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**SUMMATIVE (FORMAL) ASSESSMENT: MODULE 8A**

**AUSTRALIA**

This is the **summative (formal) assessment** for **Module 8A** of this course and must be submitted by all candidates who **selected this module as one of their elective modules**.

**The mark awarded for this assessment will determine your final mark for Module 8A**. 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 (where this must be done is indicated 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 each question. More often than not, one fact / statement will earn one mark, but it is also possible that half marks are awarded (this should be clear from the context of the question, or in the context of the answer).

4. You must save this document using the following format: **[studentID.assessment8A]**. An example would be as follows 202122-336.assessment8A. **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 “studentID” 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 paragraph 7 of the Course Handbook, specifically the information on pages 15 and 16, which deals with plagiarism and dishonesty in the submission of assessments. **Please note that plagiarism includes copying text from the guidance text and pasting it into your assessment as your answer**.

6.The final time and date for the submission of this assessment is **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. The assessment submission portal will close at 23:00 (11 pm) BST (GMT +1) on 31 July 2022. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.

7. Prior to being populated with your answers, this assessment consists of **8 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**

**Select the correct answer**:

If a creditor is dissatisfied with the bankruptcy trustee or liquidator’s decision in respect of its proof of debt, the creditor may:

1. apply to AFSA or ASIC for the decision to be reversed or varied.
2. apply to the bankruptcy trustee or liquidator for the decision to be reversed or varied.
3. bring court proceedings for a money judgment in respect of the debt.
4. apply to the court for the decision to be reversed or varied.

**Question 1.2**

Which of the following **is not** a collective insolvency process:

1. Receivership.
2. Liquidation.
3. Deed of company arrangement.
4. Voluntary administration.

**Question 1.3**

**Select the correct answer**:

Which of the following insolvency procedures **requires** court involvement:

1. creditors’ scheme of arrangement.
2. deed of company arrangement.
3. creditors’ voluntary liquidation.
4. voluntary administration.
5. small company restructuring plan.

**Question 1.4**

**Select the correct answer**:

Newco Pty Ltd has three (3) employees and an annual turnover of AUD 950,000. It currently owes AUD 300,000 to its trade creditors and it has a AUD 800,000 secured loan from its bank. Which of these restructuring processes is Newco **ineligible**for?

1. A voluntary administration followed by a deed of company arrangement.
2. An informal restructuring with the agreement of creditors.
3. A small business restructuring plan.
4. A deed of company arrangement.

**Question 1.5**

**Select the correct answer**:

Which of the following **is not** “divisible property” in a bankruptcy?

1. Wages earned by the bankrupt.
2. Fine art.
3. Choses in action relating to the debtors’ assets.
4. The bankrupt’s family home.
5. Superannuation funds.

**Question 1.6**

Which of the following **is not** a relevant period for the entry into a transaction which constitutes an unfair preference in a liquidation?

1. The six-month period ending on the “relation back day”.
2. The one-year period ending on the relation back day where the creditor had reasonable grounds for suspecting that the company was insolvent.
3. The four-year period ending on the relation back day where the creditor is a related entity of the company.
4. The 10-year period ending on the relation back day where the transaction was entered into for a purpose that included defeating, delaying or interfering with the rights of creditors in the event of insolvency.
5. After the relation back day but on or before the liquidator was appointed.

**Question 1.7**

**Select the correct answer**:

A company can only be placed into voluntary administration if:

1. the directors declare that the company’s liabilities exceed its assets.
2. the creditors resolve that the company is unable to pay its debts as and when they fall due.
3. a liquidator declares that the company is insolvent or likely to become insolvent.
4. the directors resolve that the company is insolvent or likely to become insolvent.

**Question 1.8**

**Select the correct answer**:

A receiver:

1. is an agent of the secured creditor that appointed the receiver.
2. owes a duty of care to unsecured creditors.
3. is an agent of the company and not of the secured creditor that appointed the receiver.
4. is an agent of the company until the appointment of a liquidator to the company.
5. is required to meet the priority claims of employees out of assets subject to a non-circulating security interest.

**Question 1.9**

**Select the correct answer**:

Australia has excluded from the definition of “laws relating to insolvency” for the purposes of Article 1 of the Model Law the following parts of the Corporations Act:

1. The part dealing with schemes of arrangement.
2. The part dealing with windings up of companies by the court on grounds of insolvency.
3. The part dealing with taxes and penalties payable to foreign revenue creditors.
4. The part dealing with the supervision of voluntary administrators.
5. The part dealing with receivers, and other controllers, of property of the corporation.

