



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 3A

THE INSOLVENCY SYSTEM OF THE UNITED STATES

***This is the*** summative (formal) assessment ***for*** Module 3A ***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 3A. ***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.assessment3A]. An example would be something along the following lines: 202223-336.assessment3A. 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 "student number" 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 3A 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 3A 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 9 pages.

#### ANSWER ALL THE QUESTIONS

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

Commented [la2]: Total marks 10/10

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

Commented [la3]: Correct, 1 mark

Which of the following entities does not satisfy the minimum presence requirement to be a debtor under any chapter of the Bankruptcy Code?

- (a) A foreign domiciled company that pays a US attorney a retainer.
- (b) A company with several US bank accounts, but no physical presence in the United States.
- (c) A company with US patents, but no physical presence in the United States.
- (d) All of the above satisfy the minimum requirement for presence in the United States.**
- (e) None of the above satisfy the minimum requirement for presence in the United States.

#### Question 1.2

Commented [la4]: Correct, 1 mark

ABC Corp is an industrial manufacturing company that is filing for bankruptcy. Which of the following could not be considered a party in interest?

- (a) A neighboring landowner to ABC Corp's manufacturing plant.
- (b) An environmental advocacy group that opposes ABC Corp's operations.**
- (c) The landlord of ABC Corp's corporate office.

- (d) *People who live several miles downstream from ABC Corp's manufacturing plant and have been exposed to the plant's toxic waste.*
- (e) *The US Internal Revenue Service.*

Question 1.3

Commented [la5]: Correct, 1 mark

*Which of the following contracts to which ABC Corp is a party is executory and may be assigned without counterparty consent?*

- (a) A lease on a manufacturing plant that contains a provision that requires landlord approval of any assignment.**
- (b) *An employment contract between ABC Corp and a former employee, requiring the company to provide health insurance through the end of the current year.*
- (c) *A 10-year software licensing agreement with XYZ Corp that is three years into performance.*
- (d) *A lease on office space that ended the prior year, but for which ABC Corp still owes past rent.*
- (e) *None of the above are executory and may be assigned without counterparty consent.*

Question 1.4

Commented [la6]: Correct, 1 mark

*Which of the following conditions must be true about a reorganization plan for a court to confirm it under Chapter 11 proceedings?*

- (a) *Have a possibility of success, even if it relies on speculative or improbable events to be capable of execution.*
- (b) The plan is not likely to be followed by liquidation.**
- (c) *All impaired classes must accept the plan.*
- (d) *All of the above.*
- (e) *None of the above.*

Question 1.5

Commented [la7]: Correct, 1 mark

*Which of the following about cramdowns, is false?*

- (a) *The plan of reorganization must be fair and equitable to all impaired classes.*
- (b) *Differential treatment of different classes is permitted if there is a reasonable, good faith basis for doing so and such treatment is required for the plan of reorganization to be successful.*
- (c) *Class definition is often a battleground when a debtor tries to cramdown classes.*
- (d) *Dissenting creditors are permitted to challenge the classification of a creditor supporting the cramdown.*
- (e) *If one insider creditor approves of the plan of reorganization, all other impaired classes may be crammed down.*

Question 1.6

Commented [la8]: Correct, 1 mark

Which of the following about 363 sales is false?

- (a) *A good faith purchaser at a 363 sale may retain the property notwithstanding a subsequent reversal of court approval for the sale on appeal.*
- (b) *The debtor in possession must establish that the transaction is in the best interests of the estate as a whole.*
- (c) *In chapter 15 proceedings, a foreign court's approval alone suffices for a 363 sale.*
- (d) *Debtors must carry out a robust marketing process for the sale.*
- (e) *A creditor's lien on assets sold in a 363 sale attaches to the proceeds of the sale.*

Question 1.7

Commented [la9]: Correct, 1 mark

Which of the following is true of both an actual fraudulent conveyance and a constructive fraudulent conveyance?

