

TOTAL = 32/50
64%



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]: 0, correct answer is B

Question 1.6

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

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

Commented [FV6]: 0, correct answer is C

Question 1.7

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

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

Commented [FV7]: 0, correct answer is a

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?

A setoff lets a creditor subtract what the debtor owes them from what they owe the debtor. In many circumstances, creditors are not allowed to do this because it effectively gives them an unfair advantage over other creditors who aren't owed anything 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 way for a debtor in possession to fund its business after filing for Chapter 11 bankruptcy. The lien is secured against the debtor's assets and can rank equally with or above existing security. The debtor can pursue a priming lien if it has tried and failed to get unsecured debt but has to demonstrate to the court that it adequately protects the interests of the relevant secured creditor.

Commented [FV12]: 2, correct

Question 2.3 [2 marks]

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

Depending on the circuit where the bankruptcy case is being heard, the action taken in violation of the automatic stay may be void or voidable. This applies even if the party was unaware of the automatic stay at the time of the action.

Commented [FV13]: 1. Full credit not given because answer does not note that violator may be sanctioned for 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) *Those that are unimpaired.*

(ii) *Those that will receive nothing.*

(iii) *The following:*

- a. *Creditors secured by real property*
- b. *Creditors secured by personal property*
- c. *Unsecured creditors*

For a class of creditors to accept a plan, a simple majority of the creditors in the class must vote in favour i.e. at least two-thirds of the value of claims in the class. For equity interests, at least two-thirds in amount of interests to vote in favour is necessary.

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?**

A preference claim.

(b) **Which cause of action requires that the debtor be presumed or proven to have been insolvent at the time of the transfer?**

A constructive fraudulent conveyance.

(c) **Which cause of action requires that the debtor be proven to have intended to frustrate creditors' recoveries?**

An actual fraudulent conveyance.

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

Question 3.1 [3 marks]

Commented [FV14]: 1.5. The answer for iii is impaired classes that will receive something under the plan are permitted to vote.

Commented [FV15]: 2, Correct answer for b is also a preference.

Commented [la16]: 11.5/15 marks

Commented [la17]: 2.5/3 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.

To enter a final order consistent with the US Constitution, a bankruptcy court must resolve all issues in the litigation, leaving no further matters to be decided. Additionally, the parties involved must consent to the jurisdiction of the bankruptcy court.

Commented [la18]: Incorrect, the resolution of the whole litigation is the test for appellate finality, not constitutional finality. A bankruptcy court can enter a constitutionally final order on a core proceeding if it is exclusive to the Bankruptcy Code, like a challenge to a petition.

Appeals from bankruptcy court orders are typically reviewed by the district court in the relevant jurisdiction. However, some circuits have Bankruptcy Appellate Panels (BAPs) comprising judges from the bankruptcy courts within the circuit. In these circuits, parties can choose whether to have their appeal heard by the BAP or the district court.

Commented [la19]: Partially correct, 1/2 mark, this is an alternative basis for constitutional finality, not an additional requirement.

Commented [la20]: Correct, 1/2 mark

Commented [la21]: Correct, 1/2 mark

In cases where bankruptcy court orders lack constitutional finality, the district court or BAP will conduct a de novo review of all objected findings of fact and conclusions of law i.e. a fresh examination of the facts and issues at hand.

Commented [la22]: Correct, 1 mark

Question 3.2 [3 marks]

Commented [la23]: 0/3

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?

Certain provisions of the Bankruptcy Code cannot be invoked automatically by a foreign representative in a Chapter 15 proceeding like the automatic stay, which typically applies in Chapter 7 and Chapter 11 proceedings, as well as provisions allowing, for example, the operation of the debtor's business in the ordinary course of business.

Commented [la24]: The avoidance provisions of the Bankruptcy Code cannot be exercised by the foreign representative in a chapter 15 proceeding. The alternatives are to pursue equivalent claims under US or foreign law or to commence a plenary proceeding under chapter 7 or 11.

Equivalent relief can be obtained through two methods. Either recognition of the foreign proceedings as foreign main proceedings (if initiated in the debtor's COMI) or foreign non-main proceedings (if initiated in a jurisdiction where the debtor has an establishment). The stay would be automatically granted in the case of the former. Otherwise, the grant of the types of relief discussed are at the discretion of the court.

Question 3.3 [4 marks]

Commented [la25]: 4/4 marks

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

The Bankruptcy Rules, the Federal Rules of Civil Procedure, the local rules of the bankruptcy court and the assigned judge's personal practices.

