

TOTAL = 32.5/50
65%



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]: 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]: 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.

Commented [FV5]: 1, correct

(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.

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?

(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.

Commented [FV7]: 1, correct

(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?

It is the netting out of a debtor's monetary obligations against a creditor's claim on the same debtor. This is generally not permitted, with the exception of specific derivative structured contracts, as setoffs allow a single (or a number) of creditors to improve position/s or amount/s of recovery relative to other creditors who do not have the option of a setoff.

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?

It is the granting of a lien that is equivalent or higher in priority to pre-petition liens, in such cases where post-petition financing is unattractive and unattainable without the granting of such priming liens and where it can be validated that primed secured creditors have met the requirement of 'adequate protection'.

Commented [FV12]: 2, correct

Question 2.3 [2 marks]

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

Violations of the automatic stay result in serious consequences, particularly leading to contempt of court and relevant sanctions (payment of various fees, damages and

coercive fines), as well as a need for the violating party to seek affirmative actions to unmake such violation and its subsequent effects.

Commented [FV13]: 1. Full credit not given because it fails to mention that 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?

Those classes of creditors which are not impaired are deemed to accept the plan while those which will not receive any recovery are deemed to reject the plan. Voting is permitted to those who are in an impaired class, of which a simple majority is required for creditors that hold 2/3 of the claim value is necessary. For equity holders (as an impaired class), the requirement is 2/3 of the value of interest.

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?**

Commented [FV15]: 1. correct answer to b is preference. correct answer to c is actual fraudulent conveyance

Cause of action that applies are as follows:

- (a) *Preference action, where payment is made specifically for pre-existing debt/s.*
- (b) *Actual fraudulent conveyance, where such transfers may show 'badges of fraud' based on circumstances as set forth by fraudulent transfer laws of the state.*
- (c) *Constructive fraudulent conveyance, where such transfers or obligations incurred affirm an unequal exchange of value for the debtor, in addition to signs of bad faith such as undue benefits to company insiders, unjustified undercapitalization and debt servicing intentions and insolvency during or because of the transaction.*

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

Commented [la16]: 11/15 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.

Bankruptcy courts were established through legislation and not as set forth in the United States Constitution's creation of a federal court system and, hence, have limited powers that allow entering of final orders only for such 'core proceedings' set forth in the U.S. Code's 157 - Procedures and 1334 - Bankruptcy cases and proceedings. A judge that is assigned in random from the specific district court in which the bankruptcy court sits typically reviews appeals, with certain exception wherein a Bankruptcy Appellate Panel does so, or an escalation is made to the district's court of appeals. Reviews are made on objections or abuse of discretion, based on fact findings.

Commented [la18]: Specifically, the core proceeding must be specific to the Bankruptcy Code (like a challenge to a petition) or the parties must consent

Commented [la19]: Correct, 1/2 mark

Commented [la20]: Correct, 1/2 mark

Commented [la21]: Correct, 1 mark

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?

A foreign representative is unable to exercise power related to avoidance actions as set forth in the Model Law's Article 23. Relief may be granted through a plenary proceeding post-recognition proceedings (primarily main proceedings) for Chapter 15, though this is more commonly done through such proceedings before the inclusion of a foreign representative, typically through Chapter 7 or Chapter 11.

Commented [la23]: Correct, 1 mark

Commented [la24]: Correct, 1 mark; alternatively the foreign representative can bring equivalent claims under applicable US and foreign law

Question 3.3 [4 marks]

Commented [la25]: 4/4 marks

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

It is of utmost importance to review Federal Rules of Civil Procedures, relevant Bankruptcy Rules (such as Federal Rules of Bankruptcy Procedures and relevant Local Rules & Orders of the court), specific practices in the court and understanding of the assigned judge, including case law on past judgments and the individual's professional approach towards such judgments.

Commented [la26]: Correct, 1 mark

Commented [la27]: Correct, 1 mark

Commented [la28]: Correct, 1 mark

Commented [la29]: Correct, 1 mark

Question 3.4 [5 marks]

Commented [la30]: 3/5 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?

