

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.**
- (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.

(d) A retired employee of Car Corp who receives payments from the company's pension plan.

Commented [FV2]: 1, correct

(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.

Commented [FV3]: 1, correct

(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.

Commented [FV4]: 1, correct

(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 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]: 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?

The instrument of setoff gives a creditor the option of offsetting the debtor's claims against this creditor against their own payment obligations to the debtor. In the best case scenario, the creditor can use this method to completely cancel the debtor's claim or at least significantly reduce it.

Commented [FV11]: 1, correct

The justification for a ban on setoff in various scenarios under US insolvency law arises from the resulting unequal treatment of the debtor's creditors.

Every other creditor who has no security for their claims and has no claim against the debtor is disadvantaged when it comes to the possibility of offsetting against their own claims. The debtor's assets are reduced by the amount offset, which is no longer available to the other creditors.

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 lien is a loan security, i.e. a means of securing payment claims against the debtor for the debtor's default. A lien can be granted by the court as a so-called "priming" lien, which has priority over other liens with regard to the fulfilment of the claim secured by it after the insolvency proceedings.

The creditors who have a "priming lien" are considered first in the distribution of the proceeds at the end of the proceedings. Unsecured claims are satisfied from the unencumbered assets according to a statutory order of priority. Depending on how many assets remain at the end of the insolvency proceedings, the unsecured creditors are satisfied in proportion to their claims. These creditors therefore receive a dividend.

*A "priming lien" is granted under the following conditions: Due to the very high costs that a debtor has to bear in the course of the proceedings, financing of the proceedings, so-called DIP financing, is regularly required to enable the debtor to be reorganized. If the debtor is not in a position to obtain such external financing of the proceedings because it cannot provide sufficient security, the court can grant the "priming" lien. To do so, the debtor **must** prove that the interests of the creditor then secured are sufficiently protected.*

Commented [FV12]: 1.5. Full credit not given because answer did not refer to adequate protection which is defined in the Bankruptcy Code

Question 2.3 [2 marks]

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

The concept of the automatic stay protects the debtor's assets from enforcement measures by creditors in respect of claims that are already due.

If a creditor violates the automatic stay and continues to carry out enforcement measures against the debtor's assets, these measures are voidable due to contempt of court. According to the case law of the US Supreme Court, the stay conveys such action that the status quo of the debtor's assets.

*If the parties do not take the opportunity to lift the stay, the court can impose **sanctions** against the creditor for contempt of court. The court is also able to impose coercive measures in cases of particular urgency, such as daily fines.*

Commented [FV13]: 1.5. Full credit not given because the answer does not mention that the act may be void (and not just voidable).

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) *Creditors, who are deemed to accept the plan*

In principle, not all creditors have to accept a reorganization plan. The Bankruptcy Code allows the court to carry out a "cramdown".

Consent is always expected from the creditor group that is not considered to be severely "impaired", i.e. that does not expect a significant loss of its claims. This is also the case if impending maturities are announced and the due dates are postponed.

(ii) *Creditors, who are deemed to reject the plan*

A rejection of the reorganization plan is regularly expected from the group that must expect a significant loss of its claims in connection with the reorganization plan.

(iii) Creditors, who are permitted to vote on the plan

Only those classes of creditors whose claims are affected by the plan of reorganization are entitled to vote on the plan of reorganization. An "impaired" creditor is any creditor whose claims are affected by the plan of reorganization. Delayed payment also constitutes an impairment.

The approval of a certain class of creditors if a simple majority votes in favor of the plan. However, this simple majority must unite two-thirds of the total creditor claims. In the case of equity investments, two thirds of the value of the investment must vote in favor of the plan.

Commented [FV14]: 1 point. Correct answer for (i) is Unimpaired creditors are deemed to accept a plan. Correct answer for (ii) class that will receive nothing are deemed to reject.

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) Cause of Action on Account of antecedent Debt

For an action for restitution of an amount that the debtor has spent to settle old liabilities from the debtor's assets, there must be no simultaneous consideration for the debtor's payment to the debtor's assets.

The prerequisite for a claim arising from a liability that has already arisen is based precisely on the fundamental idea that there must be a veritable period of time between the creation of the liability and its settlement by the debtor. A claim can therefore not be considered if the transfer of assets takes place as a simultaneous exchange for a new value.

The cause of action is based on "preferences", i.e. transfers of the debtor's assets that took place in a suspicious period before the petition date and must be returned to the estate. The avoidance of preferential rights is intended to ensure equal treatment of creditors and prevent a race between creditors.

