



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 2024**. The assessment submission portal will close at 23:00 (11 pm) GMT on 1 March 2024. 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 2024** or by **23:00 (11 pm) BST (GMT +1) on 31 July 2024**. If you elect to submit by 1 March 2024, you **may not** submit the assessment again by 31 July 2024 (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

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 eight weeks of the commencement of the administration.**
- (c) within four weeks of the commencement of the administration.
- (d) on the day the company enters administration.

Question 1.2

What is the **maximum length** of a Moratorium under Part 1A of the Insolvency Act 1986 to which creditors can consent without any application to the court?

- (a) 40 business days.
- (b) One year and 20 business days.
- (c) One year and 40 business days.
- (d) One year.**

Question 1.3

Which of the following **is not** a requirement for a company that wishes to enter into a Restructuring Plan under Part 26A of the Companies Act 2006?

- (a) The company has encountered, or is likely to encounter, financial difficulties that are affecting, or will or may affect, its ability to carry on business as a going concern.
- (b) A compromise or arrangement is proposed between the company and its creditors, or any class of them, or its members, or any class of them.
- (c) The purpose of the compromise or arrangement is to eliminate, reduce or prevent, or mitigate the effect of, any of the said financial difficulties.

(d) The company is, or is likely to become, unable to pay their debts, as defined under section 123 of the Insolvency Act 1986.

Question 1.4

In cases where the Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021 apply and an independent report from an Evaluator is obtained, the independent report must be obtained by whom?

- (a) The administrator.
- (b) Any secured creditor with the benefit of a qualifying floating charge.
- (c) The purchaser.
- (d) The company's auditor.

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

Section 426 of the Insolvency Act 1986 contains provisions for UK courts to provide assistance to overseas courts from certain listed jurisdictions. Which of the following is not a listed jurisdiction under section 426?

- (a) Malaysia.
- (b) Australia.
- (c) India.
- (d) Hong Kong.

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 filing by a company's directors of a Notice of Intention to Appoint an administrator produces a short-term moratorium on actions against the company which lasts for how long?

- (a) Five business days.
- (b) Twenty business days.
- (c) Ten days.**
- (d) Three months.

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 if the director has been a director of the company during which period prior to the insolvent liquidation?

- (a) Six months.
- (b) Five years.
- (c) Two years.
- (d) Twelve months.**

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 5 marks]

Who may bring an action under: (i) section 245 of the Insolvency Act 1986, (ii) section 6 of the Company Directors Disqualification Act 1986, (iii) section 246ZB of the Insolvency Act 1986, and (iv) section 127 of the Insolvency Act 1986?

- i) Section 245 of the Insolvency Act 1986 (the "Act") applies to floating charges. If a floating charge meets the criteria under the section it will automatically be invalid, without the need for a court application. However, if the holder of the floating charge challenges the decision of the liquidator/administrator to treat the charge as invalid, then litigation as to its validity may ensue.
- ii) Disqualification orders under the CDDA 1986 are made by the Secretary of State (or the Official Receiver on the instruction of the Secretary of State).
- iii) Section 246ZB relates to wrongful trading when a company is in administration. Accordingly, it is the administrator with the power to bring an action. However, under section 246ZD the administration can assign the action.
- iv) Section 127 provides that any disposition of property, transfer of shares or alteration in the status of the company's members made after the commencement of the winding up is, unless the court otherwise orders, void. The effect is automatic, and therefore, the liquidator is not required to apply to court for a declaration a transaction is void (although may need to do so if it wants to recover property). However, anyone can apply for a validation order under s.127 so that the transaction will not be void (this will most commonly be the company itself or the third party who will receive the property).

Question 2.2 [maximum 5 marks]

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 Part A1 Moratorium only applies to pre-Moratorium debts. Debts incurred during the Moratorium there therefore not subject to the Moratorium. In addition to this, 5 types of pre-Moratorium debt that remain enforceable during the Moratorium include:

- i) Remuneration of expenses of the monitor - the "monitor" being a licenced insolvency practitioner appointed to supervise the directors during the Moratorium period;
- ii) Goods or services supplied during the Moratorium;
- iii) Rent payable during the Moratorium period;
- iv) Wages and salary under a contract of employment; and
- v) Redundancy payments.

