



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).**
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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 47/50

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

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

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)]: 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)]: 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]

Commented [H(13)]: Total marks 9/10

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 means the compensation of credits and debts between a creditor and a debtor. It permits a creditor holding a claim against the debtor and, at the same time, owing money to the same debtor to net the two or more obligations. In other words, the debtor also has a claim against the creditor and, thus, these different claims must be setoff and only the difference arising of this setoff will be paid.

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

In an insolvency proceeding, setoff is not permitted in several circumstances in order to fulfil equal treatment among the creditors. Otherwise, creditors that also owe money to the debtor would have those claims satisfied, which would not occur with all the other creditors.

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

There are several circumstances in which the setoff is not allowed, such as: (i) "the creditor's claim against the estate was acquired post-petition or in the 90 days prior to the petition at a time when the debtor was insolvent and (ii) "the creditor's obligation to the debtor was incurred in the 90 days prior to the petition at a time when the debtor was insolvent for the purposes of exercising setoff rights".

Question 2.2 [2 marks]

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

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

When preparing a filing for a bankruptcy court you should have in mind that procedures in bankruptcy proceedings are governed by the Federal Rules of Bankruptcy Procedure. These rules frequently incorporate by reference the Federal Rules of Civil Procedure. Also, forms for common bankruptcy filings are required to be used. Also, each bankruptcy court will have local rules of procedure.

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

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

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

Finally, case law is very important, and practitioners should be aware of the case law of that region / circuit, as well as the decisions of the US Supreme Court on the matter. Due to the differences between the circuits, you should consider consulting a local practitioner for advice if you are practicing in a jurisdiction different from the one you are used to.

Question 2.3 [2 marks]

Commented [H(21)]: Total marks 2/3

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

The absolute priority rule establishes an order of payment of the creditors. It means that the claims of a dissenting party shall be paid in full and before any class of creditors junior to such dissenting class. Also, the absolute priority rule sets that creditors shall receive payment in full before a junior class of creditors and the holders of equity can receive or retain assets under a plan of reorganization only after the payment of such creditors (§ 1129(b)(2), Bankruptcy Code).

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

Also, no creditor or class of creditors may receive less according to a plan of reorganization that it would receive under a liquidation based on chapter 7. Under chapter 7 the claims are not paid according to a plan of reorganization, but according to statutorily required priorities. On the other hand, it must be said that in a chapter 11 plan, a more senior creditor may agree to receive less than the absolute priority rule would require to pay a lower priority claimant in order to obtain their approval of the plan. In other words, the senior creditors may give up the absolute priority rule in order to get support for the approval of the plan of reorganization. It must be clear that deviation from the absolute priority rule is only applicable in chapter 11 proceedings, but not in chapter 7 cases, because in chapter 7 the statutory priorities must be followed.

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Commented [H(24)]: Correct, 1/2 mark

Question 2.4 [2 marks]

Commented [H(25)]: Total marks 1.5/2

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 senior guarantee under the assets of the debtor. This guarantee is senior or equal to pre-petition lien on the debtor’s assets and its aims to secure post-petition financing.

Commented [H(26)]: Partially correct, 1/2 mark, it's a security interest, not a guarantee

A very common problem in a restructuring proceeding is the financing of the debtor. The problem is that the debtor is passing through financial difficulties (which is the very reason of its restructuring proceeding) and, thus, need “new money” to pay the fees of the proceeding (which are expensive) and to keep operating its business. However, creditors, normally, don’t want to lend more money to the debtor, mainly because the financial distress of the debtor. Hence, to increase the chances of a successful reorganization, the Bankruptcy Code has rules to incentive lenders and third parties to extend credit to the debtor. This is the debtor in possession (DIP) financing.

The 11 U.S. Code § 364 provide rules on obtaining credit of the debtor in possession. There are four alternatives that the estate may obtain credit. There is an order of escalating protections to the counterparty and, at the same time, an increase in the burden of the debtor demonstrate that such protections are necessary to obtain enough money.

