



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 24.75/50

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

Commented [H(2)]: Total marks 7/10

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

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

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

Which of the following about cramdowns, is false?

Commented [H(5)]: Incorrect, the correct response is (a)

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

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

- (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

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 8.5/10

Question 2.1 (1 mark)

Commented [H(14)]: Total marks 0.5/1

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

[Unfair against all other creditors. One creditor may not be favoured over another.

Commented [H(15)]: Correct, 1/2 mark, but you have not included the definition of "setoff"

Setoff's are not permitted in a number of circumstances:

- The creditor's claim against the estate is not allowed
- The creditor's claim against the estate was acquired post-petition or in the ninety (90) days prior to the petition at a time when the debtor was insolvent
- The creditor's obligation to the debtor was incurred in the ninety (90) days prior to the petition at a time when the debtor was insolvent for the purposes of exercising setoff rights
- The creditor improves it's position by setoff as compared to it's position had setoff been exercised ninety (90) days prior to the petition]

Question 2.2 [2 marks]

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

- [
- Bankruptcy Rules
 - Federal Rules of Civil Procedure
 - The Local Rules of the Bankruptcy Court & the judge's personal practices.
-]

Commented [H(17)]: Correct, 1/2 mark

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

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

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

Question 2.3 [2 marks]

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

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

[The absolute priority rule requires that full payments are to be made in each category before the next category of claim receives anything. However, in a Chapter 11 plan, deviation from the absolute priority rule is permitted only with consent of the affected creditors.

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

Commented [H(23)]: Correct, 1/2 mark

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

Statutory priorities must be followed in Chapter 7; therefore deviation is not permitted in said Chapter.]

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?

[Only of financing cannot be obtained on any other terms, the court may grant a priming lien that is senior or equal to a pre-petition lien on the estate property to secure post-petition financing.]

The Court's approval will depend on;

- whether any other source of funds is available that doesn't contain such provisions, and;
- whether substantial additional credit is being made available to the debtor.

DIP Lenders is protected from the effects of a reversal of a DIP financing order on appeal.]

Question 2.5 [3 marks]

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

[Preferences only arise where the debtor is paying a creditor pre-existing debt. The elements is as follows:

- A transfer of an interest of the debtor in property
- To or for the benefit of a creditor
- For an account of an antecedent debt owed by the debtor before such transfer was made
- Made while debtor was insolvent
- Made during the suspected period
- That enables the creditor to receive more than it would have in Chapter 7 Liquidation

Expert valuation evidence will often be required if this element of preference claim is disputed.]

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

Question 3.1 [3 marks]

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 appeals are heard by a Bankruptcy Appellate Panel (BAP), convened from the judges of the Bankruptcy Courts within the circuit.

- A Party has the option to request that the appeal be heard by the district court instead.
- Only in rare circumstances, an appeal from bankruptcy court may go directly to court of appeals where either or both certifies either;
 - i) the appeal raises a question of law as to which there is no controlling decision of the circuit or the US Supreme Court, or requires resolving conflicting controlling decisions, or;
 - ii) immediate appeal may materially advance the progress of the case.

Commented [H(26)]: Correct, 1/2 mark

Commented [H(27)]: Correct, 1 mark, also the interest of the primed creditor must be adequately protected

Commented [H(28)]: Total marks 2.5/3

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, also there is no showing of fault required

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

Commented [H(34)]: Total marks 7.25/15

Commented [H(35)]: Total marks 1/3

Commented [H(36)]: Partially correct, 1/2 mark, this is only in some circuits, in other circuits only district courts hear bankruptcy appeals

To have standing appeal a bankruptcy court order, a party must be a "party aggrieved" by that order.

Article III of the US Constitution, bankruptcy judges are appointed by courts of appeal, rather than the president, to not have lifetime tenure and have limited jurisdiction to enter final order.

Referring to *Stern vs Marshal 564 us 462 (2011)* The US Supreme Court shocked bankruptcy practitioners by confirming that even in core proceedings, a bankruptcy court cannot issue final orders that invade Article III Jurisdiction.

In mentioned case, the Bankruptcy Court Judge, who did not enjoy tenure pursuant to Article III of the Constitution, had the statutory authority under 28 U.S.C. 157(b) to issue a final judgment. The Court held that Bankruptcy Court had the statutory authority to enter judgment on counterclaims as core proceedings under section 157(b)(2)(C).]

Commented [H(37): Partially correct, 1/2 mark, the bankruptcy court can enter a final order on certain core proceedings established by the Bankruptcy Code, such as a challenge to a petition; it can also enter final orders where the parties consent. Non-final orders are treated as a report and recommendation by the district court.

