



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 was answer (d)

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 was answer (b)

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 was answer (d)

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 was answer (c)

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

6 marks in total

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 3 marks]

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

According to section 17 *et seq.* of the *Insolvenzordnung*, “Insolvency” is defined as the general reason to open insolvency proceedings. Under that section, there are three types of reasons to open insolvency proceedings as followed.

1. Inability to pay debts as they fall due/ cash flow insolvency/ illiquidity. According to section 17, the debtor will be deemed to be illiquid if he or she is unable to meet his mature obligations to pay its debt. And if the debtor has stopped to make any payment to all its debts, the debtor is presumed to be Insolvent.

2. Imminent inability to pay debts. According to section 18, if a debtor is likely to be unable to meet his existing obligations to pay on the date of the debts’ maturity, the debtor is deemed to be imminent insolvent. However, this “imminent insolvency” can only be applicable to the person or persons filing the request who are empowered to represent the company or the partnership.

3. Overindebtedness. This insolvency reason is only applicable to a legal person. Under the *Insolvenzordnung*, overindebtedness is defined as the debtor's assets no longer cover the debtor's existing obligations to pay its debts. However, after considering the specific circumstance, if it is highly likely that the debtor entity will continue to exist, this insolvency reason cannot apply to that debtor.

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.

According to the rules provided by StaRUG and InsO, the relation between insolvency proceedings under the InsO and pre-insolvency restructuring under the StaRUG are as followed.

1. The application scopes of the proceedings are different. All insolvency proceedings are governed by InsO and the InsO is applicable to all kinds of debtors. In comparison, pre-insolvency restructuring under StaRUG, as an alternative for formal bankruptcy, only can apply to the entrepreneurs of all kinds, no matter they are natural persons or legal entities.

2. The degree of court involvement in the proceedings are different. The insolvency proceedings are controlled and supervised by courts. In comparison, in the pre-insolvency restructuring under StaRUG, the debtor may commence out-of-court negotiations with the creditor sought to be involved in the particular restructuring. The court will only provide necessary instruments by application of the debtor in pre-insolvency restructuring under StaRUG.

3. The reasons for commencement of the proceedings are different. The insolvency proceedings under InsO can be commenced on the reasons of illiquidity, Imminent insolvency and overindebtedness. However, the debtor to initiate pre-insolvency restructuring under StaRUG can only be imminent inability to pay its debts but not substantive insolvent.

4. The mechanisms for conversion of proceedings are different. In the insolvency proceedings under InsO, if a corporate rescue is attempted in that particular insolvency proceeding, conversion from the rescue to a liquidation is possible within the same proceeding. However, for a pre-insolvency restructuring under the StaRUG, once the debtor becomes illiquid or unable to pay debts. The pre-insolvency restructuring under StaRUG should be stopped as soon as possible. And the termination of pre-insolvency restructuring will not automatically lead to a conversion into the formal insolvency proceedings. It is up to the debtors and creditors to decide whether to apply for insolvency proceedings or not.

5. There are some other different factors noteworthy. Firstly, since the insolvency proceedings under InsO are formal proceedings, certain insolvency-related and procedural rules, such as the moratorium, proof of claims, executory contracts, transactions avoidance

and statutory preferential claims, are applicable to the proceedings. However, these rules are not available to pre-insolvency restructuring under StaRUG. Secondly, the rules of appointing officeholders in the proceedings are also different. Unlike the insolvency proceedings under InsO, the pre-insolvency restructuring under StaRUG can only appoint insolvency practitioners in limited circumstances. Thirdly, it should be noted the pre-insolvency restructuring under StaRUG enjoy more freedom and of more DIP factors. For example, in the pre-insolvency restructuring under StaRUG, the debtor's power to dispose properties is not restricted and only the debtor can acquire new credit. These rules are all different in comparison with those in the insolvency proceedings under InsO.

6. Similar rules apply to rescue plans in the insolvency proceedings under the InsO and pre-insolvency restructuring under the StaRUG. It is noteworthy that the StaRUG mirror the InsO's rules on insolvency plans, including the rules of division of creditors, approval threshold and cross-class cram down provisions.

