



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: 202223-336.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 "student number" 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 2023. The assessment submission portal will close at 23:00 (11 pm) GMT on 1 March 2023. 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 2023 or by 23:00 (11 pm) BST (GMT +1) on 31 July 2023. If you elect to submit by 1 March 2023, you may not**

submit the assessment again by 31 July 2023 (for example, in order to achieve a higher mark).

7. Prior to being populated with your answers, this assessment consists of 9 pages.

**ANSWER ALL THE QUESTIONS**

Commented [H(1): Total marks 39/50

**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

Which of the following entities does not satisfy the minimum presence requirement to be a debtor under any chapter of the Bankruptcy Code?

- (a) A foreign domiciled company that pays a US attorney a retainer.
- (b) A company with several US bank accounts, but no physical presence in the United States.
- (c) A company with US patents, but no physical presence in the United States.
- (d) All of the above satisfy the minimum requirement for presence in the United States.**
- (e) None of the above satisfy the minimum requirement for presence in the United States.

**Question 1.2**

Commented [H(4): Correct, 1 mark

ABC Corp is an industrial manufacturing company that is filing for bankruptcy. Which of the following could not be considered a party in interest?

- (a) A neighboring landowner to ABC Corp's manufacturing plant.
- (b) An environmental advocacy group that opposes ABC Corp's operations.**
- (c) The landlord of ABC Corp's corporate office.

- (d) *People who live several miles downstream from ABC Corp's manufacturing plant and have been exposed to the plant's toxic waste.*
- (e) *The US Internal Revenue Service.*

Question 1.3

Commented [H(5)]: Correct, 1 mark

*Which of the following contracts to which ABC Corp is a party is executory and may be assigned without counterparty consent?*

- (a) A lease on a manufacturing plant that contains a provision that requires landlord approval of any assignment.**
- (b) *An employment contract between ABC Corp and a former employee, requiring the company to provide health insurance through the end of the current year.*
- (c) *A 10-year software licensing agreement with XYZ Corp that is three years into performance.*
- (d) *A lease on office space that ended the prior year, but for which ABC Corp still owes past rent.*
- (e) *None of the above are executory and may be assigned without counterparty consent.*

Question 1.4

Commented [H(6)]: Correct, 1 mark

*Which of the following conditions must be true about a reorganization plan for a court to confirm it under Chapter 11 proceedings?*

- (a) *Have a possibility of success, even if it relies on speculative or improbable events to be capable of execution.*
- (b) The plan is not likely to be followed by liquidation.**
- (c) *All impaired classes must accept the plan.*
- (d) *All of the above.*
- (e) *None of the above.*

Question 1.5

Commented [H(7)]: Incorrect, the correct response is (e)

*Which of the following about cramdowns, is false?*

**(a) The plan of reorganization must be fair and equitable to all impaired classes.**

**(b) 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.**

**(c) Class definition is often a battleground when a debtor tries to cramdown classes.**

**(d) Dissenting creditors are permitted to challenge the classification of a creditor supporting the cramdown.**

**(e) If one insider creditor approves of the plan of reorganization, all other impaired classes may be crammed down.**

Question 1.6

Commented [H(8)]: Correct, 1 mark

Which of the following about 363 sales is false?

**(a) A good faith purchaser at a 363 sale may retain the property notwithstanding a subsequent reversal of court approval for the sale on appeal.**

**(b) The debtor in possession must establish that the transaction is in the best interests of the estate as a whole.**

**(c) In chapter 15 proceedings, a foreign court's approval alone suffices for a 363 sale.**

**(d) Debtors must carry out a robust marketing process for the sale.**

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

Question 1.7

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

Which of the following is true of both an actual fraudulent conveyance and a constructive fraudulent conveyance?

**(a) The debtor must have had an actual intent to hinder, delay, or defraud any entity to which the debtor was or became indebted.**

**(b) Both require at least circumstantial evidence of the fraudulent intent.**

**(c) The debtor must have been insolvent at the time of transaction.**

**(d) In addition to provisions in the Bankruptcy Code, the debtor or the trustee may invoke applicable state or foreign fraudulent conveyance laws.**

**(e) All of the above are true.**

Question 1.8

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

*When does an automatic stay come into effect?*

- (a) Immediately on the filing of any plenary petition.**
- (b) *On the filing of a voluntary petition but not on the filing of an involuntary petition.*
- (c) *Once the court reviews the petition and grants the stay.*
- (d) *Once the petitioner announces their intention to file for bankruptcy publicly.*
- (e) *Once a plan of reorganization is confirmed.*

