

TOTAL = 21.5/50  
43%



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 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 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 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

Car Corp, incorporated and headquartered in Michigan, owes Parts Inc, incorporated and headquartered in Mexico, USD 10,000 on a past-due invoice for components used to build Car Corp vehicles. May Parts Inc file an involuntary petition to place Car Corp into chapter 11 bankruptcy proceedings?

**(a) Yes, regardless of the circumstances.**

(b) Yes, if Car Corp has fewer than 12 non-contingent, non-insider creditors.

(c) Yes, if other creditors owed at least USD 5,775 join in the petition.

(d) No, because Parts Inc does not know whether Car Corp is insolvent.

(e) No, because Parts Inc is not a US company.

Question 1.2

Answer this question with reference to the set of facts set out in question 1.1 above: Which of the following is likely to be a party in interest in the bankruptcy of Car Corp?

**(a) A shareholder in Parts Inc, to which Car Corp is indebted.**

(b) A journalist writing about Car Corp's bankruptcy.

(c) A shareholder in Investment Corp, Car Corp's parent company.

Commented [FV1]: 0, correct answer is C

Commented [FV2]: 0, correct answer is D

- (d) *A retired employee of Car Corp who receives payments from the company's pension plan.*
- (e) *A non-profit organization that advocates for companies like Car Corp to be held responsible for climate change*

Question 1.3

*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) *Options (a) to (c) above satisfy the minimum requirement for presence in the United States.*
- (e) *None of the above (options (a) to (d)) satisfy the minimum requirement for presence in the United States.*

Commented [FV3]: 0, correct answer is D

Question 1.4

*Who may serve as a foreign representative to seek recognition of a foreign proceeding under chapter 15?*

- (a) *An officer of the debtor if it is a debtor-in-possession in the foreign proceeding.*
- (b) *The board of directors of the debtor if it is a debtor-in-possession in the foreign proceeding.*
- (c) *An insolvency professional appointed by the court overseeing the foreign proceeding.***
- (d) *An insolvency professional appointed by a creditor where the foreign proceeding is an involuntary receivership.*
- (e) *All of the above.*

Commented [FV4]: 0, correct answer is E

Question 1.5

*Which of the following regarding executory contracts is false?*

- (a) *A court will generally defer to a debtor's business judgment regarding whether to assume or reject an executory contract.*
- (b) *Executory contracts are clearly defined by the Bankruptcy Code.*
- (c) *In the most common formulation, executory contracts are defined as those where both sides to a contract have material unperformed obligations.*
- (d) **Chapter 11 debtors have greater flexibility than chapter 7 debtors on when they may assume, assign or reject an executory contract.**
- (e) *Under the hypothetical test, a debtor cannot assume an executory contract if the debtor could not also assign the contract.*

Commented [FV5]: 0, correct answer is B

Question 1.6

*Which of the following is not a requirement to confirm a "cramdown" plan?*

- (a) *That the plan is fair and equitable to dissenting classes of creditors.*
- (b) *Acceptance of the plan by at least one class of impaired, non-insider creditors.*
- (c) *Acceptance of the plan by all classes of secured creditors.*
- (d) *That the plan does not discriminate unfairly against dissenting classes of creditors.*
- (e) **That the dissenting creditors receive no less than they would under a liquidation scenario.**

Commented [FV6]: 0, correct answer is c

Question 1.7

*Which of the following statements about "pre-packs" is false?*

- (a) **A pre-pack cannot be used if the debtor wishes to reject executory contracts.**
- (b) *Creditors must have sufficient information about the debtor and the plan to make an informed voting decision.*
- (c) *A pre-pack debtor may spend as little as a single day in bankruptcy.*
- (d) *The proposed plan of reorganization is submitted to the bankruptcy court together with the voluntary petition.*
- (e) *Creditors' commitment to vote in favor of the plan may be memorialized in a restructuring support agreement.*

Commented [FV7]: 1, correct

Question 1.8

*If a debtor rejects an executory trademark license agreement under which the debtor licenses its trademark to a manufacturer, which of the following is true:*

- (a) The manufacturer has a claim for damages for breach of contract.**
- (b) The manufacturer must immediately stop using the trademark.
- (c) The manufacturer can continue using the trademark for the remaining period of the license.
- (d) Both options (a) and (b).
- (e) Both options (a) and (c).

Commented [FV8]: 0, correct answer is E

Question 1.9

*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.**

Commented [FV9]: 0, correct answer is C

Question 1.10

Which of the following regarding substantive consolidation is true?

