

TOTAL = 28/50
56%



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]: 0, correct answer is D

- (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.
- (c) In the most common formulation, executory contracts are defined as those where both sides to a contract have material unperformed obligations.
- (d) Chapter 11 debtors have greater flexibility than chapter 7 debtors on when they may assume, assign or reject an executory contract.
- (e) Under the hypothetical test, a debtor cannot assume an executory contract if the debtor could not also assign the contract.

Commented [FV5]: 1, correct

Question 1.6

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

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

Commented [FV6]: 1, correct

Question 1.7

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

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

Commented [FV7]: 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]: 0, correct answer is C

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]: 0, correct answer is B

QUESTION 2 (direct questions) [10 marks]

Question 2.1 (1 mark)

What is setoff and why is it not permitted in many circumstances?

Setoff is a right of a creditor to deduct simultaneously a debt it owes from a different transaction to the debtor from a claim it has against the debtor under non-bankruptcy law. It is not permitted in many circumstances because setoff can put a creditor in a different/privilege situation regarding others and compared with unsecured creditors, as it decreases the obligation of the amount of money from the parties (debtor and creditor) and it will reduce the money the debtor needs to have under the bankruptcy proceeding to pay the unsecured creditors.

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?

"Priming lien" is a type of lien granted by the court, equal to a pre-petition lien on estate property to secure post-petition financing.

As the requirements, the priming lien is only granted if no other financing could be offered and if the debtor demonstrates that the interest of the secured creditor is being properly protected. Also, the priming lien will have priority in collateral over the pre-petition secured lenders, which is an advantage to secure DIP financing.

Commented [FV12]: 1.5. Partial credit only given because the answer fails to use the term adequately protected, which is defined in the Bankruptcy Code. Properly protected is the wrong terminology.

Question 2.3 [2 marks]

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

There can be the imposition of sanctions against the violator and compel to take affirmative actions to undo the effect of its violation.

Those sanctions can be the payment of debtor's attorney's fees, a daily fine to be paid to the court but it's important to note the court prohibits acts that might change the status quo of the estate's property, considering that the stay only applies to property of the estate.

Commented [FV13]: 1. Full credit not given because answer does not note 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?

In voting on the plan, there are basic set of classes of creditors that are (a) creditors secured by real property; (b) creditors secured by personal property; (c) unsecured creditors and (d) shareholders. Not all classes are deemed to accept the plan, but it can be approved by cramdown of dissenting classes. (i) the unimpaired class is deemed to accept the plan and (ii) the class that will receive nothing is deemed to reject the plan. (iii) It is noted that only impaired classes have the right to vote on the plan.

Commented [FV14]: 2, correct

Creditors can approve the plan if a simple majority of the creditor in the class, with 2/3 of the value of claims in the class, or if 2/3 in number of interests votes in favor. If it will be the case of cramdown it will also be mandatory that at least one impaired class vote to accept the plan.

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?***

(a) In this case, it will be considered as preference. But it will only arise if the debtor is paying a creditor for a pre-existing debt. Exchange of value and prepayment for goods and services are not considered as a preference because the debt is not incurred until the debtor receives the product, for example.

(b) In this case, it will be considered as constructive fraudulent conveyances and should have more elements such as the transfer was made to or for the benefit of an insider, the debtor intended to or believe it would incur debts beyond its ability to pay on maturity, etc.

Commented [FV15]: 2, answer to b is also preference

(c) In this case, it will be considered as fraudulent conveyances, when it's proven that the debtor made a transfer or incurred an obligation intending to hind, delay or defraud any entity for the debtor to be expected as indebted.

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

Commented [la16]: 8.5/15 marks

Question 3.1 [3 marks]

Commented [la17]: 0.5/3

Describe the circumstances in which a bankruptcy court may enter a final order consistent with the US Constitution, who reviews appeals from bankruptcy court orders and how orders that are not constitutionally final are reviewed.

Bankruptcy proceedings are related to federal legislation and has a lot of implications for jurisdictions related to district courts, because the interpretation of the Bankruptcy Code may differ between regional circuit courts of appeal before being resolved by the US Supreme Court. Also, Bankruptcy Code and its regional courts are different (and cannot exercise jurisdiction) of other federal courts under Article III of the US Constitution.

However, there are many times when Bankruptcy proceedings discuss matters involving statutory and contract rights that would be discussed under the Article III of the US Constitution. So new jurisdictional provisions were enacted under a statute that creates a distinction between core and non-core matters.

If they are core proceedings, the bankruptcy judges will render a final order. If they are bankruptcy non-core proceedings, the court cannot make a final order and will submit the case to the district court to have a final decision, which decision will be granted not under the Bankruptcy Code, but under the Article III of the US Constitution.

Commented [la18]: Incorrect, the bankruptcy court can only enter final orders on core proceedings specific to the Bankruptcy Code (e.g., a challenge to a petition) or with the parties' consent.

Commented [la19]: Correct that the decision is appealed to the district court, 1/2 mark, but the decision of the Bankruptcy Court is treated as a report and recommendation to the District Court and reconsidered de novo as to points objected to by the parties. Alternatively, the appeal may be heard by a Bankruptcy Appellate Panel.

Question 3.2 [3 marks]

Commented [la20]: 0/3 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?

One of the provisions is that the foreign representative of the debtor must file a petition voluntarily to commence a case under chapter 15.

Commented [la21]: The foreign representative may not bring claims in a chapter 15 under the avoidance provisions of the Bankruptcy Code. It may obtain equivalent relief by commencing claims under applicable US or foreign law, or by commencing plenary proceedings under chapter 7 or 11.