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

Question 3.1 [maximum 6 marks]

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?

Section 233 of the Act allows an administrator to make a request of certain suppliers that they continue to provide supplies, and if such a request is made, the supplier shall not make it a condition of providing the supply that any outstanding charges are paid. However, the supplier can make it a condition of continuing supply that the administrator personally guarantees the payments for any charges. The supplies relevant to the section are: gas, electricity, water and "communications services" (the Act providing a list of services that meet this definition).

There are further protections of "essential" supplies (being the same as those listed in section 233(3)) under section 233A in that "insolvency-related terms" (i.e. *ipso facto* clauses that allow a party to terminate the contract upon certain insolvency trigger events) in contracts for essential services cease to have effect upon the company entering administration (or a voluntary arrangement).

Section 233B was introduced by the Corporate Insolvency and Governance Act 2020. It expanded the protections with regard to the supply of goods and services to negate the effect of *ipso facto* clauses in all contracts for goods and services not just essential supplies (with a few exceptions such as insurers and banks). The section does not just apply to clauses allowing the supplier to terminate the contract if the company enters a formal insolvency procedure, but also to clauses which allow the supplier to "do any other thing" (e.g. insisting that pre-insolvency arrears are paid as a condition to continued supply). However, under section 233B, the suppliers cannot insist on a personal guarantee from the administrator as it can under section 233.

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?

At the outset, it should be noted that secured creditors in respect of a fixed charge are generally considered to be outside of the liquidation and therefore do not feature on the following list of priority.

a) Expenses of the winding up

Section 115 of the Insolvency Act 1986 sets out certain expenses that take priority over creditors (even preferential creditors or those holding a floating charge). The first in priority is expenses properly incurred by the liquidator in preserving, realising or getting in any of the assets of the company (this includes conduct of legal proceedings). There then follow a number of expenses (without listing them exhaustively) which take priority before the remuneration of the liquidator, such as amounts payable to person assisting in preparing a statement of affairs or of someone who is employed by the liquidator to perform services for the company.

The remuneration of the liquidator is sixth in priority of expenses. After this comes corporation tax on chargeable gains accrued in realising the company's assets and, finally, any other expenses properly chargeable by the liquidator in carrying out their function.

b) Preferential creditors

Preferential creditors are next in priority, before any holders of floating charges. Preferential debts are divided into two classes: ordinary and secondary (with ordinary debts being paid before secondary debts). The debts in each of the categories rank equally amongst themselves.

Schedule 6 of the Act lists out types of preferential debt and are not regurgitated in full here. The most common preferential creditors encountered are certain claims of employees with regard to remuneration and their pension contributions. Note that the protection of employees' remuneration is very limited under the Act (being subject to maximum payment

of GBP 800). There are better protections under the Employment Rights Act 1996 and the protections under the Act are somewhat historic.

Another commonly-encountered preferential debt is in respect of certain tax liabilities (the so-called "Crown preference") which, although abolished by the Enterprise Act 2002, was reintroduced to a great extent by the Finance Act 2020.

Under Section 386(1B) of the Act, the following debts listed at Schedule 6 are "secondary preferential debts": a) amounts owed by the company in respect of eligible deposits that exceed the compensation payable under the Financial Services Compensation Scheme, b) amounts owed by the company in respect of a deposit made through a non-UK branch of an authorised credit institution that would have been an "eligible deposit" had it been made through a UK branch, and c) PAYE income tax deductions, national Insurance deductions, VAT payments, Construction Industry Scheme deductions and student loan repayments.

c) Floating charge holders

Floating charge holders rank next in priority. Where there are more than one, priority usually turns on which charge was created first. However, before any payment is made to a floating charge holder, the provisions of section 176A of the Act apply to any company with a floating charge created on or after 15 September 2003. Section 176A provides for the "prescribed part". This is a portion of the company's net assets that must be set aside to meet the claims of unsecured creditors (except that it does not apply to any excess to that required to settle all unsecured debts).

The prescribed part is 50% of the company's net property where that property does not exceed GBP 10,000. Where the net property is less than GBP 10,000 and the liquidator considers that making a distribution to unsecured creditors would be disproportionate to the benefits to those creditors, then the duty to distribute the prescribed part does not apply.

