

TOTAL = 35/50
70%



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.

Commented [FV4]: 1, correct

(e) All of the above.

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.

Commented [FV5]: 1, correct

(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.

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.

Commented [FV6]: 1, correct

(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.

Question 1.7

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

Commented [FV7]: 1, correct

(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.

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?

Setoff involves a claim by a creditor to a debtor being net off by a claim by the debtor to the creditor. It is not permitted in many circumstances as it might give a particular creditor a better position (in terms of priority) as compared to other unsecured creditors. In essence, it decreases the obligation to the estate by the full amount owed by the debtor instead of the lesser amount the debtor would otherwise pay on the unsecured claim.

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 lien that is senior or equal to a pre-petition lien on estate property to secure post-petition financing. The requirements for such a lien to be granted to secure DIP financing include (a) financing cannot be obtained on any other terms and (b) the debtor must demonstrate that the interest of the secured creditor being primed is adequately protected.

Commented [FV12]: 2, correct

Question 2.3 [2 marks]

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

Commented [FV13]: 2, correct

An act taken in violation of the automatic stay may constitute contempt of court and such an act may be rendered void or voidable. Further sanctions may flow from this contempt.

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?

(i) unimpaired classes, ie, classes whose claims and interests will receive full payment or treatment as in the plan of reorganization, will be deemed to accept the plan.

(ii) classes which receive nothing are deemed to reject the plan.

(iii) Impaired classes, ie, classes whose claim or interest will be altered by the plan, will be permitted to vote on the plan.

Commented [FV14]: 1.5. Full credit not given because answer did not address the vote necessary for a class to accept

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?

Commented [FV15]: 3, correct

(a) The cause of action is that of a preference claim because the debtor would be taken to have preferred the creditor in relation to the antecedent debt owed.

(b) The cause of action is that of a preference claim.

(c) The cause of action is that for an actual fraudulent conveyance.

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

Commented [la16]: 10/15 marks

Question 3.1 [3 marks]

Commented [la17]: 2/3 marks

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 on a motion challenging the validity of a petition. It can also enter a final order with the consent of the parties.

Commented [la18]: Correct, 1/2 mark. An order that is not constitutionally final is treated as a report and recommendation by the reviewing court.

Appeals from bankruptcy court decisions are heard by the district court for the district in which they sit. Appeals in certain circuits are however heard by a Bankruptcy Appellate Panel (BAP) which comprises judges of the bankruptcy courts within the circuit. In these circuits, a party can request that the appeal be heard by the district court instead. From the district court or BAP, parties can appeal further to the circuit court of appeals. In rare cases, the appeal may go up to the court of appeals.

Commented [la19]: Correct, 1/2 mark

Commented [la20]: Correct, 1/2 mark

Commented [la21]: Correct, 1/2 mark

An order which does not resolve the entire issue in dispute is not constitutionally final. They are reviewed by way of an appeal.

Question 3.2 [3 marks]

Commented [la22]: 2/3 marks

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?

The Bankruptcy Code's avoidance powers may not be invoked by a foreign representative. Instead, the foreign representative can commence a plenary proceeding under the Bankruptcy Code after the recognition of the foreign proceeding under chapter 15. These proceedings can also be commenced by the debtor or its creditors prior to the involvement of the foreign representative.

Commented [la23]: Correct, 1 mark

Commented [la24]: Correct, 1 mark

Commented [la25]: True, in addition, the foreign representative can pursue claims under other applicable US and foreign law

Question 3.3 [4 marks]

Commented [la26]: 1/4 marks

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

One should review the Federal Rules of Bankruptcy Procedure which govern procedures in bankruptcy proceedings. One should also review the rules under the Bankruptcy Code, which exists as federal law. Rules under US state law should also be reviewed.

Commented [la27]: Correct, 1 mark

Commented [la28]: Incorrect, even if the claim is under state law, federal rules of procedure apply. In addition to the Bankruptcy Rules, lawyers should review Federal Rules of Civil Procedure, the Local Rules of the Bankruptcy Court and the bankruptcy judge's personal practices.