In a brief summary, the insolvency proceedings under the InsO and pre-insolvency restructuring under StaRUG are different in many aspects. To a degree, they serve different goals, apply to different circumstances and complement each other functionally.

excellent (4 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 general rules on executory contracts are as followed. Under the German insolvency law, contracts will generally be wound up in insolvency proceedings. If the debtor has already fulfilled its obligation under the contract, then the counterparty of that contract has to fulfil its obligation of that contract. However, once a debtor entering into an insolvency proceeding, the claims of the counterparty under the contract against the debtor, can only be satisfied *pro rata* from the insolvency estate. As to a mutual contract which is yet not completely performed by either party, after the commencement of the insolvency proceedings, the insolvency administrator has the right to choose to perform such a contract under section 103 of the InsO. The administrator may perform the contract in replacement of the debtor and claim the counterparty to provide the consideration under such contract. If the administrator refuses to perform the contract, the counterparty will be entitled to its claims for non-performance only as an insolvency creditor. It also should be noted, according to section 103 of the InsO, If the counterparty requires the administrator to make a choice, the administrator has a duty to state his or her intention to claim performance without negligent delay.

In comparison, under German insolvency law, a tenancy agreement for real estate is a special type of contract with specific and different rules to apply. According to subsection 108(1) of the InsO, a tenancy agreement for a real estate should continue to exist, but must be existing for the credit of the insolvency estate. This rule means, in another word, as long as the tenancy agreement is for the credit of the insolvency estate, the administrator cannot refuse to perform the contract.

Moreover, according to subsection 109(1) of the InsO, if the debtor is a tenant of a tenancy agreement for real estate, the agreement can be terminated by the insolvency administrator by declaration or notice without regard to the agreed term of the contract or an agreed exclusion of a right to the legal period of notice. And if the administrator terminates the contract by notice or declaration, the counterparty may claim damages as an insolvency creditor for premature termination of such contract.

Further, according to subsection 109(2) of the InsO, If the debtor had not yet entered into possession of the real estate when an insolvency proceeding was opened against it, the administrator and the counterparty may withdraw from such contract. And if the contract has been withdrawn, the counter party may claim damages as an insolvency creditor for

premature termination of the contract. Notably, before such a tenancy agreement being withdrawn or affirmed, a party of that contract may request the other party to state within two weeks whether it intends to withdraw from the contract. If a party fails to give his or her statement, the party will lose the right to withdraw.

correct (3 marks)

10 marks in total

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

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

1. Prerequisites. According to subsection 129(1) of the InsO, transactions made prior to the opening of insolvency proceedings and disadvantaging the insolvency creditors may be contested by the insolvency administrator under the avoidable transaction provisions pursuant to sections 130 to 146. To establish an avoidable transaction, there are three prerequisites need to be satisfied as followed.

(1) The subject to be avoided should be a transaction under German law. However, the “transaction” is defined broadly as a civil legal act which has been performed, including payments, creation of security rights, waiver of claims, set-off and individual enforcement for satisfaction. **Transaction: all human behaviour having legal effects**

(2) The transaction must be made before the commencement of insolvency proceedings. As to the date of transaction, according to section 140, a transaction is deemed performed on the date when its legal effects become existent. And if legal effectiveness of a transaction requires registration in the relevant register, it is deemed performed as soon as the other conditions of its legal effectiveness are met, including the request for priority notice.

(3) The transaction should be to the disadvantages of the insolvency creditors. Under German law, the disadvantage of a transaction **means “reduction of the quota” and** must be objective. Hence, transferring assets which is not part of the insolvency assets, or transferring worthless assets are not to the disadvantage of the creditors. And to realize a security interest which is fully covered by the value of its collateral is not to the disadvantage of the creditors. Instead, for instance, according to German cases, receiving no consideration or no proper consideration,¹ promising to provide or providing considerations where no consideration is needed to provide,² and to replace an unsecured debt with a secured debt³, are all transactions disadvantaging creditors. However, it should be noted, according to section 142, the avoidance of cash transactions is restricted by the law, as the payments made by the debtor in return for which his property benefited directly from an equitable consideration may only be contested under the conditions under subsection 133(1).

2. The grounds to avoid a transaction. There are various different legal grounds provided in the InsO to avoid a transaction.

