



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 3B
THE INSOLVENCY SYSTEM OF THE UNITED KINGDOM
(ENGLAND AND WALES)

This is the **summative (formal) assessment** for **Module 3B** 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 3B. 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.assessment3B]**. An example would be something along the following lines: 202223-336.assessment3B. **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 “studentID” 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 3B 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 3B 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 **8 pages**.

ANSWER ALL THE QUESTIONS

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

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**

Commented [WA1]: 44/50 = 88% a very good effort

Commented [WA2]: 9/10 Very good

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

Please select the **most correct ending** to the following statement:

The Administration (Restrictions on Disposal etc to Connected Persons) Regulations 2021 restrict pre-pack sales which constitute a substantial disposal of the company's property to connected parties where the disposal occurs . . . :

- (a) within 10 weeks of the commencement of the administration.
- (b) within 8 weeks of the commencement of the administration.**
- (c) within 4 weeks of the commencement of the administration.
- (d) on the day the company enters administration.

Question 1.2

What is the **maximum length** of a Moratorium under Part 1A of the Insolvency Act 1986 to which creditors can consent without any application to the court?

- (a) 40 business days.
- (b) One year and 20 business days.
- (c) One year and 40 business days.
- (d) One year.**

Question 1.3

Which of the following **is not** a requirement for a company that wishes to enter into a Restructuring Plan under Part 26A of the Companies Act 2006?

- (a) The company has encountered, or is likely to encounter, financial difficulties that are affecting, or will or may affect, its ability to carry on business as a going concern.
- (b) A compromise or arrangement is proposed between the company and its creditors, or any class of them, or its members, or any class of them.
- (c) The purpose of the compromise or arrangement is to eliminate, reduce or prevent, or mitigate the effect of, any of the said financial difficulties.
- (d) The company is, or is likely to become, unable to pay their debts, as defined under section 123 of the Insolvency Act 1986.**

Question 1.4

In cases where the Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021 apply and an independent report from an Evaluator is obtained, the independent report must be obtained by whom?

- (a) The administrator.
- (b) Any secured creditor with the benefit of a qualifying floating charge.
- (c) The purchaser.
- (d) The company's auditor.

Commented [WA3]: It is the purchaser who must obtain the report

Question 1.5

Which one of the following **is not** a debtor-in-possession procedure?

- (a) Administration.
- (b) Restructuring Plan.
- (c) Scheme of Arrangement.
- (d) Company Voluntary Arrangement.

Question 1.6

A liquidator may pay dividends to small value creditors based upon the information contained within the company's statement of affairs or accounting records. In such circumstances, a creditor is deemed to have proved for the purposes of determination and payment of a dividend where the debt is **no greater than how much?**

- (a) GBP 500
- (b) GBP 750
- (c) GBP 1,000
- (d) GBP 2,000

Question 1.7

Which one of the following **is not**, in itself, a separate ground for disqualification of a director under the Company Directors Disqualification Act 1986?

- (a) Wrongful trading.
- (b) Breach of fiduciary duty.
- (c) Being found guilty of an indictable offence in Great Britain.
- (d) Being found guilty of an indictable offence overseas.

Question 1.8

The administrator is under a general duty to provide a statement for creditors' consideration setting out proposals for achieving the purpose of administration. He or she must obtain a creditors' decision on whether or not to approve the proposals **within how many weeks** of the date the company entered administration?

- (a) 6
- (b) 8
- (c) 10**
- (d) 12

Question 1.9

Which of the following statements is **incorrect**?

- (a) An insolvency officeholder from an EU Member State will be automatically recognised by the courts in the UK whether the officeholder was appointed before or after Brexit.**
- (b) An insolvency officeholder from an EU Member State is automatically recognised by the courts in the UK if appointed before Brexit.
- (c) An insolvency officeholder from an EU Member State appointed after Brexit may apply to a UK court for recognition under the Cross Border Insolvency Regulations.
- (d) An insolvency officeholder from an EU Member State cannot apply to a UK court for recognition under section 426 of the Insolvency Act 1986.

