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]: 29 out of 50 = 58%

QUESTION 1 (multiple-choice questions) [10 marks in total] 9/10

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] 0/3

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.

[Three types of voidable transactions that can be reversed by a bankruptcy trustee are as follows;

- Unfair Preferences
- Uncommercial Transactions
- Unreasonable Director Related Transactions

Following are the circumstances where the voidable transactions can't be reversed If party to the transaction has carried out the transaction:

- in good faith;
- paid valuable consideration or changed its position pursuant to the transaction and
- was unaware of the grounds for suspecting the company to be insolvent or would become insolvent at the time of making such transaction.]

The question was about *personal bankruptcy*, not *corporate liquidation*.

Question 2.2 [maximum 3 marks] 2.5/3

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?

[Australia specified the scope of the stay in relation to a corporate debtor under Australia's implementation of Article 20 of the Model Law (in CBIA, s 16) as same would apply as if the stay or suspension has happened pursuant to the provisions of Bankruptcy Act, 1966 or Corporation Act, 2001 (Chapter 5, other than Parts 5.2 and 5.4A). However while considering a recognition application in respect of a corporate debtor, the Australian Court should decide upon the scope of stay on case to case basis.

Deciding the scope of stay will depend upon the nature of proceeding (could also add that this exercise is not a question of discretion: *Tai-Soo Suk v Hanjin Shipping Co Ltd* [2016] FCA 1404 at [24])., like if foreign proceeding is in the nature of business rescue, then voluntary administration which is broader and affects secured creditors will deemed to be fit whereas if foreign proceeding is more oriented towards liquidation of the corporate debtor, then liquidation which affects only unsecured creditors will be better option. Good. However defining of scope of stay will be an strenuous task if there is lack of clarity with regard to the business rescue or liquidation intended from the proceeding.] Good answer overall.

Good answer overall, just missing a bit of detail required on the nature of administration v liquidation stays for full marks.

Question 2.3 [maximum 4 marks] 2.5/4

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

[*Ipso facto* clause is a clause in commercial contracts that permit a party to terminate (or modify) the contract (or reposess property) on the occurrence of certain pre-defined insolvency related events of the counterparty. Good, but need to have more detail about these insolvency events- e.g. upon a debtor's bankruptcy (s 301 Bankruptcy Act), or upon the company entering voluntary administration or because of the company's general financial position while it remains in voluntary administration (s 451E Corporations Act).

Generally during a compulsory or voluntary liquidation, liquidation is entitled to disclaim certain properties like unsaleable property or land with onerous covenants. Not relevant. However if a liquidator wishes to maintain a supply contract for the time being in order to keep the corporate debtor undergoing liquidation as a going concern then liquidator will not be subject to one exception i.e *ipso facto* clause. In other words allowing supplier or contractor to terminate the contract on the ground of liquidation of the company. This exception relates to the situation where prior creditors liquidation the corporate debtor was undergoing voluntary liquidation. In such case *ipso facto* moratorium will get invoked.]

The answer is that the stay on the operation of *ipso facto* clauses only applies to restructurings, 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. The "exception" noted in the Guidance Text, p 30 simply notes that, if the liquidation was preceded by a VA or negotiations for a scheme, then the ipso facto moratorium would have applied *during the VA or the scheme negotiations*.

QUESTION 3 (essay-type questions) [15 marks in total] 8/15

"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.

[The Creditors Schemes of Arrangement is a restructuring tool for distressed corporates under Corporation Act, 2001. Under this route the directors of the corporate debtor undergoing financial instability enters into negotiation with a proposed restructuring scheme with the creditors of the company to gain in their support or confidence to restructure such

company's debts and operations before the formal declaration of the insolvency of the company.

This process requires various disclosures to the creditors of the company with regard to the actual financial position and operations of the company, extent to which creditors will be repaid, assets and liabilities of the company and other on-going business operations. If directors are able to secure the necessary support from the creditors 9especially secured creditors) and key financers of the company, then a formal application is made to the Australian Court to pass an order for convening the meeting of all the creditors of the company with regard to the approval of the scheme. Court may even order for different meetings to be convened for different class of creditors.

Approval of restructuring scheme requires support of majority of creditors present in person and voting at the meeting comprising 75% of the total amount of debt and claims owed to them by the corporate debtor. Where different meeting is held for different class of creditors then separate voting is required for each meeting.

Upon obtaining the requisite voting from the creditors, again an application is made to the court for obtaining formal court approval on the restructuring scheme. Upon considering the application its completeness in terms of the necessary disclosures, proper conduct of meeting of creditors, non-existence of biasness and injustice towards any stakeholders. Upon approval of scheme by court, the scheme will be implemented in the manner provided in the scheme. Though the provisions of Corporation Act, 2001 doesn't require appointment of any administrator to monitor and supervise the implementation of restructuring scheme yet as a practise it will be appropriate to do so.

