



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 41/50

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

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.

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Question 1.5

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.

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Question 1.6

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.

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(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

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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

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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)]: Correct, 1 mark

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 [H13]: Total marks 8/10

Question 2.1 (2 marks)

Commented [H14]: Total marks 2/2

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

A voluntary petition is filed under any chapter of the US Bankruptcy Code ("UBC") by the debtor and does not require the debtor to be insolvent. An involuntary petition is filed by qualifying creditors under either chapter 7 or 11 of the UBS and does require the debtor to be insolvent.

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Commented [H16]: Correct, 1 mark

Question 2.2 (2 marks)

Commented [H17]: Total marks 2/2

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

The party violating the stay may be held in contempt of court and be subject to contempt sanctions, and the act(s) taken in violation of the stay are either void or voidable.

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Commented [H19]: Correct, 1 mark

Question 2.3 (3 marks)

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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?

Under section 11.24(1) of the UBC, a claim will be considered "impaired" if a proposed plan of reorganization would *not* leave the claim holder's "legal, equitable and contractual rights unaltered".

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Although it is typically the case that votes on plans of reorganization are only open to the holders of impaired claims, this will not be the case where such holders are "insiders" (as defined in section 101(31) of the UBC) or if they would receive nothing upon implementation of the plan. When this happens, if at least one impaired class of creditors approves the plan, the impaired claim holders who were not allowed to vote will be crammed down and will be bound if the court confirms the plan of reorganization.

Commented [H22]: Correct, 1 mark, they are deemed to reject the plan

Question 2.4 (3 marks)

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

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

Constructive fraudulent conveyances

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

Actual fraudulent conveyances

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

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Question 3.1 (3 marks)

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

Article III of the US Constitution deals with the US judicial system and underpins the establishment of (among others) state courts. Prior to *Stern v Marshall*, it was generally accepted that federal bankruptcy courts (established through the 1978 Bankruptcy Code rather than through Article III of the US Constitution) had jurisdiction to deal, and enter final orders in connection, with core proceedings (as defined in 28 U.S. Code § 157). In addition, parallel proceedings in state and federal courts are permitted under the US legal systems and the first judgment to be handed down in such proceedings is usually binding.

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Commented [H(30)]: Correct, 1 mark

However, in *Stern v Marshall*, the Supreme Court held that bankruptcy courts do not have jurisdiction to issue final determinations if these would be inconsistent with the judgment of a state court, even where core proceedings are involved and where the bankruptcy court handed down the first judgment in parallel proceedings.

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As a result, the Federal Rules of Bankruptcy Procedure, in an effort to codify various subsequent rulings by the Supreme Court, now provide that parties to a claim must specify whether or a bankruptcy court may enter final orders in relation to the proceedings, and whether any ultra vires final order from a bankruptcy court may be ratified by a district court.

Commented [H(32)]: Correct, 1/2 mark, also the bankruptcy court has jurisdiction to adjudicate a challenge to a petition

Question 3.2 (3 marks)

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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?

When a foreign representative files a petition under chapter 15, the statutory automatic stay which comes into effect upon the filing of petitions under other chapters of the UBC does not commence. This is because the statutory stay will only start once the petition for recognition of foreign main proceedings is granted. Instead, under section 1519 of the U.S. Code, if the relevant bankruptcy court is satisfied (among other things) of the likelihood of success of the petition and that granting interim relief would not cause irreparable harm, it may grant an interim stay instead – however, as already mentioned, this is not automatic.

In addition, under section 1521(a)(7) of the UBC, foreign representatives may not use the avoidance powers contained in the UBC, particularly in connection with preferences and fraudulent conveyances. If such powers are required, the foreign representative may only invoke them if plenary proceedings are running alongside the chapter 15 proceeding (for example if these were initiated before the chapter 15 proceeding, or if the foreign representative themselves starts such plenary proceedings once the chapter 15 proceeding has been recognised). Whilst this solution allows the foreign representative to make use of the avoidance powers, it must be noted that this will be restricted to the debtor's assets in the US.

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Commented [H(35)]: Correct, 1 mark, alternatively they can bring analogous claims under other US or 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?

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Interlocutory orders are orders which do not resolve all aspects of a disputed issue, and final orders are orders which, conversely, deal with all issues without leaving anything pending or undecided. The latter includes orders resolving discrete disputes, and this classification is separate from the constitutional and jurisdictional sorting of final orders explored in question 3.1 above.

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

Unless the bankruptcy court certifies that the appeal involves a question of law on which the US Supreme Court offers no precedent or an immediate appeal would be necessary to materially progress the case (in which case the court of appeals may decide to directly hear an appeal), final orders may be appealed of right by the relevant litigants and/or other adversely affected parties, whereas interlocutory orders may only be appealed with leave of the appropriate appellate court (being, depending on the circuit, either the relevant district court or a Bankruptcy Appellate Panel formed of judges from the bankruptcy courts in the relevant circuit).

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Commented [H(40)]: Correct, 1/2 mark

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Commented [H(42)]: Correct, 1 mark

Once the above appellate courts have heard the appeal and issued a ruling, this can be further appealed of right to the circuit court of appeals.

