



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).**
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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]: 41/50 = 82% a very good effort

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

Commented [WPA2]: 9/10

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.

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 [WPA3]: D is correct

QUESTION 2 (direct questions) [10 marks]

Commented [WPA4]: 10/10

Question 2.1 [maximum 5 marks]

Commented [WPA5]: 5/5

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?

[In the case of (i) section 423 of the Insolvency Act 1986 (on transactions defrauding creditors), there are three scenarios:-

(a) Where the company is wound up or subject to administration, the official receiver, the liquidator(s), the administrators and (subject to leave of the Court) the victim of the transaction(s) in question may take out the application; or

(b) Where the victim is bound by a CVA, the supervisor of the CVA may commence the action; or

(c) In all other cases, victim of the transaction(s) in question may bring an action.

In the case of (ii) section 6 of the Company Directors Disqualification Act 1986 (on disqualification of directors on the ground of unfitness), the Secretary of State, or (where the company involved is wound up by the Court) the official receiver may take out the application (see section 7 of the Company Directors Disqualification Act 1986).

In the case of (iii) section 246ZB of the Insolvency Act 1986 (on wrongful trading in case of administration), section 246ZB(1) expressly provides that the administrator may make the application to the Court.]

Question 2.2 [maximum 5 marks]

Commented [WPA6]: 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.

*[According to section A18(3) of the Act, those debts include pre-Moratorium debts consisting of amounts payable in respect of, *inter alia*:-*

(1) the monitor's expenses or remuneration;

(2) goods or services supplied in the course of the Moratorium;

(3) rent in respect of any period falling within the Moratorium;

(4) wages or salary arising under contracts of employment;

(5) redundancy payments.]

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

Commented [WPA7]: 13/15

Question 3.1 [maximum 6 marks]

Commented [WPA8]: 5/6 a good answer but it does not distinguish between the regime under ss233 and 233A and that under s233B.

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 gist, an administrator may request the continuation of supply of goods and services notwithstanding the fact that the company has entered into administration by relying on sections 233, 233A and 233B of the Insolvency Act 1986.

First, under section 233 of the Act, suppliers of "essential supplies" (as set out in section 233(3) and 233(3A)) may not make payment of outstanding debts as a

condition (or do anything which has the effect of making such condition) before they continue to supply goods or services to the company in question. That said, under section 233(2)(a), those suppliers may require the administrator to personally guarantee the payment of any charges in respect of the supply.

Second, under section 233A of the Act (introduced in 2015), suppliers are also generally prohibited from relying on any "insolvency-related terms" to increase their price, terminate their supply or "do any other thing" simply because the company becomes subject to certain insolvency procedures (including administration and voluntary arrangement). In other words, the aforesaid insolvency-related term in the contracts between the suppliers and the company would become void. That said, this provision is subject to an exception, that is, the contract or supply in question may be terminated if the conditions in section 233A(3) OR 233A(4) are satisfied. For instance, if the administrator consents to the termination of the contract or if the Court grants permission for such termination, then the contract may be validly terminated.

Third, under section 233B of the Act (introduced in 2020), a contractual term would cease to have effect if it allows the suppliers to terminate or "do any other thing" in relation to the contracts with the company where a company enters into administration (or other insolvency processes as set out in section 233B(2)). Also, suppliers may not exercise their contractual rights to terminate the contract once the company is subject to the said insolvency processes even though their rights to do so arose before the insolvency processes. Nevertheless, section 233B(5) provides for exceptions such as termination with consent from the administrator.]

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 order of priority of payment is summarized as follows:-

1. Holders of fixed charges and secured creditors (i.e. creditors that have secured proprietary interest in the Company's assets by way of security). They are entitled to look to the proprietary interests acquired by them (by way of security) in order to discharge the debts owed by the Company to them. To the extent that their claims are secured by such proprietary interests, these creditors' claims may be considered as enjoying the highest priority in the liquidation process (since their claims and the amounts they may recover thereunder may not be affected by the administration of the insolvent estate);

2. Expenses of winding up including the liquidators' remuneration (as recognized expressly in section 115, which provides that they are "payable out of the company's assets in priority to all other claims"). It should be noted that among the different

Commented [WPA9]: 8/9 a very good answer. One or two points might have been dealt with in a little more detail eg the debts covered by the s 174A rule.

expenses of winding up, there is an internal order of priority with the expenses incurred by the liquidator in preserving, realizing or getting in assets of the company being accorded with the highest priority among the costs of liquidation;

3. Claims of preferential creditors as set out in Schedule 6 of the Insolvency Act 1986 should be settled in priority to items (4) to (6) below. Examples of preferential debts include certain claims of employees of the company in respect of, e.g., their occupational pension schemes, remuneration within the 4-month period before the winding up of the company or holiday pay. They also include certain taxation liabilities. Please note that certain preferential debts are considered as "secondary" preferential debts and would only be paid after other preferential debts (being "ordinary" preferential debts) are paid;