- (a) *The debtor must have had an actual intent to hinder, delay, or defraud any entity to which the debtor was or became indebted.*
- (b) *Both require at least circumstantial evidence of the fraudulent intent.*
- (c) *The debtor must have been insolvent at the time of transaction.*
- (d) *In addition to provisions in the Bankruptcy Code, the debtor or the trustee may invoke applicable state or foreign fraudulent conveyance laws.*
- (e) *All of the above are true.*

Question 1.8

Commented [la10]: Correct, 1 mark

*When does an automatic stay come into effect?*

- (a) Immediately on the filing of any plenary petition.**
- (b) *On the filing of a voluntary petition but not on the filing of an involuntary petition.*
- (c) *Once the court reviews the petition and grants the stay.*
- (d) *Once the petitioner announces their intention to file for bankruptcy publicly.*
- (e) *Once a plan of reorganization is confirmed.*

Question 1.9

Commented [la11]: Correct, 1 mark

*Which of the following regarding substantive consolidation is true?*

- (a) *It respects the boundaries of corporate separateness.*
- (b) *It is the treatment of two or more creditors as a single creditor to simplify the claims process.*
- (c) If a creditor can show it extended credit on the basis of corporate separateness, it has a valid objection to substantive consolidation.**
- (d) *Substantive consolidation is commonly used to resolve bankruptcies of corporate groups.*
- (e) *Authority for substantive consolidation comes from the Bankruptcy Code.*

Question 1.10

Commented [la12]: Correct, 1 mark

*Which of the following are relevant factors in determining a debtor's center of main interests (COMI) in the recognition stage of a Chapter 15 bankruptcy case?*

- (a) *The location of the headquarters.*
- (b) *The location of primary assets.*
- (c) *The location of the majority of the affected creditors in the request for relief.*
- (d) *The jurisdiction whose law will apply to most disputes.*
- (e) All of the above.**

**QUESTION 2** (direct questions) [10 marks]

**Commented [la13]:** Total marks 8.5/10

**Question 2.1** [1 mark]

**Commented [la14]:** Total marks 1/1

**What is setoff and why is it not permitted in many circumstances?**

*Setoff is where a creditor simultaneously holds a creditor claim against a debtor and owes the debtor monies. It is not permitted typically as it disadvantages other unsecured creditors given that a creditor employing setoff can decrease the amount it owes by the full amount of its claim which typically would not be paid in full by the debtor.*

**Commented [la15]:** Correct, 1 mark

**Question 2.2** [2 marks]

**Commented [la16]:** Total marks 2/2

**What rules should you review when preparing a filing for a bankruptcy court?**

*When preparing a filing for a bankruptcy court you should review the judges rulings and personal preferences, the Bankruptcy Rules, the local bankruptcy rules and the Federal Rules of Civil Procedure.*

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**Commented [la18]:** Correct, 1/2 mark

**Commented [la19]:** Correct, 1/2 mark

**Commented [la20]:** Correct, 1/2 mark

**Commented [la21]:** Total marks 1/2

**Question 2.3** [2 marks]

**What does the absolute priority rule require and when can it be deviated from?**

*The absolute priority rule requires that no creditor or class of creditors can receive worse treatment under a reorganisation plan than they would get under a chapter 7 liquidation unless they consent. It can be deviated from if a creditor consents to receiving less than the absolute priority rule in order to obtain approval of the plan from other classes.*

**Commented [la22]:** Partially correct, 1 mark, specifically the absolute priority rule requires that no junior class of creditors can receive anything unless all senior classes have been paid in full

**Question 2.4** [2 marks]

**Commented [la23]:** Total marks 1.5/2

**What is a "priming lien" and what requirements must be met for such a lien to be granted to secure DIP financing?**

*A priming lien is a lien on estate property that is of equal or senior priority to a pre-petition lien on the estate property used in order to gain post-petition financing. In order for such a lien to be granted the debtor by the court, it needs to demonstrate that the interest of the secured creditor that is being primed is protected adequately.*

**Commented [la24]:** Correct, 1 mark

**Commented [la25]:** Correct, 1/2 mark, also the debtor must show that financing is not available without the priming lien

**Question 2.5** [3 marks]

**Commented [la26]:** Total marks 3/3

**What is a preference? What are the elements of a preference claim that need to be proved? Is a showing of fault, by either the debtor or creditor, required?**

A preference is a transfer of property belonging to a debtor made in the 'suspect period' prior to the petition date, it must be returned back to the the debtor estate if it is in excess of the amount the recipient would received in a chapter 7 liquidation had the transfer not taken place. In order to qualify as a preference the transfer must have been made to a creditor at the time, it must have been a transfer of an interest of the debtors property, the debtor must have been insolvent at the time. Additionally the transfer must have been during the suspect period of 90 days pre-petition of 1 year pre-petition if to an insider. Unlike a fraudulent conveyance there is no need to show any fault by either the debtor or creditor in order to qualify as a preference transfer.