**Question 1.10**

**Select the correct answer**:

Laws regarding the following came into effect on 1 January 2021:

1. an *ipso facto* moratorium in voluntary administrations and liquidations.
2. simplified restructuring and liquidation regimes for small companies.
3. reducing the default bankruptcy period from three years to one year.
4. a safe harbour from insolvent trading liability*.*

**QUESTION 2 (direct questions) [10 marks]**

**Question 2.1 [maximum 3 marks]**

Name the three types of voidable transactions that can be reversed by a bankruptcy trustee and describe the circumstances in which such a transaction will not be reversible.

Voidable transactions include:

1. Unfair preferences
2. Uncommercial transactions,
3. Unreasonable director-related transactions or unfair loans.

The unfair preference and uncommercial transactions provisions can be reversed if a transaction was entered into when the company was insolvent or resulted in the company’s insolvency. If there are new consideration (eg. Services or goods) provided to the company by a creditor in exchange for payment, this is not constituted as an unfair preference. If a reasonable person would have entered into the transaction under the company’s circumstances, then it is not an “uncommercial transaction” and may not be reversed.

The unreasonable director-related transactions and unfair loan provisions do not have the same insolvency limitation, but only apply to a limited range of transactions. If there is no payment, transfer of property in favour of director or their associate, and a reasonable person would have entered into the transaction under those circumstances, then the transaction would not be deemed “unreasonable director-related” transaction and may not be reversed.

In a simplified liquidation, only unfair preferences of more than AUD30,000 that were made to related parties of the company three months prior winding up can be recovered as voidable transactions.

**Question 2.2 [maximum 3 marks]**

How does a court determine the scope of the stay in relation to a corporate debtor under Australia’s implementation of Article 20 of the Model Law?

Australia has specified the scope of stay under Article 20 of Model Law as the same that would apply if the stay or suspension arose under:

1. The Bankruptcy Act; or
2. Chapter 5 (other than Parts 5.2 and 5.4A) of the Corporations Act,

As the case requires.

Under Australian’s implementation of Article 20 of the Model Law, the Australian courts have to decide if the case requires a broader voluntary administration stay affecting secured creditors or a limited liquidation stay affecting only unsecured creditors, which depends on the nature of the proceeding, rather than the scope of stay that is available in the foreign jurisdiction. If the foreign proceeding is one that is of a corporate rescue nature, then the former will be more appropriate; if the foreign proceeding is one that is of a liquidation nature, then the latter is more appropriate.

**Question 2.3 [maximum 4 marks]**

What is an *ipso facto* clause and what is the relevance of *ipso facto* clauses in liquidations?

*Ipso facto* clause allows the contracting party, in event of insolvency or commencement of insolvency-related proceeding, to terminate, amend any terms or rights in any agreement.

Subject to certain exclusions, as of 1 July 2018, when a company is in the process of voluntary administration, creditors are no longer able to enforce on *ipso facto* contractual rights contingent only on a company’s insolvency or entry into an external administration to terminate or amend contracts.

For personal bankruptcies, pursuant to the Bankruptcy Act, *ipso facto* clauses are voided upon the bankruptcy of an individual.

Liquidators are not able to utilize the benefit of *ipso facto* enforcement prohibition which applies during bankruptcy. A creditor or supplier has the right to terminate its contract upon the company being wound up, which will restrict the ability of liquidators to conduct an orderly wind down process to preserve value.

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

“Australia’s insolvency and restructuring options have in the past been very creditor-friendly. However, recent reforms have made Australia more of a debtor-friendly jurisdiction.“

Critically discuss this statement and indicate whether you agree or disagree with it, providing reasons for your answer.

In the past, Australia is often considered a creditor-friendly jurisdiction due to its focus on protecting creditors’ rights in insolvency processes. Australia’s bankruptcy and insolvency cases predominantly requires a third-party administrator be appointed, rather than it being a debtor-in-possession restructuring. The exceptions are for schemes of arrangement, and small business restructurings where directors retain their positions, however, a qualified insolvency practitioner must still be appointed as advisor, and these are recent reforms that have just been introduced

Generally, it is observed that secured creditors retain their rights to enforcement, to the extent they are allowed for in insolvency processes (where moratorium doesn’t apply). For example, during bankruptcy and winding up of businesses, secured creditors remain entitled to enforce their rights against their security. Where the whole of or substantially whole of company’s assets are charged to a creditor, even if a voluntary administrator has been appointed, the creditor may choose to appoint a receiver over the top of the appointed voluntary administrator.

Similarly, existing Australian laws lean towards protecting creditors’ interests such as insolvent trading liability for directors and voidable transactions, which are designed to allow clawback of funds owed to creditors for wrongdoings.

The above being said, recent reforms are designed to make the existing laws more debtor-friendly and provide breathing room for businesses to restructure / turn around. Examples of recent reforms include:

1. *Ipso Facto* moratorium

In the case of an appointment of voluntary administrator to perform formal corporate rescue, it is often observed that creditors would invoke their *ipso facto* contractual rights and/or enforce their securities where the voluntary administration moratorium did not apply. This resulted in limited success of corporate rescues under Deed of Company Agreement (DOCA).

