



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 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.**

Commented [WPA1]: 43/50 = 86% a generally very good effort indeed.

Commented [WPA2]: 10/10 well done!

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.

QUESTION 2 (direct questions) [10 marks]

Commented [WPA3]: 9/10

Question 2.1 [maximum 5 marks]

Commented [WPA4]: 4/5 a very sound answer. Technically, under s 6 CDDA the action is not brought by the IS but either by the Sec of State or the official receiver 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?

S246ZB of the Insolvency Act deals with the offence of wrongful trading which a director can be held liable for if they knew or ought to have known at some time before the company entered insolvency administration that there was no reasonable prospect of the company avoiding such administration. Liability only arises if, on a net basis, it is shown that the company is worse off as a result of continuing trading. An administrator can bring an action under s 246ZB to look into a director's conduct. If a director is found guilty of this offence, he may be liable to contribute to the assets of the company.

Under s 6 of the CDDA, deals with disqualification of current or former directors of insolvent companies where the director's conduct makes him unfit to be concerned in the management of a company. An action under s 6 is brought by the Insolvency Service on behalf of the relevant Secretary of State and is determined by the court. The court is obliged to make a disqualification order where the requirements of s 6 are met.

Section 423 of the Insolvency Act deals with the setting aside of transactions that were aimed at defrauding creditors. If a company is in liquidation or administration, a liquidator or administrator or with the court's consent, any victim of the transaction such as a creditor would be entitled to bring a claim under s 423. If the company is subject to a company voluntary arrangement, the supervisor of the CVA or any victim of the transaction whether bound by a CVA or not. In all other cases, an application can be brought by the victim of the transaction. It will be necessary for the applicant to show:

- 1. That the company entered into the transaction with another party at an undervalue; and*
- 2. The purpose of the transaction was either to put the assets beyond the reach of the applicant or a potential claimant or prejudice the interests of the applicant or a potential claimant in relation to the claim they are making or may make (as the case may be)*

Question 2.2 [maximum 5 marks]

Commented [WPA5]: 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 payment holiday relates to debts that arose pre-Moratorium that a company is entitled to stop paying during the Moratorium period. However, the company is still required to pay the following amounts:

- 1. The fees and expenses of the monitor who supervises the Moratorium*
- 2. Goods and services supplied during the Moratorium*
- 3. Rent payments falling due during the Moratorium*
- 4. Employee wages under an employment contract*
- 5. Redundancy payments*

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

Commented [WPA6]: 14/15

Question 3.1 [maximum 6 marks]

Commented [WPA7]: 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?

Yes, section 233 and 233A of the Insolvency Act 1986 make ipso facto clauses which are contained in contracts for the supply of essential goods and services void. Essential goods and services are gas, electricity, water and communications services. Communications services are IT related services and include the supply of POS terminals, computers- both hardware and software, information, advice, technical assistance, data storage and processing and website hosting.

Under these sections, a supplier of such services is prohibited from terminating or negatively altering a contract based on a company's insolvency or requiring payment of arrears to continue supplying the company if the company is in administration or has entered into a company voluntary arrangement (CVA).

If the company is in administration, as in this case, the administrator can require the essential supplier to continue supplying the company but that supplier is permitted to request the administrator to personally guarantee the payment of costs in relation to the continued supply of goods and services. The arrears will however rank as unsecured debts.

Section 233B of the Insolvency Act which was introduced by the Corporate Insolvency and Governance Act 2020, expands the net to cover all suppliers of goods and services except a limited number of suppliers such as banks, insurance companies, securitization companies, clearing houses, electronic money institutions, recognized investment exchanges and companies which perform similar functions overseas. All suppliers are now prohibited from terminating or doing any other thing in relation to a contract if a company enters into administration, or an administrative receiver is appointed, or the company goes into liquidation or a CVA or a Part A1 Moratorium under the Insolvency Act or a Part 26A Restructuring Plan under the Companies Act.

That means that all suppliers cannot change the terms of the contract to negatively impact the company such as demanding higher prices or require payment of arrears before they can continue to supply the company. The administrator can therefore require suppliers of the company to continue supplying the company.