4. Holders of floating charges (subject to the "prescribed part" as explained below). It should be noted that, for floating charge created on or after 15 September 2003, the liquidator is obliged to set aside a "prescribed part" for the benefit of the unsecured creditors. Such "prescribed part" must not be distributed to a floating charge holders unless the "prescribed part" is in excess of the claims of the unsecured creditors. Where the company's net assets are not more than GBP 10,000 then the "prescribed part" would be 50% of such net assets (unless the liquidator takes the view that making a distribution to unsecured creditors would be disproportionate to the benefits). Where the company's net assets are more than GBP 10,000, the "prescribed part" would be (i) 50% of the first GBP 10,000 plus (ii) 20% of the remaining sum of assets, subject to the overall cap of "prescribed part" being GBP 800,000;

5. Unsecured creditors who would be paid on a *pari passu* basis, meaning that they would be paid out of the remainder of the insolvent estate *pro rata* based on the relative size of their respective claims. While they only enjoy a relative lower priority, they are generally entitled to vote on a number of important decisions in the administration of the insolvent estate such as the appointment of liquidators and the remuneration of liquidators; and

6. Shareholders, who would only be paid *pro rata* according to their respective shareholdings only if there is a surplus after all the creditors are paid.

Please however note that, the aforesaid order of priority would be disturbed where the company is subject to a Moratorium under Part A1 to the Insolvency Act 1986 (introduced in 2020). Specifically, under section 174A of the Act, certain outstanding debts incurred prior to or during the Moratorium would be accorded with "super priority" and would be paid in priority over expenses of winding up including the liquidators' remuneration (i.e. item (2) above). This is expressly recognized in section 115 of the Act which expressly provides that section 115 is subject to section 174A.]

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

Commented [WPA10]: 9/15

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 [WPA11]: 5/5

The floating charge in favour of Fretus Bank plc;

[In gist, the liquidator may apply to the Court to avoid the floating charge in favour of Fretus Bank plc based on section 245 of the Insolvency Act 1986, and there may be a high chance that the floating charge would be avoided.

Generally speaking, floating charges created during the 12-month period before the "onset of insolvency" (or during the 2-year period before the "onset of insolvency" if the floating charge holder is a connected person) would be invalidated by section 245 except to the extent that "new" consideration has been provided for such floating charge.

In general terms, insofar as the "new" consideration is concerned, it may either be in the form of (a) gain on the part of the Company or (b) deduction or discharge of the Company's existing liabilities.

As regards the meaning of "onset of insolvency", it would mean the date of commencement of winding up in the context of corporate liquidation (see section 245(5)(d)), which in turn means the date of presentation of winding-up petition against the company (see section 129(2)).

On the facts of this case, the winding-up petition was presented on 14 October 2022 and the company was wound up on 23 December 2022. As such, the "onset of insolvency" of the Company would be 14 October 2022. As regards the "relevant time" triggering the application of section 245, since nothing in the facts suggests that Fretus Bank plc is connected to the Company, the relevant time there would be a 1-year period before 14 October 2022. In any event, since the floating charge in question was created in February 2022, it would fall within the scope of section 245 regardless of whether or not Fretus Bank plc is connected to the Company.

Finally, based on the facts available to us, the bank appeared to have provided no consideration for the floating charge. As such, there is no "new" consideration involved. In the premises, there may be a high chance that the floating charge would be avoided under section 245. The liquidators should take out application to the Court accordingly.

For completeness, the invalidation of the floating charge would not affect the validity of the underlying debts owed by the Company to Fretus Bank plc under the debenture.]

Question 4.2 [maximum 6 marks]

The sale of the marble cutting machines; and

[The liquidator may apply to the Court to set aside the sale of marble cutting machines on the ground that it amounts to a transaction at an undervalue under section 238 of the Insolvency Act 1986 but there may only be an even chance that the sale would be set aside.

According to section 238, where the Company has at a "relevant time" (defined in section 240) entered into a transaction at an undervalue, the liquidator may make an application to the Court, upon which the Court may, as expressly provided for under section 238(3), "make such order as it thinks fit for restoring the position to what it would have been if the company had not entered into that transaction". In this regard, "relevant time" would be 2 years ending with the "onset of insolvency" if the transaction was made with a connected person (otherwise than by the reason only of being its employee) or, in other cases, 6 months ending with the "onset of insolvency". "Onset of insolvency" means the date of presentation of winding-up petition against the company (see sections 129 and 245).

Commented [WPA12]: 4/6 a generally good answer but there are some omissions/errors. The timeframe is never 6 months under s238 - it is always 2 years. The effect of a connected party sale is that insolvency is presumed.

Under section 238(4), there are two scenarios falling within the scope of “transactions at an undervalue”. The first one (under section 238(4)(a)) is that the Company makes a gift to a person or otherwise enters into a transaction with that person on terms that provide for the company to receive no consideration. The second one (under section 238(4)(b)) is that the Company enters into a transaction with that person for a 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.