(1) Congruent coverage. According to section 130, a transaction granting or facilitating an insolvency creditor with security or satisfaction may be contested under the following two circumstances. First, the transaction was made during the last three months prior to the request to open insolvency proceedings, the debtor was already illiquid and the creditor was aware of his insolvency on this date. Second, the transaction was made after the request to open insolvency proceedings, and the creditor was aware of the debtor's insolvency or of the request to open insolvency proceedings. Further, according to section 130 of the InsO, certain types of the financial security agreement are excluded from the application of “congruent coverage”. And “a person with a close relationship” to the debtor under section 138 is presumed to have been aware of the debtor's insolvency or of the request to open insolvency proceedings.

¹ BGH ZIP 2012,285 Rdnr.6.

² BGH ZIP 2009,1674 Rdnr.24 ff.

³ BGH ZIP 1999,1674 973、974.

(2) Incongruent coverage. According to section 131, a transaction granting or facilitating an insolvency creditor with security or satisfaction without entitlement can be contested in three different types of suspect period. First, during the last month prior to the request to open insolvency proceedings or after such request; Second, within the second or third month prior to the request to open insolvency proceedings, if the debtor was illiquid on the date of the transaction; Third, within the second or third month prior to the request to open insolvency proceedings, if the creditor was aware of the disadvantage to the insolvency creditors arising from such transaction on its date. And “a person with a close relationship” to the debtor on the date of such transaction under section 138 is presumed to have been aware of the disadvantage to the insolvency creditors.

(3) Transactions immediately disadvantaging the Insolvency creditors. According to section 132 of the InsO, transactions made by the debtor constituting a direct disadvantage to insolvency creditors are contestable under two circumstances. First, the transaction was made during the last three months prior to the request to open insolvency proceedings, while the debtor was illiquid on the date of such transaction, and the counterparty was aware of such insolvency on this date; Second, the transaction was made subsequent to the request to open insolvency proceedings and the counterparty was aware of such insolvency or of the request to open insolvency proceedings at that time. Notably, where section 130 and 131 apply, the section 132 is not applicable.

(4) Wilful disadvantage. According to section 133, a transaction made by the debtor during the last ten years prior to the request to open insolvency proceedings, or subsequent to such request, with the intention to disadvantage his creditors can be contested if the counterparty was aware of the debtor's intention on the date of that transaction. And if the counterparty knew of the debtor's imminent insolvency and the transaction constituting disadvantage for the creditors, it is presumed the counterparty had such awareness at the time. And an onerous contract entered into by the debtor with “a person with a close relationship” directly constitutes a disadvantage to the creditors, unless the contract was entered into earlier than two years prior to the request to open insolvency proceedings, or if the other party was not aware of the debtor's intention to disadvantage the creditors on the date of such contract.

(5) Gratuitous benefit. According to section 134, a gratuitous benefit granted by the debtor within four years prior to the request to open insolvency proceedings can be contested. However, a usual casual gift of minor value is not contestable.

(6) Other specific grounds. Certain specific grounds to avoid a transaction are also provided under the InsO, including : where loans replacing equity capital were secured with 10 years or satisfied within 1 year,⁴ and where silent partner's share in accrued losses was waived.⁵

It should be noted, to defend a transaction, a counterparty of that transaction can argue that the aforementioned grounds are not established as the requirements mentioned above are not satisfied. Then in order to avoid a transaction, the administrator will need to prove that all the prerequisites and requirements are satisfied. However, if the counterparty is “a person with a close relationship”, the burden of prove shifts to the connected counterparty.

3. Legal consequences. According to section 143, once a transaction was successfully contested and avoided, any property of the debtor disposed under the transaction must be to retribute to the insolvency estate as the transaction has never occurred. Notably, after the opening of proceedings, the claims of restitution are formed by the force of law, and are not formed upon the administrator's declaration.

Further, if a transaction is successfully contested and avoided, the counterparty's claim to the contested transaction will revive. Relevant considerations should be refunded from the insolvency estate to the extent to which such consideration continues to exist in a distinct form or were augmented by its value.⁶ Moreover, for a recipient of a gratuitous benefit, he or she should retribute such benefit only to the extent of his enrichment.

⁴ Section 135 of the InsO.

