



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 38.5/50

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

Commented [H(2)]: Total marks 9/10

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

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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

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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 6/10

Question 2.1 (2 marks)

Commented [H(14)]: Total marks 1/2

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

A voluntary petition requires no allegation of insolvency, whereas an involuntary petition requires the petitioner to allege that the debtor is unable to pay its debts as and when they fall due or that a custodian has been appointed or has taken possession within the last 120 days, with the exception of Receivers, Trustees or agents appointed over less than substantially all of the property of the Company.

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Commented [H(16)]: Partially correct, 1/2 mark, also an involuntary petition is filed by creditors

Question 2.2 (2 marks)

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

Violating the automatic stay is considered contempt of court. Such a violation may result in the court enforcing that a creditor becomes responsible for the debtors' legal costs and take affirmative actions to undo the effects of its violation of the automatic stay. If the court is concerned a violator will not act promptly to rectify the violation they can impose a coercive sanction such as a daily fine paid to the court until the issue is resolved.

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Commented [H(19)]: Also the act is void or voidable depending on the circuit

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?

A claim is considered impaired where the claimants legal, equitable or contractual rights are altered by the imposition of the restructuring plan.

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A holder of an impaired claim may not be entitled to vote on a restructuring plan where they are a dissenting creditor holding out on voting for plan if they are part of a class of creditors that are subject to a cramdown. If all of the requirements of confirmation are met and one other class of impaired creditors approves the plan then the plan is considered accepted and is imposed on the dissenting impaired creditors without their vote.

Commented [H(22): A holder of an impaired claim that will receive nothing under a plan is not entitled to vote and is deemed to reject.

Question 2.4 (3 marks)

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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?

Preference as a cause for action would only apply where the debtor is paying for a pre-existing debt. Non-bankruptcy law is applicable for the determining of when a debt arose and when a transfer of interest in the debtors property took place. If the date of transfer is delayed then it may move the date of transfer into the preference period. Additionally, if the transfer does not take place before the petition date then it is subject to the automatic stay and the transfer cannot be perfected.

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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?

Preference as a cause for action would apply if the transfer was made in the 90 days prior to the petition date as the debtor is deemed insolvent at this time. A creditor can rebut this assumption, however, the ultimate burden of proof is on the debtor to evidence that they were balance sheet solvent at the time of the transfer.

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

Actual Fraudulent conveyance as a cause for action would apply where it is proven that the debtor made a transfer with the actual intent to hinder, delay or defraud any entities to which the debtor is or may become indebted to.

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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?

Stern v Marshall found that even in core proceedings the bankruptcy court does not have jurisdiction to issue final orders that impact Article III jurisdiction. The Supreme Court found that in *Stern v Marshall* the bankruptcy court's issuance of final order over a state law claim was unconstitutional and therefore the outcome of the state law claim was the first and final judgement. Further guidance has since been provided for similar fact patterns to the above which set out that the bankruptcy court may provide a recommendations report to the district courts for review in advance of the district court issuing its final orders.

Commented [H(29): Correct, 1 mark, whereas previously jurisdiction had been understood to depend on the core / non-core distinction and a bankruptcy court can now enter a final order on a challenge to a petition or on a core matter with consent of the parties

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?

Chapter 15 proceedings do not provide for foreign representatives to invoke the avoidance powers of the bankruptcy code which are granted under chapter 7 and chapter 11 codes. Foreign representatives can obtain equivalent relief by seeking to avoid pre-petition transactions under other applicable US and foreign laws as is consistent with practices under section 304 of the bankruptcy code pre-dating chapter 15. Additionally, a foreign representative may open its own concurrent plenary proceeding in chapter 7 or 11 to obtain the avoidance powers not granted under chapter 15 though this is rare.

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

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?

An interlocutory order only resolves some issues or claims, whereas, a final order resolves and disposes of all issues leaving nothing further to be decided. Final orders may be appealed as a right whereas interlocutory orders can only be appealed with the leave of the appellate court.

This is the same framework in bankruptcy proceedings, however, any order that extends the period of exclusivity is appealable as a right and does not need leave of any court.

In general appeals are heard by the district court, however, in certain circuits bankruptcy appeals may be heard by a bankruptcy appeal panel. A further right of appeal, if the initial order allowed for a right of appeal, to the circuit court of appeals and in rare circumstances an appeal may go directly to the court of appeals.

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

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

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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 a duty of loyalty to the Company and its shareholders best interests and a duty of care and educated decision making. Directors are protected by the business judgement rule from any liability stemming from errors of judgement in carrying out their duties. There is no fiduciary duty of a director to the company's creditors. Therefore, there is no such concept of wrongful trading or furthering insolvency.

Per the business judgement rule, directors are assumed to have acted in good faith unless it can be proved that the board were not reasonably informed, were not honest in their belief that such a decision was in the company's best interests or were not acting in good faith. Additionally, the Company's bye laws may exculpate the directors from liability for breach of duty of care, but not a breach of the loyalty requirement. Further, the business judgement rule does not apply where a transaction involves personal interest from the majority of the board or where a controlling shareholder sits on both sides of the transaction.

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

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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.

English schemes of arrangement are able to be granted chapter 15 recognition. Chapter 15 recognition is available to foreign representatives and proceedings so long as foreign representative can establish that a court or administrative proceeding regarding a debtor is pending and that the foreign representative is empowered to act by that proceeding.