(b) Cause of Action when debtor is presumed or insolvent

An action for reimbursement of asset disposals in connection with the insolvency of a debtor, which presupposes that insolvency was at least imminent or had already occurred at the time of payment, concerns the cause of action of "constructive fraudulent conveyance".

A so-called constructive fraudulent conveyance presupposes that the debtor has received less than the appropriate equivalent value in return for his own performance or the assumption of liabilities and that the debtor was already insolvent at the time of performance or became insolvent as a result of the transaction, for example.

(c) Cause of Action when debtor intended to frustrate creditors' recoveries

If an action for restitution of assets in connection with the insolvency of a debtor presupposes that the debtor demonstrably intended to damage the debtor's assets

Commented [FV15]: 2. Credit was not given for (b) as the answer is also a preference.

and thereby frustrate the claims of the creditors, this is the cause of action for "actual fraudulent conveyance".

This variant of a fraudulent transfer of assets essentially requires the debtor's intention to cause damage to assets through the transfer, as insolvency was at least imminent at the time.

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

Commented [la16]: 12.5/15

Question 3.1 [3 marks]

Commented [la17]: 3/3 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.

1. Final Order

The so-called bankruptcy courts have emerged in the course of legislative history, in particular from the Bankruptcy Code of 1978, and do not find their justification in Art. 3 of the US Constitution like the other federal courts. As numerous issues arise in insolvency proceedings that do not fall within the jurisdiction of the courts, the district courts initially have jurisdiction over bankruptcy proceedings, which then refer these proceedings to bankruptcy courts in their own jurisdiction.

According to the provisions on the referral procedure, only so-called "core matters" can be referred to the bankruptcy court. These matters are derived from a list contained in the referral regulations. The "other" matters are heard by the bankruptcy courts and referred to the district courts with proposals. When an application is made for a bankruptcy matter, it must be emphasized in the application whether it is a "core" matter or an "other" matter.

Based on a decision from 2011, the US Supreme Court will also make a further differentiation with regard to the jurisdiction of the bankruptcy courts. Thus, even in "core" matters, the bankruptcy courts do not have exclusive jurisdiction if the jurisdiction under Art. 3 and thus the jurisdiction of the federal courts is encroached upon.

Following the Supreme Court's decision, case law has helped to bring clarity to jurisdictional structures. For example, the courts always have jurisdiction for applications to open bankruptcy proceedings, but the final decision on the application can then be made by the bankruptcy courts. If a "core" matter is involved, as in Art. 3, the matter is treated in the same way as other matters and the bankruptcy court refers the matter back to the district court with a proposal.

Commented [la18]: Correct, 1/2 mark, also the bankruptcy court can enter a final order in a core matter with the consent of the parties

Commented [la19]: Correct, 1 mark, called a report and recommendation or findings of fact and conclusions of law

2. Review Appeals

If an appeal is filed against final orders in connection with bankruptcy proceedings, these appeals must typically be filed with the district courts in which the bankruptcy court that issued the contested order sits.

Commented [la20]: Correct, 1/2 mark

There are exceptions to this in certain judicial districts where special Bankruptcy Appellate Panels (BAP) have been established, which are made up of judges from the bankruptcy courts in the respective districts. In these jurisdictions, those who wish to

Commented [la21]: Correct, 1/2 mark

appeal against final orders of the bankruptcy courts may also file such appeals with the respective district courts.

Appeals can be filed against the decisions of the district courts or the BAP on the appeals filed, which must then be directed to the Circuit Court of Appeal.

In some cases, if the bankruptcy court or the district court certifies that there is not yet a court decision, including the Supreme Court, on the specific question of the appeal, appeals against decisions of the bankruptcy courts can be directed to the Circuit Courts of Appeal directly.

3. Review Orders

If the bankruptcy court has not made a "final" order, it is not up to the district court or the BAP to review the correctness of all findings of fact and conclusions of law.

Question 3.2 [3 marks]

Commented [la22]: 2.5/3

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?

1. Provisions not be invoked by a Foreign Representative

If a foreign representative of the debtor files for bankruptcy proceedings in the USA under Chapter 15 of the Bankruptcy Code, a foreign main or ancillary proceeding is regularly recognized in the USA. The requirements for recognition are rather low. Although Chapter 15 is closely modelled on the UNCITRAL Model Law, it is narrower in one place or another.

Thus, Art. 23 of the Model Law provides that the foreign representative should have the right to contest insolvency in the same way as domestic representatives. However, Chapter 15 actually excludes the option of avoidance under the Bankruptcy Code for foreign representatives.

