



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

Commented [la1]: Total marks 36/50

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

Commented [la2]: Total marks 6/10

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

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.*

Commented [la5]: Incorrect, the correct response is (a), the software agreement will include a copyright license that requires consent to assign

Question 1.4

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.*

Commented [la6]: Incorrect, the correct response is (b)

Question 1.5

Which of the following about cramdowns, is false?

Commented [la7]: Correct, 1 mark

- (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]: Incorrect, the correct response is (d) because insolvency is not required for actual fraudulent transfer

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]: Incorrect, the correct response is (c)

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 9/10

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 the process of dealing with creditor claims where there is a claim against the Debtor however the debtor simultaneously has money owing to the debtor. Setoff would net the two obligations.

Commented [la15]: Correct, 1/2 mark, I understand you to mean "creditor" rather than "debtor" at the end of the first sentence

It is not permitted in a number of cases as it reduces the amount available to general unsecured by the total amount owed to a creditor, applying setoff, and the setoff rights can improve the position of a creditor against the general unsecured creditors. This can mean they are better than what might be paid off in a dividend on the unsecured claim.

Commented [la16]: Correct, 1/2 mark

Question 2.2 [2 marks]

Commented [la17]: Total marks 2/2

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

- Bankruptcy Rules
- Federal Rules of Civil Procedure
- Local Rules of the bankruptcy court
- Judges Personal Practices

Commented [la18]: Correct, 1/2 mark

Commented [la19]: Correct, 1/2 mark

Commented [la20]: Correct, 1/2 mark

Commented [la21]: Correct, 1/2 mark

Question 2.3 [2 marks]

Commented [la22]: Total marks 2/2

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

It requires that payment in full must be made to each category of creditors claims before the next category can receive anything, and must not be deviated in Chapter 7. It can be deviated during a Chapter 11 plan only with consent from affected creditors.

Commented [la23]: Correct, 1 mark

Commented [la24]: Correct, 1/2 mark

Commented [la25]: Correct, 1/2 mark

Question 2.4 [2 marks]

Commented [la26]: Total marks 1/2

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 one where a debtor is unable to obtain any other type of financing such as unsecured loans. It can be granted if the debtors can ensure that secured creditors are adequately protected from the diminution in value of their collateral as a result of the priming lien

Commented [la27]: Specifically, the lien is of equal or higher seniority to an existing lien on estate property

Commented [la28]: Correct, 1/2 mark

Commented [la29]: Correct, 1/2 mark

Question 2.5 [3 marks]

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 a debtors property made with in a certain period (90 days) before the petition date which must be returned to the estate if it exceeds the amount the recipient would have received in a chapter 7, if the transfer had not been made.

The elements that need to be proved are

- 1) *It is the transfer or the interest of the debtor in property*
- 2) *It is to or for the benefit of a creditor*
- 3) *It is on account of the debt owed by the debtor before the transfer was made*
- 4) *It was made when the debtor was insolvent*
- 5) *It is made during a "suspect period" which is within 90 days prior to the petition date*
- 6) *And it enables the creditor to receive more then it would in a Ch 7 liquidation.*

There is not a requirement to show fault of either the debtor or the creditor in connection with the transfer, the creditor will not receive a penalty other than the requirement to return the transfer.

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

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?

As bankruptcy courts are a special federal court for bankruptcy matters, bankruptcy judges are appointed by courts of appeal rather than the president, and therefore do not have lifetime tenure and have limited jurisdiction to enter final orders other than on core bankruptcy issues. Core and non-core is important and at the start of each motion or pleading, the parties must state whether the matter at issue is core or non-core so that the bankruptcy court can determine the scope of its jurisdictions and the power to rend a final order or judgement Final Orders are those that dispose of all issues and leave nothing to be decided.

The bankruptcy court must identify the complete unitary procedural unit and second the court must determine whether the court order definitively and conclusively resolves that proceeding.

