INSOL INTERNATIONAL
FOUNDATION CERTIFICATE
in INTERNATIONAL INSOLVENCY LAW

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]: 34.5 out of 50 = 69%

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.(Section 6.4.3)

(d) is an agent of the company until the appointment of a liquidator to the company.(Section 6.4.3)

(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.

There are three types of voidable transactions that can be reversed by a bankruptcy trustee are :-
a) undervalued transactions;
b) transfer to defeat creditors; or
c) preferential payment to creditors.

However, if the transaction occurred during the relation back period but were transacted in good faith in the ordinary course of business and in the absence of notice of a creditor's petition or debtor's petition, such a transaction will not be reversible (s 123). Also, if the original debtor transferred the property to a third party who received in good faith and for market value, such transfer is not reversible by a bankruptcy trustee (s 120(1)).

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?

Under Australia's implementation of Article 20 of the Model Law (in s 16 *CBIA*), it was specified that the stay would apply if the stay or suspension arose under the Bankruptcy Act or Chapter 5 (other than Parts 5.2 and 5.4A) of the Corporations Act as the case requires. Hence, the court has to consider the nature of the case whether the cases required to grant a recognition application and determine the extent of the stay which was required in the case Good- could also add that it is not a question of discretion:*Tai-Soo Suk v Hanjin Shipping Co Ltd* [2016] FCA 1404 at [24]). Under the case law of Rizzo-Bottiglieri-De Carlini Armatori SpA v Rizzo-Bottiglieri-De Carlini Armatori SpA [2018], the Judge commented that the court

should determine the scope of the stay by the nature of the proceeding so as to determine whether it is more analogous to an Australian voluntary administration or a liquidation. If the foreign proceeding is clearly a business rescue procedure, it requires the boarder voluntary administration stay which affects secured creditors. However, if the foreign proceeding is more analogous to liquidation, a standard liquidation stay should be apply (only affects unsecured creditors).

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?

An ipso facto clause is a contractual provision which was entered into prior to a specified insolvency related event of restructuring (such as the appointment of an administrator, receiver or liquidator). It allows one party to the contract to terminate, not to enforce or modify the operation of the contract upon the occurrence of a specified insolvency related event of restructuring in respect of another party eg on the company entering voluntary administration or because of the company's general financial position while it remains in voluntary administration (s 451E Corporations Act). However, such clause to stay on enforcing rights should be created in the contracts prior to the company comes under restructuring. Otherwise, such rights are not stayed. Subject to the Court's approval, the ipso facto clauses could be extended or limited or enforced with its leave.

Need to come back to the specific question asked – what is their relevance *in liquidations*? The answer is that the stay on the operation of *ipso facto* clauses only applies to restructurings (as you've identified above), 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.

Undeniably, the creditors' scheme of arrangement is a complex, costly and time-consuming process compared with other corporate rescue process, such as voluntary administration or deed of company arrangement process.

The complexity and the cost of the creditors' scheme of arrangement is due to the significant involvement of the court and high percentage of creditors' agreement being required. The creditors' scheme of arrangement requires 2 court applications. Firstly, after the directors obtain a good level of support for the proposed scheme of arrangement, they would make an initial application to court for an order to convene the creditors' meeting. The court will require resolutions to be obtained in multiple meetings each class of creditors. In each class of the creditor's meeting, the majority of creditors should be present and voting at the meeting while 75 percent of the total amount of the debts and claims of creditors present and voting at the meeting should be in support of the Scheme. To achieve the approval from creditors in each class, it was not uncommon to take months to come up with a treatment which are widely accepted by each class and/ or take more time to reach consent from creditors from each class at the multiple meetings.

This arrangement requested the company to provide a scheme which could be widely accepted by the majority of the creditors in each class. Also, creditors in each class are

given the chance to vote separately which lower the chance of unfairness or unjust situation such as major creditors being given preferential treatment dominate the creditors' meeting.

After the scheme is approved, a subsequent court application is required to formally approve the Scheme. The court would review the before granting the approval. Such arrangement would create less subsequent challenges from creditors as the fairness of the meeting was reviewed by court. The arrangement was also approved by court. Hence, the chance of further rebut was slim. Excellent point.