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

Commented [FV10]: 1, correct

QUESTION 2 (direct questions) [10 marks]

Question 2.1 (1 mark)

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

Setoff is an equitable right of a creditor to deduct a debt it owes to the debtor from a claim it has against the debtor arising out of a separate transaction. It is not permitted in many circumstances because;

1. The creditor's claim against the estate is disallowed,
2. The creditor's claim against the estate was acquired post-petition or in the 90 days prior to the petition at the time when the debtor was insolvent,
3. The creditor's obligation to the debtor was incurred in the 90 days prior to the petition at the time when the debtor was insolvency for purposes of exercising setoff rights, and
4. The creditor improves its position by setoff as compared to its position had setoff been exercised 90 days prior to the petition.

Commented [FV11]: .5 fails to mention that not allowed in many circumstances because it improves creditor's position.

Question 2.2 [2 marks]

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

A debtor can seek to entice lenders to provide debtor-in-possession (DIP) financing and debtor may seek court approval to grant the proposed creditor a lien on encumbered assets that is equal or senior to pre-petition existing liens to secure the post-petition financing. However, the debtor must establish that it is unable to obtain such credit or financing on any other terms and must establish that the interest of the secured creditor being primed is adequately protected.

Commented [FV12]: 2, correct

d) If financing cannot be obtained on any other terms, the court may grant a **priming lien** that is senior or equal to a pre-petition lien on estate property to secure post-petition financing. The debtor also must demonstrate that the interest of the secured creditor being primed is adequately protected.

Question 2.3 [2 marks]

**What are two potential consequences of a violation of the automatic stay?**

*They may include payment of debtor's attorney fees and requiring the violator to take affirmative acts to undo the effects of its violation. Pg21.*

**Commented [FV13]:** 1. Fails to mention that the act may be void or voidable depending on the Circuit.

Question 2.4 [2 marks]

**In voting on a plan of reorganization, which class(es) of creditors are (i) deemed to accept the plan, (ii) deemed to reject the plan and (iii) permitted to vote on the plan? What vote is necessary for a class of creditors to accept a plan?**

*The impaired class(es) of creditors have the right to vote on the plan. The class is deemed to accept a plan if voting creditors in the class hold at least two-thirds of the value of claims in the class or, for equity interest, if two thirds in amount of interest vote in favour.*

**Commented [FV14]:** 1. Fails to mention that unimpaired class is deemed to accept and that class that receives nothing is deemed to reject.

Question 2.5 [3 marks]

**Answer the following questions about preferences, actual fraudulent conveyances and constructive fraudulent conveyances:**

- (a) **Which cause of action applies only to transfers made on account of antecedent debt?**
- (b) **Which cause of action requires that the debtor be presumed or proven to have been insolvent at the time of the transfer?**
- (c) **Which cause of action requires that the debtor be proven to have intended to frustrate creditors' recoveries?**

- a. Preferences
- b. Constructive fraudulent conveyances
- c. Actual fraudulent conveyances

**Commented [FV15]:** 2. Answer for (b) is also preference.

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

**Commented [la16]:** 8/15 marks

Question 3.1 [3 marks]

**Commented [la17]:** 1/3



**Describe the circumstances in which a bankruptcy court may enter a final order consistent with the US Constitution, who reviews appeals from bankruptcy court orders and how orders that are not constitutionally final are reviewed.**

The bankruptcy courts are creatures of federal legislation by Article III of the US Constitution and may enter a final order on core bankruptcy issues, which permits bankruptcy judges to hear and determine only on core proceedings, which determines the scope of its jurisdiction and power to render a final order. The bankruptcy court appeals are reviewed by the district court for the district in which they sit. If a matter is non-core the bankruptcy court cannot make a final determination. Including interlocutory orders which does not resolve the entire issue in dispute, some issues or claims are further decided on or appealed only with leave of the appellate court.

**Commented [la18]:** Partially correct, 1/2 mark, the bankruptcy court may enter a final order if the core proceeding is specific to the Bankruptcy Code (such as a challenge to a petition) or the parties consent.

**Commented [la19]:** Correct, 1/2 mark. In some circuits the appeal may be heard by a Bankruptcy Appellate Panel.

**Commented [la20]:** In these cases, the bankruptcy court's order is treated as a report and recommendation

**Question 3.2** [3 marks]

**Commented [la21]:** 1/3

**What provisions of the Bankruptcy Code may not be invoked by a foreign representative in a chapter 15 proceeding? What are two ways that the foreign representative can obtain equivalent relief?**

Article 23 of the Model Law addressed the powers granted to a foreign representative and Chapter 15 excludes from the rights granted to foreign representatives the use of avoidance powers provided by the Bankruptcy Code.

