etc., to facilitate the burden of proof of the insolvency practitioner that all requirements are present. There will for example be a shift of the burden of proof to the opposing party who is closely connected to the debtor; it is assumed that related parties (to the transaction) have knowledge of the placement of creditors at a disadvantage. In the case of most avoidance grounds, the opposing party to the claim for restitution will try to convince the court that not all prerequisites are met, and especially that he or she did not possess the required knowledge.

As regards the avoidance grounds, first the provisions of §§130 and 131 InsO concentrate on transactions granting or facilitating an insolvency creditor a security or satisfaction. Whereas §130 InsO is applicable to transactions of so-called 'congruent coverage' (i.e., the insolvency creditor was entitled to such a security or satisfaction), §131 InsO is applicable to transactions of so-called 'incongruent coverage' (i.e., the insolvency creditor was not entitled to such a security or satisfaction).

Under §130 InsO the (congruent) transactions can only be challenged if they were made within three months prior to the request to open insolvency proceedings, or after it (in which case the knowledge of such a request is sufficient grounds to contest), and if the debtor was already cash flow insolvent or illiquid at that time and the creditor was aware of that or knew of the illiquidity. Whether the transaction occurred in the relevant suspect period must be dealt with in accordance with §140 InsO.

Under §131 InsO the suspect period in relation to (incongruent) transactions is (no more than) three months prior to the request to open insolvency proceedings. However, no further subjective requirements apply; also any knowledge or awareness of the creditor is irrelevant and must not be proven by the insolvency practitioner. Although in case the transaction was made within two or three months prior to the request to open insolvency proceedings, the insolvency practitioner will still have to prove that the debtor was illiquid at the time of the transaction (but not in case the transaction was made within one month prior to the request).

Further, §§132, 133 and 134 InsO are more general and cover all kinds of transactions.

Under §132 InsO transactions constituting a direct disadvantage to insolvency creditors can be challenged if they were made within three months prior to the request to open insolvency proceedings, or after it (in which case the knowledge of such a request is sufficient grounds to contest), and if the debtor was already illiquid at that time and the creditor was aware of that or knew of the illiquidity.

Under §133 InsO transactions entered into by the debtor within ten years prior to the request to open insolvency proceedings can be challenged if they were made with the intention to disadvantage creditors and if the other party to the transaction was aware of such intent at the time of the transaction.

Under §134 InsO (partially) gratuitous transactions or transactions under value performed by the debtor can be challenged if they were made within four years prior to the request to open insolvency proceedings.

Finally, §135 InsO concentrates on transactions granting shareholders a security or satisfaction (payment). All payments can be challenged if they were made within one year prior to the request to open insolvency proceedings, and all securities can be challenged if they were made within ten years prior to the request to open insolvency proceedings. No further subjective requirements apply, nor must the insolvency practitioner prove any other prerequisites.

The legal consequence of a successful contestation by the insolvency practitioner is that any assets of the debtor sold, transferred or relinquished under the challenged transaction must be returned to the insolvency estate, even if the third party has already relied on their disposition. According to §143(1) (sentence 1) InsO the claim for restitution becomes due when the insolvency proceedings are opened.

It is also worth highlighting that for pre-insolvency restructuring, no provisions under the StaRUG relating to transactions avoidance exist. However, the StaRUG provides for protection of transactions contained in, or executing, a restructuring plan in subsequent insolvency proceedings.

excellent

15 marks

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

In January 2020, Bank (B) has granted debtor (D) a loan of EUR 50,000. Since B asked for security, D has assigned all her current and future receivables against her customers by way of security. Sixteen (16) months later, in May 2021, D is unable to pay her debts when they fall due. On 3 July 2021, insolvency proceedings are opened against D and IA is appointed as insolvency administrator. IA collects two receivables, both amounting to EUR 11,900 (including 19% VAT). The first claim is rooted in a service contract between D and X concluded in June 2020. D has rendered the services on 7 July 2020. The second claim stems from a contract which IA, who decided to maintain D's business, concluded with Z on 20 July 2021 and which IA performed on 16 August 2021. X and Z pay the consideration for the services rendered to them by IA. B demands surrender of these payments (together EUR 23,800) from IA.

Does B have a claim against IA? Test this based on the norms.

The assignment in January 2020 of all D's current and future receivables against her customers by way of security (§§398 and 413 BGB) is a popular security right in Germany on intangibles (rights), and more in particular on claims. Following the assignment, B acquired the ownership of the claim(s) but is bound by the security agreement as a fiduciary. Because of the so-called 'separation principle' under German Law, the contractual agreement (loan) between B and D on creating the assignment as a matter of property law must be firmly distinguished from the underlying security agreement as a matter of the law of obligations.

As regards the future claims against D's customers, such claims were not affected by the assignment before they were created as a security right cannot exist without a security object (collateral).

- This primarily means that such claims can be challenged on the basis of §130 InsO if they are created within three months prior to the request to open insolvency proceedings, and if the debtor was already cash flow insolvent or illiquid at that time and the creditor was aware of that or knew of the illiquidity. *In casu* the claim against X was already created in June 2020 by concluding the service contract between D and X, which is more than eighteen months prior to the request to open insolvency proceedings. D was also not yet cash flow insolvent (i.e., unable to pay the debts when they fall due) at the time of creation of the claim, but this only happened later in May 2021. This claim thus cannot be successfully contested by IA under §130 InsO. Based upon the factual elements of the case there are also no indications that IA would be able to do so on other avoidance grounds. Moreover, it is difficult to see how the mere realisation of the security right in favour of B would be voidable under the provisions of transactions avoidance since there is no reason why it would place the general body of D's creditors at a disadvantage.
- This also means that claims created after the opening of the insolvency proceedings are not covered by the security right at all, since it comes into existence after the opening of the insolvency proceedings and pursuant to §91 InsO, after the opening of insolvency proceedings, rights in the assets of the insolvency estate cannot be acquired with legal effect even if such acquisition is not based on a transfer by the debtor or compulsory enforcement on behalf of an insolvency creditor. *In casu* the claim against Z was created on 20 July 2021 by concluding the contract between IA and Z, which is after the opening of the insolvency proceedings on 3 July 2021. This claim is thus not covered by B's security right since it only came into existence after the opening of the insolvency proceedings and §91 InsO does not allow for improvement of B's position (as creditor) after the opening of the proceedings.

Given the above, B will likely have a claim against IA but only for the amount of 11,900 EUR (being the first claim stemming from the service contract between D and X). After all, B's security right also provides for a so-called right to separate satisfaction (see §§49-51 InsO), which *inter alia* means that B is granted the right to demand preferential satisfaction up to the amount of B's secured claim out of the receivables of D's underlying claim against X in the context of the service contract between D and X.

Here, you should have referred to §§ 166(2), 171, 172 InsO

B will however not have a claim against IA for the other amount of 11,900 EUR (being the second claim stemming from the contract that was concluded between IA and Z) since those receivables were created after the opening of the insolvency proceedings and are thus not covered by B's security right (and no such right seems to have been created by IA in favour of B).

12 marks

*** End of Assessment ***

45 marks in total