

TOTAL = 40.5/50
81%



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]: 1, correct

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.

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.

Question 1.5

Which of the following regarding executory contracts is false?

Commented [FV3]: 1, correct

Commented [FV4]: 0, correct answer is E

(a) A court will generally defer to a debtor's business judgment regarding whether to assume or reject an executory contract.

Commented [FV5]: 1, correct

(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.

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.

Commented [FV6]: 1, correct

(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.

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.

Commented [FV7]: 1, correct

(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?

Where a debtor has a cross-claim against a creditor, setoff has the effect of reducing the creditor's claim against the debtor by the extent of the debtor's cross-claim. It is not permitted in many circumstances because it has the effect of reducing a debtor's property (which includes its cross-claims against a creditor), when creditors against whom the debtor has cross-claims should be treated in the same way as other creditors (of the same class) without factoring in any setoff.

Commented [FV11]: .5 Full credit not given because answer did not clearly explain that set off is not allowed because it may improve the position of a creditor as compared to others.

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?

Priming lien is security over pre-petition encumbered estate property that ranks above or no less than the pre-petition lien on the encumbered estate property. The court permits priming lien where it is necessary to secure post-petition financing and the interest of the secured creditor with the pre-petition lien is adequately protected.

Commented [FV12]: 1.5. Full credit not given because answer does not note that priming is only granted where no alternative DIP is available.

Question 2.3 [2 marks]

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

Violation of the automatic stay is tantamount to contempt of court. Acts committed in violation of the automatic stay can be rendered void or voidable.

Commented [FV13]: 2, correct

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?

Creditors deemed to accept a plan of reorganization are those whose rights are not adversely affected by the plan. Creditors deemed to reject the plan are those who will receive nothing under the plan. Creditors permitted to vote on the plan are those whose rights may be adversely affected by the plan. For a class of creditors to accept a plan, a simple majority (more than 50%) of the creditors in the class holding at least two-thirds in value of the claims in the class must vote in favour of the plan.

Commented [FV14]: 1.5. Full credit not given because the answer did not refer to creditors being unimpaired in the first sentence or impaired in the third.

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) Preferences.

(b) Preferences.

(c) Actual fraudulent conveyances.

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

Commented [la16]: 13/15 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 consistent with the US Constitution if the order is in respect of "core proceedings" (essentially cases under the Bankruptcy Code or proceedings arising under the Bankruptcy Code) to the extent that they do not involve the determination of rights that also come within the jurisdiction of courts provided under the US Constitution (as opposed to bankruptcy courts which are

Commented [la18]: Correct, 1/2 mark

creatures of statute, the Bankruptcy Code). Notwithstanding, a bankruptcy court may also enter a final order where the parties so consent.

Commented [la19]: Correct, 1/2 mark

Orders that are not constitutionally final are reviewed *de novo* (i.e., afresh) both as to findings of fact and conclusions of law.

Commented [la20]: Correct, 1 mark; the review is by the district court or Bankruptcy Appellate Panel

Question 3.2 [3 marks]

Commented [la21]: 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's filing of a Chapter 15 petition does not give rise to an automatic stay of creditor action. The automatic stay arises only if the foreign proceeding in a Chapter 15 petition is recognized as a foreign main proceeding. A foreign representative can obtain equivalent relief by applying for a stay of creditor action on an interim basis under Chapter 15 of the Bankruptcy Code, or by commencing plenary proceedings under the Bankruptcy Code.

A foreign representative in a Chapter 15 proceeding also does not have access to the provisions of the Bankruptcy Code for avoidance powers. A foreign representative can overcome this by commencing a plenary proceeding under the Bankruptcy Code after recognition of the foreign proceeding.

Commented [la22]: Correct, 1 mark

Commented [la23]: Correct, 1 mark; alternatively, the foreign representative may bring equivalent claims under applicable US or foreign law

Question 3.3 [4 marks]

Commented [la24]: 4/4 marks

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

Aside the Bankruptcy Code, when preparing a filing for a bankruptcy court, one should review the Federal Rules of Bankruptcy Procedure, the Federal Rules of Civil Procedure incorporated in the Federal Rules of Bankruptcy Procedure, as well as the local rules of procedure and the personal practices of the judges of the relevant court where filing is contemplated.

Commented [la25]: Correct, 1 mark

Commented [la26]: Correct, 1 mark

Commented [la27]: Correct, 1 mark

Commented [la28]: Correct, 1 mark

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 of Delaware corporations owe a fiduciary duty of loyalty to their corporation, to act in the best interest of their corporation, in good faith on the basis of reasonable information. They also owe a duty of care in managing the affairs of their corporation.

