



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]: 45/50 = 90% a very good effort

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.*

Commented [WPA3]: C is correct

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 [WPA4]: B is correct

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]

Commented [WPA5]: 9/10

Question 2.1 [maximum 5 marks]

Commented [WPA6]: 4/5 only the SoS (or the OR acting on their instructions) can bring an action under s 6 CDDA.

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?

The following people may bring an action in respect of the below provisions:

- **Section 423 of Insolvency Act 1986** – there are several people who can bring an action under section 423 of the Insolvency Act 1986 for transactions designed to defraud creditors such as:

- In instances where the company is in liquidation or administration, the official receiver, liquidator, administrator or any victim of the transaction (like a creditor);
 - Where victims are bound by a CVA, the supervisor of the CVA or any victim of the transaction involving the CVA despite being bound to the arrangement or not; and
 - The victim of a transaction in any other case.
- **Section 6 of Company Directors Disqualification Act 1986** – the Secretary of State, liquidator, administrator and the Official Receiver, in situations where he may come across any evidence of unfit behavior by the directors of the company, an action can be taken to disqualify the directors to prevent further involvement in the management of the company.
- **Section 246ZB of Insolvency Act 1986**- since this section deals with wrongful trading in an administration, the administrator is the only one who can bring an action against the directors of the insolvent company for wrongful trading and hence, making them liable for some of the company's debts and liabilities. The equivalent in a liquidation would be for the liquidator to bring an action under section 214 of the Insolvency Act 1986.
- However, a defence is available to directors accused of wrongful trading which is if the director took every step with a view to minimize the potential loss to the company's creditors (assuming he knew there was no reasonable prospect of the company avoiding insolvent liquidation/administration) and he knew or ought to have known that the insolvent winding-up/administration was inevitable. Burden of proof is on the administrator, or liquidators (if a liquidation) or person bringing action to prove that the director knew or ought to have known there was no reasonable prospect of avoiding insolvent liquidation. If this is proven, the burden will be on the director in question to show he took every step to minimize the loss to creditors.

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.

Five debts that do not form part of payment holiday when a company is subject to a Moratorium under Part A1 of the Insolvency Act 1986 are as follows:

- Debts owed to employees or financial services debts;
- the monitor's fees and expenses;
- any goods and services supplied during the moratorium;
- rent payments during the moratorium period;
- wages and salaries from employment contracts; and
- redundancy payments.

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

Commented [WPA8]: 13/15

Question 3.1 [maximum 6 marks]

Commented [WPA9]: 6/6

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?

All sections referenced below are sections laid out in the Insolvency Act 1986.

Yes, an administrator can require suppliers of goods or services to continue to supply those goods and services during the administration because the appointment of an administrator does not automatically terminate the contracts for a supply of goods and services involving the company. Under section 233 of the Insolvency Act 1986, communications, services and the supply of electricity, water and gas are prohibited from requiring payment of outstanding debts in order to secure a new or continued supply of such services to the company in an administration. However, this section allows suppliers to specify that the administrator may be required to personally guarantee payment of charges for such services or supplies. Section 233A prevents suppliers relying on insolvency related terms in a contract of supply which would otherwise give the supplier the option to terminate the supply, change the terms of such services or demand higher payments should the services or supplies be continued.

Section 233B prevents suppliers of goods or services from including clauses which allow them to terminate or doing other things under the contract of the company if the receiving debtor company of such goods or services enters a formal insolvency procedure; hence, these provisions of contracts relating to the goods or services supplied are ineffective or have very little effect when a debtor company enters an insolvency procedure because this section not only prevents suppliers from terminating the supply of goods or services but also stops them from including conditions of payment of arrears for the continued supply of goods and services as well as being able to increase the prices of such. This section also takes away the option for a supplier to be able to stipulate that a personal guarantee is needed from the administrator. Any contracts under section 233B can only be terminated if the administrator consents to such action or by court order, upon an application whereby the court is satisfied that continuing such contracts would cause hardship for the suppliers.¹

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 payment² in a liquidation is as follows:

- Holders of fixed charges paid first outside of formal insolvency from proceeds of the sale of assets which were subject to fixed charges.
- Expenses of the liquidation procedure (remuneration of officeholder). These being those expenses properly incurred by the liquidator in preserving, realizing or getting in the assets of the company including conduct of legal proceedings; any amount payable to people assisting with the statement of affair; the cost of security; disbursement in the court of winding-up like members incurring on the liquidation committee; remuneration