Question 1.10

Under section 216 of the Insolvency Act 1986, a director of a company which has been wound up insolvent may not, unless an exception applies, be a director of a company that is known by a prohibited name **for what period of time**?

- (a) 6 months.
- (b) 12 months.
- (c) 2 years.
- (d) 5 years.**

QUESTION 2 (direct questions) [10 marks]

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Question 2.1 [maximum 5 marks]

Commented [WA5]: 3/5

Who may bring an action under: (i) section 423 of the Insolvency Act 1986; (ii) section 6 of the Company Directors Disqualification Act 1986; and (iii) section 246ZB of the Insolvency Act 1986?

- (i) In case of winding up and administration, the official receiver, the liquidator, the administrator and victim of the transaction with leave of the court (e.g. creditor) may bring an action. In case of Company Voluntary Arrangement, the CVA's supervisor and victim may bring an action. In other cases, a victim of the transaction may bring an action.
- (ii) The Insolvency Service which employs the Official Receivers
- (iii) Liquidator of a company

Commented [WA6]: The action is brought by the Secretary of State or an OR on the instructions of the Secretary of State

Commented [WA7]: This provision only applies to an administrator

Commented [WA8]: 5/5

Question 2.2 [maximum 5 marks]

List any **five (5)** of the debts which do not form part of the payment holiday under Part A1 of the Insolvency Act 1986 when a company is subject to a Moratorium.

- (1) Remuneration or expenses of the monitor
- (2) Goods or services supplied during the Moratorium
- (3) Rent payable during the Moratorium
- (4) Wages or salary payable to employees under contract of employment
- (5) Redundancy payment payable to employees

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

Commented [WA9]: 14/15

Question 3.1 [maximum 6 marks]

Commented [WA10]: 6/6 VG

Can an administrator who wishes to continue to operate the business of the company in administration require suppliers of goods and services to continue to supply those goods and services during the administration?

In considering whether suppliers are required to supply goods and services to administrator, the focus is on how an administration would affect executory contracts of the company. Once an administrator is appointed, the company's executory contracts would not be terminated automatically. It is usual to have terms in contracts providing for automatic termination but those terms are now subject to increasing statutory exception making them void.

Administrator who wishes to continue to operate the company needs certain essential supplies and it is protected under Section 233 of the Insolvency Act 1986 ("the Act") covering supply of gas, electricity, water and communication services. Suppliers are not permitted to require settlement of outstanding debts in order to give new or continued supply but administrator may be required to give personal guarantee for payment of charges in respect of the supply.

Under Section 233A of the Act, supplier is also barred from relying on "insolvency-related term" in the contract to terminate, alter the contract, etc. By adding Section 233B to the Act, supplier of goods or services are prohibited from terminating or doing any other thing in relation to the contract in case of formal insolvency procedure.

Under Section 233B, conditions such as payment of pre-insolvency arrears and charging higher prices are prohibited, in addition to insist a personal guarantee from the administrator (which was permitted under Section 233).

Question 3.2 [maximum 9 marks]

Commented [WA11]: 8/9 VG but no mention of the position of fixed charge holders

Explain the order of priority of payments in a liquidation and explain the nature of the rights enjoyed by each class of creditor or expense. How would this priority change if the company had been subject to a Moratorium under Part A1 of the Insolvency Act 1986 during the 12 week period prior to the commencement of the liquidation?

Generally, priority of payments in a liquidation is in the following order :

1. Expenses of winding up, including liquidator's remuneration : Under Section 115 of the Insolvency Act 1986 ("the Act"), certain expenses are given priority over preferential creditors, etc. Such expenses, in order of priority, include expenses properly incurred by liquidator in preserving and realizing assets, costs of security, amount payable for preparation of statement of affairs or accounts, necessary disbursements of liquidator in the course of winding up, remuneration of any person employed by liquidator, remuneration of liquidator, etc.
2. Preferential creditors : They mainly include limited claims of employees and certain statutory liabilities, etc. which are divided into ordinary and secondary preferential debts. Ordinary preferential debts are to be paid before secondary ones. Debts in the same category rank equally among themselves and would be paid in pari passu manner in case there is insufficient assets for distribution.
3. Floating charge holder : Should there be more than one floating charge holder, they would be paid in accordance with the order of creation. Before payment, liquidator is required to consider Section 176A of the Act if the floating charge was created on or after 15 September 2003 as the liquidator has to make a "prescribed part" of the company's net property available for unsecured creditors. The amount of "prescribed part" depends on whether the company's net property exceed GBP 10,000.
4. Unsecured creditors and shareholders : After payment of the above, remaining assets would be distributed to unsecured creditors and then shareholders (on pro rata basis of shareholdings).

