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.

2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 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: **[studentnumber.assessment8A]**. An example would be something along the following lines: 202021IFU-314.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 "studentnumber" 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. The final submission date for this assessment is **31 July 2021**. The assessment submission portal will close at **23:00 (11 pm) GMT on 31 July 2021**. 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 **7 pages**.

ANSWER ALL THE QUESTIONS

Commented [DB1]: 35.5 out of 50 = 71% Well done!

QUESTION 1 (multiple-choice questions) [10 marks in total] 10/10

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:

(a) apply to AFSA or ASIC for the decision to be reversed or varied.

(b) apply to the bankruptcy trustee or liquidator for the decision to be reversed or varied.

(c) bring court proceedings for a money judgment in respect of the debt.

(d) 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:

(a) Receivership.

(b) Liquidation.

(c) Deed of company arrangement.

(d) Voluntary administration.

Question 1.3

Select the correct answer:

The purpose of the Assetless Administration Fund is to:

(a) finance preliminary investigations and reports by AFSA to trustees into the bankruptcies of individuals with few or no assets, to assist trustees in deciding whether to commence enforcement action.

(b) finance preliminary investigations and reports by ASIC to liquidators into the failure of companies with few or no assets, to assist liquidators in deciding whether to commence enforcement action.

(c) finance preliminary investigations and reports to AFSA by trustees into the bankruptcies of individuals with few or no assets, to assist AFSA in deciding whether to commence enforcement action.

(d) finance preliminary investigations and reports to ASIC by liquidators into the failure of companies with few or no assets, to assist ASIC in deciding whether to commence enforcement action.

Question 1.4

Select the correct answer:

Newco Pty Ltd has 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?

(a) A voluntary administration followed by a deed of company arrangement.

(b) An informal restructuring with the agreement of creditors.

(c) A small business restructuring plan.

(d) A deed of company arrangement.

Question 1.5

Select the correct answer:

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

(a) Wages earned by the bankrupt.

(b) Fine art.

(c) Choses in action relating to the debtors' assets.

(d) The bankrupt's family home.

(e) 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?

(a) The six-month period ending on the "relation back day".

(b) The one-year period ending on the relation back day where the creditor had reasonable grounds for suspecting that the company was insolvent.

(c) The four-year period ending on the relation back day where the creditor is a related entity of the company.

(d) 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.

(e) After the relation back day but on or before the liquidator was appointed.

Question 1.7

Select the correct answer:

A receiver:

(a) is an agent of the secured creditor that appointed the receiver.

(b) owes a duty of care to unsecured creditors.

(c) is an agent of the company and not of the secured creditor that appointed the receiver.

(d) is an agent of the company until the appointment of a liquidator to the company.

(e) is required to meet the priority claims of employees out of assets subject to a non-circulating security interest.

Question 1.8

Select the correct answer:

A voluntary administrator must convene and hold a first meeting of creditors within how many business days of his appointment?

(a) 3 business days.

(b) 8 business days.

(c) 12 business days.

(d) 24 business days.

(e) 45 business days.

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:

(a) The part dealing with schemes of arrangement.

(b) The part dealing with windings up of companies by the court on grounds of insolvency.

(c) The part dealing with taxes and penalties payable to foreign revenue creditors.

(d) The part dealing with the supervision of voluntary administrators.

(e) 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:

(a) an *ipso facto* moratorium in voluntary administrations and liquidations.

(b) simplified restructuring and liquidation regimes for small companies.

(c) reducing the default bankruptcy period from three years to one year.

(d) a safe harbour from insolvent trading liability.

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 3 marks] 3/3

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.

The three types of voidable transactions are: (a) Undervalued transactions; (b) transfers to defeat creditors; and (c) preferential payment to creditors.

Transactions that fall during the relation back period but undertaken in good faith, in the ordinary course of business and in absence of notice of creditors or debtor's petition, are not reversible i.e., voidable. It is also pertinent to highlight that in the event the property of the debtor has been transferred by the original transferee to a third party and such third party has received the property in good faith and for a market value, then such property will not be recoverable.

Excellent answer

Question 2.2 [maximum 3 marks] 3/3.

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?

The scope of stay under Article 20 of the Model Law (in CBIA, s 16) would be equal to the stay or suspension that may arise under either the Bankruptcy Law or Chapter 5 (other than Parts 5.2 and 5.4A) of the Corporation Act. Good. When the courts are deciding the foreign proceedings recognition applications, the scope of stay of the court will be determined by considering what "the case requires" principle. This principle is applied to determine whether the court should adopt broader voluntary administration stay (affects secured creditors) or the standard liquidation stay (affects only unsecured creditors). Consequently, if a foreign proceeding is a business rescue, the broader voluntary administration will be appropriate and if it is analogous to liquidation then liquidation stay will apply. Good. Could also state that it is not a question of discretion, but rather which stay should apply according to the nature of the proceeding: *Tai-Soo Suk v Hanjin Shipping Co Ltd* [2016] FCA 1404 at [24].