Question 1.9

Commented [H(11)]: Correct, 1 mark

*Which of the following regarding substantive consolidation is true?*

- (a) *It respects the boundaries of corporate separateness.*
- (b) *It is the treatment of two or more creditors as a single creditor to simplify the claims process.*
- (c) If a creditor can show it extended credit on the basis of corporate separateness, it has a valid objection to substantive consolidation.**
- (d) *Substantive consolidation is commonly used to resolve bankruptcies of corporate groups.*
- (e) *Authority for substantive consolidation comes from the Bankruptcy Code.*

Question 1.10

Commented [H(12)]: Correct, 1 mark

*Which of the following are relevant factors in determining a debtor's center of main interests (COMI) in the recognition stage of a Chapter 15 bankruptcy case?*

- (a) *The location of the headquarters.*
- (b) *The location of primary assets.*
- (c) *The location of the majority of the affected creditors in the request for relief.*
- (d) *The jurisdiction whose law will apply to most disputes.*
- (e) All of the above.**

**QUESTION 2** (direct questions) [10 marks]

**Question 2.1** (1 mark)

**What is setoff and why is it not permitted in many circumstances?**

*Setoff is when a creditor and a debtor both have claims against each other; by setting off these amounts a net amount is determined. Setoff is not permitted in certain circumstances as it results in differential treatment of creditors with setoff rights and those without setoff rights.*

**Question 2.2** [2 marks]

**What rules should you review when preparing a filing for a bankruptcy court?**

*I would review the Federal Rules of Bankruptcy Procedure, the Federal Rules of Civil Procedure and the local rules of procedure of the relevant local court.*

**Question 2.3** [2 marks]

**What does the absolute priority rule require and when can it be deviated from?**

*The absolute priority rule requires that each senior ranking category of claims is paid in full before any subsequent ranking claim receives any payment. The rule does not apply in a cramdown as the shareholders can retain their equity without having repaid all creditors in full.*

**Question 2.4** [2 marks]

**What is a "priming lien" and what requirements must be met for such a lien to be granted to secure DIP financing?**

*A priming lien is security that is senior to or pari passu with a pre-petition lien. A priming lien is used to secure post-petition financing. As a condition to the grant of such lien, the interest of the existing secured creditor must be adequately protected (e.g. periodic cash payments or the provision of additional security).*

**Question 2.5** [3 marks]

**What is a preference? What are the elements of a preference claim that need to be proved? Is a showing of fault, by either the debtor or creditor, required?**

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

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

**Commented [H(15)]:** Correct, 1/2 mark

**Commented [H(16)]:** Correct, 1/2 mark

**Commented [H(17)]:** Total marks 1.5/2

**Commented [H(18)]:** Correct, 1/2 mark

**Commented [H(19)]:** Correct, 1/2 mark

**Commented [H(20)]:** Correct, 1/2 mark, you should also look at the judge's personal practices

**Commented [H(21)]:** Total marks 1/2

**Commented [H(22)]:** Correct, 1 mark

**Commented [H(23)]:** Incorrect, the rule may only be deviated from in a chapter 11 plan with the consent of the senior creditor

**Commented [H(24)]:** Total marks 1.5/2

**Commented [H(25)]:** Correct, 1 mark

**Commented [H(26)]:** Correct, 1/2 mark, also the financing must not be available without the priming lien

**Commented [H(27)]:** Total marks 3/3

A preference is a transfer of a debtor's property made during specified periods. The property must be returned to the state of the debtor if the value of the transferred property exceeds what the debtor would have received in a liquidation.

Commented [H(28)]: Correct, 1 mark

The criteria to claim a preference are: a transfer of an interest in the debtor's property; which is for the benefit of the relevant creditor; and is on account of a debt owed by the debtor and that existed before the transfer was made.

Commented [H(29)]: Correct, 1/2 mark

Commented [H(30)]: Correct, 1/2 mark

Commented [H(31)]: Correct, 1/2 mark

There is no need to show fault in establishing a preference claim.

Commented [H(32)]: Correct, 1/2 mark

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

Commented [H(33)]: Total marks 10.5/15

Question 3.1 [3 marks]

Commented [H(34)]: Total marks 0/3

Describe the circumstances in which a bankruptcy court may enter a final order, who reviews appeals from bankruptcy court orders and how are non-final orders reviewed?