¹ Professor Peter A Walton, Module 3B Guidance Text, Insolvency System of the United Kingdom (England and Wales) Law 2022/2023, p 21

²ibid., p5

Commented [WPA10]: 7/9 a good answer but more detail needed in places eg different classes of preferential creditors and the operation of s 176A.

of any person employed by the liquidator to perform a service; liquidator's remuneration; corporation tax; any other expenses incurred by the liquidation in carrying out his functions.

- Preferential creditors (claims from employees owed by employers & taxation debts owed to Government which the company has collected).
- Floating charges (subject to any prescribed part deduction under section 176A) – however if the company is subject to a moratorium the floating charge won't crystallise.
- Unsecured creditors (those without the benefit of security/ title to assets – ordinary trade suppliers and taxation liabilities that weren't preferential). They enjoy the right to vote on the approval of administrator's proposals, or the approval of a CVA; who is appointed as a liquidator; and house office holders are paid. These creditors are paid out last which means there's a risk of them being paid little to nothing.
- After payment of liabilities, if any surplus of solvent company is paid to members according to their rights under the company's articles of association. This wouldn't be the case in this scenario as the company is in liquidation; so, it will be highly unlikely that there will be any assets or money left over to give to shareholders.
- However, the above order of priority would slightly change if the company was subject to a Part A1 Moratorium under the Insolvency Act 1986. Pursuant to section 174A, the unpaid pre-moratorium / moratorium debts like debts owed to employees (wages/ salary for holiday pay sick pay, contributions to occupational pension schemes) or financial services like Bank debts (except accelerated debt in the financial service contract) would be given super priority which are paid in priority even before the liquidator's fees and expenses. Certain unsecured debts form super priority like director's remuneration owing to him months before the moratorium (pre-moratorium debts) because this procedure is a debtor-in possession procedure which allows the directors to still control the management of the company. Another pre-moratorium debt which may be paid in priority are debts payable for the goods or services supplied during the moratorium.

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

Commented [WPA11]: 15/15 very good

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

All sections referenced below are sections laid out in the Insolvency Act 1986.

The floating charge in favour of Fretus Bank plc;

- **Floating charge** – Section 176A applies to a company with a floating charge created on or after 15 September 2003 and the company has gone into liquidation. The liquidator is under a duty to make a prescribed part of company's net property available for the satisfaction of unsecured debts and must not distribute any of this prescribed part to a floating charge holding except insofar as it is in excess of the amount required to satisfy all unsecured debts.³ Section 245 can be used by the liquidator to prevent pre-existing unsecured creditors from obtaining security of a floating charge on the company's assets shortly before the Marbley Q Limited enters liquidation. This section would render the floating charge given by Marbley Q Limited plc invalid since it was given at a relevant time, that being within 12 months prior to the company going into liquidation and the company was unable to pay its debts. The debenture was granted prior to the company going into compulsory liquidation and therefore, falls within the relevant time. The company was, at the time of the creation of the charge, the company was unable to pay its debts in accordance with s123 of the Insolvency Act 1986 as this debenture was only granted by the company to avoid the bank from demanding repayment of the loans the company owed, having fallen behind on payments.
- No new consideration or fresh funding was given by the bank in respect of this floating charge so it doesn't qualify for the exception. If another loan was being given to the company than the floating charge could be valid for that new loan. Funds must be advanced at the same time as this section does not allow the bank to create a debenture on old debts. Where there is no more than a renegotiation of existing debt arrangement and no material brought to company from renegotiation there is no new consideration.
- Hence, this floating charge is caught by section 245 and is a transaction that can be attacked by the liquidator can for its invalidity to the fact that the company has gone into liquidation and was on the verge of being insolvent at the time of the transaction or was actually insolvent and therefore, shouldn't have been entered into. Although the floating charge may be invalid, the company's debt remains.

