



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 35/50

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

Commented [la2]: Total marks 7/10

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]: Incorrect, the correct response is (e)

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]: Incorrect, the correct response is (c)

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)

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 0.5/1

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

Setoff can improve the position of a creditor when compared with other creditors who are not owed money by the debtor because it decreases its obligation to the estate by the full amount owed by the debtor rather than the lesser amount the debtor would pay on the unsecured claim.

Commented [la15]: Correct, 1/2 mark, also setoff is defined as offsetting the amount owed by the debtor and by the creditor so that only the net amount is paid

Question 2.2 [2 marks]

Commented [la16]: Total marks 2/2

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

You should review the Bankruptcy Rules, the Federal Rules of civil procedure, the local rules of the bankruptcy court and the judges personal practices.

Commented [la17]: Correct, 1/2 mark

Commented [la18]: Correct, 1/2 mark

Commented [la19]: Correct, 1/2 mark

Question 2.3 [2 marks]

Commented [la20]: Correct, 1/2 mark

Commented [la21]: Total marks 1.5/2

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

The absolute priority rule requires that payment in full must be to each category of claims before the next category receives anything. Deviation from the absolute priority rule can be deviated from with consent of affected creditors.

Commented [la22]: Correct, 1 mark

Commented [la23]: Correct, 1/2 mark, though this is possible only in chapter 11, not chapter 7

Question 2.4 [2 marks]

Commented [la24]: 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 that is granted by court that is senior or equal to a pre-petition lien on estate property in order to secured post-petition financing. In order for the priming lien to be granted the debtor must show that the interest of the secured creditor being primed are adequately protected.

Commented [la25]: Correct, 1 mark

Commented [la26]: Correct, 1/2 mark, also the debtor must show that financing is not available without the priming lien

Question 2.5 [3 marks]

Commented [la27]: 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 the debtors property made in a period before the petition date that must be returned to the estate if it exceeds the amount the recipient would have received in a chapter 7 liquidation, had the transfer not been made. The elements of a preference claim are:

Commented [la28]: Correct, 1 mark

- A transfer of an interest of the debtor in property
- To or for the benefit of a creditor
- For an account of an antecedent debt owed by the debtor before the transfer was made.

Commented [la29]: Correct, 1/2 mark

Commented [la30]: Correct, 1/2 mark

Commented [la31]: Correct, 1/2 mark

The is no need to show fault by either the debtor or creditor.

Commented [la32]: Correct, 1/2 mark

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

Commented [la33]: Total marks 12/15

Question 3.1 [3 marks]

Commented [la34]: Total marks 1.5/3

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?

Bankruptcy Courts in the United States were created by legislation under power granted to Congress by Article I of the US Constitution. Bankruptcy Courts are special federal courts for bankruptcy matters which were created by legislation. Bankruptcy judges are appointed by the courts of appeal and have limited jurisdiction to enter final orders other than on core bankruptcy issues.

Commented [la35]: Specifically, the bankruptcy court can enter a final order if the core issue is specific to the Bankruptcy Code (such as a challenge to a petition) or with the consent of the parties

Appeal are heard by the district court for the district in which the bankruptcy court sits. The 1978 Bankruptcy Code contains a non-exhaustive list of core proceedings. The bankruptcy court can hear non-core proceedings if they are sufficiently related to the bankruptcy proceedings but they cannot make a final order. In the case of *Stern v Marshall* the court held that even in core proceedings a bankruptcy court cannot make a final order if the order invades the Article III jurisdiction. The district court reviews bankruptcy court orders. The bankruptcy court will issue a report of recommendations to the district court for review.

Commented [la36]: Correct, 1/2 mark, also in some circuits a Bankruptcy Appellate Panel hears appeals

A bankruptcy court cannot make a final order on non-core proceedings. Instead the bankruptcy court must submit it proposed findings of fact and conclusions of law to the district court for the district courts final decision.

Commented [la37]: Correct, 1 mark

Question 3.2 [3 marks]

Commented [la38]: 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?

Automatic Stay II USC, § 15209

Commented [la39]: Correct, 1/2 mark

Operation of the debtors business

Commented [la40]: Correct, 1/2 mark

Sale and transfer

Commented [la41]: Correct, 1/2 mark

Avoidance post-petition

Sections 361 and 362 apply to the property of the debtor

Sections 363, 549 and 552 apply to the transfer of an interest of the debtor of priority Foreign representative may operate the debtors business and may exercise the rights ad powers of a trustee in terms of sections 363 and 552

Section 552 applies to the debtors property within the United States

Any recognition of either the foreign main proceeding or foreign non-main proceeding the following relief may be granted:

Authorization of discovery regarding he debtors assets and liabilities

Entrusting the administration of the debtors US assets to the foreign representative

Extension of provisional relief

Any other relief " necessary to effectuate the purposes of Chapter 15 and to protect he assets of the debtor or the interests of creditors".

Commented [la42]: Correct, 1/2 mark

Commented [la43]: Correct, 1/2 mark

Commented [la44]: Correct, 1/2 mark

Question 3.3 [4 marks]

Commented [la45]: Total marks 3/4

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 owe a fiduciary duty of loyalty to the corporations best interests thus directors duties are owed to the corporation and its shareholders, not creditors. Even when the company is potentially insolvent, the directors still owe a duty towards the corporation and its shareholders, even if they potentially stand nothing to gain. The business judgement rule protects directors from liability for errors of judgement.