Commented [la23]: Correct, 1 mark

2. Ways to equivalent Relief

Alternatively, the foreign representative should be able to challenge transactions under US law other than the Bankruptcy Code. This is consistent with cases brought under Section 304 of the Bankruptcy Code.

Commented [la24]: Correct, 1/2 mark, the foreign representative can also invoke applicable foreign law

In addition, the foreign representative may exceptionally, after recognizing proceedings under Chapter 15, initiate full proceedings within the meaning of Chapters 7 or 11, which provide for the options to contest insolvency. This is possible by the foreign representative initiating plenary proceedings for determination as full proceedings. In this case, the proceedings are limited to the debtor's US assets. This is typically considered if the foreign avoidance law is not satisfactory, for example because the statute of limitations has already expired.

Commented [la25]: Correct, 1 mark

Question 3.3 [4 marks]

Commented [la26]: 2/4

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

Firstly, the legal identity of the debtor should be clarified. This is important because some organizations are already excluded from the possibility of bankruptcy under the Bankruptcy Code. For example, insurance companies or banks are excluded from bankruptcy proceedings and are instead subject to state or federal proceedings.

It must then be taken into account in which state of the USA the bankruptcy proceedings are to be conducted. The Bankruptcy Court takes precedence over the law of the individual states. However, where there are no legal conflicts, the relevant federal law must be applied. This applies, for example, to the determination of the debtor's assets and claims.

The next step is to work out which enforcement measures or other security measures have already been taken against the debtor's assets. These proceedings are deemed obsolete in favor of the debtor when bankruptcy proceedings are opened. This is relevant in order to be able to conduct constructive proceedings including the debtor's existing assets.

Finally, the provisions of the Bankruptcy Code apply to the bankruptcy proceedings. The Federal Rules of Civil Procedure, which are regularly referred to in the Bankruptcy Code, must also be included. This applies, for example, to dispute resolution. Although there are similar forms for filing for bankruptcy throughout the USA, attention must also be paid to the local practices of the competent bankruptcy courts. It is often the case that there are local procedural rules that are not generally reflected in the forms. In order to check to what extent these local deviating procedural rules exist, it is essential to visit the bankruptcy court's website before filing and to check whether such local procedural rules are provided for.

Commented [la27]: Correct, 1 mark

Commented [la28]: The Bankruptcy Rules are separate from the Bankruptcy Code,

Commented [la29]: Correct, 1 mark, in addition to the rules of the bankruptcy court, each judge in a district may have their own personal practices

It should also be noted that the interpretation of the Bankruptcy Code is largely characterized by case law, as common law applies in the USA. This can lead to different interpretations depending on the court of appeal in whose district the bankruptcy proceedings are to be conducted. Care should therefore be taken to ensure that the Bankruptcy Code is interpreted in accordance with current case law.

All in all, it is therefore advisable to consult a local specialized lawyer who is familiar with the practices.

Question 3.4 [5 marks]

Commented [la30]: 5/5 marks

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

1. Fiduciary Duties of Directors of Delaware Corporations

Under Delaware law, directors have two essential fiduciary duties that they must comply with. The first is the fiduciary duty of loyalty to the best interests of the company. The second is the fiduciary duty of care in the director's decision to manage the company.

Commented [la31]: Correct, 1 mark

Commented [la32]: Correct, 1 mark

However, potential liability of the director for wrong decisions is kept within narrow limits by the business judgement rule. According to this rule, it is generally assumed that the director always acted in good faith and with sufficient information. This presumption can be rebutted, but only by proving that the director was not sufficiently informed and did not act in good faith in the matter. The presumption protects the director as long as no gross negligence is proven.

Furthermore, exemption from liability in the event of a breach of duty of care is also possible under the articles of association.

2. Addressees of the Fiduciary Duties

The director owes the fiduciary duties "only" to the company as such and to the shareholders. There is no such duty towards the company's creditors.

Commented [la33]: Correct, 1 mark

Commented [la34]: Correct, 1 mark

3. Addressees in the Event of Illiquidity

Even in the event of illiquidity, the director remains solely obliged to the company and the shareholders. The creditors are still not the addressees of the director's fiduciary duties, even if they have the most to lose in an insolvency situation. This principle has also been confirmed by the Delaware Supreme Court. There is no concept of "wrongful trading" or "deepening insolvency" by the director.

