



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 3A
THE INSOLVENCY SYSTEM OF THE UNITED STATES

This is the **summative (formal) assessment** for **Module 3A** 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 3A. 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.assessment3A]**. An example would be something along the following lines: 202122-514.assessment3A. **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 3A 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 3A 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 **8 pages**.

ANSWER ALL THE QUESTIONS

Commented [H(1)]: Total marks 36.5/50

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

Commented [H(2)]: Total marks 8/10

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

Commented [H(3)]: Correct, 1 mark

ABC Corp is filing for bankruptcy under chapter 11. Which of the following **is not** a party in interest in that proceeding?

- (a) A neighboring land owner who has leased equipment to ABC Corp.
- (b) ABC's government regulator.
- (c) A bank that has loaned money to ABC.
- (d) A local advocacy group.**
- (e) All of the above.

Question 1.2

Commented [H(4)]: Correct, 1 mark

Which of the following statements regarding executory contracts is **false**?

- (a) Executory contracts are clearly defined by the bankruptcy code.**
- (b) Chapter 11 debtors have greater flexibility than chapter 7 debtors on when they may assume, assign or reject an executory contract.
- (c) In the most common formulation, executory contracts are defined as those where both sides to a contract have material unperformed obligations.
- (d) A court will generally defer to a debtor's business judgment regarding whether to assume or reject an executory contract.
- (e) Under the hypothetical test, a debtor cannot assume an executory contract if the debtor could not also assign the contract.

Question 1.3

Commented [H(5)]: Incorrect, the correct response is (d)

In which of the following scenarios does a bankruptcy court have constitutional authority to issue a final order? Assume in each that the counterparty to the dispute has not consented to the bankruptcy court's exercise of jurisdiction.

- (a) A counterclaim against the estate that introduces a question under state law.
- (b) Since the list of core proceedings is non-exhaustive, a bankruptcy court may issue a final determination on any matter that comes before it.

- (c) A creditor's claim against an affiliate of the debtor that has guaranteed the debtor's obligation to the creditor
- (d) A debtor's motion to dismiss an involuntary bankruptcy petition.
- (e) None of the above.

Question 1.4

Commented [H(6): Correct, 1 mark

Which of the following statements about "pre-packs" is **false**?

- (a) A pre-pack cannot be used if the debtor wishes to reject executory contracts.
- (b) Creditors must have sufficient information about the debtor and the plan to make an informed voting decision.
- (c) A pre-pack debtor may spend as little as a single day in bankruptcy.
- (d) The proposed plan of reorganization is submitted to the bankruptcy court together with the voluntary petition.
- (e) Creditors' commitment to vote in favor of the plan may be memorialized in a restructuring support agreement.

Question 1.5

Commented [H(7): Correct, 1 mark

Which of the following statements regarding cramdowns is **true**?

- (a) If one insider creditor approves of the plan of reorganization, all other impaired classes may be crammed down.
- (b) Because cramdowns do not require the consent of all classes, the plan of reorganization may not be fair and equitable to all impaired classes.
- (c) Differential treatment of different classes is permitted if there is a reasonable, good faith basis for doing so and such treatment is required for the plan of reorganization to be successful.
- (d) Class definition is rarely a battleground when a debtor tries to cramdown classes.
- (e) Dissenting creditors are not permitted to challenge the classification of a creditor supporting the cramdown.

Question 1.6

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Which of the following statements about the plan exclusivity period is **true**?

- (a) The exclusivity period is 1 year.
- (b) The exclusivity period cannot be extended.
- (c) The exclusivity period cannot be shortened.

(d) During the exclusivity period, only a creditor may propose a plan of reorganization.

(e) During the exclusivity period, only the debtor may propose a plan of reorganization.

Question 1.7

Commented [H(9)]: Correct, 1 mark

Which of the following statements about chapter 15 is **false**?

(a) The automatic stay applies upon the filing of a petition for recognition.

(b) A debtor cannot be subject to an involuntary chapter 15 proceeding.

(c) A chapter 15 petition must be filed by a foreign representative.

(d) The automatic stay applies only to property within the territorial jurisdiction of the United States.

(e) Recognition may be granted to a foreign proceeding as either foreign main or foreign non-main.