Commented [la46]: Correct, 1 mark, and also a duty of care

Commented [la47]: Correct, 1 mark

Commented [la48]: Correct, 1 mark

Question 3.4 [5 marks]

Commented [la49]: Total marks 4.5/5

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

The claim must be non-contingent. It must not rely on the execution of a future event and it must not be for an unmatured debt, in other words the requirements for liability have not yet occurred.

Commented [la50]: Correct, 1 mark

Commented [la51]: Correct, 1/2 mark, however note it can be unmatured if only the passage of time is required

The claim must not be the subject of a bona fide dispute as to liability or the amount. A bona fide dispute is one where there is a reasonable basis for a dispute either a matter of fact or law. If a portion of the amount claimed is disputed, the creditor cannot use the undisputed portion to reach the monetary threshold required. Unsecured, or under-secured, seperalty or in aggregation with all the petitioning creditors claims in the amount of at least USD 16750.

Commented [la52]: Correct, 1 mark

Commented [la53]: Correct, 1/2 mark, specifically an objectively reasonable basis

Commented [la54]: Correct, 1 mark

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

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 3/5

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) There would be no effect on the DOJ investigation as a Chapter 11 petition doesn't stay the investigation of criminal investigations because the automatic stay only applies matters relating to property of the estate, of which criminal investigations do not relate.

(ii) There would be an automatic stay on the collection of monies due in terms of the default of the margin loan because the automatic stay applies to any attempt to collect on pre-petition claims.

(iii) There would be automatic stay on collection actions by the landlord as this would be considered any attempt to collect on a pre-petition claim.

(iv) The case against the company brought by the former employee would also fall within the automatic stay as all litigation on pre-petition claims falls within the ambit of the automatic stay.

Question 4.2 [5 marks]

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?

Under Chapter 15 the filing of a petition by a foreign representative of a debtor commences Chapter 15 proceedings. The filing of the petition does not invoke automatic stay of creditors actions and the stay only arises on the petition for recognition being granted. It is also limited to the property of the debtor within the territorial jurisdiction of the United States. The requirements for recognition are minimal. In order to gain recognition 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 in the proceeding. The foreign

Commented [la58]: Correct, 1 mark, also specifically the filing of the petition would bring the automatic stay into effect

Commented [la59]: Incorrect, the margin loan is a securities contract that is exempt from the automatic stay so the broker can sell the collateral to pay down the balance of the loan

Commented [la60]: Correct, 1 mark, also the landlord cannot evict

Commented [la61]: Correct, 1 mark

Commented [la62]: Total marks 0/5

proceeding does not have to resemble a US bankruptcy case to be recognized. A foreign proceeding is defined 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 affairs of the debtor are subject to control by a foreign court for the purpose of reorganization or liquidation. This is a very wide definition which would encompass many diverse proceedings. Based on this the English scheme of arrangement would fall within the definition and would be recognized by a US bankruptcy court under Chapter 15.

In order for proceedings to be recognized as foreign main proceedings the debtor must have its center of main interest in the jurisdiction where the recognition application is being heard. The US typically uses the concepts of domicile, principal place of business and location of assets to determine the debtors center of main interest. A debtors center of main interest is ascertained on the basis of objective evidence and the court will consider the location of the debtors headquarters, location of management, location of primary assets, location of the majority of the debtors creditors and the jurisdiction of whose law will apply to most disputes.

I believe that the court will decide that the recognition by a foreign non-main proceeding because Stella is incorporated in France, not in the US. Its products are manufactured in Italy and its financing also derives from Eurobonds. These Eurobonds are governed by English law. Thus due to the fact that Stella has headquarters in a foreign jurisdiction, most of its assets are in foreign jurisdictions along with its creditors and that fact that the English law would apply to its major creditors, the court will recognize the application as 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?

Yes it is because a contract is considered to be executory if there are material unperformed obligations on both sides of the agreement. In this case GameMart has an contract to manufacture ToyCo's robot toys which contract is still operational.

Commented [la63]: Incorrect, the analysis looks to whether COMI is in the jurisdiction of the foreign proceeding, here the UK proceeding

Commented [la64]: Specifically, COMI would be presumed to be the jurisdiction of incorporation and where the headquarters is in the same jurisdiction, the presumption is unlikely to be rebutted. Here, because COMI is in France and not England, foreign non-main recognition would be appropriate as the retail store in England would be the necessary establishment

Commented [la65]: Total marks 5/5

Commented [la66]: Correct, 1 mark, specifically GameMart has to keep paying royalties and ToyCo has to keep the license exclusive (not license the same patents to others)

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

No. Because **licence agreements are not assignable without the licencors consent.**

Commented [la67]: Correct, 1 mark

Commented [la68]: Correct, 1 mark

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

Yes. GameMart may transfer the lease as part of a 363 sale without Land Corp's consent that is because **363 sales allow a debtor to transfer it interest in contracts even where those contract contain contractual restrictions.**

Commented [la69]: Correct, 1 mark

Commented [la70]: Correct, 1 mark

*** End of Assessment ***