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 (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:

(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. 0 marks

(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. 1 mark

(b) Liquidation.

(c) Deed of company arrangement.

(d) Voluntary administration.

Question 1.3

Select the correct answer:

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

(a) creditors' scheme of arrangement. 1 mark

(b) deed of company arrangement.

(c) creditors' voluntary liquidation.

(d) voluntary administration.

(e) 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?

(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. 1 mark

(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. 0 marks

(e) Superannuation funds. Correct

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. 1 mark

(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 company can only be placed into voluntary administration if:

(a) the directors declare that the company's liabilities exceed its assets.

(b) the creditors resolve that the company is unable to pay its debts as and when they fall due.

(c) a liquidator declares that the company is insolvent or likely to become insolvent.

(d) the directors resolve that the company is insolvent or likely to become insolvent. 1 mark

Question 1.8

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. 0 marks

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

(e) 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:

(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. 1 mark

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. 1 mark

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

(d) a safe harbour from insolvent trading liability.

7/10 marks

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.

[Type your answer here]

Answer:

The Bankruptcy Act has three different types of voidable transaction clauses that give the bankruptcy trustee the ability to file court documents to have the effects of:

- Undervalued transactions; or
- Transfers to defeat creditors; or
- Preferential payments to creditors.

Circumstances under which the above transactions will not be reversed:

- Undervalued transactions: According to Section 120(3) of the Bankruptcy Act, a transfer that took place more than two years ago (or more than four years ago in the event of transactions involving related parties) and during which the debtor was solvent will not be reversed.
- Transfers to defeat creditors: According to Section 121(4) of the Bankruptcy Act, a transaction cannot be reversed if the transferor paid the market value and the transferee at the time of the transferee was unaware of or could not have reasonably inferred that the transferor's primary goal was to thwart creditors or that the transferor was insolvent or about to become insolvent.
- Preferential payments to creditors: According to Section 122(2)(a) of the Bankruptcy Act, the transaction will not be reversed if the creditor received the payment in good faith, within regular business hours, and in exchange for a worthwhile consideration.

Defences for all voidables:

- Transactions which 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, are not recoverable under the voidable transaction provisions (s 123).
- Also, the bankruptcy trustee will not be able to recover property if the original transferee has since transferred the property to a third party and the third party received the property in good faith and for market value (s 120(1)).

1.5/3 marks

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?

[Type your answer here]

Answer:

Introduction:

The UNCITRAL Model Law on Cross-Border Insolvency is given legal standing in Australia by the Cross-Border Insolvency Act 2008 (Cth) (Model Law). The Federal Court of Australia or the Supreme Court of a state or territory may grant a request under the Model Law from a "foreign representative" to have a foreign insolvency action recognised as a "foreign main proceeding" in Australia. An automatic suspension of actions or processes in Australia involving the debtor's assets, rights, responsibilities, or liabilities is likely the most significant consequence that follows recognition.

Section 16 of the CBIA provides that for the purpose of article 20:

"the scope and the modification or termination of the stay or suspension … are the same as would apply if the stay or suspension arose under: (a) the Bankruptcy Act 1966; or (b) Chapter 5 (other than Parts 5.2 and 5.4A) of the Corporations Act 2001; as the case requires."

Cases:

Justice Rares in *Hur v Samsun Logix Corporation (2015) 238 FCR 483*, held that the operation of the relevant provisions was *"beguilingly ambiguous, since the Corporations Act has a variety of different stay provisions that differentially affect the position of secured creditors, sometimes at different points in the same overall process".*

Furthermore In *Suk v Hanjin Shipping Co Ltd [2016] FCA 1404*, the Federal Court provided guidance on how courts are to determine what stay arises upon recognition of foreign main proceedings under the Cross-Border Insolvency Act 2008; and demonstrated that such recognition can cause maritime lien actions to be stayed. It is also pertinent to note that *Suk v Hanjin Shipping Co Ltd [2016] FCA 1404* was the first occasion on which an Australian court was called on to deliver reasons concerning the interaction between s 16 and article 20.

According to Jagot J., Hanjin's rehabilitation process resembled a voluntary administration under Part 5.3A more closely than a plan of arrangement under Part 5.1 of the Corporations Act in several ways. No legal action against Hanjin, including one to enforce a maritime lien,

may be taken without the written authorization of the foreign representative or with the Court's permission.

Conclusion:

Thus, it can be concluded that the Court while they are considering a recognition application involving a corporate debtor, it must determine what "the case requires," or whether the case calls for either the standard liquidation stay, which only affects unsecured creditors, or the broader voluntary administration stay, which also affects secured creditors. It is not up to the judge to decide which stay should be in effect given the circumstances of the case. The former will be more suitable when the overseas action is obviously a business rescue operation. The latter will be more suitable for processes in other countries that are more like liquidations. Where the foreign procedure is not obviously either a company rescue or a liquidation, nevertheless, challenging questions will be brought up.

3/3 marks

Question 2.3 [maximum 4 marks]

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

[Type your answer here]

Answer:

Introduction:

An ipso facto clause is a clause in a contract that enables one party to call off or change the terms of the agreement if another party experiences a certain insolvency-related event (such the appointment of an administrator, receiver, or liquidation).

A ban on using "ipso facto" provisions in contracts that are activated by the counterparty experiencing specific formal corporate ~~bankruptcy~~insolvency events became effective on July 1, 2018. A note on terminology: in Australian parlance, insolvency and liquidations are for corporations, bankruptcy is for individuals only.

The scope of the moratorium was further modified on January 1, 2021, to take into account the new restructuring regime in Part 5.3B of the Corporations Act.