Unlike in section 233, a supplier of non-essential goods and services cannot compel the administrator to issue a personal guarantee for their continued supply. The only relieve that such a supplier has is to ask the administrator or the company or the

courts for permission to terminate the contract. The courts will consent if they are satisfied that continued supply 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 payment waterfall in a liquidation is as set out below in order of priority from top to bottom:

- 1. Secured creditors*
- 2. Expenses of the liquidation including the liquidator's fees*
- 3. Preferential creditors*
- 4. Floating charge holders less the prescribed part which will be paid to unsecured creditors*
- 5. Unsecured creditors*
- 6. Shareholders*

Secured creditors

These are creditors who have fixed charge securities over the company's assets. They would usually be paid from the sale of the secured assets they hold.

Expenses of the liquidation

The following are the liquidation expenses under section 115 of the Insolvency Act and rules 6.42 and 7.108 of the Insolvency Rules 2016 in order of priority:

- 1. expenses that are properly incurred by the liquidator in preserving, collecting or selling the company's assets (including the cost of legal proceedings);*
- 2. costs of any security provided by the liquidator;*
- 3. any amount payable to any person to assist in preparing the statement of affairs or accounts of the company;*
- 4. disbursements incurred during the liquidation;*
- 5. the remuneration of any person employed by the liquidator to perform services for the company;*
- 6. the liquidator's remuneration;*
- 7. corporate tax on any chargeable gains arising on the sale of the assets;*
- 8. any other expenses properly chargeable by the liquidator in carrying out his role.*

Preferential creditors

There are two classes of preferential debts- ordinary and secondary with the former ranking higher than the latter. The ordinary debt consist of payments due to employees including holiday pay and their pension contributions, levies on the

Commented [WPAB]: 8/9 a very good answer. A little more detail and explanation on one or two points would have been helpful eg detail on classes of preferential debt, detail on s 176A etc.

production of coal and steel under the European Coal and Steel Community Treaty, claims for unpaid amounts owed under the Reserve Forces (Safeguard of Employment) Act 1985 and a certain amount owed to depositors by a deposit taking financial institution in respect of eligible deposits. Secondary preferential debts relate to other payments owed to depositors by financial institutions and certain debts owed to the HMRC e.g. PAYE deductions, NI deductions, VAT payments, student loan payments and construction industry scheme deductions.

Importantly debts rank equally within each class and are subject to pro-rating if the company's assets are not sufficient to pay them in full.

Floating charge holder

These are secured creditors who hold floating charges. The priority between floating charge holders will depend on when their floating charges were created.

Floating charge holders are usually not paid in full unless the company's assets are sufficient to pay all unsecured creditors. The liquidator is required to deduct what is known as the "prescribed part" from the payment that would be due to the floating charge holders. This prescribed part is then used to satisfy unsecured debts.

The amount of the prescribed part depends on the amount of the company's net property i.e. the amount that would be due to floating charge holders if they were being paid in full. If the net property is less than GBP 10,000 and the liquidator is of the view that making the distribution to unsecured creditors would be disproportionate to the benefits, then the "prescribed part" deduction will not apply.

Importantly, where a secured creditor holding a fixed charge or a floating charge has an unsecured portion of their debt, they are not permitted to participate in the distribution of the prescribed part to unsecured creditors.

Unsecured creditors

These are creditors who have no security over the company's assets. They would usually be the trade creditors of the company. There is often very little left to pay them, so they tend to suffer the most out of all the creditor groups.

Shareholders

These are the owners of the insolvent company. They would only get paid if there is any surplus after paying all the creditor groups mentioned above. It is therefore very unlikely that they will receive any payments. The distribution to shareholder is based on the company's Articles of Association.