Commented [la30]: Correct, 1 mark

Commented [la31]: Correct, 1 mark

In the ordinary course of business, their duties are owed to their corporation and its shareholders.

Commented [la32]: Correct, 1 mark

Commented [la33]: Correct, 1 mark

Even when a Delaware corporation is potentially or actually insolvent, a director of such a corporation still owes duties to the corporation and its shareholders, and not creditors of the corporation. Consequently, directors cannot be held accountable for "wrongful trading", for example, which is a concept that has no equivalence in the US.

Commented [la34]: Correct, 1 mark

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

Commented [la35]: 11/15 marks

Question 4.1 [5 marks]

Commented [la36]: 3/5 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 lessors of office space to iWork Ltd could evict iWork Ltd if the relevant leases have expired as the automatic stay provided under the Bankruptcy Code does not extend to such creditor action.

Another protection is that, if iWork Ltd is in a Chapter 7 case, the trustee of iWork Ltd is limited to make decisions about the assumption or rejection of any unexpired lease within 60 days from petition date. While iWork Ltd would have until the confirmation of a reorganization plan to decide whether to assume and assign or reject any unexpired lease if it were a Chapter 11 case, the Bankruptcy Code specifically requires iWork Ltd to make decisions about any unexpired lease within 120 days of the order for relief. This period can be extended for 90 days for cause, but any subsequent extension requires the consent of the lessors.

Commented [la37]: Correct, 1 mark

Commented [la38]: Correct, 1 mark

Where the leases of office space to iWork Ltd were assumed and subsequently rejected, the Bankruptcy Code ranks two years of lease payments from the later of the date of rejection of a lease or turnover of lease premises as administrative expenses.

Commented [la39]: Correct, 1 mark. The debtor also has to pay post-petition rent as an administrative expense and the lessor has an unsecured claim for pre-petition unpaid rent.

Commented [la40]: 4/5 marks

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. Whether a foreign proceeding should be recognized as a foreign main or foreign non-main proceeding depends on whether the foreign proceeding was commenced in a jurisdiction where the debtor's centre of main interest (COMI) is. While COMI is not defined, a debtor's place of incorporation is presumed to be its COMI. In this case, Skin Luxe's COMI is in France as that is where Skin Luxe was incorporated and where its principal place of business is. France is where Skin Luxe develops and manufactures its skin care products. In contrast, London is but one of the various international cities in which Skin Luxe sells its skin care products, which is hardly sufficient to demonstrate that Skin Luxe's COMI lies in London/UK.

Commented [la41]: Correct, 1 mark

Commented [la42]: Correct, 1 mark

Commented [la43]: Correct, 1 mark

Commented [la44]: Correct, 1 mark

Commented [la45]: Specifically, the boutique in London is an establishment, permitting recognition of the English scheme of arrangement as foreign non-main proceedings.

Commented [la46]: 4/5 marks

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?

The filing of a Chapter 11 petition automatically gives rise to a stay of creditor action, which does not have the effect of staying the DOJ investigation.

Commented [la47]: Correct, 1 mark

Commented [la48]: Correct, 1 mark

As regards the margin loan default, the automatic stay means that the broker will not be able to enforce against the shares held as security for the margin loan, or to commence or continue any proceeding in respect of the margin loan default. Any setting off of trades with Speculation Inc's trading counterparts is, however, not affected by the automatic stay.

Commented [la49]: Incorrect, the margin loan is a securities contract exempt from the automatic stay, so the broker can sell the collateral.

As for the delinquent lease, the automatic stay means that the landlord cannot evict Speculation Inc unless the lease has already expired by the time the Chapter 11 petition was filed. If the lease has not expired, the landlord is not allowed to terminate the lease and sue for rental arrears. Speculation Inc is at liberty to continue to use the leased premises, though it is very unlikely that Speculation Inc could carry on its business of trading given the DOJ investigation. The automatic stay has no effect on the DOJ investigation. In any case, Speculation Inc has to decide, within 120 days of the order for relief, whether to assume and assign or reject the lease. This period can be extended for 90 days for cause, but any subsequent extension requires the consent of the lessor.

Commented [la50]: Correct, 1 mark

The automatic stay has the effect of staying the continuation of the employment discrimination lawsuit which the former employee had already commenced against Speculation Inc.

Commented [la51]: Correct, 1 mark

* End of Assessment *