



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.

Commented [DJ1]: TOTAL: 43 OUT OF 50
Well Done!

Commented [DJ2]: 9 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.

Commented [DJ3]: b

- (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?

- (i) Section 423 concerns transactions that defraud creditors. If the company is being wound up, the administrator, official receiver, and the liquidator can bring the action. In a CVA, the supervisor can bring the action. The victim can also bring the action if the company is being wound up or in a CVA, but may require the leave of the Court.
- (ii) The secretary of state can take action under section 6 to seek to disqualify the directors from being involved in the management of a company.
- (iii) Section s46ZB concerns wrongful trading and is an action that an administrator can take when a company is in administration.

Commented [DJ5]: 5

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.

- (a) Correspondence;
- (b) Electronic voting;
- (c) Virtual meeting;
- (d) Physical meeting; or
- (e) 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]

Commented [DJ7]: 11 out of 15

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?

The administrator can require suppliers of certain essential supplies (including gas, water, electricity, and communications services) to continue to supply the services during the insolvency under s233 and s233A of the Insolvency Act 1986 ("the Act"). The supplier is not able to require the payment of outstanding debts to continue supply. Under s233A, the supplier is unable to rely on an insolvency related term in a contract to terminate or alter the terms of supply.

Commented [JL8]: Personal guarantee?

The Act was further revised by s233B, which restricts the actions a supplier of goods and services can take when the company enters insolvency proceedings. The supplier can no longer terminate the contract, do any other thing, or demand outstanding debts be paid, because of the company entering an insolvency proceeding. Certain suppliers (mostly suppliers of financial services) are not subject to s233B.

Commented [JL9]: To which supplies does this section apply?

Accordingly, depending on who the supplier is, the Administrator will typically be able to insist the supplier continues to supply them and restricts the ability of the supplier to alter those terms of supply.

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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.

1. **Creditors with a fixed charge.** These assets are not available to general creditors and sit outside the liquidation. However, the charge holder may allow the liquidator to deal with these assets and the proceeds will be paid to the fixed charged holder. However, creditors with fixed charged securities can enforce their security without the need for a formal insolvency process.
2. **Expenses of winding up.** The fees and expense incurred in administering the liquidation, which include the liquidators' remuneration, are paid in priority to preferential creditors, holders of floating charges and other creditors.
3. **Preferential creditors.** After the fees and expenses in administering the liquidation are paid, the net proceeds are to be made available to preferential creditors. Preferential creditors are mostly comprised on employees (for wages and salary, and pension claims) and tax liabilities due to HMRC. Ordinary preferential debts rank ahead of secondary preferential debts. Ordinary preferential debts primarily relate to amounts due to employees (including pension scheme contributions), but also include certain levies and deposits made with financial institutions. Secondary preferential debts include various tax deductions and certain categories of deposits made with financial institutions.
4. **Floating charge holders.** Any net proceeds available from assets subject to floating charges will be paid to the creditor that holds the floating charge, subject to the Liquidators' duty to make the 'prescribed part' of the net proceeds available to unsecured creditors.
5. **Unsecured creditors.** Unsecured creditors are paid out last, noting that the prescribed part deduction may be available for unsecured creditors from the floating charge.
6. **Shareholders.** Any surplus funds after paying all creditors are payable to shareholders.

Commented [JL11]: How is the prescriber part calculated?

Creditors that hold a qualifying floating charge are able to appoint an Administrator, so in the event a petition is made to Court to appoint a Liquidator, an Administrator could be appointed beforehand with the result the winding-up petition is suspended. In the event a CVA was proposed by the company during the course of the liquidation, the floating charge holder and fixed charge holders can vote on the CVA.

Unsecured and preferential creditors of the Company retain various rights which are exercised by decision procedures. These include the ability to form a liquidation committee and, depending on how the liquidator was appointed, vote on the appointment of a liquidator (by appointment an alternative liquidator), and determine how the liquidator is to be remunerated.

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

Commented [DJ13]: 13 out of 15

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;

Under s245 of the Act, a Liquidator may seek to invalidate a floating charge if:

- they were given by the company at a relevant time;
- no new consideration was provided for the charge; and
- at the time of the transaction the company was either unable to pay its debts or became unable to do so as a result of the transaction.

Stercus Bank plc ("Stercus") is not connected with the company, so the relevant time is 12 months prior to insolvency. The charge was created within 12 months of the date of liquidation. It appears that at the time of insolvency, the company may not have been able to pay its due debts as it was under pressure from Stercus and the company wanted to avoid a demand for repayment, presumably because it could not have repaid the balance. However, further information is required to confirm whether the evidence supports this finding. It appears that no new consideration was provided through the transaction, but further evidence would be required to confirm this. Overall, it appears that there is a reasonable possibility that the charge could be invalidated. However, this would only invalidate the charge, the underlying debt between Stercus and the company would remain claimable as an unsecured creditor in the liquidation.

