



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 3B
THE INSOLVENCY SYSTEM OF THE UNITED KINGDOM
(ENGLAND AND WALES)

This is the **summative (formal) assessment** for **Module 3B** 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 3B. 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.assessment3B]**. An example would be something along the following lines: 20222-514.assessment3B. **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 3B 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 3B 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 **7 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

Please select the **most correct ending** to the following statement:

The Administration (Restrictions on Disposal etc to Connected Persons) Regulations 2021 restrict pre-pack sales which constitute a substantial disposal of the company's property to connected parties where the disposal occurs:

- (a) within 10 weeks of the commencement of the administration.
- (b) within 8 weeks of the commencement of the administration.**
- (c) within 4 weeks of the commencement of the administration.
- (d) on the day the company enters administration.

Question 1.2

What is the **maximum length** of a Moratorium under Part 1A of the Insolvency Act 1986 to which creditors can consent without any application to the court?

- (a) 40 business days.
- (b) One year and 20 business days.
- (c) One year and 40 business days.
- (d) One year.**

Question 1.3

Which of the following **is not** a requirement for a company that wishes to enter into a Restructuring Plan under Part 26A of the Companies Act 2006?

- (a) The company has encountered, or is likely to encounter, financial difficulties that are affecting, or will or may affect, its ability to carry on business as a going concern.
- (b) A compromise or arrangement is proposed between the company and its creditors, or any class of them, or its members, or any class of them.

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Well Done!

Commented [DJ2]: 10 out of 10

(c) The purpose of the compromise or arrangement is to eliminate, reduce or prevent, or mitigate the effect of, any of the said financial difficulties.

(d) The company is, or is likely to become, unable to pay their debts, as defined under section 123 of the Insolvency Act 1986.

Question 1.4

In cases where the Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021 apply and an independent report from an Evaluator is obtained, the independent report must be obtained by whom?

- (a) The administrator.
- (b) Any secured creditor with the benefit of a qualifying floating charge.
- (c) The purchaser.
- (d) The company's auditor.

Question 1.5

Which one of the following **is not** a debtor-in-possession procedure?

- (a) Administration.
- (b) Restructuring Plan.
- (c) Scheme of Arrangement.
- (d) Company Voluntary Arrangement.

Question 1.6

A liquidator may pay dividends to small value creditors based upon the information contained within the company's statement of affairs or accounting records. In such circumstances, a creditor is deemed to have proved for the purposes of determination and payment of a dividend where the debt is **no greater than how much?**

- (a) £500
- (b) £750
- (c) £1,000
- (d) £2,000

Question 1.7

Which one of the following **is not**, in itself, a separate ground for disqualification of a director under the Company Directors Disqualification Act 1986?

- (a) Wrongful trading.
- (b) Breach of fiduciary duty.

- (c) Being found guilty of an indictable offence in Great Britain.
- (d) Being found guilty of an indictable offence overseas.

Question 1.8

The administrator is under a general duty to provide a statement for creditors' consideration setting out proposals for achieving the purpose of administration. He or she must obtain a creditors' decision on whether or not to approve the proposals **within how many weeks** of the date the company entered administration?

- (a) 6
- (b) 8
- (c) 10**
- (d) 12

Question 1.9

Which of the following statements is **incorrect**?

- (a) An insolvency officeholder from an EU Member State will be automatically recognised by the courts in the UK whether the officeholder was appointed before or after Brexit.**
- (b) An insolvency officeholder from an EU Member State is automatically recognised by the courts in the UK if appointed before Brexit.
- (c) An insolvency officeholder from an EU Member State appointed after Brexit may apply to a UK court for recognition under the Cross Border Insolvency Regulations.
- (d) An insolvency officeholder from an EU Member State cannot apply to a UK court for recognition under section 426 of the Insolvency Act 1986.

Question 1.10

Under section 216 of the Insolvency Act 1986, a director of a company which has been wound up insolvent may not, unless an exception applies, be a director of a company that is known by a prohibited name **for what period of time**?

- (a) 6 months.
- (b) 12 months.
- (c) 2 years.
- (d) 5 years.**

QUESTION 2 (direct questions) [10 marks]

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Question 2.1 [maximum 5 marks]

Who may bring an action under: (i) section 423 of the Insolvency Act 1986; (ii) section 6 of the Company Directors Disqualification Act 1986; and (iii) section 246ZB of the Insolvency Act 1986?