Ipso Facto Clause in Liquidation:

If ipso facto rights have been included in the contract, a supplier or other contractor can typically end their relationship with the company as soon as the company enters liquidation. If a liquidator wants to continue an important supply contract for a while to help with the temporary operation of the company's business before a potential sale, the liquidator will not benefit from the enforcement prohibition that applies during bankruptcy. Correct

When a debtor declares bankruptcy, the contracts they had in place before that time are still valid. A contract may be rescinded by the bankruptcy trustee, as well as certain other assets, such as land that carries onerous covenants and assets that are difficult to sell. If a contract is renounced, the other party may sue for damages, but they must first provide evidence of their debt in order to do so. This is bankruptcy disclaimer. Same exists in liquidations. But disclaimer is nothing to do with ipso facto clauses. The contracts of essential commodities are not subject to any exceptions either.

As part of recent amendments to the Corporations Act, an exemption to the ipso facto moratorium will take effect on January 1, 2016. In that situation, the moratorium will automatically apply to any creditors' voluntary liquidation that immediately follows a prior voluntary administration or any attempt to negotiate a creditors' plan of arrangement. Yes

When a creditor tries to enforce a contractual claim after a firm enters voluntary administration on the grounds that it has not met a payment or performance obligation, the moratorium will not be applicable. The administrator is free to ask the court to prolong the moratorium on the grounds that the fact that the firm has entered voluntary administration or another set of unfavourable financial conditions is the true reason the creditor is asserting its rights. Not relevant, the question was about liquidations.

2.5/4 marks

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.

[Type your answer here]

Answer:

Introduction:

I disagree with the aforementioned claim that Austalia is becoming more debtor-friendly from being creditor-friendly. Australia is regarded as a creditor-friendly state because it places a strong emphasis on the rights of creditors above those of debtors. There are certain restrictions on the alternatives that troubled corporations may otherwise have, and some rigidity in some of the instruments accessible to insolvency practitioners. For instance, receivership is still practised in Australia, unlike the United Kingdom.

In Australia, creditors are full participants in all insolvency proceedings and are able to assert their legal interests at any stage. Their enforcement rights over secured assets are otherwise unrestricted, with the exception of minor temporal restrictions in a voluntary administration scenario. Unsecured creditors, unlike secured creditors, are not granted a legal right to priority some unsecured creditors get priority over other unsecured creditors, eg employees; nonetheless, because of a special connection they may have with a debtor, they may be able to use that right to demand payment. The ability to clawback unfair preference exists specifically to prevent this from happening.

However, the corporate voluntary administration system and certain recent changes to the corporate insolvency procedure in Australia are intended to foster a trend away from the current dominance of creditors' rights and a stronger corporate and company rescue culture. In particular, the voluntary administration regime works toward increasing the likelihood that an insolvent firm, or as much of its operations as is practicable, would continue to operate under the conditions of a DOCA13 ? as its main objective. Additionally, starting of July 1, 2018, creditors are prohibited from asserting claims based only on a company's bankruptcy in Australia parlance, the word ‘insolvency’ is used in the context of companies and ‘bankruptcy’ is used only in the context of individuals or admission into an external administration. Additionally, the Bankruptcy Act effectively nullifies ipso facto clauses when a

person declares bankruptcy, and corporate directors are given a "safe harbour from insolvent trading liabilities."

Although at the outset it seems to align the debtors interest, however, If observed the main goal in enacting the aforementioned adjustments is to protect the creditor and their potential future interests. How? You need to support this assertion with reasoning.

Recent Amendments: These temporary measures do not seem to have any relevance to whether Australia is more creditor-friendly or debtor-friendly. If they do have any relevance, you have not attempted at all to explain what that relevance is.

As a part of a broader economic reaction to the COVID-19 epidemic, the Australian Government proposed a number of reforms to bankruptcy legislation in March 2020. However, it is important to remember that these were only short-term adjustments made to protect the struggling economy brought on by COVID-19. These brief modifications included:

- a rise in the debt threshold that made it possible for creditors to request a bankruptcy notification
- an extension of the time a debtor has to reply to a bankruptcy notification and the duration of their access to temporary debt protection.

Additionally, beginning of January 1, 2021, those transient adjustments are no longer occurring. Additionally, a change was made to the bankruptcy threshold. This implies:

- Instead of $20,000, the minimum debt that can cause bankruptcy is now $10,000.
- a reduction in the amount of time required for a person to respond to a bankruptcy notice from six months to 21 days;
- relief from creditors is now granted for 21 days rather than six months under temporary debt protection; and
- the legal requirements for filing for bankruptcy have been changed by the government to $10,000 or more.

Conclusion:

Thus it can be conclusively said that Australia is a creditor-friendly jurisdiction because the primary focus is on the protection of creditors' rights in insolvency situations. Instead of being debtor-in-possession processes, almost all bankruptcy and insolvency proceedings in Australia include the appointment of an external administrator. With the exception of minor business restructurings and ~~plans~~ schemes of arrangement, when it is necessary to employ a trained insolvency practitioner as an advisor. Advisor is only for small company restructurings, not for schemes of arrangement. Secured creditors have the right to enforce their claims during a company's bankruptcy and liquidation. Furthermore, Australia's legislation provides for a voidable transaction system and extensive insolvent trading liability for directors, both of which enable for the recovery of substantial sums for the benefit of creditors. The country's insolvency rules give property owners the right to designate a receiver instead of a voluntary administrator.

8/15 marks – you summarised the aspects of Australia's insolvency regime which are creditor-friendly reasonably well, but with some fundamental misunderstandings of the way Australian insolvency law works. Although you very briefly referred to the recent amendments, you did not critically examine them or explain your view that the changes are to protect creditors.

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?

[Type your answer here]

0/9 marks

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?

[Type your answer here]
0/9 marks

*** End of Assessment ***

TOTAL MARKS: 22/50