



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 35/50

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

Commented [H(2): Total marks 8/10

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

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 9.5/10

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 the reduction or discharge of a debt by setting against it a claim in favor of the debtor. It occurs when a creditor has a claim against the debtor but also owes money to the same debtor, therefore, he has a right against him but also an obligation that has to comply. Therefore, bankruptcy laws permits a "setoff" that would decrease the obligation to the proportion that wasn't reach.

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

Setoff is not always permitted because it improves the position of the particular creditor unlike the other unsecured creditors that doesn't owe money to the debtor because the decrease of the obligation would be made according to the full amount owed and not by the lesser amount the debtor would actually pay on the claim. These would mean that there would be cases in which a plan is not enough to pay to the unsecured claims but, in a certain way, it would be enough to pay, at least partially, to a particular "setoff" obligation.

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

For example, if a creditor has an "original" claim for USD100, and, applying the 'setoff' this particular obligation ends in USD20, this particular creditor has already been benefited por USD80 although the others unsecured creditor haven't received a payment, despite being in the same class.]

Question 2.2 [2 marks]

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

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

[It's important to review the Bankruptcy Rules, the Federal Rules of Civil Procedure, the local rules of the bankruptcy court, the judge's personal practices and specially review recent cases to get familiar to decisions in other cases and precedent.]

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

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

Commented [H(20)]: Correct, 1/2 mark

Commented [H(21)]: Correct, 1/2 mark

Question 2.3 [2 marks]

Commented [H(22)]: Total marks 2/2

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

[The absolute priority rule requires that no creditor or class of creditors may receive less under a plan of reorganization than it would under a hypothetical chapter 7 liquidation. It also states that payment in full must be made to each category of claims before the next category receives anything.]

Commented [H(23)]: Correct, 1 mark

It can be deviated with the consent of affected creditors but only in a chapter 11 reorganization and not in a chapter 7 liquidation.]

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

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

Question 2.4 [2 marks]

Commented [H(26)]: 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?

[Is a **lien on a property which is granted a senior or equal to a pre-petition lien position**. This means that lenders would have a priority in collateral over the pre-petition secured lenders. The requirement for the viability of granting priming lien is basically that **neither of the other three alternative for DIP financing was successful**. This is the reason why is considered a last resource when the debtor is unable to obtain any other type of financing.]

Commented [H(27)]: Correct, 1 mark

Commented [H(28)]: Correct, 1/2 mark, also the secured creditor that is primed must be adequately protected

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?

[A preference is a transfer of the debtor's property made in a suspect period before the petition date that 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 (11 USC, § 547).

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

The elements of preference are:

- (1) A **transfer of an interest of the debtor in property**.
- (2) **To or for the benefit of a creditor**.
- (3) **For or on account of an antecedent debt owed by the debtor before such transfer was made**.
- (4) **Made while the debtor was insolvent**.
- (5) **Made during the suspect period**.
- (6) **That enables the creditor to receive more than it would have in a chapter 7 liquidation**.

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

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

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

There is no need to show a fault by any of the parties involved.]

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

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

Commented [H(35)]: Total marks 11.5/15

Question 3.1 [3 marks]

Commented [H(36)]: Total marks 1.5/3

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?

[Bankruptcy courts may enter a final order in "core" proceedings. However, the US supreme court has ruled that, **even in core proceedings, if the matter invades the Article III of the Constitution, the court cannot issue final orders**.

Commented [H(37)]: Correct, 1/2 mark, specifically the bankruptcy court can enter final orders on core matters created by the Bankruptcy Code, such as a challenge to a petition, or with the consent of the affected parties. When the bankruptcy court doesn't have authority to enter a final order, the district court treats its order as a report and recommendation.

Appeals from bankruptcy court decisions are heard by the district court for the district in which they sit. In certain circuits, bankruptcy appeals may also be heard by a Bankruptcy Appellate Panel (BAP), convened from the judges of the bankruptcy courts within the circuit. From the BAP or the district court, they can also be review by the circuit court of appeals.

Commented [H(38)]: Correct, 1/2 mark

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

Non-final orders or interlocutory orders may be appealed only with leave of the appellate court.]

Question 3.2 [3 marks]

Commented [H(40)]: 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?

[Unlike a "normal" US bankruptcy proceeding, the stay arises only upon the petition for recognition of a foreign main proceeding being granted and is limited to the property of the debt or within the territorial jurisdiction of the United States. It also has the following provisions: I) operation of the debtor's business in the ordinary course by the foreign representative, II) sale, transfer or use of property outside the ordinary course and III) avoidance of post-petition transfers and post-petition perfection of security interests.