Orders can be appealed not only by litigants but also persons who are adversely affected by the ruling and therefor can seek a review. The bankruptcy Appellate Panel

Commented [la30]: Total marks 3/3

Commented [la31]: Correct, 1 mark

Commented [la32]: Correct, 1/2 mark

Commented [la33]: Correct, 1/2 mark

Commented [la34]: Correct, 1/2 mark

Commented [la35]: Correct, 1/2 mark

Commented [la36]: Total marks 13/15

Commented [la37]: Total marks 1/3

Commented [la38]: Specifically, the bankruptcy court can enter final orders on core proceedings that are specific to the bankruptcy code (such as a challenge to a petition) or with the consent of the parties. Orders that are not constitutionally final are reviewed on appeal as a report and recommendation.

(BAP) is convened by judges within the circuit and final orders where appeal is sought, are heard in front.

Commented [la39]: Correct, 1/2 mark, this is only in certain circuits; in others, appeals are heard by the district court

Question 3.2 [3 marks]

Commented [la40]: Total marks 3/3

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?

Foreign main proceedings are those that commenced in the debtors COMI. As outlined above, a debtors COMI is presumed to be its place of incorporation however relevant factors include the location of headquarters; the location of management; location of primary assets; location of the majority of affected creditors; and also, jurisdiction whose law will apply to most disputes.

Chapter 15 enacts the UNCITRAL Model Law, with some modifications and is the procedure for recognition of foreign proceedings and coordination of US and Foreign Proceedings. Upon recognition of a foreign proceedings, the following provisions of the Bankruptcy code apply to the debtors property within the territorial jurisdiction of the United States;

- 1) Automatic Stay;
- 2) Operation of the debtor's business in the ordinary course of business by foreign representatives
- 3) Sale, transfer or use of property outside the ordinary course
- 4) Avoidance of post-petition transfers and post-petition perfection of security interests.

Commented [la41]: Correct, 1/2 mark

Commented [la42]: Correct, 1/2 mark

Commented [la43]: Correct, 1/2 mark

On a discretionary basis, the following provisions may be granted

- 1) Authorisation of discovery regarding the debtors' assets and affairs
- 2) Entrusting administration of the Debtors US assets to foreign representatives or other persons
- 3) Extension of provisional relief
- 4) Any relief necessary to effectuate the purpose of Chapter 15 and to protect the assets of the debtor or the interest of creditors.

Commented [la44]: Correct, 1/2 mark

Commented [la45]: Correct, 1/2 mark

Commented [la46]: Correct, 1/2 mark

Where it is sought in non-main proceedings, the bankruptcy court must be satisfied that it is appropriate under US law for the assets in question to be administered in the foreign main proceeding.

Question 3.3 [4 marks]

Commented [la47]: Total marks 4/4

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?

Directors, on the basis of the law of Delaware, owe a fiduciary duty of loyalty to the corporations best interest and a duty of care in educated decision. The Business judgment rule book protects directors from liability for errors in judgement. Directors' duties are owed to the corporation and its shareholders, but not to creditors, even if the company is potentially or actually insolvent where the shareholders stand to receive nothing. Under the business judgement rule book, the director is believe to have shown good faith, on the basis that he received reasonable information. This can be rebutted, if the board were not reasonably informed, did not act in the corporation's best interest or were not acting in good faith.

Commented [la48]: Correct, 1 mark

Commented [la49]: Correct, 1 mark

Commented [la50]: Correct, 1 mark

Commented [la51]: Correct, 1 mark

Question 3.4 [5 marks]

Commented [la52]: Total marks 5/5

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

To qualify as a petitioning creditor the creditor must have a claim against the debtor that is;

Non Contingent and not the subject of bona fida dispute as to the liability or amount and is unsecured or undersecured in the amount of at least US\$ 16750.

Commented [la53]: Correct, 1 mark

Commented [la54]: Correct, 1 mark

Commented [la55]: Correct, 1 mark

Commented [la56]: Correct, 1/2 mark

Commented [la57]: Correct, 1/2 mark

Non contingent implies that it is not subject to claim on the occurrence of a future event eg defaulting a guaranteed obligation and that the claim is under guarantee. It also implies that the debt is matured, as all requirements for the liability have occurred.

With respect to bona fida, the creditor claim is required to not be disputed on an objectively reasonable basis as a matter of fact or law, not that the debtors belief is that it is not correct.