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Commented [la28]: Correct, 1/2 mark

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Commented [la31]: Correct, 1/2 mark

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

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**Question 3.1** [3 marks]

**Describe the circumstances in which a bankruptcy court may enter a final order, who reviews appeals from bankruptcy court orders and how are non-final orders reviewed?**

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A bankruptcy court may enter a final order where it has received a district court's delegated authority to enter a final order for a motion that challenges a petition validity. Furthermore, a bankruptcy court can also enter a final order in proceedings deemed 'core proceeding' provided that they do not invade the jurisdiction of Article III. Generally speaking appeal decisions for bankruptcy court decisions will be heard by the relevant district court, however in some circuits these appeals are heard by a Bankruptcy Appellate Panel (BAP) made up of judges from bankruptcy courts within the circuit.

Commented [la34]: Correct, 1/2 mark, the bankruptcy court also may enter final orders in core proceedings with the consent of the parties

Commented [la35]: Correct, 1/2 mark

Commented [la36]: Correct, 1/2 mark

In the case of non-final orders these are reviews by the BAP or relevant district court from the beginning with all facts and conclusions of law that have been objected to reviewed.

Commented [la37]: Correct, 1 mark

**Question 3.2** [3 marks]

Commented [la38]: Total marks 2/3

**What provisions of the Bankruptcy Code automatically apply to the debtor's property within the territorial jurisdiction of the United States upon recognition of a foreign main proceeding? What relief may be granted on a discretionary basis for either foreign main or non-main proceedings?**

Section 1520 of the US Bankruptcy Code sets out the effects of recognition of a foreign main proceeding. It is stated that sections 361, 362 and 552 will apply to property of the debtor within the territorial jurisdiction of the United States. In addition to this, provided a court order is made otherwise, sections 363, 549 and 552 of the

Commented [la39]: Specifically, these sections provide for the automatic stay, use of property in the ordinary course, sale of property outside the ordinary course and avoidance of post-petition transfers and security interests.



Bankruptcy code will also apply to transfer of interests in debtor property that is located within the territorial jurisdiction of the United States.

Moreover the court presiding over the case may grant certain relief on a discretionary basis to either a foreign main or non-main proceeding, this includes the extension of any provisional relief granted, the authorisation of discovery in relation to the debtor's assets, the delegation of administration of the debtor's US assets to another person or any relief that is deemed "necessary to effectuate the purposes of chapter 15 and to protect the assets of the debtor or the interests of creditors".

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Commented [la41]: Correct, 1/2 mark

Commented [la42]: Correct, 1/2 mark

Commented [la43]: Correct, 1/2 mark

Question 3.3 [4 marks]

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What duties do directors owe to a Delaware corporation in the ordinary course of business? To whom are these duties owed when the corporation is potentially or actually insolvent? What rule protects directors from liability for errors of judgment?

In the state of Delaware directors owe a duty of care in educated decision making and a duty of loyalty for the corporation's best interests. Where potential errors of judgment are made by directors they are protected in the state by the business judgement rule which presumes that the directors have acted in good faith on the basis of reasonable information. In cases where the corporation is potentially or actually insolvent the duties of the directors are owed to the corporation and its shareholders as opposed to its creditors.

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Commented [la46]: Correct, 1 mark

Commented [la47]: Correct, 1 mark

Commented [la48]: Correct, 1 mark

Question 3.4 [5 marks]

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List and describe the requirements that a creditor's claim must fulfill in order to qualify as a petitioning creditor in an involuntary proceeding.

Under the Bankruptcy Code to qualify as a petitioning creditor in an involuntary proceeding certain criteria must be met by the creditor. First the creditor's claim against the debtor must be non-contingent, this meaning that the claim cannot be dependent on the occurrence of a future event, for these purported unmatured debts are not considered to be contingent if all requirements other than the time required for maturity have occurred.

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Commented [la51]: Correct, 1/2 mark

Secondly the petitioning creditors must be either unsecured or undersecured creditors and must collectively be at least worth USD 16,750.