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

The following relief also may be granted on a discretionary basis, as either foreign main or foreign nonmain: (I) authorization of discovery regarding the debtor's assets and affairs; (II) entrusting administration of the debtor's US assets to the foreign representative or other person; (III) extension of provisional relief; (IV) any other relief "necessary to effectuate the purposes of chapter 15 and to protect the assets of the debtor or the interests of creditors.

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

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

Is important to note that this list is not exhaustive and that a court may provide further assistance.]

Question 3.3 [4 marks]

Commented [H(47)]: Total marks 3.5/4

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 a fiduciary duty of loyalty to the corporation's best interest and a duty of care in educated decision-making, but are protected from liability for errors of judgment by the business judgment rule.

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

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

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

Directors duty are owed to the corporation and its shareholders, not the creditors.

Commented [H(51)]: Correct, 1/2 mark, this remains the case when the corporation is potentially or actually insolvent.

Directors are protected by the Business Judgment Rule. Under the business judgment rule, the board of directors is presumed to have acted in good faith on the basis of reasonable information. This presumption may be rebutted by showing that a majority of the board in fact were not reasonably informed, did not honestly believe that their decision was in the corporation's best interest, or were not acting in good faith]

Commented [H(52): Correct, 1 mark

Question 3.4 [5 marks]

Commented [H(53): 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.

[The creditor must have a claim that is:

I) Non-contingent: It does not depend on the occurrence of a future event.

Commented [H(54): Correct, 1 mark

II) Not the subject of bona fide dispute as to liability or amount

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

Commented [H(56): Correct, 1 mark, a bona fide dispute requires an objective issue of fact or law

III) The claim or the aggregate of the other creditor's claim must be, at least, the amount of USD 16,750.

Commented [H(57): Correct, 1/2 mark

Besides these requirements, it is required that the petitioning creditors allege either that the debtor is generally not paying its debts as they become due.]

Commented [H(58): Correct, 1/2 mark, or that a custodian has been appointed for debtor's assets

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

Commented [H(59): Total marks 6/15

Question 4.1 [5 marks]

Commented [H(60): Total marks 1/5

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?

[Taking into account that Speculation Inc is a trading/stock broker company, they can't be a debtor in a Chapter 11 petition. Therefore, any of the petitions would be dismissed. However, in case that it would succeed, the DOJ investigation would be an exception to the automatic stay, the lease would be subject of an election between rejecting it, assuming it and assuming and assigning it and the employment

Commented [H(61): Incorrect, simply trading stocks for its own account doesn't make it a stockbroker. However its margin loan is a securities contract that is exempt from the stay, so the broker could liquidate the collateral after the filing of the petition.

Commented [H(62): Correct, 1 mark, also the stay would come into effect on the filing of the petition

Commented [H(63): The landlord would be barred by the stay from commencing proceedings to evict Speculation Inc. or recover pre-petition rent.

discrimination lawsuit would depend the nature of the petition but would be a contingent claim.]

Commented [H(64): This is a private civil suit that would be stayed.

Question 4.2 [5 marks]

Commented [H(65): Total marks 0/5

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, if the foreign representative manage to establish that a foreign court or administrative proceeding with respect to the debtor is pending and that the foreign representative is empowered to act by the proceeding, it shall be allowed to file the petition to later be accepted and recognized.

That recognition would be a foreign main proceeding. Although Stella SA is a French incorporated company, it could be argue that, according to COMI presumptions, precisely "location of a majority of debtor's creditors or a majority of the creditors that will be affected by the relief requested by the foreign representative" would apply to the case as Stella's funding comes from English bank and bonds and the proceeding is taking place in England.]

Commented [H(66): Stella's COMI is presumed to be in France. The other factors are unlikely to outweigh that. Because COMI is not in England, foreign main recognition is not available. Foreign non-main recognition would be appropriate because England is not the COMI and the retail store in England qualifies as an establishment.

Question 4.3 [5 marks]

Commented [H(67): 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?

[Yes, it's an executory contract.]

Commented [H(68): Correct, 1/2 mark, each side has a duty--to pay royalties and to maintain exclusivity

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

[No, it can't. Although it's a executory contract, there are some restrictions just like those that provides that the counterparty cannot be compelled to accept performance from a transferee, such as intellectual property licensing law like in this case. A licensee of a third-party's intellectual property might not be able to assume and continue performing under a pre-petition license without the licensor's consent]

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

Commented [H(70)]: 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, it can be transferred. The lease of the factory is assignable without consent, notwithstanding the landlord approval provision.]

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

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

* End of Assessment *