Question 2.3 [maximum 4 marks] 2/4

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

Ipso facto means "by that very fact or act". *Ipso facto* clause means the right of a counter party to render any provision of the contract void and exercise the right to terminate, modify or repossess the property upon the debtor's insolvency or bankruptcy.

Ipso facto clauses come handy during the liquidation scenario. For example: in the event a debtor has a material supply or services agreement, which is crucial from conducting the business or selling of business as a going concern then the liquidator can take the benefit of prohibition of enforcement of ipso factor clause that applies during bankruptcy subject to one exception. The exception is *ipso facto* moratorium being invoked under a specific circumstance. No.

The stay on the operation of *ipso facto* clauses only applies to restructurings (ie during a voluntary administration, or while negotiating a scheme of arrangement), so once a company is in liquidation, the *ipso facto* clause will operate and the liquidator will not be able to keep contracts with *ipso facto* clauses on foot. See Guidance Text, p 30.

QUESTION 3 (essay-type questions) [15 marks in total] 10/15

"Creditors' schemes of arrangement are costly and time-consuming and are an ineffective corporate rescue mechanism in Australia."

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

A creditors' scheme of arrangement can be costly and time consuming but are effective in complex restructuring. In scheme of arrangement under the Corporations Act, the director enters discussions with the creditors to secure support for the proposed restructuring. They need to collect and submit a host of information to ensure that they have full information about company's financials. This is needed for the scheme document, and it is a time-consuming process to collate and discuss with each creditor. Once the directors are convinced that they have sufficient support for taking the scheme through, they will have the company make an application for convening a creditor meeting for approving the scheme. However, if the creditors are proposed to be treated differently under the scheme, the court will order meetings of each class of creditors (class being treated basis the differentiation). Further, each class of creditors will be required to satisfy two conditions on voting: (a) the majority of that class present and vote; and (b) 75% the debt and claims of creditors of that class present and vote. Consequently, even if one class of creditor does not vote in the above manner the same may result in Scheme not being approved. Hence, it runs an inherent risk of one class of creditor holding up the Scheme. Good point.

If the scheme gets approval from each class of creditor in the manner as stated above, then a second application will be required for approval of the scheme. On scheme being approved, it will be implemented as per the terms of the scheme. If it has payments to be made to the creditors over a period, then an appointment of an administrator will be appropriate for overseeing the implementation. It is also important to highlight that the moratorium on enforcement of *ipso facto* clauses will be available for creditors' scheme of arrangement. This further enhances the business rescue aspect as it prevents the dissatisfied creditors from enforcing their security interest. Good.

As mentioned above, discussion with the creditors and court involvement, the creditors' scheme of arrangement is a costly and time-consuming process as against a voluntary administration/DOCA as it may take up to six months to implement this. In case of voluntary administration/DOCA, the whole process can be completed after 25-30 business days of voluntary administration. However, it has two important and highly effective aspects. These are: (a) binds the dissenting creditors, if it meets the voting requirements as mentioned above; and (b) can release the creditors' rights in third parties other than the creditor. This is very effective in case of complex and competing creditors' interest scenario.

To conclude, the creditors' scheme of arrangement can be costly and time consuming, but it is effective in case of complex restructurings.

You have made only the points that are made on pp 54-55 of the Guidance Text.

Other points include: DOCAs can be terminated by the court, schemes are already approved by the court so are not vulnerable to being terminated by the court. In preparing a DOCA, the company has the benefit of the broad stay on all creditor action that applies during a voluntary administration. That stay does not apply while preparing a scheme.

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

Question 4.1 [maximum 9 marks] 4.5/9

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?

The prominent case relevant for ATO here is *Ackers v. Deputy Commissioner of Tax ((2014) 223 FCR 8; [2014] FCAFC 57)*, where the court was considering an application under Article 19 for granting relief upon application for recognition of a foreign proceeding. As per Article 19, the court may grant relief such as staying of execution proceedings or entrusting administration of debtor's assets. However, as per Article 22, the court while granting such as relief should consider whether the 'interests of the creditors are adequately protected'.

Facts of the above case is like the case cited herein. But here the application will be under art 20 for the automatic stay, and under art 21 for vesting of the property – not under art 19 (interim relief pending recognition).