In this case a scheme of arrangement is a proceeding codified in English law and would therefore meet the threshold set by the Chapter 15 recognition requirement.

One issue that may prove contentious is whether the chapter 15 recognition of the foreign proceeding is that of a main or non-main proceeding and therefore the scope of relief available.

In order to be considered a main proceeding, the proceeding must have been commenced in the debtors center of main interest ("COMI"). In the case study above, Greece could be considered the COMI of the Company as the place of registration and principal place of business. However, its primary assets, being casinos, are in other countries not just Greece including the UK. Additionally, the principal debts in question are governed by UK law which is likely where the majority of disputes in respect of the debt will be heard, it is not clear where the creditors of these bonds reside.

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Commented [H(50)]: Correct, 1 mark, this is the more likely outcome of the analysis

Commented [H(51)]: The London casino would qualify as an establishment for foreign non-main recognition

In this case, given the Company has a primary asset in the UK and is also dealing with bonds governed by UK law, it is likely that the US courts would give consideration to the UK as being the COMI and provide chapter 15 relief as a foreign proceeding.

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?

Oil Corp filing a petition for a chapter 11 proceeding would have differing effects on each of the scenarios, set out below are the potential effects of each.

1. The contaminated oil may be considered litigation of a pre-appointment claim for breach of contract in which case the automatic stay would apply, and the creditors action would be prohibited from continuing by the petition. However, as this is oil it may also be considered a commodity contract in which case the creditor can continue to exercise its rights under the contract, if the contract includes breach of contract remedies such as arbitration, then the creditor could continue to enforce the breach of contract remedies against the debtor.
2. The US department of justice is investigating the illegal purchase of oil from countries subject to sanctions. In this scenario, the automatic stay granted by the chapter 11 petition would not apply. Criminal proceedings are exceptions to the stay and would be allowed to continue.
3. The automatic stay is global and applies to any property of the estate in the world. Therefore, USA Bank would not be able to foreclose on the oil refinery in the Philippines as any act to obtain possession or control of property of the estate is protected by the stay.
4. The automatic stay would apply in this scenario, the landlord would therefore not be able to continue its proceeding to evict Oil Corp. were the lease to have expired then the eviction could continue, however, there is no detail of the lease having expired in the case study.

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Commented [H(54)]: Incorrect, the commodity contract exception generally is for delivery of commodities or closing out derivatives

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Commented [H(56)]: Correct, 1 mark

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

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

Question 4.3 [6 marks]

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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?

Oil Corp's approach to achieve highest possible returns for the plastic manufacturing business requires consideration around the interplay of executory contracts and section 363 sales. Set out below is an assessment of each of Oil Corps goals

1. Oil Corp would like to assume and assign the contract. This goal comes down to whether this contract is considered executory and whether the contract is assignable to meet the standard of either the hypothetical test or the actual test. At first glance, the contract would be considered executory as both the debtor and Plastic Corp have underperformed obligations as the license has not reached its expiry date and therefore Plastic Corp are obliged to continue to license the trademark and Oil Corp is still required to service the license fees. Separately, however, as a trademark is a piece of intellectual property Plastic Corp cannot be compelled to accept performance from an assignee of the contract. The contract may therefore not be considered executory is Plastic Corp were to refuse to accept performance from the assignee. Given Oil Corp are considering rejecting the patent

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Commented [H(61)]: Not quite correct, the contract is still executory, this is just an exception to the ability to assume / assign them

licenses that Plastic Corp benefits from, Plastic Corp may try to frustrate the sale goals of Oil Corp by such refusal, in which case on a hypothetical test the contract would not be executory. Therefore, Oil Corp would need Plastic Corps approval.

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2. Similarly with goal 1 above, Oil Corps licensing of its patents to Plastic Corp would be considered an executory contract as both parties have unfulfilled obligations given the contract has not reached its expiry date, Oil Corp must continue to provide the license and Plastic Corp must continue to pay. In this scenario Oil Corp would be entitled to reject the contract at which point Oil Corp are deemed to have breached the contract giving Plastic Corp an unsecured pre-petition claim in damages. This would allow the patent assets to vest in the debtors estate for onward sale. Therefore, Oil Corp does not need Plastic Corps approval.

Commented [H(63)]: Incorrect, 365(n) lets Plastic Corp continue to exercise its rights under the license and therefore exclusivity for the transferee is not possible without Plastic Corp's consent

3. Under a 363 sale, Oil Corp would be able to sell the property in Dallas without the lien. A 363 sale allows for the debtor to sell the asset with free and clear title. In this scenario, as a sale of a manufacturing plant is unlikely to be a normal course of business transaction, Oil Corp will need to demonstrate that the sale of the property is in its best business judgement in line with its fiduciary duty to the best interest of its creditors. If the sale of the manufacturing plant was made as a grouped sale with the patents and licenses, then Oil Corp may achieve a good result for its creditors as a premium would be payable by any purchaser. Without the added benefit of the trademark, they may achieve a lower sum than would demonstrate it is in the best interests of creditors given it is a specialized facility it may not attract competing bids. Plastic Corp would be able to make this sale without the USA Bank approval, though USA Bank would be the first beneficiary of the sale proceeds of this particular asset.

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*** End of Assessment ***