

TOTAL = 38.5/50
77%



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.

Commented [FV1]: 0, correct answer is C

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 [FV2]: 1, correct

- (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]: 1, correct

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]: 1, correct

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]: 1, correct

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]: 1, correct

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]: 1, correct

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?

The setoff permits a creditor holding a claim against the debtor and simultaneously owing money to the debtor to net out the two (or more) obligations. For example, if the creditor has a claim against the debtor of US\$ 100.000 and at the same time owns US\$ 80.000 to the debtor, then the setoff would allow the creditor to setoff both obligations so as to only be involved in the insolvency proceedings as a holder of a credit of US\$ 20.000. Setoff rights, which arises under non-bankruptcy law, can improve the position of the creditor (as, in the example case, the creditors reduced by 80% its exposition in the debtor's insolvency proceedings) as compared to other unsecured creditors who are not owed money by the debtor.

Commented [FV11]: 1, correct

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 "priming lien" is a senior or equal to a pre-petition lien on the estate property to secure post-petition financing. The requirements for a "priming lien" are:

- The estate shall have any unencumbered assets or encumbered assets with sufficient equity value to support a junior lien.
- The debtor must demonstrate that the interest of the secured creditor being primed is adequately protected.

Commented [FV12]: 1.5. Full credit not given because answer does not note that priming may be granted only if there is no alternative financing

Question 2.3 [2 marks]

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

An act taken in violation of the stay constitutes contempt of court and is void or voidable (depending on the circuit in which the bankruptcy is pending due to a circuit split on this issue) and also can lead to the imposition of contempt sanctions against the stay violator.

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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?

An unimpaired class is deemed to accept the plan, an impaired class that will receive nothing is deemed to reject the plan, creditors belonging to an impaired class have the right to vote. Finally, the reorganization plan will be approved if a simple majority of the creditors in the class holding at least two-thirds of the value of claims in the class vote in favor, or, for equity interest, if two-thirds in amount of interest vote in favor.

Commented [FV14]: 2, correct

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?**

The provisions related to preferences avoidance apply to the situation described in paragraph A. Therefore, if a transfer of the debtor's property is made in a suspect period before the petition date must be returned to the state if it exceeds the amount the recipient would have received in a chapter 7 liquidation had the transfer not been made.

The provisions related to preferences avoidance apply to the situation described in paragraph B. In fact, according to the provisions related to preferences avoidance, the debtor is presumed to have been insolvent on and during the 90 days prior to the petition date for purposes of determining preference claims.

Commented [FV15]: 3, correct

The provisions related to fraudulent conveyances apply to the situation described in paragraph C. In this regard, an actual fraudulent conveyance is proven by showing that the debtor made a transfer or incurred an obligation “with actual intent to hinder, delay, or defraud any entity to which the debtor was or become...indebted”.

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

Commented [la16]: 15/15 marks

Question 3.1 [3 marks]

Commented [la17]: 3/3

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.

A bankruptcy court may enter a final order consistent with the US Constitution if: 1) such order is related to core matters; and 2) if such order do not invade Article III jurisdiction, according to *Stern v. Marshall*. Moreover, a bankruptcy court may exercise a district court’s delegated authority to enter a final order consistent with the US Constitution on a motion challenging the validity of a petition. Besides this, bankruptcy courts may determine a core proceeding over which they lack constitutional authority by issuing a final order if it’s consented by the parties.

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Commented [la19]: Correct, 1/2 mark

Bankruptcy court orders can be appealed by not only the litigants involved in a particular issue, but also other persons who are adversely affected by the ruling and therefore have standing to seek review. Generally, appeals from bankruptcy court decisions are decided by the district court for the district in which they sit. In certain cases, however, the bankruptcy appeals are heard by a Bankruptcy Appellate Panel (“BAP”). Moreover, from the district court or the BAP, there is further appeal of right to the circuit court of appeals.

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Commented [la21]: Correct, 1/2 mark

With respect to how the bankruptcy appeals are reviewed, is important to highlight that if the ruling being challenged was issued in a core proceedings over which the bankruptcy court had authority to enter a final order, then the district court or BAP reviews conclusions of law *de novo* and reviews findings of fact for abuse of discretion, recognizing that the bankruptcy court had greater opportunity to weight the evidence. If the ruling was in a noncore proceeding or the bankruptcy court otherwise did not have authority to enter a final order, the district court or BAP reviews *de novo* all findings of fact and conclusions of law which a party has objected.

Commented [la22]: Correct, 1 mark

Question 3.2 [3 marks]

Commented [la23]: 3/3

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?

Chapter 15 excludes from the rights granted to foreign representatives the use of avoidance powers provided by the Bankruptcy Code. This provision has been interpreted only to apply to the use of the Bankruptcy Code's powers of avoidance of preferences and fraudulent conveyances, and not to bar a foreign representative from seeking to avoid pre-petition transaction under other applicable US or foreign law. If the foreign representative wants to invoke the Bankruptcy Code avoidance powers, it was to pursue a plenary proceeding such as chapter 11 or 7. This could be achieved by commencing a plenary proceeding by the debtor or its creditors prior to involvement of the foreign representative, or the foreign representative may choose to commence a plenary proceeding under the Bankruptcy Code after recognition of the foreign proceeding under chapter 15.

Commented [la24]: Correct, 1 mark

Commented [la25]: Correct, 1 mark

Commented [la26]: Correct, 1 mark

Question 3.3 [4 marks]

Commented [la27]: 4/4

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

When preparing a filing for a bankruptcy court one should review the US Bankruptcy Code, the Bankruptcy Rules (the Federal Rules of Bankruptcy Procedure), the Federal Rules of Civil Procedure when they are incorporated by reference in the Bankruptcy Rules, the forms for common bankruptcy filings if they are required, the local rules of procedure used by each bankruptcy court and the personal practices issued by the judge that could have competence to handle our case and relevant case law of the US Supreme Court.