Fiduciary duties are owed to the directors' company and its equity holders both during the ordinary course of business and even when the corporation is potentially or actually insolvent, affirming that there is no such fiduciary duties owed to creditors

Commented [la31]: The duties are the duty of care and the duty of loyalty

Commented [la32]: Correct, 1 mark

Commented [la33]: Correct, 1 mark

Commented [la34]: Correct, 1 mark

during insolvency, as affirmed by North Am Catholic Educational Programming Foundation, Inc vs. Gheewala, 930 A.2d 92, 103 (Del 2007).

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

Commented [la35]: 7.5/15 marks

Question 4.1 [5 marks]

Commented [la36]: 2/5 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?

Lessors of office space have certain protections under the Bankruptcy Code, such as in Chapter 11 wherein such lessors are given powers to consent or deny any deferral in decisions related to non-residential property leases that have not yet expired beyond a total of 210 (120 + 90) days of the automatic stay order.

Commented [la37]: Correct, 1 mark

Commented [la38]: Correct, 1 mark; also the lessor has an unsecured claim for pre-petition unpaid rent, an administrative claim for post-petition rent and an administrative claim for 2 years' rent if the debtor assumes and then rejects the lease

Question 4.2 [5 marks]

Commented [la39]: 3/5 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 may be granted recognition under Chapter 15 of the US Bankruptcy Code, but its status as a foreign main or foreign non-main proceeding largely depends on which jurisdiction is considered as the Center of Main Interest ('COMI'), one not easily discernable based on US law as the key determining factors include the debtor's primary place of business, assets location and domicile. In this case, although the bonds are governed by English law, it is likely that the court may decide that the COMI is in France, given the location of the principal place of business (likely including management) and primary assets (likely research, machinery and intangibles, if applicable) in the country. Unless the UK can be considered the COMI, the scheme of arrangement will likely be a foreign non-main proceeding.

Commented [la40]: Correct, 1 mark

Commented [la41]: Correct, 1 mark, and this is consistent with the presumption that place of incorporation is the COMI

Commented [la42]: Correct, 1 mark, and the boutique in London will be the necessary establishment in the jurisdiction of the foreign proceedings for non-main recognition

Question 4.3 [5 marks]

Commented [la43]: 2.5/5 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?

Chapter 11 leads to an automatic stay, however there are certain specifics to note. Hence, the following:

- (i) For the DOJ investigation, statutory exceptions exist for regulatory investigations and criminal proceedings. These may significantly affect any hold on certain financial transactions depending on various factors, such as perhaps the consideration of public good.
- (ii) Securities contracts are subject to safe harbor provisions. Any payments made on the margin loan should be exempted from fraudulent conveyances or preferences provided that it is made in good faith (i.e. not a part of a financial institution's attempt to use such provisions to protect a complex set of transactions that would not otherwise qualify). In the continued absence of such payments, the broker is deemed a secured, pre-petition creditor of Speculation, Inc.
- (iii) The delinquent lease will be applied an automatic stay, although (as mentioned in another question), such non-residential property lessors will also be given powers to consent or deny any deferral in decisions for such leases that have not yet expired beyond a total of 210 (120 + 90) days of the automatic stay order. Should Speculation, Inc. continue to occupy the premises and the lease contract is not rejected, rent shall have to be paid as part of administrative expenses and will be on an ongoing basis.
- (iv) The suit would be considered an unsecured, pre-petition claim and any payments, if made, shall continue to follow the absolute priority rule.

Commented [la44]: Correct, 1 mark

Commented [la45]: Correct, 1 mark

Commented [la46]: Partially correct, 1/2 mark, the margin loan is a securities contract and therefore is subject to an exemption from the automatic stay so the broker can sell the collateral

Commented [la47]: Specifically, the landlord cannot pursue eviction proceedings on account of the unpaid pre-petition rent

Commented [la48]: Specifically, the pre-petition litigation will be stayed on the filing of the petition

* End of Assessment *