Question 1.8

Commented [H(10)]: Correct, 1 mark

Which of the following statements about 363 sales is **false**?

(a) A 363 sale permits a debtor to sell an asset free and clear of encumbrances.

(b) A creditor's lien on assets sold in a 363 sale attaches to the proceeds of the sale.

(c) A 363 sale must be conducted as an auction with a stalking horse bidder.

(d) Purchasers may pay a higher price for assets sold in a 363 sale than in an out-of-court transaction.

(e) Sophisticated parties will insist on a 363 sale if there is any question regarding whether the sale is "in the ordinary course of business".

Question 1.9

Commented [H(11)]: Incorrect, the correct response is (e)

If a debtor rejects an executory trademark license agreement under which it licenses a trademark to its counterparty, which of the following is **true**?

(a) The counterparty has a claim for damages for breach of contract.

(b) The counterparty must immediately stop using the trademark.

(c) The counterparty can continue using the trademark for the remaining period of the license.

(d) Both (a) and (b).

(e) Both (a) and (c).

Question 1.10

Who may serve as a foreign representative to seek recognition of a foreign proceeding under chapter 15?

- (a) The board of directors of the debtor if it is a debtor-in-possession in the foreign proceeding.
- (b) An insolvency professional appointed by a creditor where the foreign proceeding is an involuntary receivership.
- (c) An officer of the debtor if it is a debtor-in-possession in the foreign proceeding.
- (d) An insolvency professional appointed by the court overseeing the foreign proceeding.
- (e) All of the above.

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QUESTION 2 (direct questions) [10 marks]

Commented [H(13)]: Total marks 8/10

Question 2.1 (2 marks)

Commented [H(14)]: Total marks 2/2

What is the difference between a voluntary petition for bankruptcy and an involuntary petition for bankruptcy?

A voluntary petition is commenced by a debtor under any applicable chapter by filing a petition, together with a number of schedules. However, "naked" petition may also be sufficient to invoke automatic stay and a debtor need not be or claim to be insolvent.

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An involuntary petition is commenced by a creditor against an eligible under chapter 7 or chapter 11 but not other chapters or against a farmer, family farmer or not-for-profit corporation. Only one creditor (non-contingent and non-insider) is required if there are less than 12 such creditors while at least 3 would be required if there are more.

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Question 2.2 (2 marks)

Commented [H(17)]: Total marks 2/2

What are two potential consequences of a violation of the automatic stay?

An act violating the automatic stay (even without notice of the petition filed) constitutes contempt of court and is void or voidable. Should the parties in interest fail to obtain relief from the stay, it may result in the imposition of contempt sanctions against the stay violator and possible results include payment of the debtors' attorneys' fees and requiring the violator to take affirmative acts to undo the effects of violation.

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Commented [H(19)]: Correct, 1 mark

Question 2.3 (3 marks)

Commented [H(20)]: Total marks 1/3

In what circumstances is a claim considered "impaired"? When is a holder of an impaired claim not entitled to vote on a proposed plan of reorganization and what happens instead?

A holder's claim is considered "impaired" unless, as to every claim or interest in the class of claim, holder's legal, equitable and contractual rights are unaltered under the reorganization plan. A payment in full, if delayed, would also be considered as impaired.

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A holder of an impaired claim is not entitled to vote on a proposed plan of reorganization if he is considered as "insider". If he is a dissenting creditor, he could have his grievances heard at the confirmation of the plan in the court.

Commented [H(22): Incorrect, insiders can vote but their votes aren't counted for certain purposes. A holder of an impaired claim that will receive nothing under the plan cannot vote and is deemed to reject the plan.

Question 2.4 (3 marks)

Commented [H(23): Total marks 3/3

Answer the following questions about preferences, actual fraudulent conveyances and constructive fraudulent conveyances:

(1) Which cause of action applies only to transfers made on account of antecedent debt?

Preferences

Commented [H(24): Correct, 1 mark

(2) Which cause of action requires that the debtor be presumed or proven to have been insolvent at the time of the transfer?

Preferences

Commented [H(25): Correct, 1 mark

(3) Which cause of action requires that the debtor be proven to have intended to frustrate creditors' recoveries?