The last option (which applies only if the first three options were not successful) is the court may grant a priming lien - to secure the DIP financing - that is senior or equal to pre-petition lien on the assets of the debtor. To be valid this priming lien, the debtor must demonstrate that the interest of the secured creditor being primed is adequately protected.

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Finally, it must be highlighted that a good faith DIP lender is protected from the effects of a reversal of a DIP financing order on appeal.

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Question 2.5 [3 marks]

Commented [H(29)]: 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?

Preference is a transfer of an assets of the debtor in a suspect period that must be returned to the estate if this transfer exceeds the value the recipient would have received in a liquidation proceeding if the transfer have not been made (11 U.S. Code § 547). The range of suspect period depends on certain factors, like the fact the recipient is (or it is not) an insider of the debtor (like a manager of the debtor).

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It must be point out that there is no need to show any fault of either the recipient or the debtor in connection to the payment made. Hence, once a preference is found out, the asset/payment is returned to the estate to equalize the treatment of the creditors. The parties involved in that transaction suffer no penalty other than return the transfer to the estate.

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The elements of a preference claim that need to be proved are foreseen in (11 U.S. Code § 547 (b)), which are a transfer of and interest of the debtor in property:

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

“(1) to or for the benefit of a creditor;

Commented [H(33)]: Correct, 1/2 mark

(2) for or on account of an antecedent debt owed by the debtor before such transfer was made;

Commented [H(34)]: Correct, 1/2 mark

(3) made while the debtor was insolvent;

(4) made—

(A) on or within 90 days before the date of the filing of the petition; or

(B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and

(5) that enables such creditor to receive more than such creditor would receive if—

(A) the case were a case under chapter 7 of this title;

(B) the transfer had not been made; and

(C) such creditor received payment of such debt to the extent provided by the provisions of this title”.

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

Commented [H(35)]: Total marks 15/15

Question 3.1 [3 marks]

Commented [H(36)]: 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?

The US judicial system is set forth in article III of the US constitution, which explains which courts exist in the USA and what powers they have, including their jurisdiction. The bankruptcy courts, on the other hand, were created by federal legislation, specifically the 1978 Bankruptcy Code. Hence, federal courts are created by Article III of the US Constitution, whereas bankruptcy courts are created by federal law.

Because the bankruptcy courts were not created by the Article III of the US Constitution, Bankruptcy Courts' authority is different, according to the US Supreme Court. Initially, the Bankruptcy Code created a distinction between "core" and "non-core" matters and permits bankruptcy judges to hear and decide only core proceedings. Besides, bankruptcy court may hear non-core proceedings if they are sufficiently related to a bankruptcy proceeding. However, in this situation, the bankruptcy court cannot make a final decision, instead, should send its conclusion to the district court to decide the matter. So, the bankruptcy court was created by adjuncts to the district court and had its jurisdiction for final decision just over the core-proceedings.

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This situation changed in 2011, when the US Supreme court decided the Stern v. Marshall Case, in which the Supreme Court ruled that Bankruptcy Courts did not have jurisdiction to make final decisions, even about core proceeding, because this was unconstitutional, because bankruptcy court cannot make final decisions about matters subject to Article III of the US Constitution. The US Supreme Court decided that (i) bankruptcy court may analyze core and non-core proceedings, but its decision must be reviewed by the district court related to that bankruptcy court and (ii) bankruptcy court may have authority to decide about those proceedings if parties consent to it. Besides, bankruptcy court has jurisdiction to adjudicate a challenge to a petition.

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Commented [H(39)]: Correct, 1/2 mark

Finally, appeals from the bankruptcy court decisions are decided by the district court for the district in which they sit. However, in some circuits, the appeals are decided by a Bankruptcy Appellate Panel (BAP). In this last case, a party has the option to request the appeal should be decided by the district court. After that there is a further appeal of right to the circuit court of Appeals. After that, in rare occasions, there might be another appeal to the Supreme Court of the USA.

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

Question 3.2 [3 marks]

Commented [H(42)]: 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?