If a company's net property exceeds GBP 10,000 then the prescribed part is 50% of the first GBP 10,000 and 20% of anything in excess of GBP 10,000, up to a maximum of GBP 800,000.

Floating charge holders (and fixed charge holders) are not able to participate in the distribution of the prescribed part.

d) Unsecured creditors

Last in the order prescribed by statute are unsecured creditors who are paid out *pari passu*. In an insolvent liquidation, there is often little or nothing left to pay them.

e) Shareholders

If there is anything left after paying all unsecured creditors, then any surplus is distributed amongst the company's shareholders according to their rights under the company's constitution.

Moratorium under Part A1 of the Act

There is a slightly peculiar feature under Part A1 of the Act which alters the priority of debts in relation to a company that enters liquidation or administration within 12 weeks of the end of the Part A1 Moratorium.

Under section 174A of the Act, certain unpaid pre-Moratorium or Moratorium debts (such as debts owed to employees and some bank debts) are paid in priority to even the liquidator's fees and expenses in any subsequent liquidation. Thus it creates a kind of "super priority" debt.

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

Prior to going into compulsory liquidation on 28 February 2024, under pressure from its bank, Ambitus Bank plc, and in order to prevent it from demanding repayment of the company's loans, Blazer Laser Limited (the Company), granted a debenture in favour of Ambitus Bank plc in June 2023. 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 13 January 2024.

Sometime in January 2023, as the Company continued to suffer cash flow problems, the directors approved the sale of two laser cutting machines to Angela Bannister (a director) for GBP 40,000 in cash. The machines had been bought for GBP 100,000 a year before.

A month before the winding up order was made, Angela Bannister received an email from Aluminium Alumini 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 metal was seen as essential by the Company, the board authorised a payment of GBP 20,000 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 8,000 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 Ambitus 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 Ambitus Bank plc;

Preference

It would appear that the preference provisions of section 239 of the Act will not apply. This is because where the preference has been given to a person who is not a "connected person", transactions are only reviewable if they took place in the six months prior to the insolvency. This is extended to two years in the case of a "connected person" but there is nothing to suggest that Ambitus Bank (a publically listed company) is connected to Blazer Laser.

If Ambitus Bank were a connected person, the charge created by the debenture would be within the two year window for challenge. In this case, the court shall not make an order under the section unless Blazer Laser was "influenced by a desire" to put Ambitus Bank in a better position on insolvent liquidation than if the charge had not been granted.

Where the preference is given to a connected person (which, on the basis of timing, would be the only circumstance in which the floating charge granted to Ambitus Bank could be

captured), there is a presumption, which can be rebutted, that there was the requisite "desire to prefer".

Millet J, in *Re MC Bacon Ltd* [1990] BCC 78 distinguished between a "desire" and an "intention". Thus it would be relevant that the bank was applying pressure to the company. Blazer Laser may have intended to give a preference to Ambitus Bank in order to avoid the bank from calling in its loans, but this does not mean it had a "desire" to prefer Ambitus, especially if the company was entirely dependent on Ambitus to keep trading.

Floating charge avoidance

The alternative provisions of section 245 of the Act may apply even if Ambitus Bank is not a connected person. Section 245 prevents existing secured creditors from obtaining a floating charge shortly before the commencement of the insolvency (and has not provided any "new" consideration).

The relevant time in this case for reviewing the charge is 12 months prior to the onset of insolvency (or two years in the case of a connected person) so the charge granted to Ambitus Bank is potentially captured. However, for a floating charge to be avoided under the section, it must be the case that at the time of creating the charge the company was unable to pay its debts. It is not clear whether this was the case in June 2023.

As there is seemingly no new consideration provided by the bank (on the facts given), then if Blazer Laser did grant the charge at the time when it was unable to pay its debts then the floating charge is invalid (although the underlying debt is still valid).

Question 4.2 [maximum 6 marks]

The sale of the laser cutting machines; and

The main consideration in respect of the laser cutting machines is whether there has been a transaction at undervalue under section 238 of the Act.

