



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

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

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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

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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

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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

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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

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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

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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

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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

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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

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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

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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

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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]

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Question 2.1 (1 mark)

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

Where a creditor holds a claim against the debtor and simultaneously owes money to the debtor, setoff allows the creditor to net out the two obligations. Setoff is not permitted in many circumstances because it allows the creditor to improve his/her position relative to other unsecured creditors who are not owed money by the debtor. This occurs as the setoff decreases the obligation of the debtor to the estate by the full amount owed by the debtor, as opposed to the lesser amount the debtor would pay on the unsecured claim, ie, the creditor who exercises setoff would recover more from the debtor than other unsecured creditors compared to if the debtor's assets were distributed among the unsecured creditors.

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Question 2.2 [2 marks]

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

When preparing a filing for a bankruptcy court, one should review the Federal Rules of Bankruptcy Procedure (the Bankruptcy Rules). The Bankruptcy Rules often incorporate by reference the Federal Rules of Civil Procedure. Additionally, one should review the local rules of the bankruptcy court as well as the personal practices of the judge involved, because each bankruptcy court will have local rules of procedure and each judge issues personal practices (which may be found on the website of the bankruptcy court).

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Question 2.3 [2 marks]

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

The absolute priority rule requires that payment must be made in full to each category of claims before payment is made to the next category, according to the statutorily prescribed priorities. The absolute priority rule may be departed from in a chapter 11 plan with the consent of creditors who are affected. However, deviation from the absolute priority rule is not permitted in a chapter 7 liquidation, whereby the statutory priorities must be strictly followed.

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Question 2.4 [2 marks]

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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 lien on property that is senior to, or has equal priority to, an existing pre-petition lien on the same property of the estate, in order to secure post-petition financing.

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In order for a "priming lien" to be granted to secure debtor-in-possession ("DIP") financing, the debtor must be unable to obtain financing on any of the following terms:

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- (1) obtaining unsecured credit in the ordinary course of business without court approval, with the debt being granted administrative priority expense;
- (2) obtaining unsecured credit outside the ordinary course of business with court approval after notice and a hearing, with the debt having administrative expense priority; and
- (3) upon showing that the debtor is unable to secure financing under (1) and (2), by obtaining the court's authorisation, after notice and a hearing, to incur:
 - (a) unsecured debt having priority ahead of all other administrative expenses;
 - (b) secured debt with a lien on unencumbered estate property; or (c) secured debt with a junior lien on encumbered estate property.

Additionally, the debtor must demonstrate the interest of the secured creditor being primed is adequately protected.

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Question 2.5 [3 marks]

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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 refers to the transfer of the debtor's property during a suspect period before the petition date, whereby the property must be returned to the estate if it exceeds the amount the recipient would have received in a chapter 7 liquidation had the transfer not been made.

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The elements of a preference claim that need to be proved are: (1) a transfer of property in which the debtor has an interest; (2) the transfer must be to or for the benefit of a creditor; (3) the transfer must be for or on account of an antecedent debt owed by the debtor before such transfer was made; (4) the transfer must be made while the debtor was insolvent; (5) the transfer must be made during the suspect period (which is 90 days prior to the petition date for transfers to third parties and one year prior to the petition date for transfers to insiders); and (6) the transfer must enable the creditor to receive more than it would have in a chapter 7 liquidation.

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It is not necessary to show any fault on either the debtor's part or the recipient's part in relation to the preference / transfer having been made.

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

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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?

A bankruptcy court may enter a final order in core proceedings, where such an order would not invade Article III jurisdiction (*Stern v Marshall* 564 US 462 (2011)). A bankruptcy court may exercise a district court's delegated authority to enter a final order on a motion challenging the validity of a petition. A bankruptcy court may also enter a final order with the consent of the parties (*Wellness Int'l Network v Sharif* 135 S Ct 1932 (2015)).

Appeals against decisions of the bankruptcy court are generally heard by the district court for the district in which they sit. However, in certain circuits bankruptcy appeals are heard by a Bankruptcy Appeal Panel ("BAP"), convened from judges of the bankruptcy courts within the circuit. These include the first, sixth, eighth, ninth, and tenth circuits which have elected to form Bankruptcy Appellate Panels. From the district court or BAP, there is a further appeal of right (assuming the initial order was one from which an appeal was available as of right) to the circuit court of appeals. In rare circumstances, an appeal against a bankruptcy court order may go directly to the court of appeals if the bankruptcy court or district court certifies that either: (1) 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 the resolution of conflicting controlling decisions; or (2) an immediate appeal may advance the progress of the case materially.