Question 3.4 (5 marks)

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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 of Delaware corporations owe a duty of loyalty to the corporation's best interests and a duty of care in educated decision-making. As confirmed in *North Am Catholic Educational Programming Foundation, Inc v Gheewalla*, these duties are owed, at all times, to the corporation and to the corporation's shareholders. It is not relevant, for the purpose of the duties, that the corporation is insolvent or approaching insolvency. As a result, the concept of wrongful trading found in English insolvency law does not apply in connection to directors of a Delaware corporation (See *Trenwick Am Litig Trust v Ernst & Young, LLP*) and, unlike

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

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

directors of English companies, directors of Delaware corporations are not required to act in the best interests of the corporation's creditors after a corporation becomes insolvent.

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

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Question 4.1 [4 marks]

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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.

Because an English scheme of arrangement is "a collective judicial or administrative proceeding in a foreign country (...) 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" in accordance with 11 U.S. Code § 1520(a)(1), it is likely that such a scheme will be capable of being granted recognition under a US chapter 15 proceeding.

The issue is whether this recognition would be as a foreign main proceeding (in which case a number of provisions and relief methods found in the UBC would automatically apply upon recognition) or a foreign non-main proceeding (in which case the above-mentioned provisions and relief would be discretionary rather than automatic).

In order for the English scheme to be recognised as a foreign main proceeding, Gambling Corp would need to have its center of main interests ("COMI") in England. On the facts, there is a rebuttable presumption that Gambling Corp's COMI will be in Greece, as this is its jurisdiction of incorporation. In addition, Greece is also Gambling Corp's principal place of business – if this means that its headquarters, management and primary assets are in Greece, then this would further strengthen the presumption that its COMI is in Greece. In order to have more certainty, we would need to determine whether Gambling Corp's bondholders are able to ascertain its COMI through objective evidence. The identity of the bondholders and their location may also be a factor in establishing Gambling Corp's COMI, and it is also relevant that the bond instrument appears to be governed by English law.

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Although on balance, and on the facts available, it may be more likely that Gambling Corp's COMI is in Greece, if additional information rebutted that presumption and it was determined that Gambling Corp's COMI was in England, then the English proceeding could be a foreign main proceeding. If however it was established that Gambling Corp's COMI was in Greece, then the English proceeding may be recognised as a foreign non-main proceeding if the casinos and betting parlors which Gambling Corp operates in London generate non-transitory economic activity for Gambling Corp, since they would qualify as an establishment in England.

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Question 4.2 [5 marks]

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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?

Filing of a chapter 11 petition triggers the start of an automatic statutory stay under 11 U.S. Code § 362, for a duration of at least 120 days. This stay, however, is subject to certain exclusions and on the facts provided this means that:

- ShipCo's lawsuit, which represents litigation on a claim predating the chapter 11 petition, would be suspended during the stay;
- the US Department's of Justice investigation would be allowed to continue during the stay, as regulatory investigations are excepted from the statutory stay in accordance with 11 U.S. Code § 362(b);
- USA Bank would not be allowed to enforce the security it holds over the Oil Corp refinery; and
- Oil Corp's landlord could not evict oil Corp from its Texas premises as actions aimed as obtaining possession of the property Oil Corp's estate are prohibited – although the landlord would be allowed to evict Oil Corp if the lease of the premises had expired, which does not appear to be the case here.

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

Commented [H(58)]: Correct, 1 mark

Commented [H(59)]: Correct, 1 mark

Commented [H(60)]: Correct, 1 mark

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?

A 363 sale under 11 U.S. Code § 363 broadly enables a debtor to deal with, sell or otherwise dispose of its property free from creditor interests and (in some cases) without the need for creditor consent to the disposal. It is relevant to note that this will only be the case where debtors can show that the disposal is in accordance with the debtor's business judgment, taking into account the interests of its creditors, and in the best interests of the debtor's estate. Assuming that this is the case, on the facts:

- here, although 11 U.S. Code § 365(a) and (e) allows debtors to assume and assign certain agreements even if the right to do so is contractually restricted or excluded, this probably would not apply to the "Interconnect" trademark license. Although we would need to examine the terms of the agreement to be certain, this is because, in accordance with 11 U.S. Code § 365(c), the trademark license is subject to non-bankruptcy law under which it is likely that Plastic Corp cannot be forced to accept performance of the licensing agreement from the potential transferee. Plastic Corp's consent would therefore be required before Oil Corp could assume and transfer its rights in the trademark license.

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Commented [H(63)]: Correct, 1 mark

- the patent licenses for plastic manufacturing, conversely, relate to rights granted to Plastic Corp in connection with patents owned by Oil Corp. Under 11 U.S. Code § 365(n), Oil Corp would not be allowed to reject these licenses without the prior consent of Plastic Corp;
- we do not know the value of the Dallas manufacturing facility, however if we assume that this is below the value of USA Bank's USD 500,000,000 interest then the premises can be sold by Oil Corp free and clear of USA Bank's lien (in accordance with 11 U.S. Code § 363(f)) without USA Bank's consent – although leave of the bankruptcy court will be necessary. If the sale is conducted via an auction, then it is open to USA Bank to "credit bid" and only pay, as the purchase price, an amount equivalent to the difference between USD 500,000,000 and the sale price of the property.

Commented [H(64)]: Partially correct, 1 mark, Oil Corp could reject the license but Plastic Corp could continue to practice the patent at its option

Commented [H(65)]: This is reversed, the consent is not needed if the value of the property is above the amount of the lien, and the lien will then attach to the proceeds

*** End of Assessment ***