Commented [la28]: Correct, 1 mark

Commented [la29]: Correct, 1 mark

Commented [la30]: Correct, 1 mark

Commented [la31]: Correct, 1 mark

Question 3.4 [5 marks]

Commented [la32]: 5/5

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?

This question is relevant because, according to US law, director liability is a matter of state law of the state of incorporation. Delaware is the pre-eminent US jurisdiction for corporate law probably, because US director liability is more limited than that elsewhere. Directors owe a fiduciary duty of loyalty to the corporation's best interest and a duty of care in educated decision-making, but are protected from liability for errors of judgment by the business judgment rule. Under the business judgment rule, the board of directors is presumed to have acted in good faith on the basis of reasonable information. Unless the presumption is rebutted, the directors will not be liable in the absence of a showing of gross negligence. In addition, directors may be exculpated by a corporation's certificate of incorporation from liability for breach of the duty of care. The business judgment rule does not apply where a transaction is approved by a board majority that is not disinterested and independent or a controlling shareholder in on both sides of the transaction. In such circumstances, the transaction will be void unless the entire fairness standard is satisfied. Directors' duties are owed to the corporation and its shareholders, not to creditors, even in

Commented [la33]: Correct, 1 mark

Commented [la34]: Correct, 1 mark

Commented [la35]: Correct, 1 mark

Commented [la36]: Correct, 1 mark

circumstances where the corporation is potentially insolvent and therefore the shareholders stand to receive nothing in bankruptcy.

Commented [la37]: Correct, 1 mark

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

Commented [la38]: 6/15 marks

Question 4.1 [5 marks]

Commented [la39]: 0/5

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?

I believe a clarification should be made before answering the question. The Bankruptcy Code does not provide direct protection mechanism to lessors of office space to iWork Ltd, but certain provisions of the Bankruptcy Code provide the debtor with certain advantages that could indirectly be beneficial to the lessors. As it seems that the debtor is struggling financially and economically because of the effects of remote working after the COVID-19 pandemic, it could be assumed that if this situation is addressed early enough the company could find a long-term solution to its problems. Therefore, I would start mentioning the relevant provisions under chapter 7 of the Bankruptcy Code. The lessors would benefit from the automatic stay of proceedings (preventing the office building owners from taking actions to collect pre-bankruptcy debts) and from the provisions related to the executory contracts (which would give the debtor the possibility to assume the leases). Moreover, the debtor could benefit from the reorganization plan provided that the majority required by law are obtained. Similar provisions would be available under Chapter 7 of the Bankruptcy Code, with the exception of the reorganization plan.

Commented [la40]: iWork only has 120 days to decide whether to assume or reject the leases because they are of non-residential real estate. This period can be extended by 90 days for cause, but not further without lessor consent. iWork must pay rent as an administrative expense for the period prior to rejection of a lease. Administrative priority treatment for 2 years of rental payments for leases that are assumed and subsequently rejected. Lessors have a claim in the bankruptcy for unpaid pre-petition rent.

Question 4.2 [5 marks]

Commented [la41]: 3/5

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.

Skin Luxe is incorporated in France. Moreover, its principal place of business (where it develops and manufactures high end skincare products) is also in France. Therefore, there are solid arguments to consider that Skin Luxe has its COMI in France. Therefore, Skin Luxe shall be entitled to commence the main insolvency proceedings in France. Nevertheless, Skin Luxe is considering using an English scheme of arrangement to

Commented [la42]: Correct, 1 mark. France is presumed to be the COMI because of incorporation and on these facts, that presumption is unlikely to be rebutted.

restructure the English law-governed bonds (which are due to mature in one year, but it is unable to repay or refinance them). It is also important to consider that Skin Luxe has an establishment in England (a boutique). Therefore, the debtor shall be entitled to commence secondary insolvency proceedings in England.

Commented [la43]: Correct, 1 mark.

In this regard, if the debtor commences an insolvency proceeding in England (a place different to that where it has its COMI), that insolvency proceeding would probably be regarded as a foreign non-main proceeding under Chapter 15 of the US Bankruptcy Code, which would limit the scope of the relief available to the debtor following recognition.

Commented [la44]: Correct, 1 mark. Whereas a foreign main proceeding would be one in the jurisdiction of the debtor's COMI.

Question 4.3 [5 marks]

Commented [la45]: 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 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) **The DOJ investigation would not be subject to the stay of proceedings (because it is a regulatory proceeding and, as such, is excepted from that effect).**
- (ii) **The margin loan default will be subject to the stay of proceedings and the creditor shall file a petition for recognition of its credit and vote the reorganization plan.**
- (iii) **The delinquent lease will be subject to the stay of proceedings and the lease will be subject to the executory contract's provisions.**
- (iv) **If we were to apply literally the US Bankruptcy Code, then employment discrimination lawsuit would be subject to the stay of proceedings because there no exception on this ground. However, Article 362(b)(4) of the U.S. Bankruptcy Code could be interpreted as also covering this type of personal claims against the debtor and, therefore, not subject to the automatic stay of proceedings.**

Commented [la46]: Correct, 1 mark. Also the automatic stay would come into effect on the filing of the petition.

Commented [la47]: Incorrect, the margin loan is a securities contract that is exempt from the automatic stay. The broker can sell the collateral to settle the loan.

Commented [la48]: Correct, 1 mark.

Commented [la49]: Correct, 1 mark.

Commented [la50]: I think this is a mistaken citation as this provision exempts proceedings under the Convention on Chemical Weapons from the automatic stay.

* End of Assessment *