A bankruptcy court may enter a final order in respect of a "core" bankruptcy issue and in respect of which there are no further issues to decide. Appeals are heard by the district court for the relevant district in which the bankruptcy court sits, although some jurisdictions have a Bankruptcy Appellate Panel. There is a further right of appeal to the circuit court of appeals.

Commented [H(35)]: Partially correct, 1/2 mark, this is only true if it is a challenge to the petition or the parties consent.

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

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

Non-final orders can be appealed with leave of the appellate court.

Commented [H(38)]: Orders that are not constitutionally final are treated as a report and recommendation / proposed findings of fact and conclusions of law

Question 3.2 [3 marks]

Commented [H(39)]: Total marks 3/3

What provisions of the Bankruptcy Code automatically apply to the debtor's property within the territorial jurisdiction of the United States upon recognition of a foreign main proceeding? What relief may be granted on a discretionary basis for either foreign main or non-main proceedings?

The provisions of the Bankruptcy Code that automatically apply within the US upon recognition of foreign main proceedings are: an automatic stay; the right of the foreign representative to operate the debtor's business in the ordinary course; the sale, use or transfer of property outside of the ordinary course; and the avoidance of post-petition transfers and post-petition perfection of security interests. The foregoing may be granted by way of relief upon the recognition of non-main proceedings. In addition, for either foreign main or non-main proceedings, the following discretionary relief may be granted: discovery of assets and affairs; entrusting affairs of debtor with the foreign representative; and any other relief necessary to protect the assets of the debtor and the interest of creditors.

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

Commented [H(41)]: Correct, 1/2 mark

Commented [H(42)]: Correct, 1/2 mark

Commented [H(43)]: Correct, 1/2 mark

Commented [H(44)]: Correct, 1/2 mark

Commented [H(45)]: Correct, 1/2 mark

Question 3.3 [4 marks]

Commented [H(46)]: Total marks 4/4



**What duties do directors owe to a Delaware corporation in the ordinary course of business? To whom are these duties owed when the corporation is potentially or actually insolvent? What rule protects directors from liability for errors of judgment?**

Directors owe fiduciary duties of loyalty to act in the corporation's best interests and a duty of care in making educated business decisions. The duties are owed to the corporation and its shareholders (not to the creditors - this is also the case when the corporation is near insolvency or is in insolvency).

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

Commented [H(48)]: Correct, 1 mark

Commented [H(49)]: Correct, 1 mark

The rule that protects directors from errors of judgment is the business judgment rule - this is a rebuttable presumption that a director acted in good faith on the basis of reasonable information.

Commented [H(50)]: Correct, 1 mark

Question 3.4 [5 marks]

Commented [H(51)]: Total marks 3.5/5

**List and describe the requirements that a creditor's claim must fulfill in order to qualify as a petitioning creditor in an involuntary proceeding.**

To qualify as a petitioning creditor, its claim must:

Commented [H(52)]: The claim must also be unsecured or undersecured

- not be contingent i.e. not dependent on the occurrence of a future event (other than, in respect of an unmatured debt, the passage of time);
- not be the subject of a bona fide dispute as to liability or amount i.e. an objectively reasonable basis for the dispute as a matter of law or fact; and
- be at least for USD16,750 in aggregate with other petitioning creditor claims.

Commented [H(53)]: Correct, 1/2 mark

Commented [H(54)]: Correct, 1 mark

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

Commented [H(56)]: Correct, 1/2 mark

Commented [H(57)]: Correct, 1/2 mark, also must allege that the debtor is not paying its debts as they come due or that "within 120 days before the filing of this petition, a custodian, other than a trustee, receiver, or an agent appointed or authorized to take charge of less than substantially all of the property of the debtor for the purpose of enforcing a lien against such property, was appointed or took possession."

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

Question 4.1 [5 marks]

Commented [H(58)]: Total marks 11.5/15

Commented [H(59)]: Total marks 5/5

**Speculation Inc is engaged in day-trading stocks from leased office space with two employees. It funds its trading through a margin loan from its broker, where the shares it purchases are held as collateral. For a while, Speculation Inc was very successful in trading, and the US Department of Justice (DOJ) has announced an investigation into whether its success was due to illegally trading on insider information. More recently, Speculation Inc has had serious trading losses, causing its broker to declare a default on the margin loan. It also has fallen behind on its rent, and been sued by a former employee alleging she was fired due to gender bias.**

**What would be the effect of a Chapter 11 petition being filed by Speculation Inc on each of the (i) DOJ investigation, (ii) margin loan default; (iii) delinquent lease and (iv) employment discrimination lawsuit?**