An exception under section 238(5) is that the transaction should not be set aside if:- (i) the Company entered into the transaction did so in good faith and for the purpose of carrying on its business; and (ii) (at the time of the transaction) there were reasonable grounds for believing that the transaction would benefit the Company.

At the time of the transaction, the Company must also be unable to pay its debts (within the meaning of section 123) (see section 240(2)).

On the facts of this case, the Company sold marble cutting machines to its director, Rita Perkins, in July 2022. Pursuant to section 249, the director is connected to the Company and thus the “relevant time” would be 2 years before the date of winding-up petition (14 October 2022). Yet, since the sale took place in July 2022 (3 months before the said date), the sale would fall within the “relevant time” regardless of whether the director is a connected person. Also, at the time of the sale, the Company was clearly “unable to pay its debts”.

It seems more likely than not that the sale was made “for a 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”. While the machines were bought for GBP 25,000 a year before, they were sold at GBP 10,000 in cash (i.e. giving of a 60% discount).

Assuming that the aforesaid test is satisfied, the director may purport to rely on the exception in section 238(5) and argue that (1) the Company sold the machines in good faith and for the purpose of carrying on its business and (2) there were reasonable grounds for believing that the sale would benefit the Company. Particularly, at the time of the sale, the Company was suffering cash flow problems. The fact that a director may purchase the Company’s machines with cash might have significantly assisted the Company with addressing its cash flow problems notwithstanding the fact that the selling price was relatively low. Also, notwithstanding the difference in price, one may need to take into account the discounts arising from depreciation of the machines and the time that could be saved from locating purchasers from open market.

In the premises, it seems that there may only be an even chance that the sale would be set aside under section 238.

For completeness, while the liquidators may possibly consider taking action on the basis of wrongful trading or transactions defrauding creditors, those applications enjoy a relative low chance of success based on the facts available to us.]

Question 4.3 [maximum 4 marks]

The payments to Hard and Fast Ltd.

[While the liquidator may apply to the Court to avoid the payments on the ground of preference under section 239 of the Insolvency Act 1986, there is a low chance that the payment may be avoided on this ground.

In gist, four conditions must be met:- (1) something must have been done (or suffered to be done) by the Company which had the effect of putting the creditor in a better position in the event of liquidation of the Company than the position he/she would have been in if that thing had not been done; (2) the party involved must be a creditor of the Company at the time of the act in question; (3) the Company was influenced by a "desire to prefer"; and (4) the preference was given at a "relevant time".

Under section 240, "relevant time" would be either (a) a 2-year period before the "onset of insolvency" where the creditor is connected to the company (otherwise than by the reason only of being its employee) or (b) in other cases, a 6-month period before the "onset of insolvency". "Onset of insolvency" here means the date of the winding-up petition against the Company (see sections 129 and 245).

*As regards "desire to prefer", there would be a presumption (to be rebutted by the creditor) that there is a "desire to prefer" if the creditor is a connected person. In the landmark case of *Re MC Bacon Ltd*, where a company is entirely dependent upon support from a creditor (e.g. a bank) for continued trading, the company may not have been motivated by a "desire to prefer" such creditor in doing a *prima facie* preferential act. It is because, in doing such act, the company was not motivated by a desire to prefer the creditor but a desire to continue trading.*

At the time of the transaction, the Company must also be "unable to pay its debts" as per section 123 (see section 240(2)).

On the facts of this case, Hard and Fast Ltd. as the Company's key suppliers, was a creditor of the Company at the same of the payments. The first payment was made a month before the winding-up order and thus such payment (as well as the subsequent payment) would fall within the "relevant time" regardless of whether the supplier is connected to the Company (noting that, for completeness, nothing in the facts suggests that the supplier is connected). At the time of the payments, the Company was clearly "unable to pay its debts".

Commented [WPA13]: 0/4 although a very clear explanation of s 239, that section cannot apply here. The issue is covered by s127. The payments were made after the commencement of the winding up not before it so s239 cannot apply.

By getting paid GBP 8,000 to cover existing liabilities (with further payment of GBP 3,000), Hard and Fast Ltd. was clearly "preferred" since it has become better off than other creditors in the event of liquidation of the Company but for the said payments.

*Notwithstanding the above, it is unlikely to prove that there is a "desire to prefer". This is because, as suggested by the factual background of this case, Hard and Fast Ltd., as a key supplier of the Company, demanded the Company to make 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. In other words, if the Company did not pay, it is probable that the Company would have become unable to continue to obtain supply of marble from the supplier. In the circumstances, as in the case of *Re MC Bacon Ltd*, the Court is likely to find that the Company was not motivated by a desire to prefer the supplier but a desire to continue trading in making the payment.*

As such, there is a low chance that the payments would constitute "preference" under section 239.]

*** End of Assessment ***