Commented [la26]: Correct, 1 mark

Commented [la27]: Correct, 1 mark

Commented [la28]: Correct, 1 mark

Commented [la29]: Correct, 1 mark

Commented [la30]: 5/5 marks

Question 3.4 [5 marks]

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

Under Delaware law, directors of corporations owe fiduciary duties of **loyalty and care** to act in the best interests of the corporation. The duty of loyalty entails avoiding conflicts of interest and prioritizing the corporation's welfare. The duty of care involves making informed decisions based on reasonable information. The application of the business judgment rule protects directors from liability for errors in judgment, presuming (which presumptions can be rebutted) that they acted in good faith and with reasonable information.

Directors' duties are owed to the **corporation and its shareholders, not to creditors**, even in situations where the corporation is insolvent (see *North Am Catholic Educational Programming, Inc v. Gheewalla*). Unlike some other jurisdictions like England and Wales, Delaware law does not impose a duty on directors to consider the interests of creditors when the company is insolvent or approaching insolvency.

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?

Assuming iWork files a petition:

1. The lease agreements between iWork Ltd and lessors would be considered executory contracts and the trustee or debtor-in-possession must decide whether to assume, reject, or assume and assign the agreements. If the lease is assumed, iWork Ltd must cure any outstanding defaults such as unpaid rent to continue occupying the leased space. If the lease is rejected, the lessor has a claim for damages arising from the rejection, which is treated as a pre-petition claim in the bankruptcy proceedings.
2. The lessors can seek relief from the automatic stay to pursue remedies outside of the bankruptcy process if they can demonstrate cause.
3. **Unpaid rent owed to lessors is typically treated as an administrative expense priority claim in bankruptcy proceedings so the lessors are entitled to payment ahead of most other unsecured creditors.**

Question 4.2 [5 marks]

Commented [la31]: Correct, 1 mark

Commented [la32]: Correct, 1 mark

Commented [la33]: Correct, 1 mark

Commented [la34]: Correct, 1 mark

Commented [la35]: Correct, 1 mark

Commented [la36]: 8/15 marks

Commented [la37]: 1/5 marks

Commented [la38]: Specifically, the debtor has only 120 days to assume or reject, with a maximum 90 days extension for cause, after which extensions require landlord consent.

Commented [la39]: Correct, 1 mark, this is only for post-petition rent. Pre-petition rent is an unsecured claim. If a debtor assumes and then rejects a lease, the landlord has an administrative claim for 2 years' rent.

Commented [la40]: 4/5 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.

For recognition under Chapter 15, the scheme must not be solely for investigation purposes and must involve debt adjustment. Based on the information provided, it seems the English scheme would meet this criteria.

It will be presumed that France is Skin Luxe's COMI as that's where it's incorporated. Further supporting this conclusion is the fact that Skin Luxe's PPB is in France and it manufactures its products there (and thus likely has employees and management in France). Skin Luxe has a boutique in London which likely qualifies as an establishment. Therefore, it's likely the Chapter 15 proceedings would result in the English scheme being recognised a foreign non-main proceeding.

Commented [la41]: Correct, 1 mark

Commented [la42]: Correct, 1 mark

Commented [la43]: Correct, 1 mark

Commented [la44]: Correct, 1 mark, this is because a foreign main proceeding is one in the debtor's COMI jurisdiction.

Commented [la45]: 3/5 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?

- (i) *The bankruptcy filing / stay wouldn't affect the investigation. The DOJ would be a party in interest in the proceedings. Any penalty would be treated as a (post-petition) claim in the proceedings.*
- (ii) *The lender becomes a creditor and would be able to vote on Speculation Inc.'s reorganization plan.*
- (iii) *Speculation Inc. could reject the overdue lease (giving the landlord a claim for damages).*

Commented [la46]: Correct, 1 mark, the filing would cause the automatic stay to come into effect.

Commented [la47]: Correct, 1 mark

Commented [la48]: The margin loan is a securities contract that is exempt from the automatic stay, so the lender can sell the collateral even after the petition is filed.

Commented [la49]: The automatic stay will bar the landlord from pursuing eviction on account of the unpaid rent.

(iv) *The automatic stay in bankruptcy freezes the discrimination lawsuit until the bankruptcy court decides otherwise.*

Commented [la50]: Correct, 1 mark

* End of Assessment *