Actual fraudulent conveyances

Commented [H(26): Correct, 1 mark

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

Commented [H(27): Total marks 12.5/15

Question 3.1 (3 marks)

Commented [H(28): Total marks 2.5/3

How did *Stern v Marshall* change the law of bankruptcy court jurisdiction and authority to enter a final order?

Before *Stern v Marshall*, there were jurisdictional provisions enacted to grant jurisdiction over bankruptcy proceedings to district courts and permit district courts to refer such proceedings to the bankruptcy courts of respective district.

Such referral arrangement creates distinction between "core" and "non-core" matters and bankruptcy judges would hear and determine only core proceedings. Bankruptcy court hear non-core proceedings only if they are sufficiently related to a bankruptcy proceeding but no final determination may be made. It would submit proposed findings of fact and conclusion of law to the district court for a final decision.

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In *Stern v Marshall*, it was held that bankruptcy court cannot issue final orders that invade Article III jurisdiction even in core proceedings. In that case, although a counterclaim is a core proceeding which a bankruptcy court can issue a final order under 28 USC s.157, the US Supreme Court held that the bankruptcy court's issuance of a final order over a state law claim (heard in federal courts) was unconstitutional under Article III.

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It was held by US Supreme Court that bankruptcy judges may determine a core proceeding over which they lack constitutional authority by issuing a report and recommendation for review by district court, as in non-core proceedings, or may issue final orders with consent of the parties.

Commented [H(31): Correct, 1/2 mark, the bankruptcy court may also issue a final order on a challenge to a petition

Question 3.2 (3 marks)

What provisions of the Bankruptcy Code may not be invoked by a foreign representative in a chapter 15 proceeding? What are two ways that the foreign representative can obtain equivalent relief?

Under s.1521(7), discretionary relief that may be granted upon recognition had excluded those under sections 522, 544, 545, 547, 548, 550, and 724(a).

A foreign representative can only invoke avoidance powers under Bankruptcy Code in a plenary proceedings such as chapter 7 or 11 (under s.1523(a)).

A foreign representative may commence plenary proceedings to obtain access to the Bankruptcy Code's avoidance powers where relief under other applicable law is unsatisfactory, such as where the statute of limitations has expired or applicable law does not allow claims for constructive fraudulent conveyance.

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Commented [H(33)]: Correct, 1 mark

Commented [H(34)]: Correct, 1 mark, also the foreign representative may seek analogous relief under other applicable US and foreign law

Question 3.3 (4 marks)

Describe the differences between interlocutory and final orders and how an appeal may be taken from each. Which courts hear direct appeals from bankruptcy court orders?

Interlocutory orders resolve only some of the issues or claims while final orders dispose of all issues, leaving nothing further to be decided. Interlocutory orders may only be appealed with leave of the appellate court while final orders may be appealed as of right. It was held by the US Supreme Court that a bankruptcy order resolving a discrete dispute is a final order for appeals purpose.

Appeals from bankruptcy court are heard by the district court in the district where it locates. In some circuits (e.g. 1st and 6th), bankruptcy appeals are heard by a Bankruptcy Appellate Panel (BAP) forming by bankruptcy judges of the bankruptcy courts within the circuit. A party in those circuits may choose to have the appeal be heard by the district court or the BAP. Further to district court or BAP, the appeals would be heard by circuit court of appeals.

In rare situations, appeals from bankruptcy courts would go directly to the court of appeals upon certification of certain conditions by the bankruptcy court or district court.

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Commented [H(36)]: Correct, 1/2 mark

Commented [H(37)]: Correct, 1/2 mark

Commented [H(38)]: Correct, 1/2 mark

Commented [H(39)]: Correct, 1/2 mark

Commented [H(40)]: Correct, 1 mark

Commented [H(41)]: Correct, 1 mark

Question 3.4 (5 marks)

What fiduciary duties do directors of Delaware corporations owe and to whom are the duties owed in the ordinary course of business? To whom are duties owed when the corporation is potentially or actually insolvent?

Directors owe fiduciary duty of loyalty to the corporation's best interest and a duty of care in educated decision-making. It is well-established under Delaware law that when a corporation is solvent, directors' duties run to the corporation and the corporation should be managed for the benefit of its shareholders. They are protected from liability for errors of judgment by the business judgment rule. It is presumed that they have acted in good faith on the basis of reasonable information.