Following are the parties who have the right to bring action

1. Section 423 of the Insolvency Act 1986
 - A. Where the company is being wound up or is in administration
 - a) the official receiver
 - b) the liquidator
 - c) the administrator
 - d) the victim (with leave of the court)
 - B. Where the victim is bound by CVA
 - a) the supervisor of the CVA
 - b) any victim of the transaction (whether bound by CA or not)
 - C. In any other case, victim of the transaction
2. Section 6 of the Company Directors Disqualification Act 1986
 - a) the official receiver
 - b) the liquidator
 - c) the administrator
 - d) the secretary of state
3. Section 246ZB of the Insolvency Act 1986
 - e) The administrator of the company which is into administration

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Question 2.2 [maximum 5 marks]

List the **five (5)** qualifying decision procedures by which creditors may make decisions in the context of an insolvent company.

Following are the qualifying decision procedures (Insolvency Rules 2016, Section 15.3) by which creditors may make decisions in the context of an insolvent company.

1. Correspondence
2. Electronic voting
3. Virtual meetings
4. Physical meeting
5. Any other decision-making procedure which enables all creditors who are entitled to participate in the making of the decision to participate equally.

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

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Question 3.1 [maximum 6 marks]

Can an administrator who wishes to continue to operate the business of the company in administration require suppliers of goods and services to continue to supply those goods and services during the administration?

Section 233B prevents suppliers from terminating a supply upon the company's insolvency. It also prevents suppliers from making it a condition for continued supply that pre-insolvency

arrears are paid and from making other changes to the contract such as increasing the prices. Section 233B also disallows any clause which allows the supplier of goods or services to terminate or “do any other thing” in relation to the contract if the company enters a formal insolvency procedure.

Similarly, section 233 prevents essential suppliers from terminating a supply upon the company’s insolvency. Essential suppliers include supply of gas, electricity, water, and communication services. However, section 233 permits essential suppliers to stipulate that the administrator must personally guarantee payment of charges in respect to the supply (excluding past arrears).

Section 233A disallows essential suppliers from having any clause in contracts which allows the supplier to terminate or alter contract in case of company enters any insolvency procedure.

Considering all of the above, an administrator who wishes to continue to operate the business of the company in administration may be able to force suppliers of goods and services to continue to supply those goods and services during the administration. Under section 233B, suppliers may terminate the contract only with the consent of the company or office holder including administrator or court.

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Question 3.2 [maximum 9 marks]

Explain the order of priority of payments in a liquidation and explain the nature of the rights enjoyed by each class of creditor or expense.

Liquidator may only realize assets which belong to the company. In case of assets subject to receivable financiers, hire purchase agreements and retention of title contracts liquidator has no rights on such assets as they do not belong to the company.

Additionally, fixed charge secured creditors will usually enforce their security outside of any formal insolvency process including liquidation.

Thus, the remaining class of creditors/expenses to be paid through the liquidation process in the priorities stated below.

1. Winding-up expenses

Section 115 of the Act gives priority to number of expenses (related to liquidation process) over the preferential creditors, floating charge holders and unsecured creditors. Following are the main expenses which are payable in priority to those creditors and are payable in the following order of priority –

- a) Expenses related to preserving, realizing or getting in any assets of the company (including legal costs)
- b) Cost of any security provided by the liquidator
- c) Amount payable to a person in preparation of statement of accounts
- d) Any disbursement by liquidator in course of winding up (such as expenses by liquidation committee)
- e) Remuneration of any person employed by liquidator to person any services for the company
- f) Remuneration of liquidator as approved by creditors
- g) Any corporation tax on chargeable gains accruing on the realization of assets of the company
- h) Any other expense incurred by liquidator in carrying out his function in liquidation.

2. Ordinary preferential creditors

All ordinary preferential creditors rank equal among themselves and will get equal proportion of monies. Following is the list of ordinary preferential creditors as per schedule 6 of Act.