Non-final orders (or interlocutory orders) may only be appealed with the leave of the appellate court, save that orders extending the period of exclusivity to propose a plan are appealable as of right. If the ruling below was in a core proceeding over which the bankruptcy court had authority to enter a final order, the district court or BAP reviews conclusions of law on a *de novo* basis and reviews findings of fact for abuse of discretion. Contrarily, if the ruling was in a non-core proceeding or the bankruptcy court did not otherwise have authority to enter a final order, the district court or BAP reviews all findings of fact and conclusions of law to which a party has objected on a *de novo* basis.

Question 3.2 [3 marks]

What provisions of the Bankruptcy Code automatically apply to the debtor's property within the territorial jurisdiction of the United States upon recognition of a foreign main proceeding? What relief may be granted on a discretionary basis for either foreign main or non-main proceedings?

The provisions that automatically apply to the debtors property within the territorial jurisdiction of the United States upon recognition of a foreign proceeding that is a foreign main proceeding may be found in s 1520 of the Bankruptcy Code. In particular, the following apply to the debtor's property situated within the territorial jurisdiction of the United States, upon recognition of a foreign main proceeding: (1) automatic stay

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(see also s 362 of the Bankruptcy Code); (2) operation of the debtor's business in the ordinary course by the foreign representative; (3) sale, transfer or use of property outside the ordinary course (see also s 363 of the Bankruptcy Code); and (4) avoidance of post-petition transfers and post-petition perfection of security interests (see also s 549 of the Bankruptcy Code).

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Following the recognition of either foreign main or non-main proceedings, the relief that may be granted on a discretionary basis for either foreign main or non-main proceedings is set out under s 1521 of the Bankruptcy Code. In particular, the following relief may be granted on a discretionary basis: (1) authorisation of discovery regarding the debtor's assets and affairs; (2) entrusting administration of the debtor's assets in the US to the foreign representative or other person; (3) extension of provisional relief; and (4) any other relief necessary to effectuate the purposes of chapter 15 and to protect the assets of the debtor or the interests of creditors. A court may also provide additional assistance under the Bankruptcy Code or other US law consistent with the principle of comity and the values underlying the Bankruptcy Code.

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Question 3.3 [4 marks]

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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?

A director of a Delaware corporation owes to the corporation a fiduciary duty of loyalty to act in the corporation's best interest, as well as a duty of care to make educated decisions.

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A director of a Delaware corporation owes these duties to the corporation and its shareholders, and not to creditors, even where the corporation is potentially insolvent such that the shareholders stand to receive nothing in bankruptcy. In *North Am Catholic Educational Programming Foundation, Inc v Gheewalla*, 930 A.2d 92, 103 (Del 2007), the Delaware Supreme Court put to rest any suggestion that directors owe duties to creditors when a company is operating in the realm of insolvency or is actually insolvent. The Delaware Supreme Court observed that individual creditors of an insolvent corporation have no right to assert direct claims for breach of fiduciary duty against corporate directors, but creditors may nonetheless protect their interest by bringing derivative claims on behalf of the insolvent corporation.

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The business judgment rule protects directors from liability for making errors of judgment. Under this rule, the board of directors is presumed to have acted in good faith, and on the basis of reasonable information. This presumption can be rebutted only by showing that a majority of the board of directors: (1) were in fact not reasonably informed; (2) did not honestly believe that their decision was in the corporation's best interest; or (3) were not acting in good faith. Unless the presumption is rebutted, the directors will not be liable except where it is shown that

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there was gross negligence. It bears noting, however, that the business judgment rule does not apply where a transaction is approved by a majority of the board of directors that is not disinterested and independent, or a controlling shareholder who is on both sides of the transaction.

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 requirements must be satisfied by a creditor's claim in order for the creditor to qualify as a petitioning creditor in an involuntary proceeding.

First, the creditor's claim must be non-contingent. In other words, it cannot be a claim which is dependent on the occurrence of a future event, such as a claim under a guarantee which is contingent on the occurrence of a default under the guaranteed obligation.

Second, the claim cannot be the subject of a bona fide dispute as to liability or amount. A bona fide dispute would exist if there is an objectively reasonable basis for a dispute as a matter of fact or law. In this regard, the debtor's subjective belief that the debt is not owed or that the amount claimed is incorrect does not suffice to constitute a bona fide dispute. Moreover, it bears noting that if only a portion of the amount claimed is disputed, the creditor cannot use the undisputed portion to reach the monetary threshold of USD 16,750. However, a dispute as to one claim does not disqualify the application of other undisputed claims held by the same creditor to meet the requirements of the creditor's claim for the creditor to qualify as a petitioning creditor.

Third, the debt must be unsecured or under-secured, separately or in the aggregate with all other petitioning creditors' claims, in the amount of at least USD 16,750 (which amount may be periodically increased due to inflation).

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

Question 4.1 [5 marks]

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.

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Commented [H(58): Correct, 1 mark

Commented [H(59): Correct, 1/2 mark

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

Commented [H(61): Correct, 1 mark, also the creditor must allege that the debtor is not paying debts as they come due or has had a custodian appointed over its assets.