Commented [la58]: Correct, 1/2 mark

An involuntary petiton form also requires the petitioning creditor to allege either that the debtor is not paying its debts as they fall due, unless subject to bona fida dispute or within 120 days before the filing date a trustee, receiver or an agent appointed or authorised to take charge of less than substantially all of the property of the debtor for the purpose of enforcing a lien against such property was appointed or took possession.,

Commented [la59]: Correct, 1/2 mark

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

Commented [la60]: Total marks 9/15

Question 4.1 [5 marks]

Commented [la61]: Total marks 2/5

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?

(i) **DOJ Investigation**

The effect of a chapter 11 petition being filed by Speculation Inc with respect to DOJ investigation would be that they stay in proceeding against the debtor so the DoJ will not be able to launch any action against Spectrum whilst it is Ch11

Commented [la62]: Correct, 1 mark

Commented [la63]: Incorrect, there is an exception to the automatic stay for regulatory investigations, so the DOJ could proceed

(ii) **Margin Loan Default**

The effect of the Chapter 11 will be that the company can look to restructure its debt with the broker to understand whether it will be able to come to an agreement with the broker and look to restructure the payment terms

Commented [la64]: Incorrect, the margin loan is a securities contract that is exempt from the automatic stay so the broker is free to sell the shares and apply the proceeds to the loan balance

(iii) **Delinquent Lease**

Should a Ch11 process be initiated then this will put a stay on creditor action during the proceeding and therefore cannot launch a claim for the monies back.

Commented [la65]: Correct, 1 mark, also the landlord cannot initiate eviction proceedings

(iv) **Employment discrimination lawsuit**

Effect of the chapter 11 would not have any impact on speculation, if there is a lawsuit against the Company prior to Ch11 then this will carry on through the CH11

Commented [la66]: Incorrect, the automatic stay applies to pre-bankruptcy civil litigation like this

Question 4.2 [5 marks]

Commented [la67]: Total marks 4/5

Stella SA (Stella) is 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?

A foreign proceeding is defined by the Bankruptcy code as “a collective judicial or administrative proceeding in a foreign country...under a law relating to insolvency or adjustment of debt in which proceeding the assets and the affairs of the debtor are subject to control or supervision by a foreign court for the purpose of re-organisation or liquidation”.

Where there is a issue is whether foreign proceedings is treated as foreign main or foreign non main. Foreign main proceedings are comments in the Debtors Centre of Main interest (COMI) and as defined above COMI is presumed to be its placed of incorporation however can also include the location of headquarters; the location of management; location of primary assets; location of the majority of affected creditors; and also, jurisdiction whose law will apply to most disputes. Proceedings in the a jurisdiction other then the Debtors COMI can be recognised as foreign non maim proceedings.

An English scheme or arrangement can be recognised by a US Bankruptcy Court and the requirements of recognition are minimal. The foreign representative must establish that a foreign court or administrative proceeding with respect to the debtor is pending and that the foreign representative is empowered to act by the proceeding.

With respect to the above, we understand that Stella is incorporated in France with headquarters in Paris and therefore would be assumed that this would be its COMI. Therefore, France would be the foreign main proceeding, and as a result the English scheme of arrangement would be under a foreign non main proceeding

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?

A contract is said to be executory if there are material unperformed obligations on both sides. Where it is said to be executory in this case is if, at the time of the petition date the obligation to make toys is only partially complete and the payment of said manufacturing is not complete then it would executory. In this case, it is an executory contract.

Commented [la68]: Correct, 1 mark

Commented [la69]: Correct, 1 mark

Commented [la70]: Correct, 1 mark

Commented [la71]: Correct, 1 mark, because the retail store in England is the necessary establishment

Commented [la72]: Total marks 3/5

Commented [la73]: Correct, 1 mark, though specifically the obligations are to pay royalties (GameMart) and to maintain exclusivity (ToyCo)

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

No, given that Toygo is paid royalties it will mean that there is some form of property, probably intellectual property and therefore any licensees of patents are owned by Toygo can not be sold with out the consent from Toygo

Commented [la74]: Correct, 1 mark

Commented [la75]: Correct, 1 mark

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

Given that the factory lease is not free of creditor interest and that the lease prohibits assignment without land corps consent then GameMart cannot transfer the factory lease as part of a 363 sale.

Commented [la76]: Incorrect, the anti-assignment provisions of the lease are not effective in bankruptcy so the lease can be assigned without consent

* End of Assessment *