A court held that the good faith filing requirement applicable to plenary proceedings was not applicable in Chapter 15. However, where a debtor does not have an establishment - to conduct non transitory economic activity in the foreign jurisdiction in which it commences its plenary foreign proceeding, the necessity to establish COMI in order to obtain relief in its Chapter 15 case may be unavoidable. This does not provide for an efficient liquidation and limited to the debtor's US assets or applicable law does not allow claims for constructive fraudulent conveyance.

**Commented [la22]:** Correct, 1 mark. The foreign representative may obtain equivalent relief under other applicable US or foreign law or by commencing a plenary proceeding under chapter 7 or 11

Only upon recognition can a foreign representative obtain equivalent relief of either foreign main proceedings or foreign non-main proceedings as defined by the Bankruptcy Code. Further, the bankruptcy court must be satisfied that a foreign representative has satisfied its statutory requirements before granting relief and the right to intervene in any US state or federal court proceedings in which the debtor is party.

**Question 3.3** [4 marks]

**Commented [la23]:** 1/4

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

The Federal Rules of Bankruptcy Procedure specify a number of schedules, such as list of assets and creditors, that to be files with a voluntary petition but even if they are absent, a naked petition is sufficient to invoke the automatic stay and commence a

**Commented [la24]:** Correct, 1 mark. This question is about all filings in bankruptcy court, not just the petition. You should also consult the Federal Rules of Civil Procedure, the local bankruptcy rules, and the judge's personal practices.

case under the Bankruptcy Code. However, it does not required the debtor to assert that it is insolvent

The filing of a petition acts as a stay of certain acts and proceedings against the debtor, property of the debtor, and property of the estate.

Question 3.4 [5 marks]

**What fiduciary duties do directors of Delaware corporations owe and to whom are the duties owed in the ordinary course of business? To whom are duties owed when the corporation is potentially or actually insolvent?**

Under Delaware case law, directors owe fiduciary duties to a corporation's shareholders which include both a duty of care and a duty of loyalty. In general, the duty of care requires, among other things, that directors keep themselves reasonably informed when making decisions on behalf of the corporation. The duty of loyalty requires a director to act in good faith and in a manner it reasonably believes to be in the best interests of the corporation and its stockholders, and to avoid engaging in acts of conflict of interest dealing, but are protected from liability for errors of judgment by the business judgment rule. The Director duties are owed to the corporation and its shareholders, not to the creditors, even in circumstances where the corporation is potentially or actually insolvent and therefore the shareholders stand to receive nothing in bankruptcy. The Delaware Supreme Court has put to rest any suggestion that directors owe duties to creditors when a company is operating in the zone of insolvency or indeed is actually insolvent. Thus, there is no equivalent under the US law of the concept of "wrongful trading" or "deepening insolvency." However, a claim for breach of fiduciary duty is governed by the law of the state of incorporation. *Brandt v. Hicks, Muse & Co. (In re Healthco Int'l., Inc.)*, 208 B.R. 288, 300 n.18 (Bankr. D. Mass. 1997).

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

Question 4.1 [5 marks]

**iWork Ltd leases office space from office building owners and sublets the space to small businesses. Due to the increases in the numbers of businesses operating remotely, iWork Ltd has suffered a decline in revenues. As a result, it has failed to pay rent on some of its office space leases. What protections does the Bankruptcy Code provide to lessors of office space to iWork Ltd?**

The Bankruptcy Code instructs a trustee or debtor to perform an act or make an election within a certain time. In this case, the contract would be considered executory if iWork Ltd and the lessors have material unperformed obligations on both sides as at petition date. The lease of office space is assignable by lessors. Notwithstanding, the landlord approval provision of any assignment.

Commented [la25]: 5/5

Commented [la26]: Correct, 1 mark

Commented [la27]: Correct, 1 mark

Commented [la28]: Correct, 1 mark

Commented [la29]: Correct, 1 mark

Commented [la30]: Correct, 1 mark

Commented [la31]: 5/15 marks

Commented [la32]: 3.5/5

Therefore, in Chapter 7, the trustee must make decisions about assumption and assignment or rejection of executory contracts within 60 days of the petition date. In Chapter 11 bankruptcy, it allows for the lessor to assume or reject commercial leases. The debtor or lessor can also freely assign leases without consent, provided the cure and adequate assurances of future performance are provided. Under section 365 of the Bankruptcy Code, a chapter 11 lessor has 120 days from the order of relief (currently 210 days pursuant to an extension in the CARES Act) by court order for that additional 90 days) to assume or reject leases, which must be based on the business judgement of the debtor in possession or trustee that the reorganization of the debtor or liquidation of assets to pay creditors will be facilitated thereby. The court may only deny approval of the election where the choice to assume or reject the lease is not made in good faith or in a reasonable exercise of business judgement. Any further extension requires agreement of the lessor and landlord (iWork Ltd).