Commented [H(42)]: Total marks 4/5

Commented [H(43)]: Correct, 1 mark

Commented [H(44)]: Correct, 1 mark

Directors owe duties to the corporation and shareholders but not creditors even when the corporation is potentially insolvent. It was held by Delaware Supreme Court that directors' fiduciary duties do not shift from shareholders to creditors.

Commented [H(45)]: Correct, 1 mark

Commented [H(46)]: Correct, 1 mark

Commented [H(47)]: Correct, 1 mark

Even when a corporation becomes actually insolvent, the board's fiduciary duties are to all of the corporation's residual claimants, including both the creditors and the shareholders. Directors must continue to make decisions based on what they believe will be in the best interests of the corporation but with the consideration directed to the interests of creditors as well as shareholders.

Commented [H(48)]: Incorrect, this proposition was rejected in Gheewala, -1 mark

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

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Question 4.1 [4 marks]

Commented [H(50)]: Total marks 3/4

Gambling Corporation is incorporated and has a principal place of business in Greece and it operates casinos and betting parlors in many international cities, including Athens, Las Vegas, London and Macau. Gambling Corp's bonds (governed by English law) are due to mature in one (1) year, but it is unable to repay or refinance them. Gambling Corp is considering using an English scheme of arrangement to restructure the bonds.

Discuss whether the English scheme of arrangement could be granted recognition under US chapter 15 as a foreign main or foreign non-main proceeding.

The English scheme of arrangement can be classified as "foreign proceeding" which is recognizable and defined broadly by the Bankruptcy Code as "a collective judicial or administrative proceeding in a foreign country, including an interim proceeding, under a law relating to insolvency or adjustment of debt in which proceeding the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganization or liquidation."

Furthermore, Gambling Corp operates casinos and betting parlors in cities including Las Vegas therefore it should have assets in United States.

Contention would arise at the recognition stage on whether the proceeding is characterized as foreign main or foreign non-main, which would affect the scope of relief available to debtor. Foreign main proceedings are commenced in the debtor's center of main interest (COMI), presuming to be the location of incorporation (but is rebuttable). Factors to be considered includes location of headquarters, management and primary assets, etc.

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In this case, although the bonds were governed by English law, Gambling Corp is incorporated and has a principal place of business in Greece. It does not appear that the COMI of Gambling Corp is in England considering those factors therefore the English scheme of arrangement could be granted recognition under US chapter 15 as a foreign non-main proceeding.

Commented [H(52)]: Correct, 1 mark

Commented [H(53)]: Correct, 1 mark, also note that the casino in London would constitute the necessary establishment in the jurisdiction of the foreign proceedings

Question 4.2 [5 marks]

Commented [H(54)]: Total marks 2/5

Oil Corporation is incorporated in Delaware and has its principal place of business in Texas. Oil Corp is facing a number of challenges to its business. First, ShipCo, one of its key customers, has filed a breach of contract lawsuit in Texas state court alleging that Oil Corp sold it contaminated oil that caused USD 1 billion in damage to ShipCo's container ships. Second, the US Department of Justice is investigating whether Oil Corp illegally purchased oil from countries subject to US sanctions. Third, Oil Corp. has missed a payment on its secured loan from USA Bank, and USA Bank is threatening to foreclose on an Oil Corp refinery located

in the Philippines. Fourth, because of all these distractions, Oil Corp has forgotten to pay rent on its Houston, Texas office space and its landlord is threatening to evict it. What would be the effect of Oil Corp filing a chapter 11 petition on each of these four situations?

ShipCo : Once Oil Corp file a chapter 11 petition, the worldwide automatic stay comes into effect immediately under s.362 since ShipCo's claim is a litigation on pre-petition claim. ShipCo as a claim holder becomes a creditor of Oil Corp and would have the right to vote for or against the reorganization plan if being classified into an impaired class.

US Department of Justice : The automatic stay is subject to certain statutory exceptions under s.362, including criminal proceedings and regulatory investigations therefore the Department may continue to conduct necessary investigation and commence prosecution action, if necessary.