Question 3.2 [3 marks]

Commented [H(38): Total marks 1/3

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?

[Chapter 15. Here we can refer to Section 1520(a)(1). Provisions that apply upon recognition include the automatic stay as mentioned in Section 362 of the Bankruptcy Code and the right to "adequate protection" mentioned in Section 361 of the Bankruptcy Code

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

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

We can refer to Section 20 of the Cross Border Insolvency Act 42 of 200, which state as follows:

Commented [H(41): Incorrect, this legislation is not applicable in the US

"(1) Upon recognition of foreign proceedings that are foreign main proceedings-(a) commencement or continuation of individual legal actions or

individual legal proceedings concerning the debtor's assets, rights, obligations or liabilities is stayed;

(b) execution against the debtor's assets is stayed;

(c) the right to transfer, encumber or otherwise dispose of any assets of the debtor is suspended; and

(d) section 21 of the Insolvency Act, 1936 (Act 24 of 1936), applies with regard to assets situated in the Republic to the same extent as it would have if the debtor had been sequestrated by a court.

(2) The scope, and the modification or termination, of the stay and suspension referred to in subsection (1) are subject to sections 20, 23 and 75 of the Insolvency Act, 1936, and sections 341 and 359 of the Companies Act, 1973 (Act 61 of 1973), and the court may, at the request of the foreign

representative or a person affected by subsection (1), modify or terminate the scope of the stay and suspension.

(3) Subsection (1) (a) does not affect the right to commence individual actions or proceedings to the extent necessary to preserve a claim against the debtor.

(4) Subsection (1) does not affect the right to request the commencement of proceedings under the laws of the Republic relating to insolvency or the right to file claims in such proceedings.]

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?

[Director Liability = Business Judgment Rule

The directors owe a duty of loyalty to the corporation's best interest. The directors for Delaware Corporation duties are owed to the corporation and its shareholders and not the creditors, even in the event that the company is potentially insolvent and therefore the shareholders stand to receive nothing in the bankruptcy. The Delaware Supreme Court has confirmed that all suggestions that directors owes duties to creditors whenever a company is trading "in the zone of insolvency", or is actually insolvent.]

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 following claim requirements is to be met by a creditor in order for them to qualify as a petitioning creditor:

- The creditor holds a claim against the debtor that (a) is "not contingent as to liability or the subject of a bona fide dispute as to liability or amount" and (b) equals at least \$15.32.
- The creditor demonstrates that the debtor is "generally not paying the debts as such debts become due"
- An involuntary petition may be filed by a single qualifying creditor (if the debtor has less than 12 qualifying creditors).

A creditor must file a proof of claim on or before the bar date set by the court.]

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

Question 4.1 [5 marks]

Commented [H(42)]: Total marks 3/4

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

Commented [H(44)]: Correct, 1 mark, also they have a duty of care

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

Commented [H(46)]: Total marks 2.25/5

Commented [H(47)]: Correct, 1 mark, that is it does not depend on the occurrence of a future event

Commented [H(48)]: Correct, 1 mark, the test is whether there is an objective basis in fact or law to dispute liability

Commented [H(49)]: Incorrect, the claims must total \$16,750 and they must be unsecured or undersecured

Commented [H(50)]: Correct, 1/4 mark, alternately they can allege that a custodian has been appointed over the debtor's assets

Commented [H(51)]: Total marks 2/15

Commented [H(52)]: Total marks 0/5

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?

[Type your answer here]

Question 4.2 [5 marks]

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?

[This would be a **foreign non-main proceeding** due to the **COMI being in Italy.**]

Question 4.3 [5 marks]

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, the contract has not yet been fully performed and/or executed, seeing that it is a 10 year exclusive license with still seven (7) years to go.]

Commented [H(53)]: Total marks 1/5

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

Commented [H(55)]: Incorrect, the facts are unlikely to overcome the presumption in favor of France as the COMI and there is an establishment in England so non-main recognition is appropriate.

Commented [H(56)]: Total marks 1/5

Commented [H(57)]: Correct, 1 mark, one side has to pay royalties and the other side has to maintain exclusivity

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

[GameMart can transfer the license as part of the 363 sale because it is owed by the debtor(GameMart), therefore it is protected and may not be terminated in connection with the sale of the intellectual property without their consent]

Commented [H(58): Incorrect, because the owner of the patent isn't the debtor, the licensee isn't protected by 365(n). Instead, IP law entitles the owner to object to performance by another party and therefore its consent is required.

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

[They cannot transfer the lease as part of 363 sale without the Land Corp's consent. The landlord approval provision.]

Commented [H(59): Incorrect, the landlord approval provision is not effective in bankruptcy.

* End of Assessment *