According to the 11 U.S. Code § 1520, the automatic effects of recognition of a foreign main proceeding are:

"(1) sections 361 and 362 apply with respect to the debtor and the property of the debtor that is within the territorial jurisdiction of the United States; [automatic stay]
(2) sections 363, 549, and 552 apply to a transfer of an interest of the debtor in property that is within the territorial jurisdiction of the United States to the same extent that the sections would apply to property of an estate; [operation of the debtor's business in the ordinary course by the foreign representative]
(3) unless the court orders otherwise, the foreign representative may operate the debtor's business and may exercise the rights and powers of a trustee under and to the extent provided by sections 363 and 552; [sale transfer or use of property outside the ordinary course] and
(4) section 552 applies to property of the debtor that is within the territorial jurisdiction of the United States" [avoidance of post-petition transfers and post-petition perfection of security interests].

However, these effects don't affect (i) the right to commence an individual action or proceeding in a foreign country to the extent necessary to preserve a claim against the debtor and (ii) the right of a foreign representative or an entity to file a petition commencing a case under this title or the right of any party to file claims or take other proper actions in such a case.

Besides, following recognition, as either foreign main or foreign non-main proceeding, there are some reliefs that also may be granted on a discretionary basis, according to 11 U.S. Code § 1521, such as:

"(i) authorization of discovery regarding the debtor's assets and affairs;
(ii) entrusting administration of the debtor's US assets to a foreign representative or other person;
(iii) extension of provisional relief;
(iv) any other relief necessary to effectuate the purpose of chapter 15 and to protect the assets of the debtor on the interests of creditors".

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?

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

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

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

Commented [H(46)]: Correct, 1/2 mark

Commented [H(47)]: Correct, 1/2 mark

Commented [H(48)]: Correct, 1/2 mark

Commented [H(49)]: Total marks 4/4

The directors, in a Delaware corporation, owe a fiduciary duty of loyalty and due care to the corporation's best interest on the decision-making process. These duties are owed to the corporation and its shareholders, not to its creditors, even if the corporation is potentially or actually insolvent.

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

Commented [H(51)]: Correct, 1 mark

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

The directors are protected from liability for errors of judgments if they comply with the business judgment rule. According to this rule, the board of directors is presumed to have acted in good faith based on reasonable information. However, this presumption can be rebutted if it is demonstrated that the board were not reasonably informed, did not honestly believe that their decision was in the corporation's best interest, or the directors was found not be acting in good faith. In other words, unless the director is negligent or is acting in bad faith, he is not liable for the acts taken on behalf of the corporation.

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

In addition, if there is an interested party involved in the transaction (like the controlling shareholder), the director is supposed to prove, the entire fairness of the transaction between related parties.

Question 3.4 [5 marks]

Commented [H(54)]: Total marks 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.

Creditors may initiate an involuntary insolvency proceeding against a debtor either based on chapter 7 or chapter 11 of the Bankruptcy Code. The number of petitioner creditors depends on how many non-contingent, non-insider creditors the debtor has. The 11 U.S. Code § 303 provide rules on involuntary cases.

To qualify as a petitioning creditor, the creditor must have a claim against the debtor that is:

(a) non-contingent, which means that: (i) doesn't depend on a future event, neither (ii) the debt is unmatured (in other words, the payment is already late);

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

(b) not subject of bona fide dispute as to liability or amount, which means that: (i) there is no reasonable basis for a dispute as a matter of law or fact and the debtor know that the debt is owed (in other words, there is no reasonable doubt on the existence of the debt, the "an debeatur") and (ii) the amount of the claim is not disputed (in other words, there is no reasonable doubt on the "quantum debeatur");

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

Commented [H(58)]: Correct, 1/2 mark

(c) unsecured or undersecured, separately or in the aggregate with all other petitioning creditors' claims, in the amount of at least USD 16,750 (this amount is periodically increased due to inflation).

Commented [H(59)]: Correct, 1 mark

Commented [H(60)]: Correct, 1/2 mark

It must be pointed out that the involuntary petition form requires the petitioning creditors to allege that debtor is not paying its debts as they become 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." (Form B205 at 2).

Commented [H(61)]: Correct, 1/2 mark

Finally, a foreign representative of an estate in a foreign proceeding may as well commence an involuntary insolvency proceeding against the debtor.

