



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

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)]: 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

When does an automatic stay come into effect?

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

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

Question 1.9

Which of the following regarding substantive consolidation is true?

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

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

Question 1.10

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

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

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QUESTION 2 (direct questions) [10 marks]

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

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 to permit a creditor holding a claim against a debtor and owing money to the debtor to net out the two (or more) obligations. There is no permission to exercise the setoff right in many cases because a creditor owing money to the debtor can improve its position by exercising the setoff right and such exercise can decrease obligations to the estate by the full amount owed by the debtor.]

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

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

Question 2.2 [2 marks]

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

[The Bankruptcy Rules, the Federal Rules of Civil Procedure, the local rules of the bankruptcy court and the judge's personal practice should be reviewed. It may be useful to consult with a local practitioner.]

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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 1.5/2

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

[The payment in full to be completed prior to the next categories is required, but the deviation is permitted when the affected creditors give the consent.]

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Commented [H(24)]: Correct, 1/2 mark, though this can only happen in a chapter 11 plan

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?

[Priming lien is to give the senior or equal priority to a pre-petition lien on the debtor's property for the security of the post-petition financing. The protection of the interest of such secured creditor must be demonstrated by the debtor.]

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Commented [H(27)]: Correct, 1/2 mark, also the financing must not be available without the priming lien

Question 2.5 [3 marks]

Commented [H(28)]: Total marks 2/3

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 to return to the debtor from a receiver who receives the debtor's property in a doubtful period before the filing date. It is required to prove if its amount

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

is more than the amount which such receiver would have received under the chapter 7 procedure, but there is no requirement to prove any fault of either the debtor or the receiver.]

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

Commented [H(32)]: Correct, 1/2 mark, the recipient must have been a creditor of the debtor and the transfer made on account of an antecedent debt

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

Commented [H(33)]: Total marks 12.5/15

Question 3.1 [3 marks]

Commented [H(34)]: 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?

[A bankruptcy may order a final order if the parties consent to the entry of the final orders. The district court or the Bankruptcy Appellate Panel (in certain circumstances) reviews the appeals from the bankruptcy court. Conclusions of law de novo and findings of fact for abuse of discretion are reviewed by the district court or the Bankruptcy Appellate Panel.]

Commented [H(35)]: Correct, 1/2 mark, and on certain core matters such as a challenge to a petition

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

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

Commented [H(38)]: This is only for review of final orders, non-final orders are treated as a report and recommendation.

Question 3.2 [3 marks]

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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?

[When a foreign main proceeding is recognised, the following provisions shall be automatically applied;

- (i) automatic stay;
- (ii) operation of the debtor's business in the ordinary course by the foreign representative;
- (iii) sale, transfer or use of property outside the ordinary course; and
- (iv) avoidance of post-petition transfers and post-petition perfection of security interests.

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

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

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

When a foreign main or non-foreign main proceeding is recognised, the following relief may be given on a discretionary basis;

- (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 purpose of [chapter 15] and to protect the assets of the debtors or the interests of creditors".]

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

Question 3.3 [4 marks]

Commented [H(46)]: 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 duties to the Delaware corporation and its shareholders as fiduciary duty of loyalty and a duty of care. On the other hand, according to the Delaware Supreme Court, when a Delaware corporation is actually insolvent, the directors owe duties to its creditor. Business judgement rule, which gives the presumption that board of directors has acted in good faith with the reasonable information, protects director's liability from errors of judgement. Unless this presumption is rebutted, the director will owe the liability caused by its misjudgement.]

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

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

Commented [H(50)]: Incorrect, the duty remains owed to the corporation and its shareholders

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

Question 3.4 [5 marks]

Commented [H(52)]: Total marks 4.5/5

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

[To qualify as a petitioning creditor, there are the following requirements;

- (i) the number of petitioning creditors is three or more or if the number of all creditors is less than 12, only one;
- (ii) its claims are non-contingent, including unmatured claim;
- (iii) its claims are not subject of bona fide dispute as to liability or amount (if the amount of claim is disputed but the undisputed amount is over threshold as below, this requirement is met); and
- (iv) its claims are unsecured or undersecured, separately, aggregating USD 16,750.]