The other provision is that the filing of the petition does not grant an automatic relief - the stay of creditor action.

The stay will be granted (i) upon the petition for recognition of a foreign main proceeding, limited to the property of the debtor in the territorial of US; (ii) if there is pending recognition or following recognition oof a non-main proceeding.

Question 3.3 [4 marks]

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

*The person should review the **Federal Rules of Bankruptcy Procedure**, related to litigation disputes and forms incorporated by reference the **Federal Rules of Civil Procedure**.*

It is also important to review the Bankruptcy rule considering the definition of courts jurisdiction and to previously have an idea if it will be a core or non-core bankruptcy proceeding.

*The **local rules of the bankruptcy court** because they preferred working procedures of the judges, and can modify deadlines of the process.*

*The **judge's personal practices**, because they are periodically updated and available on the website of the bankruptcy court.*

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?

Many of corporate groups include one or more Delaware corporations, making Delaware a venue of choice for many large group bankruptcies and the third circuit court.

*The directors have the fiduciary duties of **loyalty** to the corporation's best interest and **care** in educated decision-making.*

The directors are protected by the "business judgment rule", which consider the presumption that the directors, to make decisions, acted in good faith on with reasonable information, concluding that they didn't act with negligence and with intention to cause any loss to the company.

This rule does not apply when a transaction is approved by a board majority of directors that is not disinterested and independent, or if a shareholder is on both sides

Commented [la22]: 3/4 marks

Commented [la23]: Correct, 1 mark

Commented [la24]: You should also review these as they are not set out in full in the Federal Rules of Bankruptcy Procedure

Commented [la25]: Correct, 1 mark

Commented [la26]: Correct, 1 mark

Commented [la27]: 5/5 marks

Commented [la28]: Correct, 1 mark

Commented [la29]: Correct, 1 mark

of the transaction, for example, because the transaction will be considered as not fair enough.

In case of the corporation is potentially or already insolvent, the director duties are owed to the corporation and its shareholders, not to creditors.

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?

The Bankruptcy Code provides a lift stay or relief from stay to protect the lessor and to protect the value of the property not to decline during the course of the bankruptcy proceeding.

To the lessors, the Bankruptcy Code can also protect the law of the contract and will considered the lessor as a secured creditor.

If the protection is still considered as lacking, the debtor can avoid the stay being lifted to allow the lessor to pursue remedies with respect to the property if it provides indubitable equivalent of the value that may be lost.

It is important to note that the stay period can change from case to case as can change on situations of decisions about executory contracts (chapter 7 - 60 days of the petition date, chapter 11 - until the confirmation of its plan of reorganization).

However, there is an exception that is that decisions about unexpired leases of non-residential property are required to be made within 120 days of the order of stay, and while this period can be extended until more 90 days, any other extension will require the consent of the lessor.

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.

Commented [la30]: Correct, 1 mark

Commented [la31]: Correct, 1 mark

Commented [la32]: Correct, 1 mark

Commented [la33]: 9/15 marks

Commented [la34]: 3/5 marks

Commented [la35]: Correct, 1 mark

Commented [la36]: Post-petition rent is due as an administrative priority, there is an unsecured claim for pre-petition unpaid rent, and if the debtor assumes and then rejects a lease, it must pay 2 years' rent as an administrative priority.

Commented [la37]: Correct, 1 mark

Commented [la38]: Correct, 1 mark

Commented [la39]: 3/5 marks

Discuss whether the English scheme of arrangement could be granted recognition under US chapter 15 as a foreign main or foreign non-main proceeding.

There won't be a problem to Skin Luxe to use an English scheme of arrangement to restructure the bonds that are governed by English law.

However, according to the Model Law it's important to understand what is considered as the center of main interest (COMI) to define if the proceeding will be recognized as a foreign main or non-main proceeding.

According to the text, Skin Luxe is incorporated and has a principal place of business in France, where it develops and manufactures high end skincare products. The definition of "principal place of business and the explanation that this is the place where the company develops and manufactures the products results on the conclusion that there are a lot of employees, information and evidence that fits on the definitions of what COMI is presumed to be.

In this case, considering that the COMI might be France, the US proceeding will be considered 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, 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 provides an automatic stay of any proceeding against the debtor or its property, providing space for a debtor to continue operating in the ordinary business to propose a plan of reorganization that will adjust its debts.

However, regarding the automatic stay, there are some statutory exceptions that the debtor needs to accept and comply with, under penalty of violation of the court decision.

Commented [la40]: Correct, 1 mark

Commented [la41]: Correct, 1 mark

Commented [la42]: Correct, 1 mark, because COMI must be in the jurisdiction of the foreign proceedings for foreign main recognition and the boutique in London constitutes the necessary establishment in the jurisdiction of the foreign proceeding.

Commented [la43]: 3/5 marks

Commented [la44]: Correct, 1 mark

These exceptions include criminal proceedings, regulatory investigations, eviction and other occasions such as the ones mentioned above: delinquent lease and the employment discrimination, the DOJ and the margin loan default investigation.

These stay exceptions reflect a legislative judgment that effects on the debtor's assets, for example, and can not provide the best protection to the debtor.

More than that, the stay exception for the investigation and judgment of this cases can reflect in the daily routine of the company and affect its possibility to keep on progress to adjust its debts, reflecting on the possibilities to propose a reorganization plan.

*** End of Assessment ***

Commented [la45]: The stay does not affect the investigation or the broker's recovery on the margin loan collateral (because it is a securities contract), 2 marks. The lessor will be stayed from pursuing eviction proceedings and the employment discrimination case will also be stayed as it is pre-petition litigation against the debtor.