The scheme of arrangement procedure is established under the Corporations Act. Even the proposed scheme documents are prescribed which required certain matters being compulsory to be disclosed to creditors, such as creditors' expected dividends under the scheme compared to a winding up of the company, the extent and amount of creditors' claim and comprehensive information about the company's financial and other affairs. The strict requirement, even its format and content of the documents, creates more transparency to the scheme and allow a easy comparison for the creditors to make their decision. It allows the creditors to make a rational decision after receiving a rather full picture of the financial situation of the company.

Hence, these processes, though lengthy and costly, increases its recognition and legitimacy among other voluntary administration. It permits less challenges from dissent stakeholders which might also release the creditor's rights against third parties other than the company. Hence, this is an effective corporate rescue mechanism in Australia.

Important points: schemes offer considerable advantages which cannot be achieved under a DOCA, of particular note the ability to bind dissenting secured creditors and to include third party releases within the scope of a scheme. When a company is in voluntary administration and considering a DOCA, the company has the benefit of a broad stay on creditor action. The same does not apply when 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 liquidator of the Aussiebee applied to the Federal Court of Australia for recognition of Lyonessian liquidation as a foreign main proceeding in Australia. However, Aussiebee owes AUD 12 million in taxes in Australia being payable to the Australian Taxation Office ("ATO") which was not admissible to proof in Lyonessian Liquidation. To improve the situation of ATO, when the liquidator was applying orders entrusting Aussiebee's assets (including Aussiebee's shares in NewYums which are worth AUD 20 million) to her, ATO could make an application seeking modification of the recognition orders to issue statutory notices and take other recovery action, including action to obtain payment of the tax debt on a pari passu basis from the assets in Australia. Yes.

The Model Law which imported foreign insolvency law into Australia do not disallow domestic tax debts not to be recovered. Also, there was no legislative or common law basis which destroyed the rights of the ATO to seek leave to proceed against Aussiebee in liquidation or to employ his enforcement rights under tax legislation.

When granting or modifying relief under the Model Law, the Court must ensure that the interest of local creditors are protected. The Courts in Australia have the power to make orders under the Model Law to protect the ATO's ability to recover revenue liabilities from assets located in Australia in circumstances where the debt would not be admitted in a foreign liquidation. Refer expressly here to *Ackers v Seputy Commissioner of Taxation* and the requirement to provide "adequate protection" under art 22 of the Model Law. The court could exercise discretion by making the modification orders that the ATO's rights as a local creditor would have been transformed into a foreign creditor. Also, the court permitted the ATO to recover a pari passu entitlement which also uphold the principles of fairness between all creditors.

You missed the first issue, which is whether Model Law recognition would be granted at all, and whether as a main or non-main proceeding. 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.
- These arguments might not succeed, the Court might still find that the COMI is in Lyonesse and grant main recognition.

Question 4.2 [maximum 6 marks] 2/6

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.

Shipmin owes AUD 20 million to the Commonwealth Bank of Australia ("CBA"), which is secured by a mortgage over the remaining ship (a cargo ship which worth around AUD 15 million. However, such mortgage is not registered on the Personal Property Securities Register. Failure to register or otherwise perfect a security interest can cause the loss of the security on insolvency unless an application by CBA to court to extend the time for registration showing sufficient cause or the security interest was granted more than six months before the external administration or it was registered within 20 days of its having been created. Good. Shipmin owed AUD 180 million to Shipmax who was the largest creditor of Shipmin. To maximize the return to Shipmax from the assets of Shipmin, Shipmax's liquidator should consider to pursue a creditors' voluntary liquidation/ compulsory liquidation against Shipmin. Yes, or a voluntary administration. The moment before a liquidation or voluntary administration commences, CBA's security interest in the ship will automatically vest back in Shipmin. When the liquidator was appointed, the liquidator could proceed to take possession of the Shipmin's property. After realizing the assets, Shipmax and CBA could be paid pari passu from the remaining assets.

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 one of the issues: a 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).