The above priority would change if the company had been subject to a Moratorium under Part A1 of the Act during the 12 week period prior to the commencement of the liquidation.

Under Section 174A of the Act, (1) any prescribed fees or expenses of the official receiver acting in any capacity in relation to the company and (2) **moratorium debts and priority pre-moratorium debts** are payable out of the company's assets in preference to all other claims. As a result, certain unsecured debts would be given "super priority" in the liquidation subsequent to a Moratorium.

However, such "super priority" would not be acquired by accelerated debt, i.e. pre-moratorium debt that fell due during the relevant period by reason of the operation of, or the exercise of rights under, an acceleration or early termination clause in a contract or other instrument involving financial services (Section 174A(4) of the Act).

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

Commented [WA12]: 13/15

Prior to going into compulsory liquidation on 23rd December 2022, under pressure from its bank, Fretus Bank plc, and in order to prevent it from demanding repayment of the company's loans, Marbley Q Limited ("the Company"), granted a debenture in favour of Fretus Bank plc in February 2022. The debenture contained a floating charge over the whole of the Company's undertaking.

The winding up order followed a creditor's winding up petition issued on 14th October 2022.

In July 2022, as the Company continued to suffer cash flow problems, the directors approved the sale of two (2) marble cutting machines to Rita Perkins (a director) for GBP 10,000 in cash. The machines had been bought for GBP 25,000 a year before.

A month before the winding up order was made, Rita Perkins received an email from Hard and Fast Ltd, one of the Company's key suppliers. The supplier demanded immediate payment of all sums owing to it and informed the Company that further supplies would only be made on a cash on delivery basis. As the continued supply of marble was seen as essential by the Company, the board authorised a payment of GBP 8,000 to cover existing liabilities and agreed to further payments, on a cash on delivery basis, for further supplies which amounted to further payment of GBP 3,000 up to the date of the winding up order.

The liquidator has asked for advice whether any action may be taken in respect of the floating charge in favour of Fretus Bank plc and the two subsequent transactions.

Using the facts above, answer the questions that follow.

Identify the relevant issues and statutory provisions and consider whether the liquidator may take any action in relation to:

Question 4.1 [maximum 5 marks]

The floating charge in favour of Fretus Bank plc;

For the floating charge in favour of Fretus Bank plc, the liquidator may consider to take action under (1) preference under Section 239 of the Insolvency Act 1986 ("the Act") and (2) floating charge avoidance under Section 245 of the Act.

Under Section 239 of the Act, a company is prevented from placing one of its creditors in a better position than others shortly before entering a insolvency procedure. The Company, by granting a debenture in favour of Fretus Bank plc which contained a floating charge over the whole of the Company's undertaking, put Fretus Bank plc in a more favorable position (comparing to other unsecured creditors, as they were before) by granting the security.

However, despite certain conditions (person preferred was a creditor of the Company, something was done to put such creditor in a better position and the desire to prefer) may be established, the debenture was not granted within 6 months prior to the onset of insolvency as Fretus Bank plc is unlikely to be a connected person of the Company. Accordingly, the liquidation should not be able to commence action under Section 239 of the Act.

On the other hand, Section 245 of the Act aims at preventing pre-existing unsecured creditor of a company to obtain security by way of floating charge shortly before formal insolvency procedure.

In this case, despite Fretus Bank plc is not a connected person of the Company, the floating charge granted was still caught by the relevant time of 12 months prior to the onset of insolvency. However, in establishing the case, the applicant (i.e. the liquidator in this case) still needs to be satisfied that the Company was either unable to pay its debts or became unable to pay its debt as a result of the relevant transaction.