The decision to reject a lease may result in substantial, albeit capped, rejection damages claims for any landlord whose lease is rejected.

Commented [la33]: Correct, 1 mark

Commented [la34]: Correct, 1 mark

Commented [la35]: Correct, 1 mark

Commented [la36]: Partially correct, 1/2 mark, the landlord has an administrative priority claim for 2 years' rent if the lease is assumed and then rejected. The landlord also has an unsecured claim for unpaid pre-petition rent (if not satisfied in connection with assumption).

Commented [la37]: 1.5/5

Question 4.2 [5 marks]

**Skin Luxe is incorporated and has a principal place of business in France where it develops and manufactures high end skincare products. Skin Luxe sells its skin care products through its own boutiques in many international cities, including Paris, Las Vegas, London and Hong Kong. Skin Luxe's English law-governed bonds are due to mature in one year, but it is unable to repay or refinance them. Skin Luxe is considering using an English scheme of arrangement to restructure the bonds.**

**Discuss whether the English scheme of arrangement could be granted recognition under US chapter 15 as a foreign main or foreign non-main proceeding.**

The English scheme of arrangement could be granted recognition under US chapter 15 as a foreign non-main proceeding, due to the fact that the debtor, herein Skin Luxe has its COMI in France by virtue of its principal place of business. Therefore, in the US the debtor qualifies for foreign non-main proceedings since it has an establishment in that jurisdiction, which is where the debtor carries out a non-transitory economic activity with human means and goods or services.

Commented [la38]: Correct, 1 mark

Commented [la39]: Correct, 1 mark, under these facts the presumption in favor of COMI in the jurisdiction of incorporation is unlikely to be rebutted. Foreign main recognition is not available because the proceeding is not in the jurisdiction of the debtor's COMI.

Commented [la40]: Partially correct, 1/2 mark, it's unclear which establishment you are referring to. The relevant establishment is the boutique in London, where the foreign proceedings are pending.

After recognition of the foreign non-main proceeding, the bankruptcy court has authority upon the request of the foreign representative, and if satisfied to grant a relief in the jurisdiction designed to preserve the Skin Luxe's assets together with the interests of creditors.

Such as authorization of discovery regarding the debtor's assets and affairs; entrusting administration of the debtor's US assets to the foreign representative or other person, the extension of provisional relief and any other relief necessary to effectuate the purposes of protecting the assets of the debtor and interest of creditors.

*Subject to the bankruptcy court's approval it may extend those above-mentioned provisions to the foreign representatives. Of the relief available is discretionary by the bankruptcy court, which must be satisfied that it is appropriate under the US Law for the assets in question to be administered under foreign non-main proceedings and the foreign representative should be able to show that the interests of creditors are sufficiently protected. Further, the relief is subject to limitations and the court may provide additional assistance the Bankruptcy Code or other US law consistent with the principle comity and the respective values.*

**Question 4.3** [5 marks]

*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 has been sued in civil suit 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 (i) the DOJ investigation, (ii) margin loan default; (iii) the delinquent lease and (iv) the employment discrimination lawsuit?*

*(i) Alleged debtor is not a qualified debtor under Bankruptcy Code because they do not own a property in the US.*

*(ii) The broker may file for bankruptcy of the debtor under Chapter 11 and the company is place under reorganization by an appointed administrator*

*(iii) In Chapter 11 bankruptcy, it allows for the lessor to assume or reject commercial leases.*

*The company need not be insolvent to file for voluntary petition for bankruptcy. The petition may however be dismissed if it has been filed for an improper purpose.*

*(iv) The employment contract is not executory, because at the time of filing the contract was already terminated and outside the ordinary course of business, however, should the lawsuit favour the former employee the obligations would not be complete.*

\* End of Assessment \*

Commented [la41]: 0/5

Commented [la42]: Incorrect. At a minimum, the debtor has property interests in the lease and the shares it owns.

Commented [la43]: Incorrect, even in an involuntary proceeding, the debtor usually remains in possession.

Commented [la44]: Upon filing the petition, the automatic stay would come into effect. It would bar any action for eviction on account of unpaid rent and would stay the pending discrimination litigation. It would not stay the DOJ investigation or action to liquidate the collateral securing the margin loan because it is a securities contract exempt from the automatic stay.