

**TOTAL = 33.5/50**  
**67%**



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

- (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?**

(a) *A court will generally defer to a debtor's business judgment regarding whether to <sup>[FV5]</sup> 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?*

**(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.*

[FV7]

(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.**

[FV8]

**(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).**

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.**[FV9]

**(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.**

[FV10]

**(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.**

QUESTION 2 (direct questions) [10 marks]

Question 2.1 (1 mark)

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

*In many circumstances, setoff, which involves a creditor offsetting a claim against a debtor with a debt owed to the same debtor, is restricted. This limitation is in place because it has the potential to enhance one creditor's position at the expense of other unsecured creditors, [FV11] given that it reduces the overall obligation to the debtor's estate. This netting off process can involve two or more obligations.*

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?**

*In the pursuit of post-petition funding, a Debtor may seek a priming lien from the court. This type of lien, granted on estate property, holds either a higher or equal priority compared to pre-petition liens on the same property. The court will consider approving a priming lien only if the debtor is unable to secure unsecured credit in the ordinary course of business without court approval, secured unsecured debt outside the ordinary course of business with [court, FV12] approval, or secure secured debt with a lien on unencumbered estate property or with a junior lien on encumbered estate property. To gain court approval, the debtor must demonstrate the adequate protection of the secured creditor's interest with the priming lien.*

Question 2.3 [2 marks]

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

*A violation of the automatic stay in bankruptcy can lead to various consequences. Firstly, if parties are found to have willfully violated the automatic stay could face penalties and sanctions which would be imposed by the bankruptcy court and can include fines or other legal measures. Furthermore, the violator could be held liable for any damages incurred by the debtor due to the violation, this includes emotional distress, financial losses or other<sup>[FV13]</sup> adverse effects.*

**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?***

*A plan is considered approved and accepted by a class of creditors when a majority of the creditors in the class (at least two-thirds) vote in favor of the plan. Furthermore, if certain classes of creditors do not vote on the plan, but at a minimum one class of impaired creditors does vote to accept it, then the non-voting class is deemed to accept the plan.*

*Additionally, if the class of creditors votes to reject the plan, it is deemed to have rejected the plan. An unimpaired class is automatically deemed to accept the plan, while a class which will receive no distribution is deemed to reject the plan.<sup>[FV14]</sup>*

*Classes of impaired creditors, those whose contractual rights are altered under the plan, are typically permitted to vote on the plan. This ensures that decision-making authority rests with those who have the most to gain or lose, a principle referred to as the cramdown requirement.*

**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? |***

<sup>[FV15]</sup>

*(a) Preferences - These refer to transfers made by a debtor to a creditor leading up to a bankruptcy filing, which favors the creditor over the others by repaying the debt to that creditor.*

*(b) Actual fraudulent conveyances - This is when a debtor transfers property or assets with the intent to defraud creditors, usually before a bankruptcy process.*



*(c) Constrictive fraudulent conveyances - This requires a debtor is proven to have intentionally frustrate creditor's recoveries with the intent to hinder, delay or defraud creditors, regardless of the debtor's solvency at the time.*

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

**Question 3.1** [1a17] [3 marks]

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

*Bankruptcy courts are empowered to adjudicate core proceeding's, [1a18] including matters related to the administration of the estate and orders pertaining to credit claims. [1a19] With the consent of the parties, bankruptcy courts also have the authority to enter final orders. [1a19] Although non-core proceedings can be heard by bankruptcy courts, the final determination must be made by the district court.*

*For non-core proceedings, the bankruptcy court can hear the case but the final decision mostly comes from the district court. However, with the consent of the parties, bankruptcy courts can enter final orders. Appeals from bankruptcy court orders can be initiated by parties involved in the liquidation or individuals adversely affected by the decision. [1a20] District courts typically handle appeals, but in some instances, a Bankruptcy Appellate Panel (BAP) [1a21] consisting of bankruptcy judges from the circuit may hear the case.*

*Non-final orders, also known as interlocutory orders, are issued when only some issues or claims have been resolved, or when the court lacks jurisdiction to issue a final order. [1a22] In the case of non-core proceedings or non-final orders, the BAP or district court reviews findings of fact and objections to legal conclusions de novo. [1a22] The BAP or district court order is then subject to review by a circuit court of appeals, which assesses legal conclusions de novo and examines findings of fact for abuse of discretion. For final orders in core proceedings, the district court or BAP reviews legal conclusions de novo and examines factual findings for abuse of discretion.*