Such floating charge may not be rendered invalid if new consideration was provided by the creditor in granting of security. However, as the floating charge in question was created out of pressure and fear of demanding loan repayment, it appears that no new consideration had been provided by Fretus Bank plc which could save the floating charge.

Question 4.2 [maximum 6 marks]

Commented [WA13]: 4/5 a good answer but a little more detail on s 245 would have been helpful eg meaning of unable to pay debts at the time

Commented [WA14]: 5/6 generally very good although the CDDA answer suggests the liquidator could take such action which they have no power to do.

The sale of the marble cutting machines; and

There are a few actions which the liquidator may consider regarding sale of machines to Rita Perkins :

(1) Transaction at undervalue

Under Section 238 of the Act, the liquidator may attack the sale of machines as it appears that the purchase price (GBP 10,000) was far lower than how much the Company paid for them a year ago (GBP 25,000). However, whether it is “undervalue” (or such consideration was significantly less than the value of its worth) is still subject to valuation as factors like depreciation should be considered.

The “relevant time” condition is satisfied as the transaction was made within 2 years prior to commencement of the liquidation. Since Rita Perkins is a director of the Company, the Company is presumed to be insolvent or became insolvent as a result of the transaction, unless there is evidence suggesting otherwise.

However, the court may still consider whether the sale was made in good faith and for the purpose of carrying on its business or benefiting the company (i.e. utilizing the sale proceeds for its operation) before making relevant order. If the court is satisfied that the sale was a transaction at undervalue, it may make an order restoring the position to what it would have been if the transaction was not entered.

(2) Misfeasance

The liquidator may also consider action under Section 212 of the Act regarding sale of machines. The court may consider conduct of certain persons if there was any misfeasance or breach of duty and if that is the case, order could be made for restoration, repayment or accounting for the loss by way of compensation.

In this case, if it can be established that the sale was transaction at undervalue, the directors who approved such sale (which involved sale of the Company’s asset to a director) may be found breaching their duty or care and skill. The outcome of Section 212 action usually includes order for repayment or contribution (e.g. accounting for the deficit in value of the machines)

(3) Director disqualification

Disqualification of director is governed by the Company Directors Disqualification Act 1986 (“CDDA”) which aims at protecting the public and deterring wrongdoing directors.

In this case, directors who approved the sale of machines to a director may be at fault for disposing the Company’s assets at an undervalue and ignoring any potential conflict of interest. Section 6 of CDDA which deals with unfitness against directors may be considered as a ground of disqualifying the relevant directors.

As a result of the disqualification order, such persons would be barred from acting as a director for a specified period but a minimum bracket of 2 to 5 years should be applied here as the wrongdoing was not very serious relatively.

Question 4.3 [maximum 4 marks]

The payments to Hard and Fast Ltd.

Commented [WA15]: 4/4 VG

As the payments were made a month before the winding up order was made (i.e. on 23 December 2022), they were made after the winding up petition issued on 14 October 2022. In a compulsory winding up, Section 127 of the Act avoids disposition of property of the Company made after commencement of winding up unless ordered otherwise by court.

However, Section 127 is not absolute and the court has discretionary power to declare that a disposition is not void by a "validation order". Party applying for validation order is required to prove that making of such order is justified.

In this case, the Company had made 2 payments to Hard and Fast Ltd., i.e. (1) immediate payment of existing liabilities at GBP 8,000 and (2) GBP 3,000 for further supplies on a cash on delivery basis.

In the case of *Re Changtel Solutions UK Ltd*, it was held that the court would be reluctant to make validation order if it would give a preference to a pre-liquidation creditor over other creditors. Accordingly, payment of existing liabilities is unlikely to be validated as it would prejudice the right of other creditors.

On the other hand, payment for further supplies are likely to be sanctioned as it ensures the Company is able to continue trading if such continuance of trading was in the best interest of the creditors. Given the payment is to be made on a cash on delivery basis, it is unlikely to diminish the Company's net assets unless the price was at an unreasonable high level.

*** End of Assessment ***