Question 4.2 [maximum 6 marks]

Commented [WPA13]: 6/6

³ Ibid. p 54

The sale of the marble cutting machines; and

- **Undervalue transaction** – the liquidator can attack the transaction made to Rita Perkins under section 238 of the Companies Act 1981, as it was a transaction entered into prior to the company going into liquidation and was at an undervalue. More specifically, section 238(3) applies to these facts because the Company initially bought the machines for 25k a year before (hence the machines couldn't have depreciated that much over 12 months) which Rita would have known and yet she entered into the transaction with the company for the sale of the same machines for 10k which is significantly less than the value of the consideration provided by the company. This transaction occurred in July 2022 which qualifies it to have happened at a relevant time, that being within 2 years prior to the commencement of the liquidation which happened on the presentation of the winding-up petition on October 14, 2022.
- On top of this, it was clear to Rita (as a director of the Company) at that time the company was unable to pay its debts as they fell due within the meaning of section 123, as it continued to suffer cash flow problems and having not only fallen behind on bank payments in relation to the loan from Fretus Bank plc but also the Company was unable to pay the debts owed to Hard and Fast Ltd which demanded payments of sums owed before the winding-up order was made. This transaction obviously didn't take the company's financial position any better and could potentially be seen as [stopping creditors from getting a cut – since she sold it to herself]. There's a presumption that the company had to have been insolvent or become insolvent as a result of the transaction which was clear in from the facts as the director were aware of the cash flow issues.
- There's an available defence for Rita which is if she satisfies the court that the transaction was entered into by the Company in good faith and for the purpose of carrying on its business, and at the time there were reasonable grounds for believing that the transaction would benefit the company.⁴ However, I cannot see the court being satisfied of this defense on the facts. It's unlikely that she entered into the transaction in good faith, as the Company is a marble company so, selling its marble cutting machines would not be for the purpose of carrying on the business the Company does because it does not sell marble machines, it sells marble and obviously needs the machines to carry out the business. Hence, Rita, as a director, could not have believed selling the machines would benefit the Company in reducing the number of machines the Company has to operate its business.
- There may also be a possible action for the liquidator to bring under section 423 to defraud creditors because the Company did enter into a transaction at an undervalue with Rita (a connected person) and received significantly less consideration than the company had provided and this transaction would have been putting the Company's assets (marble cutting machines) beyond the reach of creditors who would most likely make claims against the company since debts were owed by the company.

Question 4.3 [maximum 4 marks]

Commented [WPA14]: 4/4

The payments to Hard and Fast Ltd.

- **Dispositions** – The liquidator can potentially bring an action against Rita, as a director of the Company, under section 127 for the disposition of the company's assets, that being payments of money to a creditor. This section avoids any disposition of the Company's property in a compulsory liquidation made after the commencement of winding up unless

⁴ Ibid. p67

the court orders otherwise. The petition was issued don 14 December 2022 which is the date the winding-up proceedings commenced. So any disposition made after that date will be void. While it's possible for Marbley Q Limited to continue carrying out business or trading for the purpose of defending the winding-up petition, since the winding-up order was made it will avoid the dispositions of the company- that being the payments GBP 8000 and 3000 made to the Company's key suppliers, Hard and Fast Ltd. in the interim period. While the directors may have authorized these payments because the continued supply of marble was seen as essential by the company, these transactions are void under to section 127 since the winding-up order was made.

- However, the court has the discretionary power to declare this disposition shall not be void under a validation order. This order will only be made in relation to an insolvent company where the circumstances indicate that the disposition will be or has been made for the general body of unsecured creditors.⁵ Since the insolvent Marbley Q Limited made payments on cash on delivery and saw it as necessary to ensure the continued supply of marble being received to enable the company to continue its business (as it is a marble cutting company, its money is made off the sale of marble), where it could have been for the benefit of the company or in the best interest of creditors, the court may sanction such disposition. These payments appear to have been made in good faith as it was money owed for supplies and needed for continued supplies for the benefit of the company to continue in operation and so, may be authorized or validated by the court if it sees fit. However, the court may be of the opinion that such payments were made just to the benefit of the one creditor (Hard and Fast Ltd) owed and to the detriment of the other creditors (such as the bank which was most likely owed way more in respect of the loans), and the court will most likely be refused to grant a validation order.

*** End of Assessment ***

⁵ Professor Peter A Walton, Module 3B Guidance Text, Insolvency System of the United Kingdom (England and Wales) Law 2022/2023, p65