PART A1 MORATORIUM

If a company enters liquidation following a Part A1 Moratorium, the payment waterfall changes. Under section 174A of the Insolvency Act, debts which did not form part of the payment holiday during the Moratorium period rank higher in liquidation than all

other claims (except secured creditors) thereby acquiring a "super priority" in the liquidation. The super priority debts are as follows:

- *Any prescribed fees or expenses of the official receiver acting in any capacity in relation to the company*
- *Moratorium debts and priority pre- Moratorium debts.*

Priority pre-Moratorium debts are the following debts:

- *Any pre-moratorium debts relating to the debt categories set out in the response to question 2.2 above.*
- *Any pre-moratorium debts that fell due before or during the moratorium.*
- *Any pre-moratorium debt that (i) arises under a contract or other instrument involving financial services (ii) fell due before or during the Moratorium and (iii) is not relevant accelerated debt. Contracts for financial services include lending agreements, financial leasing agreements and guarantees. Relevant accelerated debt means debt which become due during the Moratorium because of the exercise of an acceleration or early termination right by the lender.*

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

Commented [WPA9]: 10/15

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;

The liquidator could apply to court to set aside the floating charge under section 245 of the Insolvency Act on the basis that the Company granted an invalid floating charge to Fretus Bank. Section 245 is designed to prevent a company from benefitting a creditor by issuing a floating charge in respect of existing debt. The floating charge is created by the debenture.

It appears from the facts that Fretus Bank did not have any security but was only granted security because of commercial pressure. Fretus Bank did not provide any consideration such as additional funding or a debt reduction to justify the grant of the debenture which contained the floating charge.

The floating charge was granted within 12 months of the Company going into liquidation and it is clear from the facts that the Company was financially distressed when the debenture was granted and was likely cash flow insolvent. The Company would only have been concerned about the company loan being accelerated if it was already in breach under the relevant loan agreement. It is unclear whether the default was a payment default or other default. A payment default would have further proved that the Company was unable to pay its debts as they fell due when the debenture was granted.

Question 4.2 [maximum 6 marks]

The sale of the marble cutting machines; and

The liquidator could apply to court to set aside this sale on the basis that the transaction was done at an undervalue pursuant to section 238 of the Insolvency Act. The liquidator will need to show that :

- 1. the Company received significantly less value from Rita Perkins than what it paid for the machines. It is arguable whether the GBP 10,000 Rita paid is significantly less than what the Company paid. It will depend on whether a valuation of the machines was done before they were sold which would have guided the Company on what the sale price should be.*
- 2. The transaction was done 2 years before the liquidation. This is clear from the facts*
- 3. The Company was unable to pay its debt as they fell due or became unable to pay its debts as a consequence of the sale. This is presumed because Rita is*

Commented [WPA10]: 4/5 a good answer - perhaps a little more detail on possible defences by the bank and the proving of inability to pay debts would have strengthened the answer further.

Commented [WPA11]: 6/6

connected to the Company by virtue of being a director. It is also clear from the facts that the Company was having cash flow problems before the sale.

Rita's defence could be that the transaction was entered into by the Company in good faith and for the purpose of continued trading and that at the time of the sale, there were reasonable grounds for believing that the transaction would benefit the Company. She may be able to prove this easily if she has access to or is in possession of the minutes of the board meeting in which the sale was approved and those minutes show the grounds for approval of the sale.

Question 4.3 [maximum 4 marks]

The payments to Hard and Fast Ltd.

The liquidator could apply to court to set aside the payments made on Hard and Fast Ltd on the basis that they are a preferential transaction under section 239 of the Insolvency Act. The liquidator will need to show that:

- 1. Hard and Fast Ltd is a creditor of the company which is clear from the facts. They are a trade creditor.*
- 2. The Company did something which put Hard and Fast in a better position that they would have been if the company went into liquidation without making the payment. From the facts it's clear that the payments have placed Hard and Fast Ltd in a better position than they would have been in. If the payments hadn't been made, they would have ranked as an unsecured creditor in liquidation and probably not received full payment of their outstanding debt.*
- 3. The Company was influenced by a desire to put Hard and Fast in a better position. From the facts, the Company was influenced by the desire to continue trading rather than preferring Hard and Fast. It has been determined by the courts that where a company was influenced solely by commercial considerations, particularly an attempt to ensure that the company continued trading, there could be no such desire to prefer a creditor. This limb is therefore likely to fail.*
- 4. The preference was made 6 months before the liquidation. This is clear from the facts since the preference was made one month before the liquidation.*

*** End of Assessment ***

Commented [WPA12]: 0/4 unfortunately the issue is misidentified. The payments were made after the commencement of the winding up so s 239 cannot apply. The answer required consideration of s.127.