**Question 3.2** [1a23] [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?**

*In Chapter 15 proceedings, foreign representatives cannot trigger specific provisions of the U.S. Bankruptcy code including avoidance powers [1a24] and priority rules. Avoidance powers are such as the authority to set aside preferential transfers or fraudulent conveyances.*

*Priority rules are used to determine the distribution of assets among the creditors and usually flow down from secured creditors.*

*One way for a foreign representative to obtain equivalent relief is by seeking recognition of the foreign proceeding in the U.S. bankruptcy court. Once this occurs,*

the court could grant assistance to the foreign representative by providing relief equivalent to what would be available under the Bankruptcy Code. Further, the foreign representative can cooperate with domestic courts to utilize the legal mechanisms available in the U.S. to achieve relief<sup>[1a25]f</sup>.

**Question 3.3<sup>[1a26]</sup> [4 marks]**

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

To prepare for a filing with a bankruptcy court, an individual should consult the following:

- The **local Bankruptcy Rules<sup>[1a27]</sup>**, this is as each court will have its own local rules that must be followed, they can include specific procedures and requirements which are particular to that specific State.
- The **Federal Rules of Civil Procedure<sup>[1a28]</sup>**, these outline procedures for a range of necessities including the procedures for filing, conducting hearings and objecting to claims, among others.
- The U.S. itself contains provisions under title 11 of the bankruptcy court relating to substantive provisions, so reviewing the Bankruptcy Code is essential.
- **Judge's personal practices<sup>[1a29]</sup>** should also be considered as judges may develop their own practices for the management of cases, the handling of motions and other areas within the broader framework of the established rules, understanding these can enable a bankruptcy filing to be more or less successful.
- Any provision under local district court rules can also affect a bankruptcy filing, and those who are filing should be aware of these rules to ensure that their filings are complicit with these to maintain a successful application.

All of these considerations are usually available on the website of the relevant bankruptcy court to which they are applying. Particularly as local rules and practices can modify the deadlines for filings and responding to pleadings.

**Question 3.4<sup>[1a30]</sup> [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?**

In the state of incorporation, director liability is governed by state law and is generally more restricted in the U.S. compared to other jurisdictions. Under Delaware law, directors owe a fiduciary duty exclusively to **shareholders<sup>[1a31]</sup>**, both in solvent and insolvent situations, with **no obligation to creditors even when shareholders may not recover anything<sup>[1a32]</sup>**. Directors are mandated to act in the best interest of the company and exercise care in informed decision-making. They owe a duty of **loyalty<sup>[1a33]</sup>** and a duty of **care<sup>[1a34]</sup>** to the shareholders, which obligates them to act in the best interest of the corporation and its shareholders, avoid conflicts of interest and prioritize the

welfare of the corporation over personal interests whilst exercising reasonable care, skill and diligence. When the corporation is potentially or actually insolvent, the duties extend to include consideration of the interests of the creditors, while maintaining a duty to act in the best interest of the shareholders.

The business judgement rule operates on the assumption that directors have acted with adequate information, good faith, and an honest belief in the best interest of the company and its shareholders. Unless this assumption is challenged, directors remain shielded from liability. Consequently, concepts akin to wrongful trading or deepening insolvency, prevalent in some legal systems, do not have equivalents in U.S. law.

**QUESTION 4** [1a35] (fact-based application-type question) [15 marks in total]

**Question 4.1** [1a36] [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?***

*If iWork Ltd was to file a proceeding under the bankruptcy code, unpaid rent accrued after the filing of such a petition would be considered as an administrative expense [1a37], these expenses are given priority over the distribution of assets which will increase the likelihood that the building owners will receive payment for post-petition rent ahead of other unsecured creditors.*

*The lessor could bring an insolvency proceeding against iWork, this would grant an automatic worldwide stay which would prevent other interested parties from bringing any other action against iWork to collect the debts. However, it should be noted that the stay can be lifted on creditor request by way of a lift-stay or relief from stay motion due to a lack of adequate protection where the value of the buildings could decline during the course of proceedings [1a38] which may prevent the creditor from making a less than full recovery. If adequate protection is found to be lacking, then the building owners could avoid this stay from being lifted.*