The new *ipso facto* moratorium is intended to improve the likelihood of a company being restructured or preserved as a going concern to improve returns to creditors, whilst investigations into the company’s affairs are being conducted by the voluntary administrator and proposing to creditors whether DOCA is feasible. This, however, does not prevent secured creditors from exercising their rights to appoint a receiver over the top of a voluntary administrator. The success of a restructuring is still dependent on the support of lenders, which are often secured creditors.

1. Safe harbour from insolvent trading

Prior to section 588GA of the Corporations Act, which allows for safe harbour from insolvent trading, being in force, directors would be personally liable for insolvent trading. Hence, it is commonly observed that if the business is insolvent or could be insolvent, directors would appoint a voluntary administrator to shield themselves from personal liability.

With Section 588GA in place, this will allow directors to pursue informal restructuring attempts with the financial advice of restructuring experts to improve business viability over time, where there is a reasonable prospect of turning around the company. In the case of an informal restructuring, the *ipso facto* moratorium does not apply, creditors and suppliers may still choose to enforce their rights to terminate and/or amend key contracts. Hence, the success of the turnaround of the business is still dependent on the support of creditors. Similarly, this is not immunity for directors from personal liability as they have to remain actively involved in formulating and executing a restructuring plan and to continue managing the business finances with their best effort.

While the safe harbour and *ipso facto* moratorium reforms are important steps in the right direction in promoting corporate rescue and moving Australia to be a more debtor-friendly regime, the success of any restructuring still depends on a mindset shift in the creditor enforcement culture, which will require some time to materialize. Until then, Australia would continue to be seen as a more creditor-friendly jurisdiction than a debtor-friendly jurisdiction where creditors interests are protected as priority, sometimes at the expense of businesses.

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

**Question 4.1 [maximum 9 marks]**

Aussiebee Pty Ltd (Aussiebee), a company incorporated in the fictional country of Lyonesse, sells chocolates flavoured with Australian native plants. The chocolates are manufactured in Australia by NewYums Pty Ltd (NewYums), an Australian-incorporated wholly-owned subsidiary of Aussiebee.

Aussiebee has offices and warehouses in both Sydney and in Lyonesse. Aussiebee regularly sells its chocolates all over the world, from both its Lyonesse and its Sydney offices and warehouses. Aussiebee and NewYums share a board of directors, made up of six Australians and one Lyonessian. Aussiebee employed 40 staff: 20 in Sydney and 20 in Lyonesse. Aussiebee’s CEO is an Australian, but resident in Lyonesse. Aussiebee’s CFO is an Australian, resident in Australia.

Aussiebee is insolvent. NewYums, however, remains solvent.

A liquidator has been appointed to Aussiebee in Lyonesse. She applies to the Federal Court of Australia for recognition of the Lyonessian liquidation as a foreign main proceeding, and for orders entrusting Aussiebee’s assets (including Aussiebee’s shares in NewYums which are worth AUD 20 million) to her, so that she can realise them for the benefit of creditors in the Lyonessian liquidation.

Aussiebee owes AUD 12 million in taxes in Australia, payable to the Australian Taxation Office (ATO). Assume that revenue creditors such as the ATO are not entitled to prove in the Lyonessian liquidation.

You are advising the ATO. What should the ATO do to protect or improve its position?

This is a similar case to that of *Ackers v Deputy Commissioner of Taxation* where a Cayman Islands liquidator applied for recognition in Australia to remit proceeds from sale of Australian assets to Cayman Islands for distribution as Cayman Islands liquidation is recognised at the foreign main proceeding*.* In that case, the Deputy Commissioner of Taxation (DCT), applied to the Federal Court for modification of recognition orders to provide leave to DCT to enforce its claim in Australia for up to the amount of the *pari passu* amount that the ATO would be entitled to as an unsecured creditor in the foreign main proceeding. On subsequent appeal, the Full Court also held that the modification of recognition order was an appropriate way to ensure that interests of DCT is adequately protected as required by Article 22 of the Model Law when court grants relief under Article 19 of the Model Law.

As the situation here is similar, ATO may rely on the previous judgment in *Ackers v Deputy Commissioner of Taxation* to request that the recognition order provide leave for ATO to take steps to enforce its claim in Australia to recover the amount up to the *pari passu* amount the ATO would have received if entitled to prove for the tax debt as an unsecured creditor is the foreign main proceeding.

In addition to the above, as Aussiebee employs 20 staff in Australia, there could be tax fillings that Aussiebee may not have complied with in relation to employee tax obligations. If applicable, the ATO may issue penalty notice to directors regarding Aussiebee’s failure to remit withholding amounts for employee personal income tax and superannuation.