⁵ Section 136 of the InsO.

⁶ Subsection 143(2) of the InsO.

Lastly, according to section 145, as to the legal successors, a transaction can be contested against another legal successor under the following three circumstances. First, the legal successor was aware of the circumstances giving rise to the enrichment of his predecessor being subject to contention on the date of his enrichment. Second, the legal successor is a “persons with a close relationship” under section 138 save that he was unaware of the circumstances giving rise to the enrichment on such date; Third, the legal successor received the enrichment by way of a gratuitous transfer.

13 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.

B does have a claim against IA. But not all the payments of EUR 23,800 can be covered by such a secured claim. Specifically, B has a secured right to separate satisfaction of the remaining amount of the proceeds from the first claim, the amount of which is EUR 9600. However, as to the second claim, B can only claim as an ordinary insolvency creditor and be paid *pro rata* from the insolvency estate which include the proceed of the second claim. The reasons are as below.

The first issue here is whether the security interest is validly created between B and D, and if it is, what can the security interests cover. According to German law and established practices, it is effective to assign D’s current and future receivables against her customers to create a security. And if such a security has been created, B is holding the ownership of the claims and are bound by the security as a fiduciary.

However, in this case, the security was created 16 months before D fell into illiquid, and 18 months before the commencement of D’s proceeding. Hence there were some “future claims” back then which were not yet created. These “future claims” would not be affected by the assignment between B and D, because no security right can exist without a collateral. Therefore, the security interests were validly created in this case but could not cover all the subsequent receivables of D.

Instead, according to section 91 of the InsO, once an insolvency proceeding is opened, the rights in objects which will form part of the insolvency estate cannot be acquired with legal effect. Therefore, the claims created after the commencement of an insolvency proceeding should become part of the insolvency estate and cannot be covered by the security set before. Further, according to section 130 and 131, the claims created within the suspect period of three months prior to the application for insolvency are subjected to the transaction avoidance rules and may be contested. Therefore, as to whether a future claim can be covered by a security interest. The creation time of the specific claim matters.

In this case, the first claim is rooted in a service contract concluded in June 2020, under which D has rendered its services on 7 July 2020. Hence the creation time of the first claim was after the security created for B to cover future claims, but was more than 3 months prior to D becoming insolvent. As a result, the first claim is covered by B’s security interests, and is not neither void or voidable. The second claim is rooted in a contract concluded on 20 July

2021 and performed on 16 August 2021. Hence, no matter what the contract's terms were, the claim was created after the commencement of the proceeding, which means, B's security cannot cover the second claim, as the rules discussed above. Therefore, the second claim has formed part of the insolvency estate, which is not covered by B's security interests. To the second claim, B can only be paid as an ordinary insolvency creditor in the insolvency proceeding.

Since only the first claim can be covered by the B's security interests, the second issue here is what is the amount claimable by B. First of all, according to section 47, 49 and subsection 50(1), the creditor to whom the debtor has assigned a movable item or a right in order to secure a claim, enjoy a right to separation and can be satisfied outside the proceeding. And according to subsection 166(2), the insolvency administrator may collect or in another way dispose of a claim assigned by the debtor in order to secure a claim. Since IA has already disposed the first claim to which B enjoyed a right to separate satisfaction, the section 170 should apply to the distribution of the proceed. According to subsection 170(1), after the disposition of a claim by the insolvency administrator, the costs of determining and disposing of the object should be credited to the insolvency estate in advance using the proceeds. The remaining amount should be used without delay to satisfy the creditor with a right to separate satisfaction. to calculate the costs of determining and disposing, the section 171 should be followed. In this case, the costs of determining should be rated as the lump sum of 4% of the proceed.⁷ As to the costs of disposing, since the claim was paid voluntarily by X with no actual cost, which is considerably lower than the lump sum of 5%, the costs of disposing should be only rated as the TVA of 19% incurred. Hence the remaining amount is EUR 9600, which should be used without delay to satisfy B as B's security interests has already covered claim. Therefore, to the first claim, B has the right to separate satisfaction of a claim of EUR 9600.

excellent: 15 marks

*** End of Assessment ***

44 marks in total

⁷ Subsection 171(1) of the InsO.