Accordingly the moratorium on the enforcement of ipso facto clauses under the contracts entered into by the corporate debtor will apply which in turn will ensure the scheme being implemented in efficient and effective manner. Like a two sides of coins, even the Creditors Scheme of Arrangement has both merits as well as some demerits, however the degree of merits outweighs its demerits making it widely use corporate rescue tool across Australia.

Though Creditors Scheme of Arrangement is time consuming, complex, costly and involve huge judicial intervention yet it bind dissenting secured creditors and it can include the release of creditors right against third parties other than the creditors and that's why preferred over other restructuring modes. Creditors Scheme of Arrangement promotes wider restructuring of a distressed corporate with creditors support hand in hand and therefore widely used tool across Australia even for resolving huge stressed accounts.] DOCAs are *much* more widely used than schemes. Schemes are rare. The point is that they are very useful for large corporate group restructurings.

You could have gone beyond pp 54-55 of the Guidance text by making the following points: 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?

[Pursuant to the common law provisions applicable in Australia, an Australian Court will not recognise a foreign judgment if such judgement is contrary to the public policy and also includes proceedings which provides for the non-enforcement of the judgement based on foreign revenue debts or penalties imposed by foreign law. Not relevant. No foreign judgment here.

In the above mentioned case, Aussiebee who owes the statutory liability worth AUD 12 Million towards Australian Taxation Office (ATO) has applied for recognition of the liquidation proceedings against Aussiebee going in Lyonessia before the Federal Court of Australia. Also as per the facts of the case ATO is not entitled to prove its debt in Lyonessian liquidation. Therefore on grounds of the prevailing law of land, Federal Court of Australia will not recognise the liquidation proceeding as a foreign proceeding in Australia on grounds of outstanding foreign revenue debt. No. Australia is likely to recognise the foreign proceeding, but to give the ATO special orders to protect its position.

In order to improve its position in the prevalent situation and also to safeguard its interest as an unsecured creditor, ***ATO shall make an application to Federal Court of Australia that in case such proceeding is getting recognised in Australia then recognition order shall provide for authority to ATO to take adequate measures to enforce its claim in such proceeding for the purpose of recovering an amount upto the pari pasu amount that the ATO would have received if ATO would be entitled to prove its debt as an unsecured creditor in the liquidation proceeding against Aussiebee in Lyonessian***. The similar stand of ATO was upheld by the Federal Court of Australia in the landmark judgment Ackers V Deputy Commissioner of Taxation 92014) 223 FCR 8; [2014]FCAFC 57.] Yes.

You missed the other major issue, that is whether recognition should be granted to the Lyonessian proceeding as a foreign 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.

If only recognised as a foreign non-main proceeding, then the ATO could argue that the shares should not be vested in the Lyonessian liquidator at all.

Question 4.2 [maximum 6 marks] 2.5/6

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.

[As per the facts of the case, the security interest created by Shipmin over the cargo ship with a value of AUD 15 million in respect of amount borrowed from Commonwealth Bank of Australia is not registered on Personal Property Securities Register under Personal Property Securities Act,2009. It means that the unperfected security interest over cargo ship will automatically vest in the hands of Shipmin (only if Shipmin is placed into voluntary administrator or liquidation) thereby resulting in loss of security interest from Commonwealth Bank of Australia thereby making them unsecured creditors.

Since Shipmin's debt has been guaranteed by Shipmax, in order to make Shipmax pay to Commonwealth Bank of Australia, the liquidator of Shipmin has to apply to the court to invoke the guarantee provided by Shipmax.. Upon sale of assets of Shipmin during liquidation and while distribution of proceeds realised from the sale of assets of Shipmin, the liquidator will first pay towards its fees and cost incurred by him towards liquidation proceeding. Afterwards payment will be made to the unsecured creditor Commonwealth Bank of Australia in case any amount is still outstanding after invoking of guarantee by

Shipmax and then remaining amount will be paid to Shipmax towards adjustment of AUD 180 Million. No, CBA and Shipmax will rank equally as unsecured creditors.

Post this, liquidator may apply to the Court for dissolution of the Shipmin.]

The better option is voluntary administration. Shipmax's liquidator should, using her power as the sole shareholder of Shipmin, have the directors of Shipmin place Shipmin into voluntary administration on the grounds of insolvency or likely future insolvency (it owes CBA more than the present value of its only major asset – whilst this is balance sheet insolvency, it may well lead to cash flow insolvency when combined with the collapse of its parent company).

Immediately before the Shipmin enters voluntary administration, the mortgage over the ship will vest in the voluntary administrator because CBA failed to register its security interest on the PPSA. Unperfected (ie unregistered) interests vest in the voluntary administrator immediately before the commencement of a voluntary administration (*Personal Property Securities Act*, s 267).

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 this other important issue: 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).