To be attacked under section 238, the transaction must have taken place at the "relevant time", which is two years before the commencement of the liquidation. The sale of the laser machines therefore falls within this period.

The relevant "undervalue" in this case falls under section 238(4)(b) which provides: "*the company enters into a transaction with that person for a consideration the value of which, in money or money's worth, is significantly less than the value, in money or money's worth, of the consideration provided by the company.*"

There will thus be a valuation question as to whether the laser machines were sold for significantly less than their money's worth. Although on the face of it there is a large difference between what Angela Bannister paid (GBP 40,000) and what the company paid one year previously (GBP 100,000) we would need to know more about a) the depreciation typical of laser machines and b) the overall value of laser machines in the market at the time of the transaction.

Another requirement is that there will only be liability if the sale of the laser machines took place at a time when Blazer Laser was unable to pay its debts as they fell due within the meaning of section 123 of the Act (or became unable to pay them as a result of the

transaction). As a director, Angela Bannister is deemed a "connected person", the consequence of which is there is a presumption the company was insolvent. However, this is rebuttable with proof to the contrary. Given the sale of the lasers was a year before the winding up petition, it may be that this is possible to prove, although we are told that even in January 2023 the company was suffering cash flow problems

If it finds there has been a transaction at undervalue, the Court can make an order restoring the company to the position it would have been in had the transaction not occurred (so possibly unwinding the transaction or ordering Angela Bannister to pay the difference in value between what she actually paid and the market value for the lasers at the time).

Question 4.3 [maximum 4 marks]

The payments to Aluminium Alumini Ltd.

Section 127 - void dispositions

Section 127 of the Act provides that any disposition of company property after the commencement of the winding up is void unless the Court orders otherwise. The commencement of the winding up is the date of presentation of the petition, so in this case, 13 January 2024. Any dispositions of property after this date are void.

We are told that the Aluminium Alumini Ltd's email approach was a month before the winding up order was made on 28 February 2024. So if this was a month exact, it would have been on 28 January and, accordingly, after the commencement of the winding-up.

"Disposition of property" has a wide meaning under section 127 and can include payments out of the company's bank account (*Bank of Ireland v Hollicourt (Contracts) Ltd* [2000] EWCA Civ 263). The liquidator could seek to recover both the GBP 20,000 and the GBP 8,000 payments from Aluminium Alumini. Aluminium Alumini may well apply for a validation order from the Court in respect of the payments, arguing, for example, that it was a transaction in the ordinary course of business and was essential to allow the company to fulfil existing contracts that might be profitable and of benefit to creditors as a whole.

Section 214 - Wrongful trading

With regard to the GBP 8,000 liability in respect of further supplies incurred, the liquidator could consider a claim against the directors for wrongful trading under section 214 of the Act. This clause gives the court the discretion, upon the application of the liquidator, to declare a director of a company in insolvent liquidation make a contribution to the company's assets.

The conditions for making an order are (section 214(2)):

- (a) the company has gone into insolvent liquidation;
- (b) at some time before the commencement of the winding up of the company, that person [i.e. the director] knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation; and
- (c) that person was a director of the company at that time.

In this case, when the directors decided to continue to purchase supplies from Aluminium Alumini Ltd, there was already a winding-up petition due to be heard and, given the

company's financial struggle, an insolvent liquidator may have been inevitable. However, the directors could try to argue that they reasonably believed that the company could avoid insolvent liquidation. The standard of knowledge the court will attribute to the director under section 214(2)(b) has both an objective and subjective element. The director is taken to have the general knowledge, skill and experience that may be reasonably expected of a person carrying out the director function and the general knowledge, skill and experience that particular director has.

If the section 214(2) requirements are met, the court may order the director(s) to compensate the company in an amount in line with the increase in liabilities (i.e. GBP 8,000). However, under Section 214(3) there is an exoneration provision that the court shall not make a declaration if it is satisfied that the director took every step with a view to minimising the potential loss to the company's creditors as he ought to have taken. Thus, in this case the directors may argue that they genuinely believed the metal supplies from Aluminium Alumini would allow them to fulfil a contract that would benefit all creditors.

On a practical level, the liquidator may well not view the application in relation to section 214 as being worth it given the relatively small amount.

*** End of Assessment ***