



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 34/50

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

Commented [H(2): Total marks 6/10

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)]: Incorrect, the correct response is (a)

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)]: Incorrect, the correct response is (b)

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)]: Correct, 1 mark

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)]: Incorrect, the correct response is (d)

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

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.

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

Question 1.9

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.

Commented [H(11)]: Incorrect, the correct response is (c)

Question 1.10

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.

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

QUESTION 2 (direct questions) [10 marks]

Commented [H(13): Total marks 8.5/10

Question 2.1 (1 mark)

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

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

Setoff is a right that permits a creditor that is simultaneously holding a claim against the debtor and owing money to the debtor to net out the obligations. This right is limited because it can improve the position of a creditor compared to another unsecured creditors.

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

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

Question 2.2 [2 marks]

Commented [H(17): Total marks 1/2

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

First, the Bankruptcy Code (Title 11 of the U.S. Code). Second, the Federal Rules of Bankruptcy Procedure (Title 11a of the U.S. Code). Also, for the determination of claims and the property of the debtor, is important to review the applicable non-bankruptcy law, such a State law. And for the requirements on the filing, is worth to review the local bankruptcy rules of the court of filing.

Commented [H(18): Correct, 1/2 mark, also the Federal Rules of Civil Procedure which are incorporated by reference

Commented [H(19): Correct, 1/2 mark, also the judge's personal practices

Question 2.3 [2 marks]

Commented [H(20): Total marks 1.5/2

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

The absolute priority rule is a mechanism to ensure that all creditors are treated equally, based on the priority of their claims. It requires that payment in full must be made to each category of claims before the next category receives anything. It can be deviated if the creditor consents.

Commented [H(21): Correct, 1 mark

Commented [H(22): Correct, 1/2 mark, but only in a chapter 11 plan, not in chapter 7

Question 2.4 [2 marks]

Commented [H(23): Total marks 2/2

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 a type of post-petition financing that the debtor can use if is unable to secure another type of financing (§ 364 of the Bankruptcy Code establish an order for the debtor to obtaining credit). To opt for the priming lien, the debtor must demonstrate that is unable to obtain credit otherwise and there is adequate protection of the interest of the holder of the lien on the property of the estate on which such senior or equal lien is proposed to be granted. The court authorize the priming lien after notice and hearing (§ 364(d))

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Commented [H(25): Correct, 1/2 mark

Commented [H(26): Correct, 1 mark

Question 2.5 [3 marks]

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

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?

A preference is a transfer of the debtor's property made in a suspect period before the petition date. The property must be returned to the estate if it exceeds the amount the recipient would have

received in a chapter 7 liquidation had the transfer not been made. The elements that need to be proved are: (1) the transfer is of an property that the debtor had an interest. (2) The recipient of the transfer was a creditor or the transfer was made for the benefit of a creditor. (3) The transfer was made for or on account of an antecedent debt owed by the debtor before such transfer was made. (4) The transfer was made while the debtor was insolvent. (5) The transfer was made during the suspect period (90 days prior to petition date for third parties and one year prior to petition date for insiders). (6) The transfer had enabled the creditor to receive more than it would have received in a chapter 7 liquidation. Last, on preferences there is no need to show any fault of either the debtor or the creditor.

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

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

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

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

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

Commented [H(33)]: Total marks 14.5/15

Question 3.1 [3 marks]

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

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?

In general, a bankruptcy court may enter a final order only in core bankruptcy matters. In non-core matters, the jurisdiction is retained by the district court, but the district court may withdraw the reference of its jurisdiction to bankruptcy court. For example, core bankruptcy matters are matters concerning the administration of the estate, orders in respect to obtaining credit and proceedings to determine, avoid, or recover preferences.

Commented [H(35)]: Partially correct, 1/2 mark, the bankruptcy court can only enter a final order in core matters when they concern a challenge to a petition or the parties consent

In the appeals, we need to distinct between final and interlocutory orders. Final orders issued by a bankruptcy court may be appealed as of right. Interlocutory orders may be appealed only with a leave of the appellate court. One exception are orders extending the period of exclusivity to propose a plan, that are appealable as of right. Orders are generally reviewed by the district court of the district in which the bankruptcy court is sit. In some circuits, orders are reviewed by a Bankruptcy Appellate Panel, convened from the judges of the bankruptcy courts within the circuit. About the standard for review non-final orders, if the ruling was in a noncore proceeding or the bankruptcy court otherwise did not have authority to enter a final order, the district court or BAP reviews all findings of fact and conclusions of law to which a party has objected. The order of a district court or BAP is reviewed by a circuit court of appeal de novo as to conclusions of law and for abuse of discretion for findings of fact.

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

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

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

Question 3.2 [3 marks]

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 that automatically apply upon recognition of a foreign main proceeding are: automatic stay; operation of the debtor's business in the ordinary course by the foreign representative; sale, transfer or use of property outside the ordinary course and avoidance of post-petition transfers and post-petition perfection of security interests.

The relief that may be granted on a discretionary basis, following recognition as either main or non-main proceeding are: authorization of discovery regarding the debtor's assets and affairs; entrusting administration of the debtor's US assets to the foreign representative or other person; extension of provisional relief and any other relief necessary to effectuate the purposes of chapter 15 and to protect the assets of the debtor or the interests of creditors (any additional relief according to § 1521(a)(7)).