Commented [H(53)]: Correct, 1 mark, the claim may not be dependent on a future event

Commented [H(54)]: Correct, 1 mark, to be a bona fide dispute, there must be an objective basis in fact or law

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

Commented [H(56)]: Correct, 1/2 mark, also the creditors must allege that the debtor is not paying its debts as they come due or has had a custodian appointed over its assets

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

Commented [H(57)]: Total marks 7.5/15

Question 4.1 [5 marks]

Commented [H(58)]: Total marks 4.5/5

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

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

[The Chapter 11 petition cause the effect of automatic stay, which provides the debtor with the breathing space to make a reorganisation plan and negotiate with creditors. Under the automatic stay, the lessor cannot pursue its delinquent lease fee to Speculation Inc. Also, the employment discrimination may be suspended because the litigation on pre-petition claim is prohibited under the automatic stay. On the other hand, as the DOJ investigation is subject to the certain statutory exception, there is no effect of automatic stay. Similarly, the secured creditor can exercise its rights under the security contract because such contract is subject to the exception of automatic stay.]

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

Commented [H(60)]: Correct, 1/2 mark, also the landlord cannot pursue eviction

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

Commented [H(62)]: Correct, 1 mark

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

Question 4.2 [5 marks]

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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?

[To recognise a foreign proceeding under Chapter 15, the proceeding must be "a collective judicial or administrative proceeding in a foreign country, including an interim proceeding, under a law relating to insolvency or adjustment of debt 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". As English scheme of arrangement is included in such definition, this proceeding could be recognised under Chapter 15.

To recognise the English scheme of arrangement as foreign main proceeding, whether England is Stella's centre of main interests (COMI) is important. Although a place of incorporation is presumed as the debtor's COMI, in considering Stella's COMI other factors should be considered because its place of incorporation is France, not England. The following factors as the determination of COMI are analysed;

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

- (i) location of headquarters
- (ii) location of management;
- (iii) location of primary assets;
- (iv) location of majority of creditors, including those who will be affected by the proceeding; and
- (v) jurisdiction whose law will apply to most disputes.

Although Stella's headquarter is in Paris, its products are made in Italy and its retail shops are located in several countries, its retail shops are also located in England. In addition, Stella's liabilities, bank loans and Eurobonds, to be restructured are governed by English law. Therefore, it is possible to recognise the English scheme of arrangement as foreign main proceeding, but we have to consider other factors in detail.]

Commented [H(66)]: Incorrect, the COMI analysis has to look to all creditors, not just the ones affected by the scheme. On these facts, the presumption in favor of France is unlikely to be rebutted. Because COMI is in France, not England, recognition as foreign main is inappropriate. Instead, foreign non-main recognition is appropriate and the retail store in England qualifies as the necessary establishment.

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?

[No, license granted by ToyCo is not assignable nor continuable without the licensor's consent.]

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

[Yes, GameMart can transfer the Xblox license as part of 363 sale without ToyCo's consent because Xblox is the most important product for GameMart and the license contract with ToyCo is required to operate GameMart's business as key contract.]

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

[Yes, GameMart transfer the factory lease, which is indispensable for the company's business operation, as part of 363 sale without Land Corp's consent, though the lease agreement requires GameMart to transfer it with Land Corp's consent. It is for reasons why 363 sales provision can permit the debtor to assign its property absent licensor consent.]

* End of Assessment *

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

Commented [H(68)]: You're answering the wrong question here. The license is an executory contract because both sides have ongoing obligations to pay royalties and maintain exclusivity.

Commented [H(69)]: Incorrect, the licensor's consent is required under substantive IP law.

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

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