USA Bank : After the chapter 11 petition is filed, USA Bank as a secured creditor would continue to retain the lien securing such claim. Should the security falls over the refinery located in Philippines, USA Bank can continue to foreclose the same and sale proceeds (after settling their claim) would form part of the Oil Corp's estate. If the refinery is sold under the plan, USA Bank would be paid in full (subject to payment of costs to trustee), including interest and costs if the value of the collateral allows.

Landlord : The lease is an executory contract. Under chapter 11 petition, Oil Corp could decide (upon confirmation of the plan) on whether to reject, assume or "assume and assign" the contract. Should Oil Corp decide to reject the lease, the landlord would have an unsecured pre-petition claim in damages. Should they decide to assume the lease, Oil Corp must cure defaults and give the landlord sufficient assurance of future performance. If Oil Corp continue to occupy the premises, it is deemed to have assumed the lease based on conduct.

Question 4.3 [6 marks]

Oil Corp has filed for bankruptcy and is planning to sell its plastic manufacturing business through a 363 sale. The plastic manufacturing business operates under the trademark "Interconnect", which is licensed from Plastic Corp. Oil Corp has invented several patented processes for plastic manufacturing, which it licenses to Plastic Corp. The main manufacturing facility for the plastic business is in Dallas, and Oil Corp has granted a lien on the facility to USA Bank to secure its USD 500 million loan.

Oil Corp thinks it will get the highest return for the plastics manufacturing business if it can (i) assume and assign the trademark license; (ii) reject the patent licenses so the purchaser has the exclusive right to use the patents; and (iii) sell the manufacturing facility free and clear of the USA Bank lien. Can Oil Corp achieve each of these goals without the consent of Plastic Corp and USA Bank? Why or why not?

(i) The trademark license agreement is an executory contract and is not assignable in the absence of licensor's consent as held in *Re Trump Entertainment Resorts, Inc* and under s.365(c) of the Bankruptcy Code. Oil Corp must be certain that the agreement expressly permits assignment or have the Plastic Corp's express consent in order to assume and assign. The absence of a provision clearly and expressly consenting to assignment will most likely result in a court determining that a trademark license is not assignable to a third party without the licensor's consent and thus prevent the debtor from assuming and assigning it.

(ii) If the Oil Corp reject the patent licenses, Plastic Corp would not be able to use the patent which would be disastrous to their business. However, Plastic Corp have a

Commented [H(55)]: Correct, 1 mark

Commented [H(56)]: litigation on a pre-petition claim would be stayed by the automatic stay

Commented [H(57)]: Correct, 1 mark

Commented [H(58)]: Incorrect, the stay bars an action to take control of estate assets anywhere in the world

Commented [H(59)]: Because the lease has not expired prior to the bankruptcy, the automatic stay prevents the landlord from evicting Oil Corp

Commented [H(60)]: Total marks 3/6

Commented [H(61)]: Correct, 1 mark, this is because trademark law permits a licensor to refuse to accept performance from an assignee

remedy under Section 365(n) of the Bankruptcy Code. Should Oil Corp reject the patent license, then Plastic Corp may consider the agreement terminated or retain its rights in the license that existed before filing of bankruptcy petition. However, Plastic Corp must continue to pay royalties if they choose to retain its rights, and Oil Corp must ensure the patents remain exclusive or confidential. However, Oil Corp are no longer required to perform future affirmative obligations with respect to the patents such as providing technical support.

- (iii) USA Bank, who is a holding security interest in the facility, may “credit bid” by offsetting a portion of the purchase price of the facility against the amount of their claim secured. Under s.363(k), a 363 sale that is subject to a lien that secures an allowed claim, unless the court for cause orders otherwise the holder of such claim may bid at such sale, and, if the holder of such claim purchases such property, such holder may offset such claim against the purchase price of such property. According, the sale of the facility free and clear of the lien is subject to USA Bank’s right to “credit bid” and the return would be diminished as a result.

*** End of Assessment ***

Commented [H(62)]: Correct, 1 mark, as a result there could be no exclusivity for a purchase of the patents without Plastic Corp’s consent

Commented [H(63)]: Correct, 1 mark, though the ability to credit bid would not necessarily affect the amount received by the estate because, in the absence of a credit bid the proceeds of the sale would be subject to USA Bank’s lien