



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

Commented [WPA1]: 38/50 = 76% a generally strong performance.

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

Commented [WPA2]: 8/10

Questions 1.1. - 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and mark your selection on the answer sheet by highlighting the relevant paragraph in yellow. Select only ONE answer. Candidates who select more than one answer will receive no mark for that specific question.

Question 1.1

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.*

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.

Commented [WPA3]: B is the correct answer

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.

Commented [WPA4]: D is the correct answer

QUESTION 2 (direct questions) [10 marks]

Commented [WPA5]: 8/10

Question 2.1 [maximum 5 marks]

Commented [WPA6]: 3/5 - although correct the answer to (i) is incomplete as it only deals with actions where the company is in WU or administration. The Official Receiver may also bring s 6 CDDA actions on the instructions of the Sec of State

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?

Under 423 of the Insolvency Act, the following people can apply (i) where the company is being wound up or in administration, the application can be brought by

the official receiver, the liquidator, the administrator and any victim of the transaction such as a creditor (with leave of the court).

Proceedings under section 6 of the Company Directors Disqualification Act 1986 are typically brought by the Insolvency Service on behalf of the Secretary of State.

An administrator can bring an action under section 246ZB of the Insolvency Act if the company is in insolvent administration.

Question 2.2 [maximum 5 marks]

Commented [WPA7]: 5/5

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.

The following debts do not form part of the payment holiday under Part 1A of the Insolvency Act 1986 (i) the monitor's remuneration or expenses; (ii) goods or services supplied during the moratorium; (iii) rent in respect of a period during the moratorium; (iv) wages or salary arising under a contract of employment; (v) redundancy payments; or (vi) debts or liabilities arising under contracts or other instruments involving "financial services" which is defined as including a contract consisting of lending, financial leasing or providing guarantees.

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

Commented [WPA8]: 11/15

Question 3.1 [maximum 6 marks]

Commented [WPA9]: 4/6 a reasonable answer but lacks detail in places especially as to how s 233B operates.

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?

Yes, the company going into administration does not automatically terminate contracts for the supply of goods and services. The supplier may however make it a condition of giving the supply that the administrator personally guarantees the payment of any charges in respect of that supply. However, the supplier cannot insist upon outstanding charges being paid as a condition of continued supply. These provisions apply to gas, electricity, water, communications. They also include services provided in connection with point of sales terminals, computer hardware or software, IT use, data storage and processing and website hosting (see section 233 of the Insolvency Act 1986).

Further, an insolvency related provision will cease to have effect if the company is placed into administration because the law recognizes the need for companies to continue to get essential supplies, either to facilitate a rescue or a better return to creditors (section 233A). Again, the supplier can request a personal guarantee from the administrator.

Section 233B provides further protections in that if the company has gone into administration, any provision purporting to terminate upon administration or would entitle the supplier to hold the company to ransom cease to have effect.

However, a contract under section 233B can be terminated either with the consent of the administrator or upon an application to court, if the administrator can show the contract would cause the supplier hardship.

Question 3.2 [maximum 9 marks]

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?

The holders of a fixed charge will usually be paid out first and generally outside of the formal insolvency procedure (as they will likely have a right to sell the secured assets for the purposes of settling the secured obligations from the proceeds of sale).

Creditors with a proprietary claim to the company's assets will also fall outside of the statutory priority of payments waterfall applying to the insolvent estate if that creditor can show that it has a beneficial interest in the assets in question. This is because these assets are not generally available for the general body of the creditors to be realized as part of the liquidation distribution.

After secured creditors have been paid out, the expenses of the liquidation will be paid out of the assets of the company (including the remuneration and expenses of the liquidator and any provisional liquidator and the costs of the petitioner), except that see the caveat to this in relation to moratorium and pre-moratorium debts under Part A1 of the Insolvency Act.

After the expenses of the liquidation have been paid out, preferential creditors are next in terms of priority of payments. There are two types of preferential debts - ordinary and secondary. Ordinary preferential debts include contributions to occupational and state pension schemes; wages and salaries of employees for work done in the four months prior to the insolvency date up to a maximum of £800; holiday pay due to an employee whose contract has been terminated (whether termination is before or after the insolvency date); levies on the production of coal and steel (though these are very rare); debts owed to the Financial Services Compensation Scheme; and eligible deposits whose amount is protected under the Financial Services Compensation Scheme. (HMRC and landlords may also become preferential creditors in certain circumstances). Secondary preferential debts include deposits owed to depositors but not protected by the Financial Services Compensation Scheme and certain taxes. Where the company has both ordinary and secondary preferential debts, the ordinary debts rank in priority. All debts in each category rank equally as against each other.

