

TOTAL = 33/50  
66%



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. [FV1]**
- (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. [FV2]**
- (c) A shareholder in Investment Corp, Car Corp's parent company.**

**(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.**

[FV3]

**(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.**

[FV4]

**(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?**

[FV5]

- (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.*

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.* [FV6]
- (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?*

[FV7]

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

Question 1.8

***If a debtor rejects an executory trademark license agreement under which the debtor licenses its trademark to a manufacturer, which of the following is true:***

- (a) The manufacturer has a claim for damages for breach of contract.***
- (b) The manufacturer must immediately stop using the trademark.***
- (c) The manufacturer can continue using the trademark for the remaining period of the <sup>[FV8]</sup> license.***
- (d) Both options (a) and (b).***
- (e) Both options (a) and (c).***

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.***
- <sup>[FV9]</sup> ***(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.***

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.*<sup>[FV10]</sup>
- (d) *Substantive consolidation is commonly used to resolve bankruptcies of corporate groups.*
- (e) *Authority for substantive consolidation comes from the Bankruptcy Code.*

QUESTION 2 (direct questions) [10 marks]

Question 2.1 (1 mark)

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

*[Setoff means to adjust and offset the mutual claims between the parties thereby a higher claim of a party reduces to the extent of liability of such party against the counter-party. Thus, it occurs only in such circumstances when there is a simultaneous existence of claim as well as liability of a party against another. In cases of bankruptcy, setoff is not permitted <sup>in</sup><sup>[FV11]</sup> many circumstances as it results in placing the creditor's seeking setoff at better footing than other unsecured creditors of the debtor.]*

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 lien which is superior or equivalent to the lien already existing on the estate of the debtor against the secured loan. The court may grant financing by way of creating priming lien on the estate of debtor provided the court is satisfied with the requirement <sup>that</sup><sup>[FV12]</sup> the possibility of securing financing by way of other methods remained futile; the debtor has no alternative but to opt for priming; and the interest of the secured creditor who is being primed is adequately protected.]*

Question 2.3 [2 marks]

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

*[Automatic stay kicks in immediately upon filing of bankruptcy petition and no separate notice is required to be given to this effect. The worldwide automatic stay operates qua the[FV13] debtor's estate anywhere in the world. All acts in violation of stay tantamount to - (i) contempt of court leading contempt sanctions by the court; and (ii) making such acts void ab initio or voidable at the option of the aggrieved party]*

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 a plan of reorganization, (i) unimpaired class is deemed to accept the plan, (ii) the class which would receive nothing is deemed to reject the plan and (iii) all other class(es) of creditors would be permitted to vote on the plan. A plan would be treated as approved by[FV14] a class of creditor if a simple majority of the creditors holding at least two-third of the value of the claims or for equity interests, if two-thirds in amount of interests, as the case may be; vote in favour of 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) All transfer of the property of the debtor made in favour of a creditor on account of antecedent debt would give rise to a cause of action for filing of a preference application and avoidance thereof if the transfer is made within the suspect period.*

*(b) A debtor is presumed or proven to have been insolvent during the 90 days prior to the petition date for the purposes of adjudication of preference motion. However, the creditor[FV15] may rebut the presumption of insolvency by producing such evidence as it may deem appropriate.*

*(c) The transactions/ payments pertaining to securities and commodities contracts are ordinarily treated/ presumed as non-preferential transaction to maintain certainty and finality in the operation of the financial markets. However, such presumption and safe harbors for securities and commodities contracts can be rebutted by demonstrating that such transfer/ payment was made with intent to defraud creditors and to frustrate creditors' recoveries.]*



**QUESTION 3**<sup>[1a16]</sup> (essay-type questions) [15 marks in total]

**Question 3.1**<sup>[1a17]</sup> [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.**

*[Ordinarily, final order refers to such order which determines the rights and contentions of the parties conclusively and nothing remains pending to be decided and adjudicated upon by the court. However, in context of bankruptcy proceedings, certain orders, which do not conclusively determine the issue, are also treated as final orders for the purposes of appeal. Bankruptcy courts are creature of statute and are not federal courts which derive its jurisdiction and power from Article III of the US Constitution and thus, the jurisdiction of bankruptcy court is limited and narrower than a federal court. The bankruptcy court derive its jurisdiction and power from the delegated authority of district court and it may pass a final order on a motion challenging the validity of a petition<sup>[1a18]</sup>. Additionally, the bankruptcy court is also empowered to render a final order on core proceedings with the consents of the parties.<sup>[1a19]</sup>*

*A final order passed by bankruptcy court can be reviewed in appeal by the jurisdictional district court<sup>[1a20]</sup> or the Bankruptcy Appellate Panel (BAP)<sup>[1a21]</sup>, as the case may be. Further appeals are entertained by the circuit court of appeals. There is a possibility of direct appeal to the circuit court of appeals in a circumstance where either the bankruptcy court or the district court certifies that one of the following circumstances exists: (i) the appeal raises a question of law as to which there is no controlling decision of the circuit or the US Supreme court, or requires resolving conflicting controlling decisions, or (ii) immediate appeal may materially advance the progress of the case.*

*As per my understanding, orders passed by the bankruptcy court on non-core proceedings are the orders that are not constitutionally final and such rulings are reviewed by the district court or BAP, as the case may be, on finding of facts and law.<sup>[1a22]</sup> Further the order passed by the district court or BAP is appealable before a circuit court of appeal de novo as to conclusions of law and for abuse of discretion for finding of fact.]*