- a) Sum owed on account of employees' contribution to occupational pension scheme deducted from earnings of the company's employees paid in the period of four months prior to commencement of winding up.
- b) Sum owed on account of employer's contribution to occupational pension scheme in the period of 12 months before the relevant date.
- c) Employee remuneration for a period of 4 months prior to commencement of winding up with maximum at GBP 800.
- d) Employee remuneration due to accrued holiday or absence of work through sickness or other good cause for any period of employment before the winding up.
- e) Claims for monies (debt taken for) used to pay wages or holiday remuneration
- f) Levies on production of coal and steel as per article 49/50 of European coal and steel community treaty
- g) Claims under Reserve Forces (Safeguard of employment) Act 1985 and in relation to default of any order made under the said Act.
- h) Amount owed due to eligible deposit as does not exceed the compensation that would be payable in respect of the deposit under the Financial Services Compensation Scheme.

3. Secondary preferential creditors

These creditors are eligible to be paid only after the ordinary preferential creditors. Following is the list of ordinary preferential creditors as per schedule 6 of Act.

- a) Amount owed due to eligible deposit that exceed the compensation that would be payable in respect of the deposit under the Financial Services Compensation Scheme.
- b) Amount owed due to deposit that
 - I. Was made through a non-UK branch of credit institution
 - II. Would have been eligible if the deposit was made through UK branch of the credit institution
- c) PAYE income tax deductions, national insurance deductions, VAT payments, construction industry scheme deductions and student loan repayments.

4. Floating charge holders

Floating charge holders may choose to enforce its charge by appointing an administrator which will prevent liquidator to be appointed until administration is complete. In liquidation, after preferential creditors, floating charge holders are next to be paid. In case of multiple floating charge holders, the one that created charge earlier has priority.

Liquidator is required to deduct a "prescribed part" as per section 176A (if applicable) before making payment to floating charge holders. Section 176A is applicable to company with floating charge created on or after 15th September 2003 and the company gone into liquidation. The prescribed part of the net property (amount available post deductions of winding up expense and preferential claims) is made available for payment to the unsecured creditors

The calculation of prescribed part is as follows

1. In case of net property < GBP 10,000 then prescribed part is 50% of net property unless liquidator believes that distribution to unsecured creditors would be disproportionate to the benefit.
2. In case of net property > GBP 10,000 then prescribed part is 50% of first GBP 10,000 and 20% of excess over GBP 10,000

Floating charge holders or secured charge holders who may have outstanding unsecured balance is not permitted to participate in prescribed part.

5. Unsecured creditors

Unsecured creditors are paid last in the statutory order.

6. Shareholders/member of company

If there are sufficient funds post payment of all creditors, then surplus can be distributed to shareholders of the companies.

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

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Prior to going into compulsory liquidation on 23rd December 2021, under pressure from its bank, Stercus Bank plc, and in order to prevent it from demanding repayment of the company's loans, Corfee Zero Limited ("the Company"), granted a debenture in favour of Stercus Bank plc in February 2021. The debenture contained a floating charge over the whole of the Company's undertaking.

The winding up order followed a creditor's winding up petition issued on 14th October 2021.

In July 2021, as the Company continued to suffer cash flow problems, the directors approved the sale of 5 coffee roasting machines to Ann Young (a director) for £10,000 in cash. The machines had been bought for £25,000 a year before.

A month before the winding up order was made, Ann Young received an email from Beans and Leaves Ltd, one of the Company's key suppliers. The supplier demanded immediate payment of all sums owing to it and informed the Company that further supplies would only be made on a cash on delivery basis. As the continued supply of coffee beans was seen as essential by the Company, the board authorised a payment of £8,000 to cover existing liabilities and agreed to further payments, on a cash on delivery basis, for further supplies which amounted to further payment of £3,000 up to the date of the winding up order.

The liquidator has asked for advice whether any action may be taken in respect of the floating charge in favour of Stercus Bank plc and the two subsequent transactions.

Using the facts above, answer the questions that follow.

Identify the relevant issues and statutory provisions and consider whether the liquidator may take any action in relation to:

Question 4.1 [maximum 5 marks]

The floating charge in favour of Stercus Bank plc;

Section 245 of Act i.e. Avoidance of certain floating charges is applicable. The section states that a floating charge created for no consideration up to 12 months before insolvency proceedings is invalid and can be set aside. The period is extended to two years if the floating charge holder is connected to the company.