Commented [WPA10]: 7/9 generally a very sound answer although more detail in places would have been helpful especially eg expenses.

Following the payment of preferential creditors, the holders of floating charges are next in terms of priority. Where there is more than one floating charge, priority will typically turn upon which charge was created first. Payment to the floating chargeholder(s) may be subject to a deduction by the liquidator to make a prescribed part of the company's net property available for the satisfaction of unsecured debt. "Net property" for these purposes is the amount of the company's property available for the satisfaction of floating charge holders, calculated after liquidation expenses and preferential debts have been paid. Where the company's property does not exceed GBP10,000, the prescribed part is 50% however where the liquidator considers making such a distribution to unsecured creditors would be disproportionate to the benefits, then the duty to make a distribution of the prescribed part falls away. Where the net property exceeds GBP 10,000 a certain calculation is applied subject to a maximum of GBP 800,000.

Unsecured creditors come next in the statutory waterfall and will be paid a dividend if there is anything left in the liquidation estate.

Finally, if all creditors have been paid (including interest), any surplus is distributed to the company's shareholders pro rata to the shareholders' respective shareholdings.

The above priority changes where the company is subject to a moratorium under Part A1 of the Insolvency Act. In particular, pursuant to section 174A of the Insolvency Act, certain unpaid pre-moratorium and moratorium debts (which are not subject to the payment holiday), such as debts owed to employees and "financial services" debts are paid in priority to even the liquidators fees and expenses. Section 174A therefore affords "super priority" to certain unsecured debts in a later liquidation. This could include the wages of a director or bank debt falling in the definition of "financial services" (except where the debt is an accelerated debt).

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

Commented [WPA11]: 11/15

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]

Commented [WPA12]: 5/5 vg

The floating charge in favour of Fretus Bank plc;

The floating charge may be rendered invalid pursuant to section 245 of the Insolvency Act 1986 because (i) it was created within 12 months of the onset of insolvency of the company (the floating charge was created in February 2022 and the onset of insolvency was 14th October 2022 (ie the date on which the creditor petition was presented); (ii) it was created in favour of an unconnected party (ie the Bank) but the liquidator would need to show that the company was either unable to pay its debts (within the meaning of 123 of the Insolvency Act) or became unable to do so as a result of the transaction. It appears from the factual scenario that the company may have been unable to pay its debts (ie cash flow insolvent) in February given that the Bank requested the security "to prevent it from demanding repayment of the company's loans". It also appears that the Bank was purporting to better its position by insisting upon security being granted in support of what appears to have been an unsecured debt.

Pursuant to section 245, a floating charge will not be invalidated to the extent that (i) "the value of so much of the consideration for the creation of the charge as consists of money paid, or goods or services supplied, to the company at the same time as, or after, the creation of the charge;" and (ii) "the value of so much of that consideration as consists of the discharge or reduction, at the same time as, or after, the creation of the charge, of any debt of the company", i.e. the creation of security can be provided in support of new funding or the provision of goods and services or in consideration for a discharge or reduction of debt. In other words, the security has to be provided in support of some value received by the company. The floating charge appears to have been given with no "new" consideration in that it seems to have been given solely for the purposes of the Bank forbearing on repayment. No new money appears to have

been advanced, neither does there appear to have been a reduction or discharge of the outstanding debt, meaning that it doesn't appear to fall within the safe harbours outlined above.

Assuming the floating charge falls within section 245, it will be rendered invalid given that the relevant test has been met (assuming the company was cash flow insolvent at the time the floating charge was created). The invalidity of the floating charge does not operate to invalidate the underlying debt.

The factual scenario notes that the directors approved the sale to a director, RP. It's not clear from the factual scenario whether RP declared her interest in the sale and/or abstained from the decision to approve it. Where she purported to approve the transaction, there may be an argument that she may have been in breach of her duties to the company by approving the transaction.

Nothing in the legislation requires the liquidator to issue an application confirming that the security is invalid but to the extent the Bank challenges the decision, it is likely that the liquidator would need to make an application to court for a declaration (or other appropriate relief) that the granting of the debenture falls within section 245.

Question 4.2 [maximum 6 marks]

Commented [WPA13]: 6/6 vg

The sale of the marble cutting machines; and

The factual scenario confirms that two marble cutting machines were sold in July 2022 when the company continued to have cash-flow problems. The machines appear to have been sold at an undervalue in that they had been purchased for GBP 25,000 each and were sold for GBP 10,000 each a year before. They were also sold to a director, RP.