Commented [la35]: Correct, 1 mark

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

Commented [la36]: 8/15 marks

Question 4.1 [5 marks]

Commented [la37]: 0/5

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 event that iWork Ltd should seek bankruptcy proceedings under the Bankruptcy Code due to its financially strained situation, iWork Ltd as debtor is initially protected from further access by debtors to its assets by the "automatic stay". The lessor of office space to iWork Ltd cannot demand any further rent. If iWork Ltd decides to take over the lease, iWork Ltd must remedy all defaults, including payment of all pre-bankruptcy obligations to the landlord. In this respect, by taking over a lease, the landlord is put back in the position it would have been in had there been no bankruptcy. If a lease is rejected, the landlord gets the rented premises back and has the right to claim unsecured damages (usually up to one year's rent).

Commented [la38]: Incorrect, while the landlord cannot evict for pre-petition unpaid rent, it has a claim in the bankruptcy for pre-petition unpaid rent and post-petition, the rent must be paid as an administrative expense prior to the date the debtor assumes or rejects the lease.

It is true that iWork Ltd can initially take its time in deciding how to deal with the rental agreement as the debtor. However, according to the Bankruptcy Code, in the case of commercial tenants, landlords are protected from losses due to the passage of time to the extent that it is provided that the debtor-tenant under a commercial lease is obliged to "fulfil all obligations of the debtor in a timely manner until the lease is assumed or rejected".

Commented [la39]: Incorrect, the debtor has 120 days to assume or reject the lease, which may be extended up to 90 days for cause, and following that only with the consent of the landlord. Also, if the debtor assumes and then later rejects the lease, the landlord has an administrative priority claim for 2 years of rent.

Question 4.2 [5 marks]

Commented [la40]: Correct, however inconsistent with the first paragraph of this response

Commented [la41]: 4.5/5

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 order to be able to address the question of recognition of the English scheme of arrangement under Chapter 15 of the Bankruptcy Code, the requirements for recognition of foreign proceedings under Chapter 15 must first be discussed in general terms. In principle, recognition is very simple. The foreign representative of the debtor "only" has to prove that foreign court or administrative proceedings are pending in relation to the debtor and that the foreign representative is authorized to act within the framework of these proceedings. A foreign proceeding is defined in the

Bankruptcy Code as "a collective judicial or administrative proceeding in a foreign country ... under a law relating to insolvency or debt settlement in which the assets and affairs of the debtor are subject to the control or supervision of a foreign court for the purpose of reorganization or liquidation."

It therefore does not matter for the time being that the Scheme of Arrangement does not involve French law, but that English insolvency law is to be applied in France. The only relevant factor for recognition as foreign proceedings is that the proceedings are based on an "insolvency law", which is the case here. English schemes of arrangement have already been recognized under these conditions.

In the recognition stage, a distinction must then be made between the main and non-main proceedings, which proves to be essential, as the scope of relief depends on this categorization.

Insolvency proceedings are deemed to be foreign main proceedings if they are conducted at the debtor's head office. It is generally assumed that the head office is the place where the debtor was founded. However, this presumption can also be rebutted. Factors in favor of the head office are the location of the management; the location of the most important assets; the location of the majority of the debtor's creditors or the majority of the creditors who will be affected by the legal protection sought by the foreign representative and the jurisdiction whose law will apply to most disputes.

Commented [la42]: Partially correct, 1/2 mark. Main proceedings are those in the jurisdiction of the debtor's COMI, which is presumed to be in the place of the headquarters, but if that presumption is rebutted, proceedings not in the jurisdiction of the headquarters

Proceedings are deemed to be non-main proceedings if they are to be conducted in a legal system other than that of the company's main office. In this case, recognition is only possible if the debtor had at least one establishment in the other legal system before the proceedings were initiated, from which it carried out a non-transitory economic activity.

Commented [la43]: Correct, 1 mark

On the basis of this presumption and the other factors, it can be assumed that Skin Luxe is headquartered in France.

Commented [la44]: Correct, 1 mark

Firstly, Skin Luxe is based in France, where it was founded. The goods are also manufactured and developed in France. The management is based in France and the main assets are located there. The fact that Skin Luxe distributes its products worldwide through boutiques does not prevent this. As the general business operations take place in France, it can also be assumed that the majority of Skin Luxe's creditors in connection with production are based in France. Although the Scheme of Arrangement is an English procedure and there are also assets in England, such as the bonds, the overall context clearly favors a head office in France.

Skin Lux's plan to achieve a restructuring via an English scheme of arrangement is a procedure in a jurisdiction outside France and therefore outside Skin Lux's COMI. It must therefore be examined whether the requirements for the recognition of non-main proceedings are met. For the procedure to be recognized as a non-main procedure,

Skin Lux would already have to have an establishment in the jurisdiction of the English Scheme of Arrangement.