In this case, Corfee Zero Limited created the floating charge in favor of Stercus Bank plc in February 2021. This is 8 months before the initiation of winding up petition (in October 2021).

This falls within the relevant period of 12 months (for non-connected party) before insolvency proceedings.

Stercus Bank did not provide any new money/funding in consideration for the floating charge. Moreover, it seems like Corfee Zero Limited was already facing insolvency when the charge was created. This aspect will need to be investigated further by the liquidator but considering the company was worried on repaying Stercus Bank points to an insolvency position.

Considering all of the above the liquidator can take appropriate actions to invalidate the floating charge created in favor of Stercus Bank. However, Stercus Bank will continue to have a valid claim in the liquidation proceedings.

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Question 4.2 [maximum 6 marks]

The sale of the coffee roasting machines; and

Section 127 - Avoidance of property dispositions

This section avoids any disposition of property of the company once the commencement of winding up, unless the court otherwise orders. The commencement date will be the date of the presentation of the petition to wind up.

In this case, the winding up petition was made in October 2021 while the coffee roasting machine was disposed in July 2021 i.e. before the winding up commencement. Hence this section is not applicable.

Section 238 – Undervalue Transaction

A transaction is at an undervalue if:

1. it is entered into by a company for no consideration or for consideration significantly less than market value; and
2. it is entered into within two years before the onset of insolvency
3. the time at which such transaction takes place, the company was insolvent or went into insolvency due to the transaction. However, for connected parties it is presumed that the company was insolvent.

In this case, the transaction is with the director of the company which falls within the connected party definition. The transaction took place 3 months prior to the insolvency commencement date and hence within the relevant period of 2 years.

While the market value of new machine is GBP 25,000 while the sale happened at GBP 10,000, the liquidator needs to find out what is the value of the used machines. Thus, the liquidator will be able to initiate action on this transaction under Section 238.

There is a defense to a claim to set aside a transaction at an undervalue if it can be shown that:

1. the company entered into the transaction in good faith for the purpose of carrying on its business; and
2. at the time it did so, there were reasonable grounds for believing that the transaction would benefit the company.

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What would the remedies be?

Commented [JL12]: Facts?

Section 423 -- Transactions defrauding creditors

Transactions at an undervalue entered into for the purpose of putting assets beyond creditors' reach or otherwise prejudicing their interests can be set aside. There is no need to show that the transaction took place in a set time period before the onset of insolvency or that the company was insolvent at the time of the transaction. Thus, liquidator can bring action against the director under section 423 in case the transaction is proved to be undervalue.

Section 239 – Preference

A transaction can be characterized as a preference if it puts a creditor, surety or guarantor in a better position on insolvency than it would otherwise have held. It must also be shown that the company was influenced by a desire to prefer the party to the transaction. The preference must occur within a "relevant time". This is six months prior to the onset of insolvency, or two years prior if the preference is given to someone connected with the company.

This section is cannot be applied as it does not look like any preference was given to the director.

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Question 4.3 [maximum 4 marks]

The payments to Beans and Leaves Ltd.

Section 127 - Avoidance of property dispositions

This section avoids any disposition of property of the company once the commencement of winding up, unless the court otherwise orders. The commencement date will be the date of the presentation of the petition to windup.

The court has the power to declare that the dispositions shall not be void. The court will consider the following general guidelines to decide on disposition

1. Transaction can be allowed unless it gives preference to any per-liquidation creditor over the other creditor.
2. Payments can be allowed to ensure continues supplies to company, enable company to continue operations and is in best interest of creditors
3. Transactions can be allowed if it does not diminish the net assets of the company
4. Transactions can be allowed if done in good faith and ordinary course of business
5. Cash of delivery can be allowed if it ensure future supplies and enable business to continue
6. Court may also authorize general continuance of trade.

In this particular case, Beans and Leaves Ltd is a key supplier and continued supply of coffee beans is essential to the company's continued operations. Company's continues operations is beneficial to the creditors as it might result in better value in liquidation. Continued operations also ensure against reduction in net assets of the company.

Considering all of the above, the court is more likely to allow all the transactions with Beans and Leaves Ltd.

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*** End of Assessment ***