ATO should file an application with the Federal Court to grant leave of the court to enforce its AUD 12 million in taxes claim in Australia on a *pari-passu* basis assuming that ATO would be entitled to prove its debt as an unsecured creditor in the foreign proceeding i.e., Lyonessian liquidation proceedings. The court will be inclined to grant this order as it will be protecting the interest of the Australian creditors. Yes.

You missed the first issue, being whether recognition should be granted at all, and whether main or non-main. The ATO should intervene on the recognition application, arguing that:

- The COMI of Aussiebee is Australia, not Lyonesse, and so the assets of Aussibee should not be entrusted to the Lyonessian liquidator.
    - *Ackers v Saad Investments* is the leading Australian decision on COMI. It followed and expressly adopted the principles in *Re Eurofoods IFSC Ltd* that COMI is to be determined having regard to the objectively ascertainable factors of the debtor.
    - Need to displace presumption that place of incorporation is COMI
    - Six of the seven directors are Australians
    - The CEO is Australian (although resident in Lyonesse)
    - The CFO is Australian and resident in Australia
    - Sells Australian product, manufactured by its subsidiary in Australia.
    - Do not know whether Aussiebee holds itself out to be an Australian-based company, but its name and its product seem to indicate that it does.

Question 4.2 [maximum 6 marks] 3/6

Shipmin Pty Ltd (Shipmin) is a company incorporated in Australia. Shipmin owned two cargo ships, one valued at AUD 20 million, the other at AUD 15 million. About 3 months ago, Shipmin sold the AUD 20 million cargo ship and paid the full proceeds of AUD 20 million to its parent company Shipmax Ltd (Shipmax) to reduce Shipmin's intercompany debt to Shipmax. Shipmax is also incorporated in Australia and owns 100% of the shares in Shipmin.

Shipmin now owns only the one cargo ship with a value of AUD 15 million. Shipmin owes AUD 20 million to the Commonwealth Bank of Australia (CBA), which is secured by a mortgage over the remaining ship. The mortgage is not registered on the Personal Property Securities Register.

Shipmin's debt to CBA has been guaranteed by Shipmax. Shipmin owes Shipmax AUD 180 million in inter-company debt. Shipmin has no other creditors.

Shipmax has been placed into liquidation. Advise Shipmax's liquidator on the best way to bring the operations of Shipmin to an end and maximise the return to Shipmax from the assets of Shipmin.

Firstly, Shipmax should enforce the AUD 180 million inter-company debt to Shipmin by taking Shipmin to insolvency. This is one option, but Shipmax could simply have the directors of Shipmin resolve to place Shipmin into creditors voluntary liquidation without needing to go to court at all. On Shipmin entering insolvency, Shipmax liquidator should focus on "mortgage over the ship" not being registered on the Personal Property Securities Register ("**PPSR**"). PPSR comes under the Personal Property Securities Act, 2009. This is

an important legislation as it creates a database for registering charges over non-circulatory (fixed charge) and circulatory assets (floating charge). As per the act, once a security interest is granted it should be perfected. Shipmin's security over the ship is not perfected as it is not registered with PPSR. Security can be perfected by registration, control or possession. In the above case, none of this has been done, consequently the mortgage is not perfected. Once the mortgage is established as non-perfected, the security will be lost once the debtor enters insolvency i.e. in this case Shipmin entering insolvency and it will vest with the debtor immediately prior to the commencement of the insolvency. Yes, good.

Shipmin will retain the ship and CAB will become an unsecured creditor. Further, if the inter-company debt is an unsecured debt, both CAB and Shipmax will be get the estate funds on a *pari-passu* basis as there are no other creditors. Yes.

The better alternative would be voluntary administration. Immediately before the Shipmin enters voluntary administration, the mortgage over the ship will vest in the voluntary administrator.

The voluntary administration can then sell the ship to provide a return to unsecured creditors, or the creditors can vote to place Shipmin into a DOCA. Shipmax will carry any vote on value, as there are only two creditors and Shipmax holds the overwhelming majority of the debt.

You missed the other major issue: liquidation would be risky, because Shipmax may find itself the target of:

- a preference claim by the liquidator for the $20 million already repaid to Shipmax in the last 12 months. Shipmax as the parent company would have had knowledge of Shipmin's insolvency.
- creditor-defeating disposition claim (see Guidance Text, pp 75-76)

If Shipmax can get Shipmin into a DOCA whereby the remaining ship is sold and the proceeds paid equally to all unsecured creditors, Shipmax will receive most of the assets of Shipmin, as its unsecred debt to Shipmax ($200m) swamps the now-unsecured debt to CBA ($20m).