Question 3.4 [5 marks]

Commented [la29]: 5/5 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?

Directors owe the fiduciary duty of loyalty to act in the company's best interests and a duty of care in educated decision-making. These duties are owed to the corporation and its shareholders in the ordinary course of business as well as in situations where the corporation is potentially or actually insolvent.

Commented [la30]: Correct, 1 mark

Commented [la31]: Correct, 1 mark

Commented [la32]: Correct, 1 mark

Commented [la33]: Correct, 1 mark

Commented [la34]: Correct, 1 mark

Commented [la35]: 7.5/15 marks

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?

Here, the lessors of office space to iWork Ltd are its creditors and iWork Ltd may be the creditor of its subtenants. In such a case, iWork Ltd is free to lease the property to the subtenants in the ordinary course of business. This is so even if chapter 11 proceedings commence. iWork Ltd also has the option to assume or reject the lease of the property. If it is assumed, iWork Ltd must cure existing defaults and provide assurance of future performance. If the lease is rejected, the lessor may assert a claim for damages resulting from the rejection.

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 is likely considered a foreign proceeding as it is an administrative proceeding in a foreign country, ie, not France. The question as to whether it may be granted recognition under US chapter 15 as a foreign main or non-main proceeding will depend if its COMI is in France or if it has an establishment in France. A debtor's COMI is presumed to be its place of incorporation. Here, the COMI is likely to be France as that was where Skin Luxe was incorporated and where it has a principal place of business. However, as Skin Luxe has an establishment, ie, a place where it carries out non-transitory economic activity, in London, the scheme in England can be recognised as a foreign non-main proceeding.

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,

Commented [la36]: 1/5 marks

Commented [la37]: Correct, 1 mark, specifically the lessors will have an unsecured claim for unpaid pre-petition rent

Commented [la38]: To protect the landlords, there is a 120 day deadline to assume or reject, with a 90 day extension for cause, but no further extension without landlord consent. Rent for the period from the petition to assumption or rejection is due as an administrative priority. If the debtor assumes and then rejects a lease, it must pay 2 years' rent as an administrative expense.

Commented [la39]: 3/5 marks

Commented [la40]: Incorrect, the proceeding is characterized as foreign because it is not in the US, not because it is in a jurisdiction other than the COMI.

Commented [la41]: Correct, 1 mark

Commented [la42]: Correct, 1 mark

Commented [la43]: Correct, 1 mark. The proceeding cannot be recognized as a main proceeding because it is not pending in the jurisdiction of the debtor's COMI.

Commented [la44]: 3.5/5 marks

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?

There is an automatic stay of enforcement proceedings from the moment the petition is filed by Speculation Inc. This provides the debtor some breathing room to formulate a restructuring plan and to negotiate and discuss matters with its creditors.

- (i) **The effect on the DOJ investigation constitutes a statutory exception to the stay.**
- (ii) **Speculation Inc's broker will be prohibited from litigating on the default on the margin loan as it is a pre-petition claim. It therefore cannot collect or sue on this claim due to the automatic stay.**
- (iii) **Similarly, its landlord cannot claim for rent but there is a statutory exception for the eviction of a debtor-tenant from non-residential property where the lease has expired.**
- (iv) **The stay will prevent the civil suit from proceeding.**

*** End of Assessment ***

Commented [la45]: Correct, 1 mark

Commented [la46]: Correct, 1 mark, the investigation would continue

Commented [la47]: Incorrect, the margin loan is a securities contract that is exempt from the automatic stay so the broker can sell the shares despite the filing of the petition.

Commented [la48]: Partially correct, 1/2 mark, the landlord has a claim for unpaid rent in the bankruptcy but cannot pursue eviction on account of unpaid rent if the lease has not expired.

Commented [la49]: Correct, 1 mark