Commented [la52]: Correct, 1 mark

Commented [la53]: Correct, 1/2 mark

Finally creditor claims against the debtor must not be disputed as to the amount or liability. This meaning that there cannot exist a legitimately reasonable reason for the liability or amount to be disputed via fact or law. The mere existence of a dispute does not require that the creditor claim be extinguished in full, in the event that a portion of

Commented [la54]: Partially correct, 1/2 mark, specifically there must be no "bona fide" dispute

Commented [la55]: Correct, 1/2 mark, also the creditor must allege that the debtor is not paying debts as they come due

*the debt claimed is disputed the creditor cannot utilise the disputed portion to meet the requirement for the collective claim to meet the USD 16,750 threshold.*

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

**Commented [la56]:** Total marks 8/15

**Question 4.1** [5 marks]

**Commented [la57]:** Total marks 4/5

***Speculation Inc is engaged in day-trading stocks from leased office space with two employees. It funds its trading through a margin loan from its broker, where the shares it purchases are held as collateral. For a while, Speculation Inc was very successful in trading, and the US Department of Justice (DOJ) has announced an investigation into whether its success was due to illegally trading on insider information. More recently, Speculation Inc has had serious trading losses, causing its broker to declare a default on the margin loan. It also has fallen behind on its rent, and been sued by a former employee alleging she was fired due to gender bias.***

***What would be the effect of a Chapter 11 petition being filed by Speculation Inc on each of the (i) DOJ investigation, (ii) margin loan default; (iii) delinquent lease and (iv) employment discrimination lawsuit?***

***The filing of a Chapter 11 petition invokes a sweeping automatic stay that prevent most actions from commencing or continuing against the debtor, albeit one of the few exceptions to the stay is for regulatory investigations. Therefore in the case of the DOJ investigation against Speculation Inc the DOJ investigation would be allowed to continue alongside the new Chapter 11 proceedings.***

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**Commented [la59]:** Correct, 1 mark

***The terms of the margin loan from the broker allowed for the shares purchased by Speculation Inc to be treated as collateral for the loan. The automatic stay provided by the filing of the Chapter 11 petition would prevent the broker from collecting on its margin loan from Speculation Inc as pre petition claims cannot be collected on. As shares were provided as collateral for the loan the claim belonging to the broker would be a secured claim and in addition to this would have additional protections in the event the collateral shares would need to be sold. If the loan was fully secured by the shares held as collateral the proceeds from selling would go to the broker (less costs to hold the shares) in settlement of the claim, in the event that the proceeds were not enough to satisfy the claim of the broker the remaining unsettled claim amount would be treated as an unsecured claim.***

**Commented [la60]:** Incorrect, the margin loan is a securities contract that is exempt from the stay, so the broker can sell the securities and apply the proceeds to the loan balance

***Upon the filing of the Chapter 11 petition the stay invoked would prevent the landlord from collecting on the delinquent rent owed by Speculation Inc., however in the event that the lease has expired at the time of the petition date, an exception is granted allowing for Speculation to be evicted from the office space. The treatment of the claim will depend on whether the lease contract can be rejected, in the event it is successfully rejected the landlord's claim will be treated as an unsecured pre-petition claim. However in the case of leases, a debtor which continues to occupy leased property cannot reject***

**Commented [la61]:** Correct, 1 mark

a lease contract, as it is assumed the contract is accepted. The assumption of the lease does not prevent Speculation Inc from later rejecting the lease, although this will raise the priority of the landlords claim and split it the claim into three priority claims, pre petition period ,the post petiion assumed lease period and the post petiton rejected lease period.

With regard to the employment discrimination lawsuit, this will likely be a civil lawsuit in the United States, in which case it will be subject to the stay granted by the Bankruptcy Code. In order for this claim to be pursued by the former employee they would either need to wait for the stay to be lifted by the ending of the Chapter 11 bankruptcy or apply for the stay to be lifted by the judge presiding over the case.

Commented [la62]: Correct, 1 mark

#### Question 4.2 [5 marks]

Commented [la63]: Total marks 1/5

**Stella SA (Stella) is a an international cosmetics company incorporated in France, with its headquarters in Paris. Stella's products are made in Italy and shipped to its retail stores in Europe (including England), Asia, and North America. Stella's funding comes from a bank loan and Eurobonds, both of which are governed by English law. Stella's retail sales have suffered due to pandemic-related closures and it is considering options to restructure its debt. One option is to use an English scheme of arrangement with respect to the Eurobonds. Could the English scheme of arrangement be recognized by a US bankruptcy court under Chapter 15, and would such recognition be as a foreign main or non-main proceeding?**

The United States Chapter 15 is closely linked to the UNCITRAL Model Law on Cross-Border Insolvency ("MLCBI") and is designed to facilitate more cooperation and efficient administration of cross-border insolvencies procesesces among other goals. Generally speaking the recognition of a foreign proceedings under Chapter 15 is a low bar to hurdle, although unlike other proceedings under the US Bankruptcy Code no automatic stay is invoked under the filings of a Chapter 15 petiton.