Another potential avenue is to consider whether the transaction results in a preference towards Stercus under section 239 of the Act. The key consideration here is whether in granting the charge, the company was influenced by a desire to prefer Stercus. In the case of *Re MC Bacon Ltd* [1990] BCC 78, the Court dealt with a similar factual scenario and considered that the charge was granted to avoid the calling in of facilities and to enable continued trading and, therefore, not by a desire to prefer that party. Accordingly, it is unlikely the granting of the charge could be attacked as a preference.

Commented [DJ14]: 5

Question 4.2 [maximum 6 marks]

The sale of the coffee roasting machines; and

Under section 238 of the Act, the liquidators may take action in respect of a transaction at an undervalue. The liquidator must prove:

- The transaction occurred within two years prior to the commencement of the liquidation;
- At the time of the transaction, the consideration paid to the company was less than the value of the consideration provided by the company; and
- At the time the transaction was entered into, the company was unable to pay its debts as they fell due, or became unable to pay its due debts because of the transaction.

The transaction occurred within two years of the liquidation and, on the face of it, the consideration paid by the director to the company was less than the value received by the director. Accordingly, two of the limbs appear to have been met.

As the transaction was with a connected person (a director), the company is presumed to have been insolvent at the time of the transaction. In any event, the sale was undertaken due to cash flow problems with the company, which indicates the company may have been unable to pay its due debts.

In order to proceed further with this action, further analysis should be undertaken to confirm the value of the coffee machines at the time of the transaction and to prove the company was unable to pay its due debts.

The director could try to avoid the transaction being attacked by proving the transaction was entered into in good faith, for the purpose of carrying on its business, and there were reasonable grounds for believing the transaction would benefit the company. Given the circumstances of the transaction, being a transaction with a connected party when it was experiencing cash flow challenges, this would be difficult to prove.

If the liquidator can prove this was a transaction at an undervalue, the court can make an order to restore the company to the position it would have been if the transaction had not occurred. This would allow the company benefit from the difference in value between what it received compared to what was transferred.

The liquidator may also want to consider the purpose of the transaction as to whether it was undertaken to provide liquidity to the company, or whether it was undertaken to remove assets from the reach of creditors. If it is the latter, then it may be attacked as a transaction to defraud creditors under section 423 of the Act.

Commented [DJ15]: Remedies?
5

Question 4.3 [maximum 4 marks]

The payments to Beans and Leaves Ltd.

Transactions which have the effect of giving a preference to a creditor a potentially avoidable under s239 of the Act. In order to avoid the transaction, the liquidator needs to prove:

- The transaction occurred within the relevant time, in this instance six months prior to insolvency;
- The person who was preferred was a creditor at the time of the transaction;
- The person received more, or was put in a better position, than they would be in the liquidation; and
- In giving the preference, the company was influenced by a desire to prefer that person.

The transaction, being the repayment of the outstanding balance of £8,000, occurred one month prior to insolvency, so was within the relevant time. At this time, Beans and Leaves Ltd ("B&L") was a creditor of the company. The transaction with B&L resulted in full repayment of their outstanding liabilities. Assuming that there will be a shortfall to other creditors, then this transaction resulted in a preference. However, there is limited evidence to suggest the transaction was influenced by a desire to prefer B&L. The Company appears to have paid B&L the outstanding balance to enable continued supply. The Courts have held that where the company was influenced solely by commercial considerations around continuity of supply (as appears to be the case here), there will be no desire to prefer.

Accordingly, it appears this will be challenging to take an action for a preference against B&L.

Another avenue would be to investigate whether B&L was a connected party. If so, it will be presumed that the preference was influenced by a desire to prefer.

The transaction is potentially voidable under section 127 of the Act. Any dispositions made after the date of the winding up petition may be voided. Disposition includes any payment of money. In this context, the payment of the £8,000 to clear the outstanding debt and the further payments for cash on delivery could all be attacked.

The court can exercise its discretion not to void the disposition and make a validation order, where the transaction was in the ordinary course of business and entered into on a *bona fide* basis. In making this decision, the court would have regard to the following factors:

- The payment of the £8,000 to clear the outstanding debt gave a preference to B&L, whereas the payment of the £3,000 did not;
- The payments to B&L enabled the continued supply of coffee and trading for the business. The court would need to evaluate whether continued trading was in the best interests of the creditors;
- The transaction did not diminish the net assets, as a liability was cleared via the transaction;
- Whether B&L was aware of the winding-up petition will be a material factor;
- Some of the coffee supplies were made on a cash on delivery basis and supported ongoing trading.

This appears to be a strong avenue for the Liquidator to consider, particularly with respect to the payment of £8,000 to B&L.

Commented [JL16]: Not potentially – this is the applicable section!

Commented [DJ17]: 3 (failure to correctly identify the section)

*** End of Assessment ***