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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?

Upon a chapter 11 petition being filed by Speculation Inc, generally speaking, an estate is created consisting of all of Speculation Inc's property interests as of the petition date. The estate of Speculation Inc will be protected by a worldwide automatic stay of creditor enforcement proceedings under s 362 of the Bankruptcy Code, which comes into effect immediately upon the filing of any plenary petition and provides Speculation Inc with breathing space to formulate a restructuring plan, negotiate with creditors, and realise the value of its assets in an orderly process in order to pay the claims of its creditors. An act taken in violation of the stay constitutes contempt of court, and is void or voidable. This response will proceed to examine the specific effect of a Chapter 11 petition being filed on the three identified scenarios.

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DOJ Investigation

The stay of proceedings under s 362 of the Bankruptcy Code is subject to statutory exceptions, including criminal proceedings and regulatory investigations. In the present case, it is further stated that the DOJ's investigation pertains to whether Speculation Inc's success was attributable to illegally trading on insider information. Thus, it appears likely that the DOJ investigations would constitute criminal (or pseudo-criminal) proceedings and/or regulatory investigations. Accordingly, it is likely that the DOJ investigations would not be affected by the stay of proceedings.

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Margin loan default

In relation to the margin loan default, the issue appears to be whether Speculation Inc's broker (the "Broker") can, having declared a default on the margin loan, recover the loan it extended to Speculation Inc. In this regard, s 362 of the Bankruptcy Code specifically prohibits any attempt to collect on pre-petition claims, including through demand letters or calls. Thus, it is likely that any attempt by the Broker to recover the loan extended on the basis of default by Speculation Inc would be prohibited by the stay of proceedings. It is also likely that the Broker would not be able to obtain possession of the shares.

However, it is stated in this case that the shares which Speculation Inc has purchased using the loans obtained from the Broker are held as collateral presumably by the Broker. In this regard, the Bankruptcy Code specifically prohibits any attempt to obtain possession or control of property of the estate. Thus, it is likely that the Broker cannot obtain control of the shares. However, the stay of proceedings under s 362 of the Bankruptcy Code is subject to the exercise of rights under a commodity, forward or security contract. Thus, more information would be required to determine if the loan agreement between the Broker and Speculation Inc is a security contract within the meaning contemplated in the Bankruptcy Code.

Commented [H(66)]: Correct, 1/2 mark, a margin loan is a securities contract so the broker would be able to liquidate the collateral

Delinquent lease

In relation to the delinquent lease, the issue appears to be what remedies are available to the landlord in relation to Speculation Inc's failure to pay rent. In this regard, the stay of proceedings does not affect the landlord's right to evict the debtor-tenant from non-residential property where the lease has expired. In this case, Speculation Inc has rented office space, which is likely to be non-residential property. However, it is only stated that Speculation Inc has fallen behind on its rental payments, but not that the lease has expired. Thus, more information is required to determine if the lease has expired. For instance, there may be a clause in the tenancy agreement which provides that the lease would expire if rental payments remain unpaid for a certain amount of time. However, as the stay of proceedings prohibits any attempt to collect on pre-petition claims, it is likely that the landlord would not be able to recover rental payments which have fallen due from Speculation Inc.

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Employment discrimination lawsuit

The effect of the filing of a chapter 11 on the employment discrimination lawsuit is that the employment discrimination law suit would likely be stayed under s 362(a) of the Bankruptcy Code. The ambit of s 362(a)(1) is extremely wide, providing that it operates as a stay applicable to all entities of "the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title...". Such a broad definition would likely include a discrimination lawsuit against the company.

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Notably, in *Equal Employment Opportunity Commission v. Tim Shepherd, M.D., P.A. and Bridges Healthcare, P.A.*, Civil Action No. 4:20-cv-60-SDJ, a Texas federal court ruled that the filing for bankruptcy did not automatically stay a lawsuit brought by the EEOC against the debtor company, as the EEOC fell under the exception to the Bankruptcy Code's automatic stay provision where a governmental unit brings an action to enforce its policy and regulatory power. What sets the present case apart, however, is that the employee here appears to be suing in her personal capacity, and therefore likely cannot rely on the regulatory investigations exception under the Bankruptcy Code. Thus, it is likely that the employment discrimination lawsuit against Speculation Inc will be stayed under s 362 of the Bankruptcy Code.

Question 4.2 [5 marks]

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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?

The English Scheme of Arrangement may be recognised by a US bankruptcy order under Chapter 15 upon the satisfaction of several requirements.

First, a case under chapter 15 is commenced only by the filing of a petition by the foreign representative of the debtor, and the debtor cannot be placed in a chapter 15 proceeding involuntarily by a creditor filing (s 151(a) of the Bankruptcy Code). Thus, a foreign representative representing Stella must commence chapter 15 proceedings by filing a petition.