Question 3.3 [4 marks]

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 a fiduciary duty of loyalty to the corporation's best interest and a duty of care in educated decision-making. These duties are owed to the corporation and its shareholders, even if the corporation is insolvent. There is the business judgements rule that protects directors from liability for errors of judgement. Under this rule, the board of directors is presumed to have acted in good faith and on the basis on reasonable information. The presumption can be rebutted only by showing that a majority of the board were in fact not reasonably informed, did not honestly believe that their decision was in the corporation best interest or were not acting in good faith.

Question 3.4 [5 marks]

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

The claim needs to be:

- Non-contingent, that is, it doesn't depend on the occurrence of a future event

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

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

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

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

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

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

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

Commented [H(51)]: Total marks 4.5/5

Commented [H(52)]: Correct, 1 mark

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

- **Not the subject of bona fide dispute as to liability or amount, that exists if there is an objectively reasonable basis for a dispute as a matter of fact or law.**
- **Unsecured or undersecured, separately or in the aggregate with all other petitioning creditors' claims, in the amount of at least USD 16,750 (adjusted periodically by inflation)**

Commented [H(54): Correct, 1 mark

Commented [H(55): Correct, 1/2 mark

Commented [H(56): Correct, 1 mark

Commented [H(57): Correct, 1/2 mark, also the creditor must allege that the debtor is not paying debts as they come due or has had a custodian appointed over its property

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

Commented [H(58): Total marks 6/15

Question 4.1 [5 marks]

Commented [H(59): Total marks 2/5

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 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) **The DOJ investigation wouldn't be affected by the filing of Chapter 11 petition, because one of the exception for the automatic stay are regulatory investigations.**
- (ii) **The opening of the Chapter 11 gives Speculation Inc room to negotiate with the creditors, which includes the broker and the loan default.**
- (iii) **As the lease is a long-term contract, it would be an executory contract under Chapter 11. So, if Speculation Inc continues to occupy the office, it may be deemed to have assumed the contract. But in general, it has the choice to reject, assume or assume and assign the contract.**
- (iv) **The lawsuit would be stayed as a result of Chapter 11 filing, unless the former employee requests a relief from the stay.**

Commented [H(60): Correct, 1 mark

Commented [H(61): Incorrect, the filing of the petition brings into effect the automatic stay, but the margin loan is a securities contract that is subject to an exception to the automatic stay so the broker can liquidate the collateral

Commented [H(62): The stay bars the landlord from bringing non-bankruptcy action to recover rent or evict Speculation Inc.

Commented [H(63): Correct, 1 mark

Question 4.2 [5 marks]

Commented [H(64): Total marks 2/5

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?

Yes, the English scheme of arrangement could be recognized as a foreign proceeding under Chapter 15. As the Center Of Main Interest (COMI) concept in Chapter 15 is broad, the recognition would be as main or non-main proceeding. It may be recognized as main proceeding as most creditors are in England, and the Eurobonds and loans are governed by English law (England as COMI). It may be recognized as a non-main proceeding in the light of Stella is headquartered in France, with management also carried in France (France as COMI). As the recognition of a main proceeding have more advantages than a non-main proceeding (relief available upon recognition), probably the interest of the foreign representative is to obtain the recognition as a foreign main proceeding.

Commented [H(65)]: Correct, 1 mark, and the retail shop in England qualifies as the necessary establishment

Commented [H(66)]: Correct, 1 mark, the other factors would not overcome the presumption that the jurisdiction of incorporation is the COMI and because COMI is not England it cannot be recognized as a foreign main proceeding

Question 4.3 [5 marks]

Commented [H(67)]: Total marks 2/5

ToyCo is an American toy company that has created a popular line of folding robot toys called Xblox. The toys are covered by several US patents. Currently, GameMart Inc (GameMart) has a 10-year exclusive license to manufacture Xblox 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 Xblox 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 Xblox an executory contract?

As the license agreement is a long-term contract and GameMart pays monthly royalties to ToyCo, it can be deemed an executory contract. However, for a complete answer, we need to know if ToyCo have obligations, as support or technical assistance.

Commented [H(68)]: Partially correct, 1/2 mark, because the license is exclusive, ToyCo has the ongoing obligation not to license the IP to anyone else and therefore the contract is executory

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

Considering the license agreement as an executory contract, GameMart cannot transfer the license without the licensor consent, because the contract is governed by substantive non-bankruptcy law (intellectual property law).

Commented [H(69)]: Correct, 1 mark

Commented [H(70)]: Partially correct, 1/2 mark, specifically a substantive non-bankruptcy law that permits a counterparty to refuse to accept performance by another party

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

Generally, leases are executory contracts. Also, according to § 365 (4)(a) of the Bankruptcy Code, "an unexpired lease of nonresidential real property under which

the debtor is the lessee shall be deemed rejected, and the trustee shall immediately surrender that nonresidential real property to the lessor, if the trustee does not assume or reject the unexpired lease by the earlier of (i)the date that is 210 days after the date of the order for relief; or (ii)the date of the entry of an order confirming a plan." So, in general, lease contracts of nonresidential real property -as the factory- shall be deemed rejected and cannot be transferred.

Commented [H(71): Incorrect, this sets a deadline to assume or be deemed to reject, so GameMart may assume and assign as long as it assumes before the deadline. The contractual requirement of landlord approval is not effective in bankruptcy

* End of Assessment *