*If iWork filed for bankruptcy, they have the option to either assume or reject the existing leases. [1a39]*

*To assume the lease, they can continue the lease agreement and fulfil contractual obligations under the lease, by paying the existing defaults to the build owners or addressing any other breaches of the lease it may have defaulted on under the executory contract clause, which applies to both chapter 7 and 11 proceedings. This would cure the existing defaults and the building owners will receive the overdue rent as part of the assumption process.*

*The building owners can also request adequate assurance of iWork's ability to meet its future lease obligations ahead of agreeing to the assumption of these leases, this would protect future defaults and ensure a more stable agreement going forward.*

*Although, the Company can reject the lease, which is when the Company is stating that they no longer want to be bound by the lease agreements, in doing this iWork surrenders the leased premises to the lessor, in this case the building owners and relieves themselves of any further obligations. This would then turn any claim the building owners have against the Company into an unsecured claim<sup>[1a40]</sup>, which would not be in favor of the building owners.*

**Question 4.2<sup>[1a41]</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.***

*If Skin Luxe was to file an English Scheme of Arrangement, which could be recognized under the US chapter 15 as a foreign proceeding, however whether it is recognized as main or non-main would be determined by whether the proceedings are opened in Skin Luxes' COMI or not.*

*In the case of Skin Luxe there are a number of factors which could decide where their COMI is. Their headquarters and primary management activities are situated in France, which suggests that the central decision-making processes and administrative functions are predominantly located in France. Furthermore, as the research and manufacturing facilities are located in France, this suggest that their primary assets are located here, which would also lend the court to thinking that the COMI is in France.<sup>[1a42]</sup> As Skin Luxe operates internationally, creditors could be found in any of these jurisdictions which could draw varying conclusions for this consideration of COMI.*

*Although the bonds are governed under English Law, this does not provide enough information to assume that English Law will apply to most of the Company disputes, therefore the above factors, based on information provided, the conclusion drawn would be that the COMI sits in France.*

*Therefore, for recognized under a chapter 15, the filing would have to be made as a non-main foreign proceeding<sup>[1a43]</sup>.*

*To be recognized under a chapter 15 there are certain requirements that Skin Luxe will have to be established:*

- *That a foreign court or administrative proceeding is pending*
- *That the foreign representative is empowered to act by the proceeding*
- *That the proceeding is commenced for the adjustment of debts*

*Skin Luxe should meet the above requirements as their proceeding is being established to adjust debts, and they will be able to appoint an appropriate foreign representative.*

*However, if Skin Luxe does not have an establishment in England, which information has not been provided<sup>[1a44]</sup>, then the scheme cannot be recognized under chapter 15.*

**Question 4.3<sup>[1a45]</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?***

*During the insolvency proceeding an automatic stay would be given<sup>[1a46]</sup>, which means that any proceeding against the debtor is suspended. This would allow the debtor an amount of breathing space to propose a plan to reorganize its debts whilst continuing to operate during the ordinary course of business.*

- (i) If a chapter 11 was filed an investigation into insider trading by the department of justice could be considered as criminal proceedings, in this case the automatic stay would not extend to these proceedings, and the investigation would not be affected by the chapter 11 proceedings, and the investigation would likely continue.<sup>[1a47]</sup>*
- (ii) The margin loan default would be affected by the chapter 11 petition's triggering of an automatic stay as it prevents creditors, including the broker who declared the default on the margin loan, from taking any further action to collect debt<sup>[1a48]</sup>s.*
- (iii) The automatic stay would also be applied to the delinquent lease, as it applies to lease-related actions. As a result, the landlord who is owed rent would be prohibited from pursuing eviction or other collection actions<sup>[1a49]</sup> during the bankruptcy proceedings. Speculation Inc would have the opportunity to negotiate with the landlord in the restructuring plan.*
- (iv) The automatic stay would also be affected by the automatic stay as it applies to civil suits. Therefore, the lawsuit would be stayed<sup>[1a50]</sup>, and the bankruptcy court would need to decide whether to allow this to proceed.*

*It's crucial to recognize that, although the automatic stay offers immediate relief, circumstances and court decisions may lead to actions to lift the stay or permit specific proceedings to proceed.*

**\* End of Assessment \***