To obtain recognition of the English scheme of arrangement, the foreign representative must establish that a foreign court or administrative proceeding with respect of Stella is pending, and that the foreign representative is empowered to act by the proceeding (s 101(23) of the Bankruptcy Code). In this regard, a foreign proceeding is defined under s 101(23) of the Bankruptcy Code as "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". In the present case, an English scheme of arrangement would likely fall within the definition set out in s 101(23) of the bankruptcy Code, since it is a collective judicial or administrative proceeding outside of the US, where the assets and affairs of Stella would be subject to the control or supervision of the English court, for the purpose of reorganising Stella's debts. Unless the English scheme of arrangement is somehow manifestly contrary to US public policy, it is likely to be recognised under chapter 15.

*Whether the English scheme of arrangement is recognised as a foreign main proceeding or a foreign non-main proceeding depends on a number of factors. Foreign main proceedings are proceedings commenced in Stella's centre of main interests ("COMI"). Under s 1516(c) of the Bankruptcy Code, it is provided that in the absence of evidence to the contrary, the debtor's registered office is presumed to be the COMI of the debtor (i.e, its place of incorporation). Other relevant factors in determining the COMI of Stella include: (1) the location of its headquarters; (2) the location of its management; (3) the location of its primary assets; (4) the location of a majority of its creditors or a majority of the creditors that will be affected by the relief requested by the foreign representative; and (5) the jurisdiction whose law will apply to most disputes (*In re SPhinX Ltd*, 351 BR 103, 117).*

In the present case, Stella is incorporated in France with its headquarters in Paris. A rebuttable presumption thus arises that Stella's COMI is France. In the absence of any information as to where its management is located, it would be reasonable to assume that Stella's management is located in France as well, with its headquarters.

As for the location of its primary assets, Stella's products are made in Italy and shipped to retail stores in Europe, Asia and North America, which is inconclusive.

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

Third, Stella receives its funding from a bank loan and Eurobonds, both of which are governed by English law. Thus, the UK will likely be the jurisdiction whose law will apply to most disputes involving Stella and its creditors. On the facts, it is unclear where the majority of Stella's creditors are located - while the loan and the Eurobonds are governed by English law, it cannot be concluded on that basis that those creditors are based in the UK.

On the whole, it is submitted that it appears that Stella's COMI is France, given that there is a presumption that France is Stella's COMI which has not been rebutted by the other factors. Moreover, Stella's operations appear to be based primarily in France. The only factor pointing in favour of UK as the COMI is that the bank loan and Eurobonds are governed by English law, which, in my view, is insufficient to rebut the presumption. It follows that the proceeding will be recognised as a foreign non-main proceeding, since it will be commenced in the UK, a jurisdiction that is not Stella's COMI.

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

It bears noting in this regard that proceedings in a jurisdiction other than Stella's COMI can be recognised as foreign non-main proceedings only if Stella had an establishment in that jurisdiction, *ie*, a place where it carried out non-transitory economic activity, prior to the commencement of chapter 15 proceedings (see s 1502(2) of the Bankruptcy Code). In the present case, this would not prevent the recognition of the English scheme of arrangement as a foreign non-main proceeding since Stella has retail stores in England, where it carries out non-transitory economic activity, *ie*, the sale of its products.

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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 refers to a contract where there are material unperformed obligations on both sides. In the present case, GameMart's 10-year exclusive license to manufacture Xblox is an executory contract. On GameMart's end, GameMart has an obligation to pay ToyCo monthly royalties, which is an unperformed obligation. On ToyCo's end, ToyCo has an obligation not to grant the license to manufacture Xblox to

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

other companies, because GameMart has an exclusive license to do so. Thus, there are material unperformed obligations on both sides.

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

GameMart cannot transfer the license to manufacture Xbox (the "Xbox license") as part of a 363 sale without ToyCo's consent. As stated in *In re Trump Entertainment Resorts Inc*, 526 BR 116, federal trademark law generally bans the assignment of trademark licenses absent the licensor's consent. Thus, the 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. In the present case, the Xbox is covered by several US patents. Accordingly, the Xbox license cannot be assigned without the consent of ToyCo, the licensor.

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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?**

It is likely that GameMart can transfer the factory lease as part of a 363 sale without the consent of Land Corp.

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First, the lease between GameMart and Land Corp is an executory contract, as there are material unperformed obligations on both sides. As there are seven years to go on the lease, Land Corp remains under an obligation to make the factory premises available to GameMart, while GameMart has an ongoing obligation to make rental payments to Land Corp.

Second, Correct, 1 mark and it is therefore likely that GameMart can transfer the factory lease as part of a 363 sale without the consent of Land Corp, the landlord.

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

* End of Assessment *