- (i) DOJ investigation: this regulatory investigation will not be subject to the stay arising from the Chapter 11 petition.
- (ii) margin loan default: the broker will be subject to the stay and will not be able to enforce on the share collateral or on the declaration of default.
- (iii) delinquent lease: the lease will be subject to the stay and will prevent the landlord taking possession or control of the property. The lease is an executory contract and will be assignable as part of the Chapter 11 reorganisation.
- (iv) employment discrimination lawsuit: the stay will prevent further action in respect of the discrimination claim. The contract is not executory and therefore not assignable as it relates to a claim of a former employee.

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

Commented [H(61)]: Correct, 1 mark

Commented [H(62)]: Incorrect, the margin loan is a securities contract that benefits from an exception to the automatic stay

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

Commented [H(64)]: Correct, 1 mark

Question 4.2 [5 marks]

Commented [H(65)]: Total marks 1.5/5

**Stella SA (Stella) is a an international cosmetics company incorporated in France, with its headquarters in Paris. Stella’s products are made in Italy and shipped to its retail stores in Europe (including England), Asia, and North America. Stella’s funding comes from a bank loan and Eurobonds, both of which are governed by English law. Stella’s retail sales have suffered due to pandemic-related closures and it is considering options to restructure its debt. One option is to use an English scheme of arrangement with respect to the Eurobonds. Could the English scheme of arrangement be recognized by a US bankruptcy court under Chapter 15, and would such recognition be as a foreign main or non-main proceeding?**

*It is unclear if the English scheme will be recognised by a US bankruptcy court under Chapter 15. The English scheme falls within the requirements of a “collective judicial or administrative proceeding in a foreign country”. The requirements for recognition are limited to the foreign representative showing that the foreign proceedings are pending and that the foreign representative is empowered to act by the foreign proceedings. However, to determine if the English scheme is a foreign main proceeding or a foreign non-main proceeding, it is necessary to determine if England is the debtor’s centre of main interest. There is a rebuttable presumption that the COMI is Stella SA’s country of incorporation - in this case France. Other factors are relevant and COMI can be established on the basis that English law governs two of the material contracts that Stella SA is party to. This suggests that the English scheme of arrangement may be recognised as the foreign main proceedings. For the recognition of foreign non-main proceedings requires that Stella SA has an establishment in England - it is not clear from the facts that this is the case.*

Commented [H(66)]: Correct, 1/2 mark, Stella is also headquartered in France and the other contacts do not overcome the presumption that Stella’s COMI is in France

Commented [H(67)]: Because England is not the COMI, these proceedings cannot be recognized as foreign main

Commented [H(68)]: Correct, 1 mark

Commented [H(69)]: Incorrect, Stella is stated to have a retail store in England

Question 4.3 [5 marks]

Commented [H(70)]: Total marks 5/5

**ToyCo is an American toy company that has created a popular line of folding robot toys called Xbox. The toys are covered by several US patents. Currently, GameMart Inc (GameMart) has a 10-year exclusive license to manufacture Xbox and pays ToyCo monthly royalties. GameMart operates a factory in California that it leases from Land Corp on a longer term lease with seven years to go; the lease prohibits assignment without Land Corp's consent. The Xbox toys are selling well, but GameMart's other toy lines are doing poorly, so it is considering a Chapter 11 bankruptcy. Answer the following questions:**

**(i) Is the license to manufacture Xbox an executory contract?**

**The licence is an executory contract. There are material obligations for both parties to fulfil under the contract. As this is a licence of patents, in the event of a purported/proposed sale of the licences by GameMart, the licences cannot be assigned without the consent of ToyCo.**

Commented [H(71)]: Correct, 1 mark

**(ii) Can GameMart transfer the Xbox license as part of 363 sale without ToyCo's consent? Why or why not?**

**As this is a licence of patents, in the event of a purported/proposed sale of the licences by GameMart, in accordance with US case law (*In re Trump*) the licences cannot be assigned without the consent of ToyCo.**

Commented [H(72)]: Correct, 1 mark

**(iii) Can GameMart transfer the factory lease as part of 363 sale without Land Corp's consent? Why or why not?**

**Notwithstanding that the lease states that it is not assignable without Land Corp's consent.** Correct, 1 mark

Commented [H(73)]: Correct, 1 mark

Commented [H(74)]: Correct, 1 mark

\* End of Assessment \*