Under the US Bankruptcy Code a process needs to meet the definition of a foreign proceeding, which is defined as a "collective judicial or adminsstrative proceeding in a foreign country... under a lwa relatin got insolvency or adjustment of debt... subject to control or supervision by a foreign court", under this definition proceedings such as the English scheme of arrangement are allowed.

In order to be granted recognition the foreign representative of Stella would need to prove that a scheme of arrangemtn has been entered into, or is pending approval with the English court and furthermore, that the representative for Stella is authorised by the court to bring the proceeding to the US bankrucptcy court.

Although relativeily uncommon it is possible for recognition to be blocked on the basis of the public polociy exception, whereby the granting of recognition was in

contrary to US public policy, albeit in this case given the facts presented this is unlikely.

In terms of whether this proceeding would be classified as a foreign main vs. non-main proceeding it would be dependent on where Stella's center of main interests ("COMI") was deemed to be. Although a debtor's COMI is assumed to be its country of incorporation, this being Italy for Stella, COMI can be argued on a variety of factors. In order to argue that the COMI for Stella was in England, the jurisdiction for its scheme of arrangement, it would likely argue that England is its COMI given that English law will apply to most of its potential disputes as its debt is all governed by English law.

That being said, it is difficult to ascertain whether this argument would be sufficient before a judge and Stella would be wise to seek counsel advice on the best way to approach their petition with this in mind. Nonetheless the recognition of the Chapter 15 proceedings would be difficult to reject as the scheme of arrangement is a recognised process under the Bankruptcy Code and the public policy exception should not stand in the way of granting recognition as it is not against US policy.

Question 4.3 [5 marks]

ToyCo is an American toy company that has created a popular line of folding robot toys called Xblox. The toys are covered by several US patents. Currently, GameMart Inc (GameMart) has a 10-year exclusive license to manufacture Xblox and pays ToyCo monthly royalties. GameMart operates a factory in California that it leases from Land Corp on a longer term lease with seven years to go; the lease prohibits assignment without Land Corp's consent. The Xblox toys are selling well, but GameMart's other toy lines are doing poorly, so it is considering a Chapter 11 bankruptcy. Answer the following questions:

(i) Is the license to manufacture Xblox an executory contract?

The license to manufacture Xblox is not an executory contract as in most cases a contract is assumed to be executory if both parties have an unperformed obligation on their side, in this case GameMart Inc has an obligation to sell Xblox and pay royalties, whereas ToyCo does not have an obligation on their side, therefore this contract is not executory.

(ii) Can GameMart transfer the Xblox license as part of 363 sale without ToyCo's consent? Why or why not?

GameMart cannot transfer the Xblox licence without ToyCo's consent as part of a 363 sale.

**Commented [la64]:** Specifically, the proceedings could not be recognized as foreign main proceedings because Stella's COMI is not in the jurisdiction of the foreign proceedings. They can be recognized as non-main because the retail store in England qualifies as an establishment.

**Commented [la65]:** Correct, 1 mark

**Commented [la66]:** Incorrect, the facts state that Stella is incorporated in France, which is also where it has its headquarters, so the presumption is unlikely to be rebutted on these facts

**Commented [la67]:** Total marks 3/5

**Commented [la68]:** Incorrect, ToyCo must not sue GameMart for infringement or license the patents to third parties

**Commented [la69]:** Correct, 1 mark

*Counterparty consent of contractual assignment is required where more substantive non-bankruptcy law e.g. intellectual property law, seeks to enforce that that the counterparty cannot be forced to accept performance from the transferee.*

Commented [la70]: Correct, 1 mark

**(iii) Can GameMart transfer the factory lease as part of 363 sale without Land Corp's consent? Why or why not?**

*GameMart can transfer the factor lease as part of a 363 sale without land Corp's consent. Under Section 363 and 365(f) Gamemart can transfer the factory lease as long as GamerMart assumes the lease contract and the new assignee provides sufficient assurance that it will provide future performance of the lease contract.*

Commented [la71]: Correct, 1 mark

Commented [la72]: This is specifically because the Bankruptcy Code renders the anti-assignment provisions of the lease ineffective

\* End of Assessment \*