**Question 3.2**<sup>[1a23]</sup> [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 in a chapter 15 proceeding cannot invoke avoidance provisions of the Bankruptcy Code as it is excluded from its purview. The only way to invoke the avoidance provisions of the Bankruptcy Code is to file a plenary proceeding under chapter 7 or chapter 11. Therefore, a foreign representative may get an access to avoidance provisions in following two ways:*

- (i) By commencing a plenary proceeding under the Bankruptcy Code before moving a petition for recognition of the foreign proceeding under chapter 15; or*
- (ii) By commencing a plenary proceeding under the Bankruptcy Code after recognition of the foreign proceeding under chapter 15.]*

**Question 3.3** [4 marks]

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

*[The Federal Rules of Bankruptcy Procedure (in short “the Bankruptcy Rules”) governs the procedure applicable in bankruptcy proceedings. The Bankruptcy Rules often refer and incorporate rules of civil procedure which governs affairs of adversarial proceedings. There are several bankruptcy forms provided in the US courts website and the parties are required to choose the appropriate form for filing an appropriate bankruptcy petition. Further each bankruptcy court has certain local rules of procedure coupled with practice direction as may be passed by a concerned judge. Additionally, a party is required to provide details of assets and list of creditors etc. which is a part of schedule to be appended along with the petition.]*

**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?**

*[Directors of Delaware corporations owe basic fiduciary duty of care and loyalty towards best interest of the corporation. Directors must act in independent and good faith basis without any personal interest and benefits. As directors are expected to act with care in decision making, it is critical that decisions are made after being fully informed and properly educated on a given issue. Additionally, the directors are responsible for keeping oversight in the affairs and making requisite regulatory and legal disclosures. It may be relevant to point out that the duty of care is in decision-making is protected by the business judgment rule.*

*Directors’ fiduciary duties always owed to the corporation and its shareholders and the same do not change even if the corporation is potentially or actually insolvent. The Delaware Supreme Court in the matter of Trenwick Am Litig Trust vs. Ernst & Young, LLP (Del Ch 2006) has held that “even when the company is insolvent, the board may pursue, in good faith, strategies to maximize the value of the firm.” Thus, the duties of directors continue to align towards best interest of the corporation and maximizing its value even in circumstances of insolvency.]*

**QUESTION 4**<sup>[1a37]</sup> (fact-based application-type question) [15 marks in total]

**Question 4.1**<sup>[1a38]</sup> [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?***

*[In the given fact situation, the lessors<sup>[1a39]</sup> of office space would be 'office building owners', who had leased out their respective office spaces to iWork Ltd. for a consideration of lease rent. As iWork Ltd. has failed to pay rent on some of its office space leases to the office building owners/ lessors, a bankruptcy petition can be filed assuming requirement of monetary threshold and number of petitioning creditors are met.*

*The moment a bankruptcy petition is filed a worldwide automatic stay of any proceeding against the debtor or its property would operate. The automatic stay would facilitate reorganization, rehabilitation, and realization of maximum value through a plan of reorganization and protect the property of estate from creditor enforcement actions with respect to pre-petition claims. Additionally, Bankruptcy Code's debtor friendly rehabilitation regime would permit the debtor in possession or trustee, as the case may be, to avoid pre-petition transactions, reject unprofitable contracts and enable selling of assets.]*

**Question 4.2**<sup>[1a40]</sup> [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.***

*[In the given fact situation, Skin Luxe is company incorporated in France and its principal place of business also remains in France which is critical for determining the debtor's center of main interests (COMI)<sup>[1a41]</sup>. The COMI further facilitate in characterization of the foreign proceedings as 'foreign main' or 'foreign non-main'. Once such characterization is achieved, it determines the scope of relief available to the debtor following recognition of the foreign proceedings under the Bankruptcy Code.*

*As in the given fact situation, Skin Luxe is considering English scheme of arrangement to restructure the bonds, the English proceedings would be taken as foreign proceedings for the purposes of chapter 15 proceedings under the Bankruptcy Code. It is relevant to point out that chapter 15 proceeding is an ancillary bankruptcy proceeding than a plenary bankruptcy proceeding. The ancillary proceeding can only be initiated by the foreign representative of the Debtor (Skin Luxe herein) and such filing of petition would not automatically stay creditors' action against the property of the debtor situated within the territorial jurisdiction of United States, unless the petition for recognition of foreign proceeding is granted.*

*As the COMI of Skin Luxe is France<sup>[1a42]</sup>, the English proceedings could be granted recognition as foreign non-main proceedings<sup>[1a43]</sup> under chapter 15 of the Bankruptcy Code.]*

**Question 4.3<sup>[1a44]</sup> [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 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 DOJ investigation would remain unaffected as the automatic stay<sup>[1a45]</sup> which ordinarily kicks in from the date of filing of the bankruptcy petition<sup>[1a46]</sup>, does not extend to regulatory investigation launched by US Department of Justice.*

*(ii) Speculations Inc. is not eligible to be treated as debtor for the purposes of chapter 11 of the Bankruptcy Code for being engaged in the business of stock broking and thus, the filing of chapter 11 petition by Speculation Inc. would have no effect on margin loan default.<sup>[1a47]</sup> A petition under chapter 7 of the Bankruptcy Code would be maintainable.*

*As per the above analogy, filing of chapter 11 petition by Speculation Inc. would have no effect and bearing on (iii) the delinquent lease and (iv) the employment discrimination lawsuit.<sup>[1a48]</sup>*

**\* End of Assessment \***