To the extent there are tax refund owing Aussiebee, ATO would be allowed to retain these funds on the basis that Aussiebee has failed to make payment of AUD12m due to ATO.

Furthermore, as the assets in Australia (NewYums) are likely to be sold and proceeds to be transferred to Lyonesse, outside of Australia, such transfer of funds will be subject to withholding tax. ATO may seek an order that requests for ATO to be notified for any sale of NewYums and other assets in Australia and for any relevant tax filings be completed and withholding tax be made in full prior to any transfer of funds be made to Lyonesse for the purposes of distribution to Aussiebee’s estate. Any transfer of funds to Lyonesse should be made net of withholding tax amounts and *pari passu* amount due to ATO as unsecured creditor if entitled to prove for tax debt in Aussiebee’s liquidation.

**Question 4.2 [maximum 6 marks]**

Hyrofine Australia Pty Ltd (HA) is a company incorporated in Australia. It is in the business of re-refining waste oil from electric substations in Australia and selling the re-refined oil. All of the shares in HA are owned by HA’s parent company, Hyrofine Group Ltd (HGL), also incorporated in Australia. The same Board of directors controls both HGL and HA.

HA operated an oil re-refining plant near Sydney, Australia as a joint venture with Best Oil Refining Pty Ltd (BOR). The joint venture proved to be unprofitable and the plant ceased operations in mid-2020.

HA’s major remaining asset is a second re-refining plant that it operates near Perth, Western Australia. This plant has only been in operation for one year. The funding for the Perth plant has been provided by a major shareholder of HGL as an unsecured loan for AUD 30 million. The loan agreement provides that the loan is repayable by monthly instalments over a term of 5 years with the first payment due at the end of 2021. The loan agreement also provides that the loan becomes automatically due and payable in full if HA enters into any formal insolvency or restructuring process in Australia.

HA also owns three large trucks that transport waste oil to the Perth re-refining plant and transport re-refined oil to HA’s customers. Those trucks were purchased with a AUD 3 million loan from the Commonwealth Bank of Australia (CBA). That loan is secured by mortgages over the three trucks. The mortgages are not registered on the Personal Property Securities Register.

In July 2020, BOR commenced proceedings against HA in the Supreme Court of New South Wales for damages in respect of the failed joint venture. On 1 October 2020, the Supreme Court found in favour of BOR, ordering that HA pay AUD 4.6 million in damages to BOR.

Between October 2020 and October 2021, HA continued to trade, incurring debts to trade creditors as well as borrowing AUD 5 million from its parent company HGL. It made only a small profit from its Perth re-refining plant.

In October 2021, you are called in to advise the Board of directors of HGL and HA about the financial predicament of HA. The Board tells you that HA has been insolvent since the judgment was handed down in October 2020, because HA does not earn enough from its second refining plant to meet the judgment debt and to start repaying CBA at the end of 2021. The Board also tells you that there is no more funding available for HA’s operations, and that they have exhausted all possibilities for refinancing HA’s debts.

What do you advise the Board to do about HA? What are the main issues that the board of HGL and HA should be aware of in light of the facts set out above?

1. The board may be personally liable for insolvent trading as they have confirmed that HA has been insolvent since the judgment was handed down in October 2020. The court may also impose civil penalties, disqualification orders and if directors have behaved dishonestly, a criminal penalty. The directors may be held liable for the debts incurred since Oct 2020, due to trade debtors, as well as the AUD5m of shareholder’s loan provided by HGL to HA. This is especially so since the directors did not attempt to appoint a restructuring expert to guide them through an informal restructuring attempt, despite being aware of the financial difficulties facing HA.
2. Given that HA is insolvent, the directors should make a decision which insolvency procedure would be best, whether it would be better to appoint a voluntary administrator or place the company into liquidation. In this case, as there is still an operating asset, i.e. the Perth re-refining plant (the “Perth Plant”), it may be viable to appoint a voluntary administrator to continue operating the Perth Plant, with a view to sell it as a going concern to maximize recoveries to creditors than if a liquidation is pursued.
3. As the 3 trucks are secured to CBA on the AUD3m loan, CBA may choose to enforce on the trucks upon the appointment of the voluntary administrator. However, as the mortgage was not registered on the Personal Property Securities Register, the security has not been perfected and CBA may face issues enforcing their rights. Upon the appointment of voluntary administrator, CBA will be deemed to have lost the security and the 3 trucks will vest in HA’s estate unless the court allows for any extension of time for registration of the security.
4. By placing HA into a voluntary administration, BOR will not be able to enforce their unsecured claims against HA. However, it is noted that the shareholders loan provided by HDL to HA will similarly become immediately due and payable and HGL will become an unsecured creditor of HA.

**\* End of Assessment \***