Section 238 of the Insolvency Act provides further a means by liquidators can claw back money into the insolvent estate for the benefit of unsecured creditors where certain transactions that were entered into before the company enters into insolvency can be challenged.

The liquidator would need to apply to the High Court of England and Wales for an order under section 238 but would need to show that (i) the company entered into the transaction at the relevant time; and (ii) the company entered into a transaction for consideration the value of which in money or money's worth is significantly less than the value in money or money's worth of the consideration provided by the company.

The "relevant time" for these purposes is defined in section 240 of the Insolvency Act and means two years ending with the onset of insolvency (ie 14th October 2022) given that the sale was to RP (who would be a connected person for the purposes of the Insolvency Act given she was a director of the company at the time of the transaction).

The company must also be cash-insolvent at the time of the transaction or become cash-flow insolvent as a result of the transaction. Given the factual scenario confirms that the company continued to have cash-flow problems at the time the transaction was entered into, it appears this requirement is met. Further, the section creates a rebuttable presumption that the company was insolvent at the time to transaction was entered into where it was to a connected person (ie RP (the likely respondent to any application) would need to show that that the company was not insolvent at the time of the sale or did not become insolvent as a result of it).

The marble cutting machines were sold at less than 50% of their purchase price a year earlier therefore unless updated valuations show that the assets have diminished to that extent, the liquidator may be able to show that the sale of the machines was for significantly less than their actual market value. However, if RP can satisfy the court that the transaction was entered into in good faith and for the purposes of carrying on its business, and there were reasonable grounds for believing that the sale of the machines would benefit the company, the court may decline to make an order under section 238 of the Insolvency Act.

If the liquidator is able to make out the relevant requirements described above, he/she may ask the court to make such order as it considers fit for restoring the company to the position to it would have been in if the company had not entered into the transaction.

Question 4.3 [maximum 4 marks]

The payments to Hard and Fast Ltd.

The payments to the supplier could constitute preferences within the meaning of section 239 of the Insolvency Act.

In this case, the supplier contacted the company in mid-November and demanded repayment of all of the sums owed to it and confirmed that further supplies would only be made on a cash on delivery basis. Given the continued supply of marble was considered essential by the company, the board authorized payment of GBP8,000 to settle existing liabilities and agreed to further cash payments on delivery of GBP 3,000 up to the date of the winding up order.

The purpose behind section 238 is to ensure that the company does not place one creditor in a better position than other creditors shortly before entering into insolvency. In other words, it can assist to prevent a creditor who would otherwise receive only a dividend as an unsecured creditor from being paid out in full ahead of the company's other unsecured creditors.

The liquidator would need to show that: (i) the supplier was a creditor of the company at the time of the transaction; (ii) something was done by the company which had the effect of putting the supplier in a better position than it would have been in the event

Commented [WPA14]: 0/4 unfortunately, s 239 cannot apply here as the transactions occurred after the winding up had commenced not before. The only possible action would be s 127.

the company goes into insolvent liquidation; (iii) the company was influenced by a desire to give that creditor a preference (ie the company was influenced by an intention to put the creditor in a better than other creditors); and (iv) it needs to be entered into at the relevant time (for these purposes, as the supplier does not appear to be connected to the company, this would be six months prior to the onset of insolvency (14th October)).

*Requirement (i) is satisfied - the supplier was a creditor at the time of the transaction (it asked for the repayment of outstanding liabilities). Requirement (ii) appears to have been satisfied too - the payment of GBP11,000 to the supplier prior to the winding up order being made has the result of taking GBP11,000 out of the insolvent estate which would disrupt the *pari passu* distribution of the company's assets to its unsecured creditors because the supplier would have been paid in full rather than being paid a dividend alongside the company's other unsecured creditors. Requirement (iv) is also satisfied - the company is deemed to have gone insolvent on 14 October 2022 (the first payment seems to have been made on or around mid-November and further payments were made up to the winding up order being made).*

Requirement (iii) is more difficult to make out - the company decided to pay this creditor to ensure the ongoing supply of marble which was considered essential for the purposes of continuing the business. There is authority which suggests that where the decision to prefer a creditor is commercial and attempts to ensure that the company continues to be able to trade, the liquidator may not be able to make out the relevant intention to prefer.

If the liquidator is able to make out the requirements set out in section 239, the court may make such order as it thinks fit to put the company in the position as if the preference had not been given.

*** End of Assessment ***