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

Commented [H(62)]: Total marks 13/15

Question 4.1 [5 marks]

Commented [H(63)]: Total marks 3/5

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?

There are several effects of a Chapter 11 petition. Let's check the situations described above:

(i) DOJ investigation. One of the effects is the automatic stay that comes into effect immediately on the filing of Chapter 11 petition. The automatic stay aims to provide the debtor breathing room to formulate a restructuring plan and negotiate with its creditors. However, stay is subject to certain statutory exceptions, like regulatory investigations (11 USC §362(b)). Hence, the DOJ investigation is not suspended by Chapter 11 petition.

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

Commented [H(65)]: Correct, 1 mark

(ii) margin loan default. The scope of the automatic stay is broad, and it applies to any interference with the property of the estate, regardless of where this property is located. Once the Chapter 11 petition is filed, the Bankruptcy Code prohibits litigation on pre-petition claims and enforcement of pre-petition judgment against the debtor or property of the estate. This means that although the debtor may be sued for the margin loan default, he may not suffer the effects of that default. For example: setoff

is not available for that default and any enforcement of a right based on that default cannot be exercised.

Commented [H(66): Incorrect, the margin loan is a securities contract so the broker benefits from an exception to the automatic stay

(iii) delinquent lease. One statutory exception of the automatic stay is the eviction of a debtor-tenant from non-residential property where the lease has expired. The Bankruptcy Code states an exception from the automatic stay "any act by a lessor to the debtor under a lease of nonresidential real property that has terminated by the expiration of the stated term of the lease before the commencement of or during a case under this title to obtain possession of such property (11 U.S. Code § 362 (b) (10)). In the above-mentioned case, the lease has not expired, but the debtor has fallen behind on its rent (the agreement is still valid, but there is a default). Thus, the debt that exists before the Chapter 11 petition still exists and is subject to the automatic stay. The debtor may not be evicted for pre-existing debts. However, the debtor-tenant shall pay the new instalments due after the 11 Chapter 11 petition, otherwise he will be subject to eviction.

Commented [H(67): Correct, 1 mark

(iv) employment discrimination lawsuit. The Chapter 11 petition doesn't freeze the employment lawsuit. For instance, the debtor may be sentenced to pay an indemnification to the former employee. However, the enforcement of that decision is subject to the automatic stay.

Commented [H(68): Incorrect, this is a private civil lawsuit, so it is stayed

Question 4.2 [5 marks]

Commented [H(69): Total marks 5/5

Stella SA (Stella) is 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?

(i) *Could the English scheme of arrangement be recognized by a US bankruptcy court under Chapter 15?*

The English scheme of arrangement can be recognized by a US bankruptcy court under Chapter 15 if it is considered a foreign proceeding. "Foreign proceeding" is a key term of the UNCITRAL Model Law of Cross-Border Insolvency (MLCBI), which was enacted by the USA in the Chapter 15 of the Bankruptcy Code.

"Foreign proceeding" means a collective judicial or administrative proceeding in a foreign State, including an interim proceeding, pursuant to a law relating to insolvency in which proceeding the assets and affairs of the debtor are subject to control or

supervision by a foreign court, for the purpose of reorganization or liquidation” (article 2 (a) of MLCBI). We must examine this definition in parts.

The Guide to Enactment and Interpretation of the MLCBI (“The Guide”) explains what a collective proceeding in its paragraphs 69 to 72 is. In short, a collective proceeding means a proceeding that deals with all the debt of the debtor as a whole. It’s a proceeding to treat collectively of all the debtor’s obligations. It’s not a proceeding of a single creditor against the debtor, but instead is a proceeding involving the debtor and all its creditors. The goal is to achieve a global solution for all the stakeholders of an insolvency proceeding. It must be pointed out that some national laws exclude some creditors of this proceeding. However, those creditors are an exception, and the proceeding is still considered a collective proceeding.