Skin Lux also sells its skincare products through its own boutique in London. The place of establishment in the legal system from which the proceedings arise is the place from which the debtor carried out its economic activity on a more than temporary basis. This applies to the Skin Lux boutique in London, as it was permanently established by Skin Lux for the purpose of distributing its products in London and therefore already existed prior to the proceedings.

Commented [la45]: Correct, 1 mark

It is therefore not apparent that there are any obstacles to recognizing the English scheme of arrangement for Skin Lux based in France as a non-main procedure.

Commented [la46]: Correct, 1 mark

Question 4.3 [5 marks]

Commented [la47]: 3.5/5

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?

1. Effect of a Chapter 11 Petition on DOJ investigation

If Speculation Inc. applies for the opening of proceedings under Chapter 11 of the Bankruptcy Act, Speculation Inc. as debtor initially enjoys the effect of the "automatic stay of payments". Any enforcement actions by creditors against Speculation Inc's assets will be stayed upon the filing of the petition.

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Speculation Inc. should be able to continue its operations in the normal course of business in order to propose a reorganization plan to its key partners that can eliminate its debts. The scope of the automatic stay is very broad.

Of course, the effect of the automatic stay also has its limits. In principle, all measures that impair the debtor's assets and make restructuring difficult or even impossible should be prevented. One legal exception to the automatic stay is, for example, criminal proceedings or official investigations.

As the investigation by the US Department of Justice (DOJ) is an official investigation, the opening of Chapter 11 proceedings has no effect on the DOJ investigation.

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2. Effect of a Chapter 11 Petition on margin loan default

In proceedings opened under Chapter 11 of the Bankruptcy Code, Speculation Inc as the debtor has the option of adjusting the debts arising from the loan by way of a plan of reorganisation.

Initially, Speculation Inc benefits from the effect of the "automatic stay", as this also suspends the outstanding loan agreement for the time being. It is precisely this effect that is intended to give Speculation Inc, as the debtor, "breathing space" to think about how to deal with the loan agreement. During the automatic stay, it is not possible for the broker to declare the loan due after Speculation Inc defaults and to enforce the outstanding claims against Speculation Inc under the agreement.

As long as the stay is in effect, Speculation Inc can propose a plan as a chapter 11 bankruptcy debtor that delays a defaulted loan, "cures" all defaults (with certain exceptions), and restores the original terms of the debt - with the result that the clock is reset to the time before the default.

If the lender's claims are not "impaired" by Speculation Inc's proposal of the plan, it is assumed that the lender agrees and the lender is not given any further opportunity to actively vote. The plan must originally provide for the defaults to be cured in full and, in particular, for the lender's default losses to be compensated.

3. Effect of a Chapter 11 Petition on the delinquent Lease

Speculation Inc also benefits significantly from the effect of the automatic stay with regard to the rental agreement in arrears. The rental agreement is also placed in a state of suspension and the landlord is prevented from enforcing overdue rental payments against Speculation Inc.

As the tenant, Speculation Inc then has the choice of how to deal with the lease. Typically, the tenant can decide to assume, reject or assume and assign the contract. Assumption and rejection is done by filing a petition with the bankruptcy court, which is served on the landlord and all affected parties. Affected parties may object to the rejection or assumption of a lease and submit arguments and evidence to the bankruptcy court.

As a rule, the debtor must continue to pay the rent and other obligations under the lease until the decision to assume or reject the lease is made, but not rent arrears and other rental obligations that arose prior to the bankruptcy (these are instead enforced in the bankruptcy proceedings).

If a debtor chooses to assume a lease, they must pay the landlord all arrears and "cure" all other breaches of contract prior to the assumption. If a debtor chooses to reject a

Commented [la50]: Incorrect, the margin loan is a securities contract that is exempt from the automatic stay so the lender can sell the shares to pay down the loan.

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lease, the landlord is entitled to damages in the amount provided for in the Bankruptcy Act.

4. Effect of a Chapter 11 Petition on the employment discrimination lawsuit

The "automatic stay" caused by the application to open proceedings under Chapter 11 also has the consequence that ongoing court proceedings against the debtor are also stayed. Unless the principle of the automatic stay is violated, the court proceedings against the debtor cannot be continued. This also applies to private actions for discrimination in the workplace.

The legal proceedings against Speculation Inc for discrimination under labour law have therefore also been suspended for the time being. The legal concept underlying this suspension is that the debtor should not be distracted from concentrating on the reorganisation efforts by legal disputes. It is not apparent that the US legislature has provided any special protection for individuals involved in a claim of employment discrimination.

The employee can apply for an "exemption from the stay" in order to continue the proceedings before a non-bankruptcy court.

* End of Assessment *

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