A foreign proceeding must be pursuant to a law relating to insolvency, which is explained in paragraph 73 of the Guide. The applicable law doesn’t need to be labelled as insolvency law, but has to “deals with or addresses insolvency or severe financial distress”. According to the Guide: “The purpose was to find a description that was sufficiently broad to encompass a range of insolvency rules irrespective of the type of statute or law in which they might be contained and irrespective of whether the law that contained the rules related exclusively to insolvency”. So, the debtor must seek to restructure the financial affairs of the entity or liquidate the entity and not only dissolve its legal status. The simple dissolution of a solvent company is not a insolvency proceeding.

A foreign proceeding must be subject to the control or supervision of by a foreign court. However, by “court”, it could be a judicial or an administrative authority, according to the definition in article 2 (e) of the MLCBI. The Guide is also explicit in admitting an administrative authority to be considered a foreign court (paragraph 87). Besides, is common in different countries that insolvencies related to banks are overseen by administrative authorities.

The Guide to Enactment and Interpretation of the MLCBI explains what a control or supervision by a foreign court in its paragraphs 74 to 76 is. The assets and affairs of the debtor are subject to control or supervision of the foreign court.

This is a very comprehensive definition, that includes very different proceedings foreseen in different national laws, including the Brazilian recuperação judicial, the Australian creditor-appointed receivers and the English schemes of arrangement, because all the above conditions are met to be considered a foreign proceeding.

So, the answer is yes, the English scheme of arrangement can be recognized by a US bankruptcy court under Chapter 15.

(ii) would such recognition be as a foreign main or non-main proceeding?

The answer for this question depends on where the centre of main interests (COMI) of the debtor is. If the COMI is in England, the English scheme of arrangement will be recognized as a foreign main proceeding. On the other hand, if there is only an establishment in England, but the COMI is elsewhere, the English scheme of arrangement will be recognized as a foreign non-main proceeding.

Commented [H(70)]: Correct, 1 mark

The COMI is the place where the debtor conducts the administration of its interests on a regular basis and which is ascertainable by third parties. There is a rebuttable presumption that in the absence of proof to the contrary, the debtor's registered office, or habitual residence in the case of an individual, is presumed to be the centre of the debtor's main interests (11 U.S. Code § 1516 (c)).

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

Having this in mind, let's check where the COMI of Stella SA is. Given the fact that the company's headquarters are in Paris that is a presumption that the COMI is in France, because in Paris probably is the centre of control of the company. Besides, in England there is only a retail stores, which can be considered an establishment. Thus, the English scheme of arrangement would be recognized as a foreign non-main proceeding.

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

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

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

Question 4.3 [5 marks]

Commented [H(75)]: Total marks 5/5

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?

An executory contract is an agreement that there are material unperformed obligations on both sides. The license to manufacture Xblox is an executory contract because the licensee shall pay monthly royalties and the owner of the license shall respect the 10-year exclusive licence to manufacture the Xblox.

Commented [H(76)]: Correct, 1 mark

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

The answer is no.

Commented [H(77)]: Correct, 1 mark

The executory contracts are regulated in 11 U.S. Code § 365. The ability to assume, reject or assume and assign executory contracts is possibility in an insolvency

proceeding in the USA. Thus, as a general rule, the debtor may transfer rights under a contract to a third party, although for such transfer shall give the counter party proofs of future performance.

The US Bankruptcy Code permits the assignment of contracts even if contractual clauses say otherwise. However, the counterparty consent is required in some circumstances where substantive non-bankruptcy law demands, like intellectual property licensing law, which is applicable to the above-mentioned situation. In these cases, the counterparty cannot be obliged to accept performance from a transferee. Hence, GameMart cannot transfer the Xbox license as part of 363 sale without ToyCo's consent.

Commented [H(78)]: Correct, 1 mark

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

Yes. This is also an executory contract and, as a general rule, the debtor may transfer rights under a contract to a third party, although for such transfer shall give the counter party proofs of future performance.

Commented [H(79)]: Correct, 1 mark

The US Bankruptcy Code permits the assignment of contracts even if contractual clauses say otherwise. However, the counterparty consent is required in some circumstances where substantive non-bankruptcy law demands. A factory lease is not one of the exceptions and, thus, GameMart may transfer the factory lease as part of 363 sale even without Land Corp's consent.

Commented [H(80)]: Correct, 1 mark

* End of Assessment *